

Commission Decision (EU) 2015/1073 of 9 January 2015 on the State aid SA.35888 (2013/C) (ex 2013/NN) SA.37220 (2014/C) (ex 2013/NN) SA.38225 (2014/C) (ex 2013/NN) implemented by Cyprus for Cyprus Airways (Public) Ltd (notified under document C(2014) 9362) (Only the English text is authentic) (Text with EEA relevance)

COMMISSION DECISION (EU) 2015/1073

of 9 January 2015

on the State aid SA.35888 (2013/C) (ex 2013/NN) SA.37220 (2014/C) (ex 2013/NN) SA.38225 (2014/C) (ex 2013/NN) implemented by Cyprus for Cyprus Airways (Public) Ltd

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union, and in particular the first subparagraph of Article 108(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1) (a) thereof,

Having called on interested parties to submit their comments pursuant to the provisions cited above<sup>(1)</sup> and having regard to their comments,

Whereas:

1. **PROCEDURE**

1.1. THE FIRST FORMAL INVESTIGATION PROCEDURE (SA.35888)

- (1) In February 2012 the Commission departments were informed through the press that the Cypriot government was contemplating an intervention in favour of Cyprus Airways (Public) Ltd ('Cyprus Airways' or 'the Company'). In order to clarify whether any State aid issues could arise, the Commission opened a case *ex officio*.
- (2) By letters dated 20 February 2012, 15 June 2012 and 23 August 2012 the Commission requested information. The Cypriot authorities replied on 6 April 2012 and on 30 August 2012. On 4 October 2012, a meeting between the Commission and the representatives of the Cypriot authorities and Cyprus Airways took place in Brussels.

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- (3) On 13 December 2012 the Cypriot authorities notified to the Commission the State aid for the rescue of Cyprus Airways (SA.35888). The Commission requested further information by letter of 19 December 2012. The Cypriot authorities replied on 4 January 2013.
  - (4) By letter dated 6 March 2013 ('the decision of 6 March 2013'), the Commission informed Cyprus that it had decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union ('the Treaty') in respect of certain State measures described in Section 3.2.1 below ('the first formal investigation procedure').
  - (5) The Commission decision of 6 March 2013 to initiate the procedure was published in the *Official Journal of the European Union*<sup>(2)</sup>. The Commission invited the Cypriot authorities and interested parties to submit their comments on the alleged aid measures.
  - (6) The Commission received comments from the Cypriot authorities on 31 May 2013. The Commission received comments from five interested parties during the period from 4 April to 3 July 2013. The Commission received the comments of the Cypriot authorities on those submitted by interested parties on 10 September 2013.
- 1.2. THE SECOND FORMAL INVESTIGATION PROCEDURE (SA.37220 AND SA.38225)
- (7) By pre-notification of 22 July 2013 the Cypriot authorities communicated to the Commission a draft restructuring plan and on 23 October 2013 they notified an updated version of that plan ('the 2013 restructuring plan') (SA.37220). The Commission requested further information by letter of 15 November 2013. The Cypriot authorities replied on 10 January 2014.
  - (8) In the context of the regular monitoring of approved or exempted schemes, the Commission services assessed the implementation of a Cypriot training aid scheme<sup>(3)</sup>. The Commission asked information amongst others on training aid to Cyprus Airways (SA.38225), with letters of 3 December 2012, 15 February 2013 and 6 May 2013. The Cypriot authorities replied on 19 December 2012, 14 March 2013 and 30 May 2013.
  - (9) By letter dated 4 February 2014 ('the decision of 4 February 2013'), the Commission informed Cyprus that it had decided to initiate the procedure laid down in Article 108(2) of the Treaty in respect of the State measures described in Section 3.2.2 ('the second formal investigation procedure').
  - (10) The Commission decision of 4 February 2013 was published in the *Official Journal of the European Union*<sup>(4)</sup>. The Commission invited the Cypriot authorities and interested parties to submit their comments on the alleged aid measures.

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- (11) The Commission received comments from the Cypriot authorities on 31 March 2014. On 16 March 2014, the Commission received comments from three interested parties. On 26 June 2014, the Commission received the comments of the Cypriot authorities on those submitted by interested parties.
- (12) The Commission requested further information by letters of 11 April 2014 and 2 July 2014. The Cypriot authorities replied on 11 May 2014 and 8 August 2014.
- (13) By letter dated 14 November 2014, Cyprus agreed to waive its rights deriving from Article 342 of the Treaty in conjunction with Article 3 of the EC Regulation (EC) No 1/1958 and to have the present decision adopted and notified in English.

## 2. THE CYPRIOT AIR TRANSPORT MARKET

- (14) Cyprus has two international airports, Larnaca (LCA — close to the capital Nicosia) and Paphos (PFO). Because of the small size of the island, most travellers from/to Cyprus can easily reach either airport.
- (15) The main origin of incoming passengers is the UK and Russia, with significantly fewer passengers coming from Germany, Sweden and Greece. The inflow of passengers fluctuates depending on the season: during the summer months (July-August) there are more than three times more passengers than during the winter months (December-February). However, traffic from Greece does not have significant seasonal fluctuation.
- (16) Cyprus Airways has an average market share of approximately 15 % of traffic to/from the island (2012 data), but its market share fluctuates depending on the season. The most important markets for the Company are the routes between Cyprus and Greece and between Cyprus and the UK. Cyprus Airways was also active in domestic flights in the Greek market until mid-2013. Certain routes to the Middle East have also been traditional markets for Cyprus Airways.
- (17) Major European airlines have been traditionally active in the same markets as Cyprus Airways. However, some routes to Cyprus are only served on a seasonal basis. More recently, Cyprus Airways has been facing competition also by low cost airlines, sometimes operating from a base in Cyprus.
- (18) The Cypriot economy has been facing difficulties, demonstrated by a GDP contraction since 2009, an increase of the budgetary deficit and an increase in unemployment. Due to the deterioration of its financing conditions, Cyprus has been receiving financial support by the euro area Member States and the International Monetary Fund ('IMF').
- (19) As a result of the recession in Cyprus, but also in other European countries, the number of passengers travelling to and from Cyprus has decreased. The average fare price has also dropped significantly. The future performance of

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the Cypriot market will depend on the recovery in Europe but also the situation of the local economy.

### 3. DESCRIPTION OF THE AID MEASURES

#### 3.1. THE BENEFICIARY

- (20) Cyprus Airways was established in 1947 and its principal activities are the transportation of passengers and cargo by air and other airline-related services. The Company is listed on the Cypriot Stock Exchange. Since the beginning of 2013, following a share capital increase (covered by both formal investigation procedures), the main shareholder of the Company is the Cypriot State with a shareholding of 93,67 % whereas private investors hold the remaining shares.
- (21) At the end of 2013, Cyprus Airways operated scheduled air services to approximately 15 destinations and had a fleet of 6 aircraft (Airbus A320) and approximately 600 employees. It therefore qualified as a large enterprise<sup>(5)</sup>.
- (22) In 2005, Cyprus Airways benefitted from CYP 30 million (approximately EUR 51 million) of rescue aid and in 2007 from a number of restructuring measures consisting mainly of (i) loans of CYP 55 million (approx. EUR 96 million), of which a loan of CYP 45 million (approx. EUR 78 million) was backed by a State guarantee, and (ii) a capital increase of CYP 14 million (approx. EUR 24 million), which involved public and private shareholders on equal terms. Those measures, which included a restructuring plan ('the 2007 restructuring plan'), were approved by the Commission as compatible restructuring State aid<sup>(6)</sup>.
- (23) Cyprus Airways receives an annual compensation for losses incurred as a result of the Turkey overflight ban on Cypriot aircraft. The compensation is based on an aid scheme authorised by the Commission pursuant to Article 107(2)(b) of the Treaty. The beneficiaries of the scheme are airline companies established in Cyprus<sup>(7)</sup>.

#### 3.2. DESCRIPTION OF THE MEASURES

##### 3.2.1. The first formal investigation procedure

- (24) The Commission initiated the formal investigation procedure on 6 March 2013 in relation to the following measures:
- 3.2.1.1. *Measure 1: Contribution by the State to the 2012 share capital increase*
- (25) During the period from September 2012 until December 2012, the State disbursed EUR 31,33 million to Cyprus Airways in the form of 'in advance' payments to a planned share capital increase of a total of EUR 45 million. The amount was paid in tranches.
- (26) In November 2012, a new business plan ('turnaround plan') was communicated to the Commission. The plan envisaged the turnaround of

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the Company in 5 years, based on a capital increase, improved cost and productivity factors, new investments and the reorganisation of the Company into a 'single-class value airline of option-based services'. The plan projected marginal profitability already as of the second year of its implementation. The plan was subject to approval by the existing shareholders, who would be participating in the capital increase necessary for its implementation. Finally, it has not been implemented.

- (27) At the time of granting of measure 1, the Cypriot authorities argued that the State acted like a market economy investor, in order to safeguard its asset until the finalisation of the turnaround plan and the conclusion of the capital increase by all shareholders.
- (28) Furthermore, the Cypriot authorities anticipated that the capital increase would be concluded with a *pro rata* participation of the private shareholders of an additional EUR 13,67 million. However, private shareholders contributed only EUR 106 000, thus the share capital of the Company was only increased by EUR 31,4 million. The shareholding of the State in Cyprus Airways was raised accordingly from 69,62 % to 93,67 %.

#### 3.2.1.2. *Measure 2: Rescue aid*

- (29) On 13 December 2012, the Cypriot authorities notified a rescue aid of EUR 73 million to Cyprus Airways. According to the Cypriot authorities' claim in the notification, that amount reflected the net cash flow needs of Cyprus Airways until 30 June 2013, that is to say, for six months. The rescue aid would be provided as a government loan with an interest of 1,76 % and should be repaid by 30 June 2013.
- (30) The Cypriot authorities claimed that out of the EUR 73 million of the rescue aid, EUR 16,3 million had already been granted to Cyprus Airways in the context of measure 1. The Commission noted in the decision of 6 March 2013 that the Cypriot authorities notified a rescue aid in the form of a loan, whereas the EUR 16,3 million payment was part of a capital increase.
- (31) The Cypriot authorities argued that the rescue aid was necessary, in order to support Cyprus Airways for a short period. They acknowledged the provision of restructuring aid in 2007, but explained that there were exceptional circumstances, which reversed the initial implementation of the 2007 restructuring plan and which impaired the long-term viability of the Company. The circumstances were linked to the financial situation in Cyprus and Greece, two of the main markets where Cyprus Airways is active, as well as the unstable political situation in the Middle East, the effect of the Turkey overflight ban on Cypriot aircraft, the entrance of a new low-fare competitor in the market, allegedly subsidised by a State scheme, and the undercapitalised position of Cyprus Airways.

#### 3.2.1.3. *Measure 3: Ex gratia compensation*

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- (32) According to the notification of 13 December 2012, the Cypriot Council of Ministers decided on 4 December 2012 to grant *ex gratia* compensation to the Cyprus Airways personnel, which would be considered redundant in the context of the Company's restructuring. According to that decision, the conditions for any *ex gratia* compensation were that (i) it would comply with State aid rules; (ii) the trade unions of the Company would accept the new business plan (that is to say the turnaround plan) and (iii) it would not exceed 50 % of the normal compensation to be paid to redundant personnel by the Cypriot Redundant Personnel Fund ('RPF').

### 3.2.2. The second formal investigation procedure

- (33) The Commission initiated the formal investigation procedure on 4 February 2014 in relation to the following measures:

#### 3.2.2.1. Measure 4: Restructuring aid

- (34) On 23 October 2013, the Cypriot authorities notified restructuring aid to Cyprus Airways of EUR 102,9 million, accompanied by a new restructuring plan (that is to say the 2013 restructuring plan), unrelated to the turnaround plan mentioned in recital 26 above. The amount of restructuring aid consisted of:
- (a) The State participation of EUR 31,33 million to the capital increase, already granted in 2012 (measure 1);
  - (b) The tranches of the rescue aid loan already granted to Cyprus Airways (measure 2) in total of EUR 34,5 million. The granted amount would not be repaid by Cyprus Airways and the corresponding debt would be converted into equity;
  - (c) In 2007 and as part of the approved restructuring package, the Cypriot State had provided a guarantee for a loan of CYP 45 million (approx. EUR 78 million), which Cyprus Airways took from Hellenic Bank (see recital 22 above). This loan had been serviced regularly by Cyprus Airways through instalments twice per year and in August 2013 the outstanding amount to be repaid was EUR 28,5 million. Under the notified restructuring aid, the Company would not repay the outstanding amount to Hellenic Bank. As a result, the State guarantee would be called, which would create a new debt of Cyprus Airways towards the State, since the latter would have to repay the loan. That debt of EUR 28,5 million would subsequently be converted by the State into equity of Cyprus Airways;
  - (d) Cyprus Airways' Provident Fund for the Cyprus-based employees (excluding pilots) is a defined benefit scheme, paid through contributions by the employees and Cyprus Airways. The entire amount allocated to the Provident Fund based on the contractual entitlements of the personnel ('purchasing power') is ultimately at the disposal of the Company. The Provident Fund's

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purchasing power is also guaranteed by the Company. As a result of poor investment performance, the Provident Fund has been facing a significant deficit, calculated on 1 January 2013 as EUR 12 million on a going concern basis (that is to say assuming that Cyprus Airways would continue to operate) or EUR 14,9 million on a discontinued basis. In the context of the restructuring aid, the Cypriot State will cover EUR 8,6 million of the Provident Fund's deficit on a going concern basis, whereas the remaining amount will be covered through real estate transactions (proceeds from the sale of the Company's property in Nicosia and transfer of the Company's property in Athens to the Provident Fund).

- (35) The elements (a) and (b) of the restructuring aid correspond to measures 1 and 2, which were subsequently notified in the context of restructuring aid to Cyprus Airways.
- (36) In addition, the 2013 restructuring plan also envisaged a possible EUR 10 million short-term loan by the State, which, according to the Cypriot authorities, would be granted on market terms. However, the envisaged granting date or conditions of this loan were not clear and it is not included in the total amount of EUR 102,9 million.
- (37) The Cypriot authorities explained that the 2007 restructuring plan had initially been implemented according to schedule. However, the revenues of the Company started declining in 2009, as a result of the financial crisis in the Union, in particular Greece and Cyprus. Other factors for the new difficulties of the Company were the Turkey overflight ban, which does not allow Cyprus Airways to reach prospective markets, such as Russia, Armenia and Ukraine in competitive flight times, the unrest in the Middle East and the operation of low-cost competitors with a base in Cyprus.

#### 3.2.2.2. *The 2013 Restructuring Plan*

- (38) The 2013 restructuring plan envisaged a restructuring period from April 2012 (first sale of an asset in the context of the own contribution of the Company to its restructuring costs) until the end of 2017. The aim is to restore the profitability of Cyprus Airways as of the financial year 2014. However, the Cypriot authorities clarified that the 2013 restructuring plan did not address the fundamental business model of the Company. The Company has already undertaken some of the measures envisaged under the 2013 restructuring plan.

#### *Restructuring of fleet and operations*

- (39) The 2013 restructuring plan envisaged a reduction of the fleet to six aircraft (from 13 in the beginning of April 2012). This reduction was achieved by 10 December 2013, through the sale of two owned aircraft in April 2012 and the expiry of the lease contracts for another five aircraft. Out of the remaining fleet of six aircraft, five aircraft, which have been leased by Cyprus Airways, would be kept in operations, whereas one aircraft, which was owned by the Company, would be held as spare.

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- (40) The reduction in the fleet would be reflected in a reduced number of routes to 13. The following routes had already been closed since April 2012: LCA-ATH-SKG-LCA; LCA-ATH-HER-LCA; LCA-ATH-RHO-LCA; LCA-LED<sup>(8)</sup>. The following routes were also planned to be closed: LCA-HER-RHO-LCA; LCA-SKG-HER-LCA; LCA-SKG-RHO-LCA; LCA-FCO; LCA-VIE and LCA-LHR, which would be replaced by LCA-STN<sup>(9)</sup>. Also, the Company would reduce the frequency of three routes: LCA-LON, LCA-SKG and LCA-HER<sup>(10)</sup>. The following routes were envisaged to be maintained: LCA-ATH, LCA-SKG, LCA-HER, LCA-AMS, LCA-CDG, LCA-SVO, LCA-SOF, LCA-FRA, LCA-MUC, LCA-ZRH, LCA-TLV, LCA-BEY, LCA-STN<sup>(11)</sup>. According to the Cypriot authorities, the 2013 restructuring plan thus envisaged a capacity reduction of 35 % in terms of ASK<sup>(12)</sup> as compared to the 2012 capacity.
- (41) The plan envisaged a better allocation of flight times, in order to maximise fleet utilisation. The route to London was changed from Heathrow to Stansted and is considered as strategic, because of its attractiveness.

*Cost reduction measures*

- (42) The 2013 restructuring plan envisaged reduction of direct costs in the total amount of EUR 45,7 million by the end of the financial year 2014 as a base scenario. Of these cost reductions, EUR 16,2 million is due to a decline in volume including part of staff redundancies and pay-cuts related to this decline while the remaining EUR 29,5 million is due to additional savings. The main components are staff redundancies (EUR 17,6 million); other staff cost reduction (EUR 4,5 million); reduction in fuel costs (stemming from a unified fleet of Airbus A320 with reconfigured seat capacity — EUR 12,5 million); passenger savings costs (such as removal of the catering option in economy class — EUR 5,5 million); reduction and renegotiation of ground handling fees at LCA airport (EUR 4,2 million); reduction and renegotiation of airport and en route fees (EUR 3,3 million); ceased aircraft lease costs (EUR 4,5 million).
- (43) In addition to the fleet and routes reduction, the following measures had been implemented by January 2014: removal of catering in economy class, renegotiation of ground handling fees at LCA airport leading to EUR 1,2 million savings (as opposed to EUR 0,6 million expected in the 2013 restructuring plan); 10 % salary and Provident Fund contribution reductions. However, the reduction of landing and parking fees at LCA airport is not expected to be achieved in the foreseeable future due to on-going disputes on other charges which do not allow for renegotiation of the landing and parking fees at this stage.
- (44) As regards staff redundancies, the staff number decreased from 1 037 since December 2011 to 650 in January 2014, whereas further redundancies of 321 staff members seem to have been agreed but pending. The Cypriot



authorities clarified that no *ex gratia* compensation had been granted for these redundancies.

*Revenue initiatives*

- (45) As regards new revenue initiatives, the 2013 restructuring plan assumed fare increases of 2-3 % per year as of 2015 in the base scenario. As a low case, the 2013 restructuring plan assumed a revenue decrease of 1 % in 2014 and no increase after 2015. In addition, the plan made reference to ancillary revenue from additional services provided to passengers, but it did not provide any amount.

*Restoration of viability — assumptions*

- (46) The 2013 restructuring plan envisaged the restoration of the Company's viability as of 2014. The plan contemplated the following financial results in the base scenario, assuming that the financial restructuring (under measure 4) would be implemented before the end of 2013:

TABLE 1

**Envisaged profit and loss (base scenario) (in million EUR)**

|                       | 2013     | 2014    | 2015    | 2016   | 2017   |
|-----------------------|----------|---------|---------|--------|--------|
| Revenues              | 168,1    | 108,2   | 109,6   | 111,7  | 113,1  |
| EBIT                  | (18,8)   | 0,4     | 2,1     | 4,6    | 6,0    |
| Net result before tax | (18,9)   | 0,4     | 2,1     | 4,6    | 6,0    |
| EBIT %                | (24,9) % | 0,4 %   | 1,9 %   | 4,1 %  | 5,3 %  |
| Capital reserves      | 0,0      | 0,0     | 0,0     | 0,0    | 0,0    |
| Total reserves        | (103,1)  | (102,7) | (100,5) | (96,0) | (90,0) |
| Total equity          | 1,4      | 1,8     | 4,0     | 8,5    | 14,5   |

- (47) Concerning profitability, the 2013 restructuring plan contemplated the following profitability:

TABLE 2

**Envisaged profitability**

*(in %)*

|                        | 2014 | 2015 | 2016 | 2017 |
|------------------------|------|------|------|------|
| ROE (Return On Equity) | 21,2 | 54,1 | 53,5 | 41,3 |

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|                                   |     |     |      |      |
|-----------------------------------|-----|-----|------|------|
| ROCE (Return On Capital Employed) | 1,2 | 6,1 | 11,4 | 13,0 |
|-----------------------------------|-----|-----|------|------|

- (48) Apart from the above-mentioned restructuring measures, the results were based on the following assumptions:
- (a) Reduction in passengers and revenue, as a result of the reduced network;
  - (b) Savings in fuel costs because of increased use of a fuel management system. The price of fuel was assumed flat;
  - (c) Planned rescheduling of third-party debt leading to no interest to accrue or be paid and no new lending;
  - (d) Stable USD/EUR exchange ratio until 2017;
  - (e) No hedging against fuel price or USD/EUR exchange rate risks due to the inability to provide any collateral for such instruments.
- (49) The profitability was mainly driven by the remaining flights LCA-BEY, LCA-TLV, LCA-SOF and LCA-SVO, which are the only flights with positive EBIT during the restructuring period. The other maintained routes are envisaged to have zero or negative net profit.
- (50) The 2013 restructuring plan included a high (best-) and low (worst-) case scenario. The low case scenario reflected only the revenue decrease described in recital 45 above and resulted (at EBIT level) in a loss of EUR 0,3 million for 2014, EUR 0 for 2015 and a profit of EUR 0,3 million for 2016 and 2017.
- (51) The plan acknowledged certain risks related to the restoration of viability, without reflecting their impact on the different scenarios, notably the low case. In particular:
- (a) Macroeconomic risk, especially related to a possible rise of the oil price or a change in the USD/EUR exchange rate. For these two risks, the plan calculated separately the impact of a 1 % variation at approximately EUR 310 thousand and EUR 425 thousand for one year, respectively.
  - (b) Risk of increased competition on the routes to Tel Aviv (due to an Open Skies deregulation agreement expected to lead to increased competition on this route as of 2015) and Moscow (due to expected increase of the frequencies operated by Cyprus Airways' competitor Transaero). The potential impact of these risks on the future revenues of Cyprus Airways was not modelled.

*Restructuring costs and funding*

- (52) The total restructuring costs amounted to EUR 147,4 million and would be allocated according to the following categories:

TABLE 3

**Restructuring costs (in EUR million)**

|  |       |
|--|-------|
| Accumulated losses   | 99,7  |
| Other restructuring costs (aircraft lease settlements, redundancy entitlements etc.) | 10,4  |
| Working capital  | 37,4  |
| Total restructuring costs  | 147,4 |

- (53) The total restructuring aid foreseen by the 2013 restructuring plan amounted to EUR 102,9 million, that is to say 69,8 % of the restructuring costs. The Company would contribute to the restructuring costs ('own contribution') through the sale or transfer of assets at an estimated total value of EUR 54,46 million. The 2013 restructuring plan envisaged that the own contribution would be composed of the following items:

TABLE 4

**Suggested own contribution in the 2013 restructuring plan**

|  | <b>Amount (in EUR million)</b> | <b>Estimated realisation date</b>   |
|--|--------------------------------|---|
| Sale of two Airbus A319 aircraft                 | 22,1                           | Concluded in April 2012   |
| Sale of evening LHR slot                         | 15                             | Under negotiation   |
| Sale of morning LHR slot                         | 10                             | Late 2014   |
| Sale of spare parts                              | 3,5                            | EUR 2,0 million in 2013;<br>EUR 1,1 million in 2014;<br>EUR 0,4 million in 2015 |
| Sale of property in Nicosia                      | 3,1                            | Concluded on 6 August 2013  |
| Transfer of property in Athens to Provident Fund | 0,76                           | Transfer agreement concluded in August 2013                                     |
| Total suggested own contribution                 | 54,46                          |   |

- (54) As regards the concluded sales (two Airbus A319 aircraft, property in Nicosia), the Cypriot authorities provided the sale contracts which confirmed the amounts assumed by the 2013 restructuring plan. As regards non-realised

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sales, the Cypriot authorities had provided valuation studies carried out by specialised companies regarding the two LHR slots and the property in Athens.

*Avoidance of undue distortions of competition*

- (55) The Cypriot authorities proposed to consider some of the afore-mentioned measures as compensatory measures, in order to minimise the impact on competition and competitors. In particular:
- a. Discontinuing profitable routes<sup>(13)</sup> representing 8,8 % of ASK of 2012: HER-SKG; LCA-FCO; LCA-LED; LCA-LED-PFO-LED-LCA; RHO-SKG-RHO. In addition, reduction of capacity on profitable routes: LCA-LON; LCA-ATH; LCA-SKG; LCA-HER. The Cypriot authorities considered that overall the ASK would be reduced by 24 % on profitable routes as compared to the 2012 capacity;
  - b. Sale of the two LHR slots. Since LHR is a fully coordinated airport, the Cypriot authorities considered that these slots would provide sufficient compensation to potential competitors;
  - c. Fleet reduction by seven aircraft.
- (56) The Cypriot authorities maintained that the participation of the State to the 2012 capital increase was not State aid but nonetheless included measure 1 in their notified restructuring aid. They also argued that the 2013 restructuring plan was prudent, it included sufficient compensatory measures, the own contribution of the Company was as high as possible and that it would restore the Company's profitability in the medium term.
- (57) Overall, the Cypriot authorities explained the importance of air transport for the Cypriot economy and repeated the exceptional and unforeseeable circumstances, which should allow Cyprus Airways to receive additional restructuring aid. They also added to those circumstances the operation of an 'illegal' airport in the occupied northern part of Cyprus, which Turkish airlines are allegedly using to bring tourists from European destinations to Cyprus.

3.2.2.3. *Measure 5: Training aid*

- (58) According to the Cypriot authorities during the period 2010-2011 Cyprus Airways received training aid of EUR 269 317.94 under the Scheme for constant training programmes for individual enterprises implemented by the Cypriot authorities pursuant to Commission Regulation (EC) No 800/2008<sup>(14)</sup> (General Block Exemption Regulation, 'GBER').
- (59) Contrary to their argumentation in relation to the notified measures (see e.g. recital 68), in their submissions regarding the training aid scheme and in particular the submission of 14 March 2013, the Cypriot authorities argued that Cyprus Airways was not in difficulty when the training aid in question was granted. The Cypriot authorities thus consider that the measure was in

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line with the national training aid scheme, which is based on the GBER, and thus compatible with the internal market.

### 3.3. GROUNDS FOR INITIATING THE FORMAL INVESTIGATION PROCEDURE

#### 3.3.1. **The first formal investigation procedure**

(60) In the decision of 6 March 2013 (recitals 41-46), the Commission reached the preliminary conclusion that Cyprus Airways could be considered a firm in difficulty within the meaning of the Communication of the Commission on Community guidelines on State aid on rescuing and restructuring firms in difficulty ('2004 Rescue and Restructuring Guidelines')<sup>(15)</sup> since at least 2010.

(61) Against that background, the Commission reached the preliminary conclusion that measures 1, 2 and 3 constituted State aid and it expressed doubts as regards their compatibility with the internal market. The measures did not seem to be in line with the 2004 Rescue and Restructuring Guidelines, due to the absence of a restructuring plan for the capital increase and the form of aid for the rescue aid, which seemed to include also part of the capital injection. The Commission also raised doubts as regards the 'one time, last time' principle, according to which a company may only receive rescue and/or restructuring aid only once every 10 years. It questioned in particular whether the justifications brought forward by the Cypriot authorities would constitute exceptional and unforeseeable circumstances that could allow further restructuring aid.

#### 3.3.2. **The second formal investigation procedure**

(62) In the decision of 4 February 2014, the Commission reiterated its preliminary conclusion that Cyprus Airways could be considered as a firm in difficulty since 2010. Thus, the Commission reached the preliminary conclusion that measures 4 (which included also measures 1 and 2) and 5 constituted State aid and it expressed doubts as regards their compatibility with the internal market, because the measures did not seem to be in line with the 2004 Rescue and Restructuring Guidelines (measures 1, 2 and 4) and the GBER (measure 5).

(63) In particular, the Commission expressed doubts that the restructuring plan was founded on prudent assumptions and would restore the viability of the Company within a reasonable timescale in line with relevant case practice. The Commission also did not consider that the level of own contribution of the Company was sufficient and questioned whether the proposed compensatory measures indeed concerned non-loss making routes.

(64) Finally, the Commission repeated its doubts as to the circumstances justifying an exception from the 'one time, last time' principle. It noted that Cyprus Airways expanded its domestic flights in Greece between 2011 and 2013 and was thus consciously increasing its exposure to the Greek market. The Turkey overflight ban on Cypriot aircraft and the operation of an airport

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on the occupied territory of the island could also not qualify as exceptional circumstances, as they had been in place for a long time.

- (65) At any rate, the Commission noted that the amount granted as training aid should have been part of the restructuring aid to Cyprus Airways and thus taken into account also in the 2013 restructuring plan.
- (66) In the decision of 4 February 2014 the Commission did not take a position on the State aid qualification of a possible EUR 10 million short term loan, since the conditions were not clear.

#### 4. COMMENTS ON THE FORMAL INVESTIGATION PROCEDURES

##### 4.1. COMMENTS BY CYPRUS

- (67) Although this decision refers to three separate procedures, the Commission notes that there is an overlap of their scope, to the extent that they refer to the same beneficiary and some measures are the same. Thus, the Commission considers it opportune to summarise the comments by Cyprus on both formal investigation procedures together.
- (68) In its comments in the context of the first formal investigation procedure, the Cypriot authorities confirmed that Cyprus Airways has been a firm in difficulty since 2009.
- (69) As regards the contribution by the State to the 2012 share capital increase, the Cypriot authorities first insisted that the State acted like a prudent market economy investor, in order to protect the value of its investment and avoid a negative impact on other commercial activities in Cyprus which are related to Cyprus Airways. The lack of participation by other shareholders was attributed to the difficult situation of the Cypriot economy at that time. However, the Cypriot authorities accepted to include the participation of the State to the 2012 share capital increase in the notified restructuring aid.
- (70) As regards the rescue aid, the Cypriot authorities claimed that this was the minimum cash required by the Company until a new restructuring plan would be finalised, replacing the turnaround plan. They claimed that the interest rate of 1,66 %<sup>(16)</sup> was the rate for healthy firms. They also pointed to the social impact of a bankruptcy of Cyprus Airways, without the rescue aid, and the importance of the Company for the connectivity of the island.
- (71) As regards the *ex gratia* compensation, the Cypriot authorities have argued that Cyprus Airways was not obliged to pay any such compensation to redundant personnel. Thus, if the State were to provide *ex gratia* compensation, this would not provide an advantage to Cyprus Airways, because it would not alleviate it from any contractual payment due.
- (72) As for the duration of the restructuring period, they pointed to the 2004 Rescue and Restructuring Guidelines, which require a restructuring period 'as short as possible', and quoted cases where the Commission had approved

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restructuring periods longer than five years<sup>(17)</sup>. They also explained that the period until December 2012 was essentially ‘lost’, due to a change in the Board of Directors, the preparation and non-implementation of the turnaround plan and the worsening financial situation of the Company, which did not allow the original plan to materialise, that is to say a *pari passu* capital increase not involving State aid and a rescue aid loan.

- (73) In relation to the 2013 restructuring plan, the Cypriot authorities maintained their view that it would allow the Company to restore its viability, despite risks of increased competition and potential loss of passengers due to the elimination of catering in the economy class. They also argued that the plan was based on prudent assumptions about the financial position of the Company, the effectiveness of the maintained network, the fluctuation of fuel prices and the EUR/USD exchange rate. In addition, they pointed out that the 2013 restructuring plan envisaged medium to long-term revenue initiatives, which were not included in the 2013 restructuring plan calculations, such as possible introduction of direct marketing and selling methods.
- (74) For the loss-making routes, which the 2013 restructuring plan envisaged to maintain, the Cypriot authorities argued that they all had positive gross contribution (that is to say covering at least their variable costs) and that the Company needed to maintain a critical size of its network, in order to attract passengers.
- (75) In addition, the Cypriot authorities pointed to elements of the 2013 restructuring plan, which had developed better than anticipated, such as the successful reduction in ground handling expenses at LCA. They also clarified that there was no outstanding debt towards the ground handling Company at LCA.
- (76) As regards the compensatory measures, the Cypriot authorities indicated that all of the routes proposed to be abandoned or to reduce capacity, except for one<sup>(18)</sup>, were profitable on a gross contribution level in 2012, that is to say covering their variable costs. They also provided a table with the ASK per route.
- (77) On the issues of aid limited to the minimum and own contribution, they provided additional assets, which Cyprus Airways intended to sell, in order to increase the level of own contribution, namely the remaining own aircraft and two engines. In the meantime, the two LHR slots had been sold for a total price that was higher than anticipated, thus increasing further the envisaged own contribution to 41,8 % of the restructuring costs.
- (78) The Cypriot authorities confirmed that the Provident Fund is part of Cyprus Airways but a separate legal entity and that the transfer of the property in Athens meant that Cyprus Airways would no longer have control over it. Thus, they insisted that the transfer of the property in Athens to the Provident

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Fund was a genuine own contribution, which reduced the restructuring costs stemming from the coverage of its deficit.

(79) In fact, the Cypriot authorities also explained that the restructuring aid under measure 4 would be adjusted to the realised own contribution, so that the sum of the two amounts would cover only the restructuring costs. Thus, higher revenue through the own contribution would mean lower restructuring aid.

(80) The final proposed own contribution was thus as follows:

TABLE 5

**Updated suggested own contribution after comments by Cyprus**

|  | <b>Amount (in EUR million)</b> | <b>Realisation — Evaluation</b>  |
|--|--------------------------------|--|
| Sale of two Airbus A319 aircraft                 | 22,1                           | Concluded in April 2012  |
| Sale of evening LHR slot                         | 6,3                            | Transfer agreement concluded in March 2014   |
| Sale of morning LHR slot                         | 22,8                           | Transfer agreement concluded in June 2014  |
| Sale of spare parts                              | 3,5                            | No expert evaluation — estimated:<br>EUR 2,0 million in 2013;<br>EUR 1,1 million in 2014;<br>EUR 0,4 million in 2015<br>Realised based on evidence provided by the Cypriot authorities: EUR 0,86 million |
| Sale of property in Nicosia                      | 3,1                            | Concluded on 6 August 2013   |
| Transfer of property in Athens to Provident Fund | 0,76                           | Backed by expert evaluation — Transfer agreement concluded in August 2013  |
| Sale of one Airbus A320                          | 2,5                            | No expert evaluation — sale pending  |
| Sale of two engines                              | 0,51                           | Concluded on 28 April 2014   |
| <b>Total suggested own contribution</b>          | <b>61,57</b>                   |  |



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- (81) The Cypriot authorities acknowledged that the envisaged own contribution of 41,8 % is less than the level required by the 2004 Rescue and Restructuring Guidelines (50 % of the restructuring costs for large firms). However, they argued that the case of Cyprus Airways was one of particular hardship, which should justify a lower own contribution, in particular due to the economic and financial situation of the country and the Turkey overflight ban. They also pointed to the significant reduction of capacity.
- (82) As regards the ‘one time, last time’ principle, the Cypriot authorities in various submissions have reiterated their arguments as regards the impact of the financial crisis on Greece and Cyprus, the Turkey overflight ban on Cypriot aircraft, the operation of an ‘illegal’ airport in the occupied northern part of Cyprus, the unstable political situation in the Middle East and the fact that the granting of rescue and/or restructuring aid should not be a sufficient ground to prohibit further such aid to the same beneficiary.
- (83) The Cypriot authorities argued that the expansion of Cyprus Airways’ domestic flights in Greece between 2011-2013 was a proof of the fact that the impact of the crisis was difficult to predict and that some Middle East routes, representing a ‘not negligible’ part of the Company’s revenues, had a significant drop in passenger numbers, such as a 94 % drop of passengers from Egypt. Relevant warnings of the adverse effect of the economic situation in Europe and unrest in the Middle East on Cyprus Airways, already found in the Company’s annual reports of 2007, 2008 and 2009 and mentioned by the Commission in the decision of 6 March 2013, were deemed ‘generic statements’.
- (84) The Cypriot authorities also pointed out that the total number of passengers in the Cypriot market remained relatively stable during the recent years, but that most passengers now originated from Israel and Russia. The Turkey overflight ban meant that Cyprus Airways had a disadvantage in operating to the Russian market, due to the additional flight time. Furthermore, they provided evidence that although passenger numbers in the Greek market dropped marginally since 2008, the average fare of Greek flights (including domestic flights) dropped significantly.
- (85) As regards the EUR 10 million short-term loan, the Cypriot authorities explained that they expected to sell the evening LHR slot for a high price and therefore the granting of the loan would not be necessary.
- (86) Finally, the Cypriot authorities justified the provision of training aid during 2010-11 by arguing that Cyprus Airways only entered in difficulties in late 2011. This was in contradiction with their previous submissions (see recital 68 above).

#### 4.2. COMMENTS BY INTERESTED PARTIES

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- (87) During the two formal investigation procedures, comments were submitted by Air France Consulting, three competitors (Ryanair, International Airlines Group and a third competitor who did not wish its identity to be disclosed), trade unions of Cyprus Airways<sup>(19)</sup> and the beneficiary.
- (88) Air France Consulting, who prepared the turnaround plan, clarified that the plan provided a turnaround in one year and full financial recovery of Cyprus Airways within two years and that the required capital could be provided through financial restructuring, as opposed to cash. It also stated its belief in the credibility of the turnaround plan and argued that the plan was based on Cyprus Airways developing operations out of Athens on international European routes. Further, it stated that decisions taken by Cyprus Airways in 2013 (reducing the fleet to 6 aircraft, making redundant 490 staff) would only make the Company's financial situation more fragile.
- (89) The three competitors disagreed with the arguments by the Cypriot authorities as regards the significance of Cyprus Airways for the infrastructure and development of Cyprus and declared themselves ready to expand routes to/from Cyprus.
- (90) As regards the existence of aid and compatibility, competitors agreed with the Commission that the participation of the State to the Company's share capital increase was not what a market economy investor would have done.
- (91) Competitors also questioned the restoration of the viability of the Company, expressing doubts as to the effectiveness of the maintained network and fleet and whether the assumptions of the plan and the envisaged profitability were realistic, especially with regard to the fuel savings and the additional revenue through a fare increase. They also pointed to increased competition risks for profitable routes envisaged to be maintained by Cyprus Airways, in addition to Tel Aviv and Moscow.
- (92) Competitors also doubted the existence of truly exceptional and unforeseeable circumstances that would justify an exception to the 'one time, last time' principle. In addition, the competitor who did not wish to disclose its identity considered that the profitability of the routes proposed as compensatory measures should be measured on a net profit level, that is to say including allocated fixed costs, and not only on a gross level, that is to say only including variable cost.
- (93) Finally, Ryanair questioned whether the Company could achieve the envisaged reduction in staff due to trade union resistance and suggested that, if the restructuring aid to Cyprus Airways was found compatible, this could be on the condition that the Company abandons routes that remained unprofitable three years after the approval. Ryanair also argued that it and other companies have been subject to the same conditions in relation to the unrest in the Middle East and the economic crisis in Greece and Cyprus. Despite that,

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Ryanair claimed that other companies have managed to adapt and grow in the new environment, citing as an example its own growth in the Greek and Cypriot market in recent years. Further, in its submission of 6 June 2014, Ryanair pointed to a press article of 19 May 2014 indicating that the Cypriot government had pledged EUR 4 million to be provided to Cyprus Airways' staff that have been made redundant and claimed this constitutes further State aid to Cyprus Airways.

- (94) Cyprus Airways and its trade unions supported the arguments of the Cypriot authorities and reiterated their belief in the viability of the Company and its role for the economy and connectivity of Cyprus.

#### 4.3. COMMENTS BY CYPRUS ON THE COMMENTS BY INTERESTED PARTIES

- (95) The Cypriot authorities considered it unnecessary to comment on the turnaround plan and the comments by Air France Consulting, given the existence of an updated restructuring plan. They repeated the important role of Cyprus Airways for the economy and connectivity of the island and insisted that the unrest in the Middle East was an exceptional and unforeseeable situation having an impact on Cyprus Airways. They doubted that competitors could fill in any gaps in connectivity resulting from a possible bankruptcy of Cyprus Airways, given the seasonality of the market.
- (96) As regards the compatibility of the measures with the 2004 Rescue and Restructuring Guidelines, the Cypriot authorities insisted that the 2013 restructuring plan was founded on realistic assumptions and was not underestimating any negative effects stemming from the small fleet or difficulties in realising cost initiatives.
- (97) Finally, the Cypriot authorities stated in their submission of 9 September 2013 that no *ex gratia* payments would be granted to employees made redundant. Subsequently, in their submission of 3 August 2014, the Cypriot authorities explained that the Government has, for socioeconomic reasons, decided to compensate directly former Cyprus Airways employees that had already resigned or had been made redundant. The decision was taken and compensations were paid only after the resignations or redundancies had been finalised and thus would not constitute State aid to Cyprus Airways. All legal obligations of Cyprus Airways towards those employees were honoured fully by the Company itself.
- (98) The Cypriot authorities also did not consider that the approval of the aid should be subject to any conditions.

## 5. ASSESSMENT

- (99) This Decision will assess whether the measures under scrutiny constitute State aid to Cyprus Airways within the meaning of Article 107(1) of the Treaty and whether such aid may be compatible with the internal market.

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- (100) The Commission notes that the aid provided by measure 4 notified together with the 2013 restructuring plan in October 2013 already includes the aid provided by measure 1 (disbursed as advanced payments between September and December 2012), as well as measure 2 (rescue aid notified in December 2012 and partially disbursed between January and July 2013). Both these measures were implemented with a view to ensure short-term survival of the Company before a comprehensive restructuring plan could be prepared. Since the turnaround plan of 2012 was not implemented, the Commission considers both these measures as part of the 2013 restructuring plan and it will thus only assess measures 1 and 2, to the extent they constitute State aid, in the context of measure 4, that is to say as one overall restructuring aid measure.

#### 5.1. EXISTENCE OF STATE AID

- (101) Article 107(1) of the Treaty 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 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.

##### 5.1.1. Measures 1, 2 and 4

- (102) In the decision of 6 March 2013, the Commission reached the preliminary conclusion that measure 1, that is to say the participation of the State to the 2012 share capital increase of Cyprus Airways, constituted State aid.
- (103) The measure involved State resources and was imputable to the State. It provided a selective advantage to Cyprus Airways, because the Commission considered that a private investor would not have provided capital to the Company under such conditions, given the serious difficulties of Cyprus Airways, the absence of viability prospects at the date of granting as well as the alternative of a shareholder loan including appropriate securities. In addition, practically no existing private shareholder of Cyprus Airways participated in the capital increase since only EUR 106 thousand were collected from private shareholders (compared to EUR 13,67 million originally expected). The shareholding of the State in Cyprus Airways thus increased from 69 % to 93,67 %. The measure was therefore not in line with the market economy investor principle<sup>(20)</sup>.
- (104) The Commission does not agree with the position of the Cypriot authorities that the State acted as a market economy investor in order to protect the value of its investment, because the capital increase of EUR 31,33 million was anyway not sufficient to allow the survival of the Company. This was proven by the fact that the Company received additional rescue funding as part of measure 2 (rescue aid) only a few months later. As regards the absence of participation of other investors due to the stressed situation of the Cypriot economy at that time, the Commission notes that if such an investment had

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been attractive for a market investor, one can expect that foreign investors would have expressed an interest.

- (105) At any rate, the Commission takes note of the intention of the Cypriot authorities to include the participation of the State to the 2012 share capital increase in the notified restructuring aid.
- (106) Measure 1 thus enabled Cyprus Airways to continue operating because the Company did not have to face the consequences normally following from its poor financial results. Since Cyprus Airways competes in the liberalised EEA market for air transport with other EEA airlines, measure 1 had the potential to distort competition and affect trade between Member States.
- (107) Measure 2 was notified as a rescue aid loan provided in the form of a government loan, which would bear an interest of 1,76 % and should be repaid by 30 June 2013. The Commission considered in its decision of 6 March 2013 that no prudent creditor would have provided a loan with such interest rate to a firm in difficulty. In addition, the Cypriot authorities have not demonstrated how Cyprus Airways would be able to repay the loan after six months. Since all other criteria under Article 107(1) of the Treaty are fulfilled (as further explained in the decision of 6 March 2013, to which the present decision refers on that point), measure 2 constitutes State aid. The Cypriot authorities acknowledge that the loan constitutes rescue aid in their reply to the decision of 6 March 2013. The Commission notes that the loan will not be repaid and has been notified by the Cypriot authorities in the context of the restructuring aid (measure 4).
- (108) Measure 4 was notified as restructuring aid. Indeed, all of its components involve State resources and are imputable to the State, either in the form of a capital injection, a conversion of debt into equity or by directly covering part of the Provident Fund's deficit. Measure 4 provides a selective advantage to Cyprus Airways, since a market economy investor would not have provided such funding to a company in such a financial situation, (with accumulated losses of EUR 99,7 million, highly over-leveraged and its capital base eliminated). Finally, for the reasons set out in recital 106 above, the measure is likely to affect trade between Member States and to distort competition.
- (109) Thus, the Commission concludes that measure 4 constitutes State aid within the meaning of Article 107(1) of the Treaty in favour of Cyprus Airways. In accordance with the notification, the aid amounts to EUR 102,9 million. The Commission takes note of the statement by the Cypriot authorities that the possible granting of the short-term loan of EUR 10 million will not be necessary and therefore does not include the loan into the total restructuring aid. As regards the granting date, the Commission notes that measure 4 has been granted in tranches.
- (110) Tranche (a) amounting to EUR 31,33 million (the State participation to the 2012 share capital increase) was granted as follows:

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TABLE 6

**Granting dates of the State's participation to the 2012 share capital increase**

| Amount (in EUR million) | Granting date     |
|-------------------------|-------------------|
| 3,0                     | 12 September 2012 |
| 3,0                     | 20 September 2012 |
| 5,0                     | 26 September 2012 |
| 4,0                     | 11 October 2012   |
| 16,33                   | 28 December 2012  |
| <b>Total: 31,33</b>     |                   |

- (111) Tranche (b) amounting to EUR 34,5 million (the rescue aid loan) was granted as follows:

TABLE 7

**Granting dates of the State's 2013 rescue aid loan**

| Amount (in EUR million) | Granting date    |
|-------------------------|------------------|
| 3,0                     | 22 January 2013  |
| 5,0                     | 29 January 2013  |
| 3,5                     | 28 February 2013 |
| 10,0                    | 2 May 2013       |
| 13,0                    | 26 July 2013     |
| <b>Total: 34,5</b>      |                  |

- (112) As regards the other tranches of measure 4, that is to say (c) the calling of the State guarantee and the subsequent conversion of the debt of EUR 28,5 million into equity, and (d) the coverage of EUR 8,6 million of the Provident Fund's deficit, the Commission does not have any indication that they have already been granted.

**5.1.2. Measure 3**

- (113) The Commission takes note of the clarification provided by the Cypriot authorities in September 2013 that no *ex gratia* compensation had been or would be granted to employees made redundant.
- (114) Almost one year later, in their submission of August 2014, the Cypriot authorities indicated that in May/June 2014 the Cypriot government has,

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for socioeconomic reasons, decided to compensate directly former Cyprus Airways employees that had already resigned or been made redundant. The decision was taken and compensations were paid only after the resignations or redundancies had been finalised. All legal obligations of Cyprus Airways towards those employees were honoured fully by the Company itself.

- (115) According to the Cypriot authorities, the resignations and redundancies of Cyprus Airways' employees under the 2013 restructuring plan were implemented without any additional compensation offered by the Cypriot government. Rather, the latter would have taken an *ex post* decision to directly compensate former Cyprus Airways employees.
- (116) It thus appears that the Cypriot authorities' initial intentions to provide *ex gratia* compensation to employees to be made redundant was abandoned and the Commission therefore considers that it is not necessary to conclude on the State aid qualification for measure 3.

#### 5.1.3. **Measure 5**

- (117) The amount of EUR 269 317.94 was granted to Cyprus Airways in 2010 and 2011 through a State aid scheme, which allowed grants from the State budget to selected companies for training purposes. Thus, the Commission concludes that measure 5 constitutes State aid within the meaning of Article 107(1) of the Treaty in favour of Cyprus Airways. This qualification is not disputed by the Cypriot authorities.
- (118) The training aid was granted to Cyprus Airways for 303 training projects during the years 2010 and 2011. However, the Cypriot authorities did not provide a breakdown of the granting date of each project.

#### 5.1.4. **Conclusion on existence of State aid**

- (119) In the light of the above, the Commission considers that it is not necessary to assess whether measure 3 constitutes State aid. The Commission considers that measures 1, 2, 4 and 5 constitute State aid within the meaning of Article 107(1) of the Treaty.
- (120) The total amount of State aid comprised in measures 1, 2 and 4 is EUR 102,9 million. The first two tranches, that is to say EUR 65,83 million, have already been granted on various dates between 12 September 2012 and 26 July 2013.
- (121) The State aid comprised in measure 5 is EUR 269 317.94 and was granted during 2010-2011.

#### 5.2. **UNLAWFUL AID**

- (122) The measures 1, 2 and, hence, measure 4 constitute State aid and were granted in breach of the notification and stand-still obligations established in

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Article 108(3) of the Treaty. The same applies to measure 5. Consequently, each of those measures constitutes unlawful State aid.

### 5.3. COMPATIBILITY OF THE AID

- (123) Inasmuch as certain measures constitute State aid within the meaning of Article 107(1) of the Treaty, 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>(21)</sup>.
- (124) The Cypriot authorities were initially of the view that measure 1 did not entail State aid and notified measure 2 as rescue aid. However, following the first formal investigation procedure and the doubts raised by the Commission therein, as well as the envisaged non-repayment of the rescue loan under measure 2, the Cypriot authorities have subsequently argued that measures 1, 2 and 4 are compatible as restructuring aid under the 2004 Rescue and Restructuring Guidelines.
- (125) In particular, the Cypriot authorities pre-notified a restructuring plan on 22 July 2013 and notified an updated plan on 23 October 2013. They subsequently provided additional clarifications. However, the main assumptions and ideas of the 2013 restructuring plan remained unchanged since the notification of 23 October 2013.
- (126) As regards measure 5, the Cypriot authorities argued that it was compatible training aid under the GBER. However, the Commission has established that Cyprus Airways has been a firm in difficulty since 2009, in line with a submission by the Cypriot authorities. According to point (c) of Article 1(6) of the GBER, companies in difficulties are excluded from its scope of application. Therefore, Cyprus Airways has not been eligible for training aid since 2009.
- (127) In addition, according to point 20 of the 2004 Rescue and Restructuring Guidelines, ‘a firm in difficulty cannot be considered an appropriate vehicle for promoting other public policy objectives until such time as its viability is assured. Consequently, the Commission considers that aid to firms in difficulty may contribute to the development of economic activities without adversely affecting trade to an extent contrary to the Community interest only if the conditions set out in these Guidelines are met.’ Thus, the Commission can only assess measure 5 as restructuring aid subject to the 2013 restructuring plan.
- (128) Given that only one compatibility basis is appropriate for measures 1, 2, 4 and 5, the Commission considers it opportune to assess all measures together. For this assessment, the Commission will make reference in particular to points 31-77 of the 2004 Rescue and Restructuring Guidelines.



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### 5.3.1. Eligibility — Firm in difficulty

- (129) In the decision of 6 March 2013 (recitals 41-46) the Commission concluded on a preliminary basis that Cyprus Airways has been a firm in difficulty since 2010. This preliminary conclusion was reiterated in the decision of 4 February 2014 (recitals 83-84). Subsequently the Cypriot authorities acknowledged that Cyprus Airways has been a firm in difficulty since 2009.
- (130) According to information from publicly available financial reports, Cyprus Airways' key financial data since 2009 were as follows:

TABLE 8

#### Cyprus Airways' key financial data 2008-H1 2012 (in EUR million)

|                           | 2008  | 2009  | 2010  | 2011   | H1 2012 <sup>a</sup> |
|---------------------------|-------|-------|-------|--------|----------------------|
| <b>Turnover</b>           | 311,4 | 247,5 | 236,3 | 212,8  | 71,3                 |
| <b>EBT</b>                | 2,1   | - 3.2 | - 2.9 | - 23.8 | - 34.2               |
| <b>Registered capital</b> | 35,2  | 35,2  | 35,2  | 35,2   | 35,2                 |
| <b>Own equity</b>         | 13,9  | 9,4   | 7,7   | - 15.9 | - 48.6               |

<sup>a</sup> Cyprus Airways has not published financial statements since the first half of 2012.

- (131) Point 10(a) of the 2004 Rescue and Restructuring Guidelines states that a limited liability company is considered to be in difficulty where 'more than half of registered capital has disappeared and more than one quarter of that capital has been lost over the preceding 12 months'.
- (132) Furthermore, according to point 11 of the 2004 Rescue and Restructuring Guidelines, a firm may be considered to be in difficulty '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'. In this respect, according to the General Court case-law, 'the existence of negative own capital [...] may be considered to be an important indicator that an undertaking is in a difficult financial situation'<sup>(22)</sup>.
- (133) Point 10(a) of the 2004 Rescue and Restructuring Guidelines reflects the assumption that a company experiencing a massive loss in its registered capital will be unable to stem losses which will almost certainly condemn it to go out of business in the short or medium term. The Commission considers that the same assumption applies *a fortiori* to a company that has lost its entire registered capital and has negative equity<sup>(23)</sup>.
- (134) As indicated in Table 8 above, Cyprus Airways had negative own equity as of 2011. Further, own equity was decreasing already in 2009 and 2010 and was

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well below the level of the registered capital. With regard to point 11, Table 8 demonstrates that Cyprus Airways had diminishing turnover and increasing losses already since 2009. In 2009, turnover fell by almost 21 % as compared to 2008 and the Company recorded a loss (EBT) of EUR 3,2 million. This trend continued in the subsequent years.

- (135) In view of the above and taking into account the submissions of the Cypriot authorities (see recital 68 above), the Commission comes to the conclusion that Cyprus Airways has been a firm in difficulty since 2009 partly in accordance with point 10 (in particular as of 2011) and in any event in accordance with point 11 of the 2004 Rescue and Restructuring Guidelines.
- (136) According to point 33 of the 2004 Rescue and Restructuring Guidelines, ‘The firm must qualify as a firm in difficulty within the meaning of these Guidelines’. This condition is therefore met.

#### 5.3.2. **Duration of the 2013 restructuring plan — Restoration of long term viability**

- (137) Points 35-37 of the 2004 Rescue and Restructuring Guidelines provide that: ‘35. The restructuring plan, the duration of which must be as short as possible, must restore the long-term viability of the firm within a reasonable timescale and on the basis of realistic assumptions as to future operating conditions. Restructuring aid must therefore be linked to a viable restructuring plan to which the Member State concerned commits itself. The plan must be submitted in all relevant detail to the Commission and include, in particular, a market survey. The improvement in viability must derive mainly from internal measures contained in the restructuring plan; it may be based on external factors such as variations in prices and demand over which the company has no great influence, but only if the market assumptions made are generally acknowledged. Restructuring must involve the abandonment of activities which would remain structurally loss-making even after restructuring.’
- (138) ‘36. The restructuring plan must describe the circumstances that led to the company’s difficulties, thereby providing a basis for assessing whether the proposed measures are appropriate. It must take account, inter alia, of the present state of and future prospects for supply and demand on the relevant product market, with scenarios reflecting best-case, worst-case and intermediate assumptions and the firm’s specific strengths and weaknesses. It must enable the firm to progress towards a new structure that offers it prospects for long-term viability and enables it to stand on its own feet.’
- (139) ‘37. The plan must provide for a turnaround that will enable the company, after completing its restructuring, to cover all its costs including depreciation and financial charges. The expected return on capital must be enough to enable the restructured firm to compete in the marketplace on its own merits. Where the firm’s difficulties stem from flaws in its corporate governance system, appropriate adaptations will have to be introduced.’

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- (140) As regards the duration, the notified restructuring plan covers the period from the first sale of an asset in the context of the own contribution of the Company to its restructuring costs in April 2012 until the end of 2017 and envisages to restore the profitability of Cyprus Airways as of the financial year 2014. The duration of the restructuring period according to the notification is thus five years and six months.
- (141) The Commission observes that this is longer than the restructuring period approved by the Commission for other airlines, which is normally five years<sup>(24)</sup>.
- (142) In addition, the Commission observes that measure 5 was granted during the period 2010-11. Given that measure 5 was granted at a time when the Company was already in financial difficulty, it did not fall under the GBER. This means that it was either incompatible training aid or would have to be considered as restructuring aid the compatibility of which would have to be assessed in that context. In the latter scenario, this would extend the restructuring period to approximately seven years (and should then also form part of the notified restructuring plan).
- (143) A longer restructuring period may be accepted by the Commission in justified cases. However, in this case, the Cypriot authorities were not able to justify why Cyprus Airways would need longer than five years to conclude its restructuring. Indeed, the Commission observes that the ‘lost’ time described by the Cypriot authorities in recital 72 above due to delays in the internal decision making process of the State<sup>(25)</sup> was within the control of the authorities. Further, unlike in other cases, the 2013 restructuring plan of Cyprus Airways does not present any of the specificities previously accepted by the Commission in the decisions referred to by the Cypriot authorities, which would allow the Commission to conclude that a longer restructuring period in the present case could be accepted. Such specificities could for instance be a very significant reduction in capacity or a particularly small market share<sup>(26)</sup>.
- (144) Consequently, the Commission does not agree that the timescale of five years and six months (and even less so seven years) is reasonable in the case of Cyprus Airways.
- (145) As regards the content of the 2013 restructuring plan, the Commission observes that the Cypriot authorities did not sufficiently address the doubts expressed in the decision of 4 February 2014.
- (146) In particular, the Cypriot authorities maintained that the plan took into account the effectiveness of the maintained network and potential loss of passenger demand, that there was no risk of adverse fluctuation of fuel price and of the EUR/USD exchange rate, based on their fluctuation during the recent past. They also maintained that the envisaged financial position of the Company

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was satisfactory in comparison to its poor past performance. They pointed at elements of the 2013 restructuring plan that had developed better than anticipated, such as the renegotiation of the ground handling fees at Larnaca airport.

- (147) However, in the decision of 4 February 2014 the Commission expressed doubts because it had reasons to consider that many assumptions of the 2013 restructuring plan were not prudent enough, in light of its experience with other restructuring plans in the airline sector, given the competitive situation in the market and the general principle that a credible restructuring must also take into account the realistic possibility of adverse developments.
- (148) Indeed, the Commission notes that the assumptions made by Cyprus Airways are neither generally acknowledged nor supported by evidence about market prospects. In fact, competitors challenged those assumptions, especially in relation to the potential pressure by competitors on envisaged profit-making routes, the fuel savings and the anticipated revenue from the fare increase.
- (149) The Commission notes that the baseline scenario of the 2013 restructuring plan envisages that the Company will have a positive EBIT of EUR 0,4 million already in 2014 and increase it in the subsequent years. However, the Commission observes that the plan presumes that no interest on third party debts accrues or is paid during the whole restructuring period. However, the 2013 restructuring plan only indicates that the third party debt will thus need to be rescheduled without providing any details of how this will be achieved. The trade and other payables (excluding Hellenic bank debt) on the balance sheet for 2013-18 are forecasted to remain at the level of EUR 27,9 million. Therefore, the third party debt amount is significant and any failure to achieve its restructuring may have serious consequences for the financial forecasts.
- (150) The Commission reiterates its argument included in the decision of 4 February 2014 that at the end of the restructuring period, Cyprus Airways would be a company with zero capital reserves and negative total reserves. Such a company cannot be considered viable, since effectively no safety margin will exist.
- (151) The Commission further notes that the measures proposed in the 2013 restructuring plan do not seem to be appropriate to address the circumstances that led to the Company's difficulties, as established in the notification. In particular, the plan envisages maintaining three non-profit-making routes to Greece and two to the Middle East, despite the fact that those two markets contributed to the Company's difficulties. The plan also envisages maintaining at least four routes in direct competition with low cost airlines and increasing the fares. Finally, it maintains at least one route, which is significantly affected by the Turkey overflight ban.
- (152) At any rate, the 2013 restructuring plan does not include any concrete assessment of the future prospects of supply and demand in the relevant

markets, apart from acknowledging the risk for competition pressure on some routes to be maintained.

- (153) The Commission further notes that the worst-case scenario does not sufficiently take into account the weaknesses of the Company and risks applicable in the relevant markets, some of which had been identified in the plan itself. Such weaknesses and risks include the pressure by competitors, the deviation of key parameters underlying the financial projections of the baseline (for example, average unit revenue per passenger (yield), fuel price, USD/EUR exchange rate, drop in demand) and the economic situation in key markets.
- (154) In fact, the worst-case scenario reflected only a revenue decrease of 1 % and projected a positive EBIT of only EUR 0,3 million in 2016 and 2017. Yet, if any additional risk as admitted by the 2013 restructuring plan would materialise, such as a 1 % rise of the oil price or 1 % change in the EUR/USD exchange rate, this would be sufficient to wipe out the envisaged profits (see recital 51 above). These risks are further aggravated by the fact that Cyprus Airways does not have the necessary collateral to be able to hedge against the fuel price or exchange rate risk. Furthermore, the Commission observes that, in order to establish a worst-case scenario, previous airline cases normally had considered much larger deviations of the baseline parameters<sup>(27)</sup>. Further, the risk of significantly increased competition in particular on routes Tel Aviv and Moscow, representing Cyprus Airways' fourth and fifth most important routes in terms of the number of passengers, were not taken into account despite being explicitly mentioned in the 2013 restructuring plan. In addition, the possibility of a prolonged recession in Greece and Cyprus should also have been taken into account.
- (155) The Commission therefore concludes that the 2013 restructuring plan does not sufficiently address the circumstances that led to Cyprus Airways' difficulties, does not fully take into account the future prospects of the market and does not include a credible worst-case scenario.
- (156) Finally, the Commission notes that the 2013 restructuring plan does not address the fundamental problems of the Company's business model, which appears to have contributed to its difficulties. Cyprus Airways' restructuring is based on the existing business model with traditional operation as a full-service airline relying mainly on intermediary parties for the sale of tickets, while it is in competition with either low-cost airlines or full-service airlines with a wider network, most of which rely on direct sales for tickets online.
- (157) The Commission therefore concludes that points 35-37 of the 2004 Rescue and Restructuring Guidelines are not fulfilled, because (i) the duration of the 2013 restructuring plan is unreasonably long, (ii) the plan does not restore the long-term viability of the Company within a reasonable timescale and is not

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based on realistic assumptions and (iii) the plan does not take into account the market situation with sufficiently variable scenarios.

### 5.3.3. **Avoidance of undue distortions of competition**

(158) According to points 38-42 of the 2004 Rescue and Restructuring Guidelines, a company receiving restructuring aid must provide compensatory measures for the distortion done by the State aid to competition. Those measures may comprise divestment of assets, reductions in capacity or market presence and reduction of entry barriers on the markets concerned and must refer to non-loss making routes or products.

(159) The Cypriot authorities have proposed compensatory measures, including discontinuing or reducing capacity of non-loss making routes, the sale of two LHR slots and the reduction of fleet and ASK.

(160) The Commission notes that the sale of two slots in LHR, a fully coordinated airport<sup>(28)</sup>, can be considered as a sufficient reduction of entry barrier for competitors, especially given the fact that Cyprus Airways would abandon this airport altogether. The significant reduction of fleet is also a significant sign of reduction in capacity.

(161) As regards the routes proposed as compensatory measures, the Commission has consistently accepted as compensatory measures abandoning or reducing capacity in non-loss making routes, that is to say routes which have a positive gross contribution, taking into account variable costs<sup>(29)</sup>.

(162) However, the Commission observes that the route LCA-ATH, for which the Cypriot authorities proposed to reduce the capacity operated by Cyprus Airways as a compensatory measure, had a negative gross contribution and the Cypriot authorities did not provide evidence to support their argument that the part of the route relevant as compensatory measure (reduction of frequency by 4 flights a week) was non-loss making.

(163) Nevertheless, the Commission notes that the proposed 24 % reduction of ASK as compared to the 2012 capacity is higher than the reduction of ASK proposed in other airline restructuring cases<sup>(30)</sup>. This means that, even if the reduction in the capacity of the LCA-ATH route (representing only 0,84 % of total ASK) would not be taken into account, the reduction of ASK would still be sufficiently high.

(164) The Commission therefore concludes that points 38-42 of the 2004 Rescue and Restructuring Guidelines are fulfilled.

### 5.3.4. **Aid limited to the minimum: real contribution, free of aid**

(165) According to points 43-45 of the 2004 Rescue and Restructuring Guidelines, beneficiaries of restructuring aid are expected to make a significant contribution to the 2013 restructuring plan from their own resources, which

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should be at least 50 % of the restructuring costs for large firms, such as Cyprus Airways, except for exceptional circumstances and in cases of particular hardship. The own contribution must be real, that is to say, actual, excluding all future profits such as cash flow.

- (166) The Commission takes note of the updated amount of proposed own contribution of EUR 61,57 million. This represents 41,8 % of the total restructuring costs of EUR 147,4 million and the restructuring aid would be adjusted to the realised own contribution, so that the sum of the two amounts covers only the restructuring costs.
- (167) The Commission observes that the proposed own contribution of 41,8 %, even if it were fully achieved, would be below the threshold of 50 % set by the 2004 Rescue and Restructuring Guidelines.
- (168) Moreover, the Commission observes that based on table 5 in recital 79, only the sale of assets worth EUR 55,67 million has actually been realised. The sale of other proposed items, such as the spare parts and the Airbus A320, has not been fully realised and their values are not backed by an expert valuation.
- (169) As regards the sale of spare parts, the actual proceeds until now (EUR 0,86 million) demonstrate that the original estimates of EUR 2,0 million in 2013 and EUR 1,1 million in 2014 were largely overestimated. In the absence of any expert valuation of the remaining spare parts to be sold and without any other evidence such as an agreement indicating clearly the future purchase commitment by the buyer, possible future proceeds from the spare parts sales cannot be taken into account as sufficiently real and actual own contribution.
- (170) As regards the sale of the Airbus A320, which the Cypriot authorities in their submission of 11 May 2014 describe as ‘an old aircraft’, four out of the five offers submitted during 2014 have been withdrawn and in the case of the fifth offer the bidder has not responded to Cyprus Airways’ counter-proposal. As the Cypriot authorities have not provided any expert valuation of the aircraft, the projected sales revenue of EUR 2,5 million cannot be accepted as a sufficiently real and actual own contribution.
- (171) In addition, the Commission does not agree with the Cypriot authorities and considers that the transfer of a property to the Provident Fund cannot be considered as an actual and real own contribution. That is because, as confirmed by the Cypriot authorities and as identified in the Company’s annual accounts, the Provident Fund is controlled by Cyprus Airways, regardless of its legal status, its funds are ultimately at the disposal of the Company and its deficit is part of the restructuring costs<sup>(31)</sup>. Therefore, by transferring an asset to the Provident Fund, Cyprus Airways does not bring any real own contribution to its restructuring costs.

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- (172) In light of the above, the Commission considers the level of actual and real own contribution as EUR 55,67 million, which is 37,8 % of the restructuring costs.
- (173) The Cypriot authorities argue that the own contribution can be exceptionally lower than 50 % in case of particular hardship. More specifically, they argue that a lower level of own contribution in case of Cyprus airways can be justified by the economic and financial crisis as well as the Turkish airspace ban putting additional burden on the Company.
- (174) The Commission takes note of the particular situation of the Cypriot economy and acknowledges that disposing assets in such a situation may not be an easy process. However, the Commission notes that Cyprus Airways operates in an international and liquid market, because the potential buyers of its assets, including aircraft, slots, spare parts, may come from any part of the world and may thus not be concerned by the situation in the Cypriot economy, as they can obtain financing easier and can transfer the assets or use them without any link to Cyprus.
- (175) Further, the Turkey overflight ban has been in place for many years and is not related in any way to the sale of airline-related assets which can be used elsewhere. In addition, the significant reduction of capacity is relevant for competitors, whereas the own contribution aims to limit the State aid required and show that the markets believe in the feasibility of the return to viability.
- (176) Finally, while the Commission has based on the 2004 Rescue and Restructuring Guidelines accepted own contributions as low as 40 % of the restructuring costs, due to exceptional circumstances<sup>(32)</sup>, this still exceeds the level of own contribution by Cyprus Airways.
- (177) The Commission therefore concludes that points 43-45 of the 2004 Rescue and Restructuring Guidelines are not fulfilled. The 2013 restructuring plan does not limit the aid to the minimum necessary, since it does not include a sufficiently high, real and actual own contribution to the restructuring costs of Cyprus Airways.

#### 5.3.5. **Special conditions in relation to companies in assisted areas**

- (178) The 2004 Rescue and Restructuring Guidelines provide that the conditions for authorising aid may be less stringent as regards the implementation of compensatory measures and the size of the beneficiary's contribution, when justified by reasons of regional development and in particular if the beneficiary of the aid is located in an assisted region.
- (179) In the case of Cyprus, for the period 2007-13 as well as 2014-20, two regions covering together 50 % of the Cypriot population are eligible to receive regional investment aid under the derogation of article 107(3)(c) of the Treaty (the Western Zone and the Easter Zone)<sup>(33)</sup>. The Cypriot authorities have also



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argued that Cyprus exhibits a number of territorial features impacting its socioeconomic development, namely the peripheral nature and its dependence on air and sea transport. Finally, they argued that the economic recession of the Cypriot economy should *a fortiori* merit the treatment of Cyprus as an assisted area.

- (180) The Commission notes that Cyprus Airways has its seat in Nicosia, which is not situated in any of the two assisted areas of Cyprus. Larnaca airport, arguably the main centre of Cyprus Airways' operations, is also not situated in one of those assisted areas. In addition, the Commission notes that, in order to ensure a level playing field, the status of an assisted area can only be established by a Commission decision, according to the criteria of the applicable Regional Aid Guidelines, and not based on other territorial characteristics or an economic recession.
- (181) Thus, the Commission cannot accept less stringent conditions as regards the criteria for the aid.

#### 5.3.6. 'One time, last time' principle

- (182) Point 73 Section 3.3 of the 2004 Rescue and Restructuring Guidelines stipulates that rescue and/or restructuring aid should be granted only once and 'where less than 10 years have elapsed since the rescue aid was granted or the restructuring period came to an end or implementation of the restructuring plan has been halted (whichever is the latest), the Commission will not allow further rescue or restructuring aid.' This condition is known as the 'one time, last time' principle.
- (183) An exception to the 'one time, last time' principle is provided for in point 73(c) of Section 3.3 [please confirm]:
- [...]
- (c) *in exceptional and unforeseeable circumstances.*
- (184) The Commission has approved restructuring aid to Cyprus Airways in 2007 on the basis of a restructuring plan. Cyprus Airways is therefore in principle not eligible for further restructuring aid at present according to the 'one time, last time' principle and the Commission raised doubts as to whether exceptional and unforeseeable circumstances within the meaning of point 73(c) exist in this case.
- (185) Despite having commented extensively on that point following the opening of two formal investigation procedures, the Cypriot authorities were not able to justify why Cyprus Airways was faced with exceptional and unforeseeable circumstances, which would merit further restructuring aid<sup>(34)</sup>.
- (186) In particular, the Turkey overflight ban was introduced in 1974<sup>(35)</sup> and Cyprus has put in place an approved scheme for compensation of the additional

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costs incurred by any affected airlines, including Cyprus Airways (see recital 23 above). Thus, this event cannot qualify as exceptional and unforeseeable circumstance and the Cypriot authorities did not bring forward new evidence in that respect.

- (187) For similar reasons, the operation of an ‘illegal’ airport in the northern part of Cyprus also cannot be considered as exceptional and unforeseeable circumstance, as the possibility for tourists to travel to and from the northern part of Cyprus has been in place at least since 2004.
- (188) The Commission also disagrees with the Cypriot authorities that the entry of any competitor, either a low-cost or full-service airline, can be considered as an exceptional and unforeseeable circumstance, given that Cyprus Airways operates in a liberalised sector and provided that its competitors are operating legally. As regards the allegation that the Cypriot State is subsidising competitors of Cyprus Airways, the Commission did not receive any substantiation of this allegation. At any rate, the Commission stresses that it cannot be argued that the State needs to provide State aid to Cyprus Airways in order to offset the harmful effects of an alleged measure that the State is claimed to have introduced itself, and qualify the latter as exceptional and unforeseeable circumstance.
- (189) As regards the unrest in the Middle East, the Commission considers that such a situation cannot be considered as exceptional, given the persistent unrest in parts of the region for many decades. As regards the economic impact of the most recent unrest referred to by the Cypriot authorities, namely the ‘Arab Spring’, the Company’s annual reports show that the revenue from routes connecting Cyprus to the Middle East and the Gulf region appears to represent traditionally approximately 10 % of the total revenues of Cyprus Airways. Thus, even a significant drop in traffic would have a relatively small (even if ‘not negligible’) impact, that is to say it would affect at maximum 10 % of the total revenues of Cyprus Airways.
- (190) As regards the deterioration of the Greek and Cypriot economies, the Commission acknowledges those events, as well as the possible drop in the average fare for the Greek flights. However, the Commission recalls that Cyprus Airways expanded its domestic flights in Greece between 2011 and 2013, and was thus consciously increasing its exposure to the Greek market.
- (191) The available evidence in the 2013 restructuring plan and the information provided by competitors suggests that the total passenger traffic in the Cypriot market has increased since 2009 while the market share of Cyprus Airways has been reduced. In addition, other airlines operating in the region have also been confronted with the economic crisis, but have adjusted their pricing policy and network, in order to remain in the market. In fact, Ryanair pointed that it has even achieved growth in those markets.

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- (192) In the light of the above, the Commission considers that Cyprus Airways, despite acknowledging the risks through explicit, albeit ‘generic’, statements in the annual reports in 2007, 2008 and 2009<sup>(36)</sup>, and despite the options available, failed to make the necessary adjustments to its business, in order to avoid the effect of the economic deterioration in its main markets and to profit from new markets, as its competitors did. Those effects can therefore not qualify as an exceptional and unforeseeable circumstance, but should rather be attributed to the poor management and performance of Cyprus Airways.
- (193) The Commission therefore concludes that the exception of point 73(c) of Section 3.3 of the 2004 Rescue and Restructuring Guidelines is not fulfilled and that restructuring aid to Cyprus Airways would breach the ‘one time, last time’ principle.

#### 5.3.7. **Conclusion**

- (194) In view of the above, the Commission finds that Cyprus has unlawfully implemented measures 1, 2, 4 and 5 in favour of Cyprus Airways, in breach of Article 108(3) of the Treaty.
- (195) The Commission also considers that measures 1, 2, 4 and 5 and the 2013 restructuring plan do not meet the conditions of the 2004 Rescue and Restructuring Guidelines. The Commission has not identified any other compatibility basis and the Cypriot authorities have also not claimed any alternative basis for compatibility of the measures (with the exception of the application of the GBER to the training aid — measure 5). Therefore, the Commission considers the aid to be incompatible with the internal market.

#### 5.4. RECOVERY

- (196) According to the Treaty and the Court’s established case-law, the Commission is competent to decide that the Member State concerned must abolish or alter aid when it has found that it is incompatible with the internal market<sup>(37)</sup>. The Court has also consistently held that the obligation on a Member State to abolish aid regarded by the Commission as being incompatible with the internal market is designed to re-establish the previously existing situation<sup>(38)</sup>.
- (197) In this context, the Court has established that this objective is attained once the recipient has repaid the amounts granted by way of unlawful aid, thus forfeiting the advantage which it had enjoyed over its competitors on the market, and the situation prior to the payment of the aid is restored<sup>(39)</sup>.
- (198) In line with the case-law, Article 14(1) of Council Regulation (EC) No 659/1999<sup>(40)</sup> stated that ‘where negative decisions are taken in cases of unlawful aid, the Commission shall decide that the Member State concerned shall take all necessary measures to recover the aid from the beneficiary [...]’.

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(199) Thus, given that the measures in question in the total amount of EUR 66 099 317.94 (EUR 31,33 million in the form of the State's participation to the capital increase (measure 1), EUR 34,5 million in the form of the rescue aid loan (measure 2) and EUR 269 317.94 in the form of the training aid (measure 5)) were implemented in violation of Article 108 of the Treaty, and are to be considered as unlawful and incompatible aid, they must be recovered in order to re-establish the situation that existed on the market prior to their granting. Recovery should cover the time from when the advantage accrued to the beneficiary, that is to say when the aid was put at the disposal of the beneficiary, until effective recovery, and the sums to be recovered should therefore bear interest until effective recovery.

## 6. CONCLUSION

(200) As regards measure 3, the procedure laid down in Article 108(2) of the Treaty has become devoid of purpose due to the non-implementation of the measure by Cyprus.

(201) The Commission finds that measures 1, 2, 4 and 5 regarding the State's participation to the capital increase, rescue aid loan, restructuring aid and training aid respectively, in favour of Cyprus Airways constitute State aid within the meaning of Article 107(1) of the Treaty and are incompatible with the internal market, because the relevant conditions of the 2004 Rescue and Restructuring Guidelines were not met and no other compatibility grounds were identified.

(202) As regards measures 1, 2, 4 and 5, the Commission finds that Cyprus has unlawfully implemented them in breach of Article 108(3) of the Treaty.

(203) Finally, the Commission notes that Cyprus agreed to have the present decision adopted and notified in English.

HAS ADOPTED THIS DECISION:

### *Article 1*

The formal investigation procedure under Article 108(2) of the Treaty initiated on 6 March 2013 in respect to potential *ex gratia* compensation by Cyprus to Cyprus Airways has become devoid of purpose, because Cyprus has abandoned the measure. That procedure is hereby closed.

### *Article 2*

The State aid amounting to at least EUR 66 099 317.94, which results from the sum of EUR 31,33 million in the form of the State's participation to the capital increase, EUR 34,5 million in the form of the rescue aid loan and EUR 269 317.94 in the form of the training aid, unlawfully granted to Cyprus Airways by Cyprus in breach of Article 108(3) of the Treaty, is incompatible with the internal market.

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### *Article 3*

Any State aid in addition to the amounts referred to in Article 2 which Cyprus has granted or might want to grant to Cyprus Airways in the context of measure 4 is incompatible with the internal market.

### *Article 4*

1 Cyprus shall recover the incompatible aid referred to in Article 2 from the beneficiary. It shall also recover any additional aid as referred to in Article 3 from the beneficiary.

2 The sums to be recovered shall bear interest from the date on which they were put at the disposal of the beneficiary until their actual recovery.

3 The interest shall be calculated on a compound basis in accordance with Chapter V of Commission Regulation (EC) No 794/2004<sup>(41)</sup>, and to Commission Regulation (EC) No 271/2008<sup>(42)</sup> amending Regulation (EC) No 794/2004.

4 As regards measure 4, Cyprus shall inform the Commission whether it has granted any additional amounts above those referred to in Article 2 in the context of this measure and shall also inform the Commission about the exact amounts granted and granting dates.

5 As regards measure 5, Cyprus shall inform the Commission about the dates when the individual amounts were granted.

6 Cyprus shall abolish measure 4 and cancel all outstanding payments of the aid referred to in Article 2 and 3 with effect from the date of adoption of this Decision.

### *Article 5*

1 Recovery of the aid referred to in Article 2 and Article 3 shall be immediate and effective.

2 Cyprus shall ensure that this Decision is implemented within four months following the date of notification of this Decision.

### *Article 6*

1 Within two months following notification of this Decision, Cyprus shall submit the following information:

- a Information requested under Article 4 paragraphs 4 and 5;
- b the total amount (principal and recovery interests) to be recovered from the beneficiary<sup>(43)</sup>;
- c a detailed description of the measures already taken and planned to comply with this Decision;
- d documents demonstrating that the beneficiary has been ordered to repay the aid.

2 Cyprus shall keep the Commission informed of the progress of the national measures taken to implement this Decision until recovery of the aid referred to in Article 2 and Article 3 has been completed. It shall immediately submit, on simple request by the Commission, information on the measures already taken and planned to comply with this Decision. It shall also provide detailed information concerning the amounts of aid and recovery interest already recovered from the beneficiary.

### *Article 7*

This Decision is addressed to the Republic of Cyprus.

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Done at Brussels, 9 January 2015.

*For the Commission*

Margrethe VESTAGER

*Member of the Commission*

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ANNEX

INFORMATION ABOUT THE AMOUNTS OF AID RECEIVED, TO BE RECOVERED AND ALREADY RECOVERED (ALL AMOUNTS IN EUR)

| Identity of the beneficiary — measure                               | Total amount of aid received | Total amount of aid to be recovered(Principal) | Total amount already reimbursed |                   |
|---|------------------------------|--|---------------------------------|-------------------|
|   |                              |  | Principal                       | Recovery interest |
| Cyprus airways — State's participation to the capital increase      | 31 330 000 <sup>a</sup>      | 31 330 000                                     |                                 |                   |
| Cyprus airways — Rescue aid loan                                    | 34 500 000 <sup>b</sup>      | 34 500 000                                     |                                 |                   |
| Cyprus airways — Training aid                                       | 269 317.94 <sup>c</sup>      | 269 317.94                                     |                                 |                   |
| <i>[Please adjust if any other aid was granted under Measure 4]</i> |                              |  |                                 |                   |

**a** Amount as referred to in recital 110 of the Decision.

**b** Amount as referred to in recital 111 of the Decision.

**c** Amount as referred to in recital 117 of the Decision.

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- (1) SA.35888: [OJ C 152, 30.5.2013, p. 12](#); SA.37220 and SA.38225: [OJ C 117, 16.4.2014, p. 125](#).
- (2) Cf. footnote 1.
- (3) SA.27573 (2012/MX) — *Scheme for constant training programmes for individual enterprises — Cyprus*, approved in Cyprus by the Decision of the Commissioner for State Aid Control, published in the Cypriot Official Gazette nr. 8025 of 21 November 2008.
- (4) Cf. footnote 1.
- (5) Commission Recommendation 2003/361/EC of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises ([OJ L 124, 20.5.2003, p. 36](#)).
- (6) Commission decision of 3 May 2005 in case N69/2005 ([OJ C 191, 5.8.2005, p. 4](#)) and Commission Decision 2008/137/EC of 7 March 2007 — State aid C 10/06 (ex N555/05) — Cyprus Airways Public Ltd — Restructuring plan ([OJ L 49, 22.2.2008, p. 25](#)).
- (7) Commission decision of 27 June 2012 in case SA.32523 (11/N) ([OJ C 230, 1.8.2012, p. 1](#)).
- (8) ATH: Athens; SKG: Thessaloniki; HER: Heraklion-Crete; RHO-Rhodes; LED: St. Petersburg.
- (9) FCO: Rome Fiumicino; VIE: Vienna, LHR: London Heathrow, STN: London-Stansted.
- (10) LON: Collectively referred to airports in the London area.
- (11) AMS: Amsterdam Schiphol; CDG: Paris Charles de Gaulle; SVO: Moscow Sheremetyevo; SOF: Sofia; FRA: Frankfurt am Main; MUC: Munich; ZRH: Zurich; TLV: Tel Aviv; BEY: Beirut.
- (12) Available seat kilometres.
- (13) The 2013 restructuring plan considered routes which have positive gross contribution to the company's costs, that is to say, revenue minus variable cost, to be profitable routes.
- (14) Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Article 87 and 88 of the Treaty ([OJ L 214, 9.8.2008, p. 3](#)).
- (15) Communication from the Commission — Community guidelines on State aid for rescuing and restructuring firms in difficulty ([OJ C 244, 1.10.2004, p. 2](#)), the validity of which was extended in 2009 ([OJ C 156, 9.7.2009, p. 3](#)) and in 2012 ([OJ C 296, 2.10.2012, p. 3](#)). Although the Commission has adopted and published new guidelines for rescue and restructuring aid ([OJ C 249, 31.7.2014, p. 1](#)), in this decision the Commission will continue to refer to the 2004 Rescue and Restructuring Guidelines, because the measures under investigation were notified before 1 August 2014. In addition, to the extent aid has already been granted without the Commission's authorisation and therefore in breach of Article 108(3) of the Treaty (i.e. measures 1, and 5), it was granted before the entry into force of the new guidelines.
- (16) This is lower than the interest rate which was reported in the notification of the rescue aid, see recital 29.
- (17) Commission decision of 22 February 2006 in case N 464/2005, restructuring aid in favour of AB Kauno ketaus liejykla ([OJ C 270, 7.11.2006, p. 2](#)); Commission decision of 18 July 2001 in case NN 92/1999, measures in favour of Zentrum Mikroelektronik Dresden AG — Sachsen ([OJ C 328, 23.11.2001, p. 5](#)); Commission decision of 1 June 2005 in case N 584/2004, restructuring aid to AB Vingriai ([OJ C 187, 30.7.2005, p. 15](#)); Commission Decision 2010/3/EC of 6 November 2008 on State aid C 19/05 (ex N 203/05) granted by Poland to Stocznia Szczecińska ([OJ L 5, 8.1.2010, p. 1](#)).
- (18) The route LCA-ATH-LCA appeared to have a negative gross contribution in 2012. The Cypriot authorities explained that this route was operated in combination with other domestic routes in Greece and that between LCA and ATH it was profitable on a gross contribution level. However, the Cypriot authorities never submitted the data that would justify this claim.
- (19) PASYPI-PALPU (Pancyprian Airline Pilots Union), SYNIKA (Cyprus Airways Employees Trade Union), ASYSEKA (Independent Trade Union of Employees in Cyprus Airways Group), SIDIKEK PEO (Trade Union of Semi-public, municipal and communal employees of Cyprus), SYPKKA (Trade Union of Flight Attendants of Cyprus Airways).
- (20) See, for example, Case C-305/89 *Italy v Commission* ('ALFA Romeo') [1991] ECR I-1603, paragraphs 18 and 19; Case T-16/96 *Cityflyer Express v Commission* [1998] ECR II-757, paragraph 51; Joined Cases T-129/95, T-2/96 and T-97/96 *Neue Maxhütte Stahlwerke and Lech-*



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**Changes to legislation:** There are currently no known outstanding effects for the Commission Decision (EU) 2015/1073. (See end of Document for details)

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- Stahlwerke v Commission* [1999] ECR II-17, paragraph 104; Joined Cases T-268/08 and T-281/08 *Land Burgenland and Austria v Commission* [2012] ECR II-0000, paragraph 48.
- (21) Case C-364/90, *Italy v Commission*, [1993] ECR I-2097, paragraph 20.
- (22) Joined Cases T-102/07 *Freistaat Sachsen v Commission* and T-120/07 *MB Immobilien and MB System v Commission*, [2010] ECR II-585, paragraph 106.
- (23) See Commission Decision 2008/716/EC of 2 April 2008 on State aid C 38/07 (ex NN 45/07) implemented by France for Arbel Fauvet Rail SA, paragraph 35 (OJ L 238, 5.9.2008, p. 27).
- (24) See Commission decision of 9 July 2014 in case SA.34191 (2012/C) regarding measures implemented by Latvia for A/S Air Baltic Corporation (airBaltic), not yet published, recital 179; Commission decision of 9 July 2014 in case SA.32715 (2012/C) regarding Adria Airways d.d., not yet published, recital 131; Commission Decision 2013/151/EU of 19 September 2012 on the State aid SA.30908 (11/C, ex N 176/10) implemented by the Czech Republic for České aerolinie, a.s. (ČSA — Czech Airlines — Restructuring plan) (OJ L 92, 3.4.2013, p. 16), recital 107 and Commission Decision 2012/661/EU of 27 June 2012 on the State aid No SA.33015 (2012/C) which Malta is planning to implement for Air Malta plc. (OJ L 301, 30.10.2012, p. 29), recital 93; Commission decision of 29 July 2014 in case SA.36874 (2013/N) regarding restructuring aid for LOT Polish Airlines S.A., not yet published, recital 241.
- (25) Around four months elapsed between the Board resolution in February 2012 and the Council of Ministers approval of a draft law allowing the capital increase in June 2012. Further, additional conditions were asked for by the House of Representatives before approving the capital increase.
- (26) In the Commission decision of 22 February 2006 in case N 464/2005, restructuring aid in favour of AB Kauno ketaus liejykla, also cited by the Cypriot authorities, the Commission approved a longer restructuring period based among others on a 46 % reduction in capacity. Cyprus Airways will only reduce its capacity by 35 %. The Commission has also approved a longer restructuring period taking into account the very small market share of the company, the fact that measures occurred before the country was being considered a functioning market economy, and dramatic operational restructuring measures. Commission decision of 1 June 2005 in case N 584/2004, restructuring aid to AB Vingriai (OJ C 187, 30.7.2005, p. 15). The precedents of Zentrum Mikroelektronik Dresden AG — Sachsen and Stocznia Szczecińska, referred to by the Cypriot authorities, are also not relevant, because in the former the aid was approved under older guidelines for rescue and restructuring and took into account the specific situation of an originally State owned enterprise in the former East Germany, while in the latter the aid was not approved.
- (27) See for instance Commission decision of 9 July 2014 in case SA.34191 (2012/C) regarding measures implemented by Latvia for A/S Air Baltic Corporation (airBaltic), not yet published, recital 185; or Commission decision of 29 July 2014 in case SA.36874 (2013/N) regarding restructuring aid for LOT Polish Airlines S.A., not yet published, recital 234.
- (28) Fully coordinated airports are defined in Article 2(g) of Council Regulation (EEC) No 95/93 of 18 January 1993 on common rules for the allocation of slots at Community airports (OJ L 14, 22.1.1993, p. 1). According to Article 3(4) of Regulation (EEC) No 95/93, those airports experience, at least during certain periods, capacity constraints.
- (29) See Commission decision of 9 July 2014 in case SA.34191 (2012/C) regarding measures implemented by Latvia for A/S Air Baltic Corporation (airBaltic), not yet published, recital 194; Commission decision of 9 July 2014 in case SA.32715 (2012/C) regarding Adria Airways d.d., not yet published, recital 143; Decision 2013/151/EU, recital 130.
- (30) See Commission decision of 9 July 2014 in case SA.34191 (2012/C) regarding measures implemented by Latvia for A/S Air Baltic Corporation (airBaltic), not yet published, recital 195; Commission decision of 9 July 2014 in case SA.32715 (2012/C) regarding Adria Airways d.d., not yet published, recital 136.
- (31) The statutes of Cyprus Airways and the Company's annual accounts reveal that it operates a number of retirement benefit plans, including the Provident Fund and that the Company assumes the liability for safeguarding the value of the Provident Fund and this liability is included in the Company's payables and provisions. In addition, the Company guarantees the purchasing power of the retirement benefits so that these are not less than a defined minimum total benefit.
- (32) See Commission Decision 2010/175/EC of 22 July 2009 on State aid C 18/05 (ex N 438/04, N 194/05 and PL 34/04) awarded by Poland to Stocznia Gdańsk (OJ L 81, 26.3.2010, p. 19), recital 276.

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- (33) See Commission decision of 24 January 2006 in case N 814/2006, on the Regional aid map 2007-13 (OJ C 68, 24.3.2007, p. 28).
- (34) The Cypriot authorities refer to the Air Malta rescue aid decision which would have acknowledged exceptional circumstances and allowed rescue aid in a period that was shorter than 10 years from a previous restructuring aid (Commission decision of 15 November 2010 in case N 504/2010 — Air Malta plc — Rescue aid (OJ C 102, 2.4.2011, p. 4). The Commission notes that there are significant differences between the Air Malta case and the current case. The previous measure in the Air Malta case was carried out in April 2004, before accession of Malta to the EU, and was thus not subject to approval by the Commission. The Maltese authorities argued that the 2004 measure was in line with the market economy investor principle and thus did not constitute State aid. Due to the urgency of the rescue aid approval, the Commission was not in a position to arrive at a definitive conclusion about the aid character of the 2004 measure. However, in the subsequent restructuring aid decision (Decision 2012/661/EU) the Commission concluded that the 2004 measure did not constitute State aid. In the current case, there is no doubt that Cyprus Airways received restructuring aid in 2007. Further, one of the exceptional circumstances accepted by the Commission concerned the fact that at the time of the 2004 measure, access to Malta International Airport was governed exclusively by traffic rights in bilateral air agreements, while in 2010 access was open to all EU carriers. There was no such fundamental change between 2007 and now as regards access to Cypriot airports. Finally, while Malta depended for more than 50 % of its air traffic on Air Malta, the share of Cyprus Airways of the Cyprus air traffic was only 15 % in 2012 and since then has been further decreasing.
- (35) See Commission decision of 27 June 2012 in case SA.32523 (11/N), paragraph 11.
- (36) See 2007 Annual Report, p. 97; 2008 Annual Report, p. 88; 2009 Annual Report, p. 91.
- (37) See Case C-70/72 *Commission v Germany* [1973] ECR 813, paragraph 13.
- (38) See Joined Cases C-278/92, C-279/92 and C-280/92 *Spain v Commission* [1994] ECR I-4103, paragraph 75.
- (39) See Case C-75/97 *Belgium v Commission* [1999] ECR I-030671 paragraphs 64 and 65.
- (40) Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union (OJ L 83, 27.3.1999, p. 1).
- (41) Commission Regulation (EC) No 794/2004 of 21 April 2004 implementing Council Regulation (EC) No 659/1999 laying down rules for the application of Article 93 of the EC Treaty (OJ L 140, 30.4.2004, p. 1).
- (42) Commission Regulation (EC) No 271/2008 of 30 January 2008 amending Regulation (EC) No 794/2004 implementing Council Regulation (EC) No 659/1999 laying down detailed rules for the application of Article 93 of the EC Treaty (OJ L 82, 25.3.2008, p. 1).
- (43) This information is to be provided in the form of the table attached to this Decision as an annex.

**Changes to legislation:**

There are currently no known outstanding effects for the Commission Decision (EU) 2015/1073.