II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 21 May 1986

on aid granted by the Federal Republic of Germany and the Land of Bavaria to a producer of polyamide and polyester yarn situated in Deggendorf

(Only the German text is authentic)

(86/509/EEC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community, and in particular the first subparagraph of Article 93 (2) thereof,

Having given notice to the parties concerned to submit their comments as provided for in the said Article 93, and having regard to those comments,

Whereas :

I

Upon repeated requests from the Commission, the Federal German Government by letters of 22 March and 25 July 1985 belatedly informed the Commission that financial assistance had been granted to a producer of polyamide and polyester yarn situated in Deggendorf.

The aid was granted between 1981 and the end of 1983 under the joint Federal Government/*Länder* regional aid programme *(Gemeinschaftsaufgabe)*, and under the Bavarian regional aid programme.

Under the joint Federal Government/*Länder* aid scheme, a grant of DM 6,12 million was paid for investments amounting to DM 61,2 million, while under the Bavarian regional aid programme a loan of DM 11 million at an interest rate of 5 %, and running for 8 years, was given for parts of the above investment amounting to DM 35,9 million. The aid therefore, represents 28 % of the total investment.

Following an initial scrutiny, the Commission considered that the aid, granted between 1981 and the end of 1983, which had not been notified to the Commission beforehand, was illegal as the German Government had failed to fulfil its obligations under Article 93 (3) of the EEC Treaty. Under the synthetic fibre and yarn aid code, established in 1977, notified to the Member States by letter of 19 July 1977 and published in the *Bulletin of the European Communities* of July/August 1977 (point 1.5.3.) and of November 1977 (point 2.1.47) and extended in 1979, 1981, 1983 and 1985, all aid proposals, of whatever type, in favour of companies in the synthetic fibre and yarn sector have to be notified to the Commission in sufficient time to enable it to submit its comments and, if necessary, initiate in respect of the proposed measure the procedure provided for in Article 93 (2).

The Commission also considered that the aid did not help to restructure the facility to produce polyamide and polyester yarn within the meaning of the Community's synthetic fibre and yarn aid code, as the assistance led neither to a decrease in capacity nor to a conversion away from synthetic fibres and yarns.

The Commission also took the view that the investment, which had been described as basic rationalization by the German Government, did not seem to concern more than a modernization of the synthetic yarn production and processing plant for the purpose of keeping it in business and at least maintaining — if

not considerably extending — its level of activity without effecting any fundamental change. Nearly 50 % of the total investments that had benefited from the two aids directly concerned the yarn production and spinning stage. However, as the remaining investment shares, linked to texturizing and twisting, dyeing and knitting of the yarn so produced, cannot be logically separated from the actual yarn production — as in most firms these are fully integrated production stages — the entirety of the investment should have been carried out by using the firm's own financial resources and without the use of State aid.

Finally, the Commission considered that, in a situation where the other Community synthetic fibre and yarn producers continued to undertake great efforts to adapt to the present market situation by considerably reducing capacities, the aid in question did not promote a development which, from the Community point of view, was adequate to counteract the trade-distorting effects of the aid, and that the aid — by favouring the undertaking in question in a sector where there is a high volume of trade and where competition is very keen — was liable to affect trade between Member States and was therefore incompatible with the common market.

Therefore, the Commission took the view that the aid did not meet the conditions that must be fulfilled for one of the exceptions laid down in Article 92 to apply, and initiated the procedure provided for in the first subparagraph of Article 93 (2) of the EEC Treaty.

By letter of 23 September 1985, it gave the German Government notice to submit its comments. The other Member States were informed on 17 October, and interested parties on 29 October 1985.

II

The German Government, in submitting its comments, by letter of 30 December 1985, under the procedure provided for in Article 93 (2) of the EEC Treay, pointed out that the investment was necessary as yarns in the required quality are not available in sufficient quantity on the international market. Furthermore, a basic rationalization had been carried out under the investment project, which has led to a fully integrated and modern production process securing the 1 400 existing and 110 additional jobs.

The German Government considered that the aid under the two aid systems in question was granted to compensate for the economic disadvantages suffered by the Zonal Border Areas to which the region of Deggendorf belongs, so that the conditions of Article 92 (2) (c) of the EEC Treaty were fulfilled and, furthermore, that it was granted to facilitate the development of the area in question where the standard of living is abnormally low and where there is serious underemployment, so that Article 92 (3) (a) of the EEC Treaty is also applicable. The German Government therefore concluded that the aid is compatible with the common market.

In commenting under the same procedure, three other Member States and four federations of firms in the sector supported the Commission's views and expressed great concern about the support measures. In these comments it was underlined that the sector of polyamide and polyester yarns still suffered from serious problems of overcapacity and depressed prices, and that, in such a situation, aid granted for modernization and — indeed — capacity increases would distort competition in the Community by giving unfair advantages to the beneficiary.

It was also pointed out that the aid was granted in contravention of the synthetic fibre and yarn aid code.

III

The financial assistance granted to the company in Deggendorf under the joint Federal Government/ *Länder* regional aid programme *(Gemeinschaftsaufgabe)* and under the Bavarian regional aid programme is aid within the meaning of Article 92 (1) of the EEC Treaty.

This conclusion is not refuted by the argument that regional aid merely compensates for the disadvantages of assisted areas from the point of view of firms choosing a location for their investment.

First of all, it should be pointed out that even compensation for the disadvantages of an area strictly speaking favours the recipient, since it reduces his costs in that area. Secondly, in most cases it is doubtful whether the disadvantages of an area can be quantified with sufficient accuracy to fix aid at a level which exactly compensates for them. Above all, however, regional aid is usually set by Member States at so high a level that it provides firms with a positive financial inducement to locate and invest in certain areas. The contention that regional aid favours the recipients is confirmed by the wording fo Article 92 (3), which provides that aid to promote or facilitate the economic development of certain areas may be held compatible with the common market. This shows that such aid falls within Article 92 (1), and that it cannot be argued that regional aid down does not favour the recipients as it merely compensates for the disadvantages of the particular location.

Therefore, this aid has to be notified to the Commission as provided for by Article 93 (3). In addition, under the synthetic fibre and yarn aid code the Commission requires the *a priori* notification of all aid proposals, of whatever type, in favour of companies in the synthetic fibre and yarn sector. Since the German Government failed to notify the aid in question in this case in advance, the Commission was unable to state its views on the measures before they were implemented. Thus, the aid is illegal in relation to Community law from the time that the measures came into operation. The situation produced by this failure to fulfil obligations is particularly serious since the aid has already been paid to the recipient. The aid in question has given rise to effects that are regarded as being incompatible with the common market.

In cases of aid incompatible with the common market the Commission, making use of a possibility given it by the Court of Justice in its Judgment of 12 July 1973 in Case No 70/72 [1], can require Member States to recover from recipients aid granted illegally.

IV

There is a very high volume of trade in synthetic fibre and yarn, and particularly in polyamide and polyester yarn, with 66 % and 65 %, respectively, of total Community production being traded within the Community.

The company in question has respectively 3,0 % and 4,9 % of the total EEC polyamide and polyester production capacities. It has increased its polyamide capacity from 7 000 tonnes in 1980 to 10 000 tonnes in 1983, and its polyester capacity from 7 000 tonnes in 1980 to 18 000 tonnes in 1983. In addition, the company participates actively in intra-Community trade, both with the yarns produced and with the final products manufactured by using the yarns as raw material.

There is substantial overcapacity in polyamide and polyester yarn in the Community as, despite a recent cyclical upswing resulting primarily from lower imports from the USA because of the higher value of the dollar, and which must also be seen in the light of very low shipment levels in previous years, the geographical shift in production shares continues in favour of the Third World. In 1984, the capacity utilization rate for polyamide was 79 %, having increased from 65 % in 1982 primarily because capacities of some 66 000 tonnes had been scrapped. Additional closures have already been announced for 1986 and the following years. Production output fell by 9 % during the last 4 years. The capacity utilization rate for polyester was 85 % in 1984 after having stood at 67 % in 1982. In the case of polyester, the main reason for the improvement was the scrapping of 73 000 tonnes of production capacity during this period. Deliveries have fallen by 3 % during the last 4 years.

As a result, there is very heavy competition amongst polyamide and polyester yarn producers in the Community, many of which continue to lose money since polyamide prices still do not exceed the 1974 levels and polyester prices have dropped to 70 % of the 1974 levels.

Both yarns concerned belong to the group of products that was the subject of industry agreements under which capacities were to be reduced.

The aid in issue in the present case distorts competition because it calculably improves the recipient's return on his investment, thereby strengthening his financial position compared with competitors who do not receive such assistance. The distortion of competition is appreciable. The aid amounts to 10,85 % net grant equivalent. A reduction in the cost of investment by such a margin gives the assisted firm a considerable advantage over its unaided competitors.

When State financial aid strengthens the position of an undertaking compared with other undertakings competing in intra-Community trade, the latter must be regarded as affected by that aid. In this case, the aid, which reduced the investment costs which the firm situated in Deggendorf would normally have to bear, is liable to affect trade and distort or threaten to distort competition between Member States by favouring the said enterprise within the meaning of Article 92 (1) of the Treaty. Article 92 (1) lays down the principle that aid having the features there described is incompatible with the common market.

The exceptions from the principle of incompatibility, as set out in Article 92 (2) (a) and (b), are not applicable in this case because of the character of the aid which, furthermore, was not intended for such purposes.

Article 92 (3) sets out which aid may be considered to be compatible with the common market. Compatibility with the Treaty must be determined in the context of the Communty and not of a single Member State. In order to safeguard the proper functioning of the common market, and taking into account the principles of Article 3 (f) of the Treaty, the exceptions from the principle of Article 92 (1) as set out in Article 92 (3) must be construed narrowly when an aid scheme or any individual award is scrutinized.

[1] ECR, 1973, p. 813.

In particular, the exceptions may be applied only when the Commission is satisfied that the free play of market forces alone, without the aid, would not induce the prospective aid recipient to adopt a course of action contributing to attainment of one of the said objectives.

To apply the exceptions to cases not contributing to such an objective, or where aid is not necessary to that end, would be to give unfair advantages to certain Member States' industries or undertakings, the financial positions of which would merely be bolstered, and could allow trading conditions between Member States to be affected, and competition to be distorted, without any justification on grounds of Community interest as set out in Article 92 (3).

The German Government has been unable to give, or the Commission to discover, any justification for a finding that the aid falls within one of the categories of exceptions in Article 92 (3).

As regards the exception provided for in Article 92 (3) (b), it is evident that the aid in quesiton was not intended to promote the execution of an important project of common European interest, or to remedy a serious disturbance in the German economy. Aid in favour of one company in the synthetic fibre and yarn industry is not adequate to remedy the kind of situation described in Article 92 (3) (b).

With regard to the exemption provided for in subparagraph 3 (c) of Article 92 EEC in favour of 'aid to facilitate the development of certain economic activities', it must be observed that, in the case of synthetic fibres and yarns in general, and particularly in the case of polyamide and and polyester yarn, there is a high level of trade between Member States and competition is very keen as a result of persistent and uncontested overcapacities and depressed prices, as documented above. For these reasons, synthetic fibres and yarns, including polyamide and polyester, are subject to the synthetic fibre discipline.

In its letter of 11 August 1981, by which it extended this system of control of aid for a further two-year period ending 19 July 1983, thus covering the period relevant to this aid case, the Commission pointed out to Member States that it would express an unfavourable *a priori* opinion with regard to proposed aid, be it sectoral, regional or general, which had the effect of increasing the net production capacity of companies in this sector. It also reminded Member States that it would continue to give sympathetic consideration to proposals to grant aid for the purpose of speeding up or facilitating the process either of conversion away from synthetic fibres into other activities or of restructuring leading to reduction in capacity.

In this letter, the Commission also reminded Member States that it requires the *a priori* notification of all aid proposals, of whatever type, in favour of companies in the synthetic fibre and yarn sector.

All aid to the synthetic fibre sector not only has to meet the conditions of the synthetic fibre discipline but is also subject to the 1971 and 1977 Commission guidelines for aid to the textile industry, under which the granting of aid to investment must be linked to be achievement of clear restructuring objectives as opposed to a simple modernization of production facilities.

The investment in this case, however, described by the German Government as basic rationalization, concerns no more than the modernization of a synthetic yarn production and processing plant for the purpose of keeping it in business without affecting any fundamental change. The investment linked to texturizing and twisting, dyeing and knitting of the yarns cannot be logically separated from the actual yarn production for which approximately 50 % of the investment was needed, as it is only after these processing stages — which in most firms, including the beneficiary, are fully integrated production stages — that the yarns are further processed or sold on the market. The continuous and integrated technique replaced the old process several years ago and most polyamide and polyester producers already use it, so that the investment in question was no more than a normal modernization of an out-of-date plant in order to remain competitive. It cannot be described as restructuring and should therefore have been carried out using the financial resources of the undertaking without the use of State aid.

Furthermore, the Commission has always been opposed in principle to operating aid and has considered that, particularly in textiles, clothing, and synthetic fibres and yarn, investment made by an enterprise for the purpose of keeping it in business or maintaining its level of business without effecting any basic change does not qualify for assistance. It should be added that this position has been supported in full by the German Government on several occasions in the past.

In this case, however, it is evident from the company's production capacity before and after the investment in question that the latter had the effect of considerably increasing the net production capacity in both polyamide and polyester yarn. Furthermore, only these increases of capacity can explain why the company was able to rationalize its production as claimed while at the same time creating 110 additional jobs. Therefore, the aid granted for this investment is contrary to the synthetic fibre and yarn aid code and there is, thus, nothing peculiar to the investment in question which would justify the Commission in exempting the aid concerned from the rules set by the aid code under which such aid is to be avoided, as any new installa-

tion of capacity backed by State aid is contrary to the Community interest, which is to reduce capacity, and aggravates the situation of other existing firms all suffering from overcapacity.

Even in this case, where the output of the assisted company is used chiefly within the company itself, the damage is no less to firms within the Community, for, faced with the additional capacity and rigid consumption patterns, they themselves had to and have to, make additional cuts to offset the new capacity at Deggendorf.

In its comments under the procedure, the German Government claims that the types of yarn produced at Deggendorf, particularly POY (pre-oriented yarn) are not available in sufficient quantities and quality. In this respect it has to be pointed out that this product is one of those fibres and yarns in surplus in the Community as a whole and that POY can be, and is being, produced in high quality by a large number of firms in the Communiy.

Moreover, it has to be pointed out that the beneficiary situated in Deggendorf is a subsidiary of a much larger parent company, engaged in synthetic yarn, textile and clothing production, whose financial strength was and is considerable, so that market forces would have been sufficient in themselves to secure normal development and the investment in question without State intervention.

In recent years, the Commission has always prohibited Member States from granting financial assistance to synthetic-fibre or yarn producers in similar or indeed identical situations, that is, when the company in question merely desired to modernize or rationalize production without effecting any of the changes required under the synthetic fibre aid discipline.

Therefore, and in view of all the foregoing considerations with regard to the exemption provided for in Article 92 (3) (c) of the Treaty in favour of 'aid to facilitate the development of certain economic activities', it must be observed that the aid, by artificially lowering the costs of the undertaking in question, weakened the competitive position of other producers in the Community and therefore had the effect of further reducing capacity utilization and depressing prices, to the detriment, and possible withdrawal from the market, of producers that have hitherto survived owing to restructuring, productivity and quality improvements undertaken from their own resources. Thus, the aid which favoured the undertaking in question, the market position of which is no longer solely determined by its own efficiency, merits and powers, cannot be considered as contributing to a development which, from the Community point of view, would be adequate to counteract the trade-distorting effects of the aid.

The exception provided for in Article 92 (3) (a) is applicable to aid that promotes the economic development of areas where the standard of living is abnormally low or where there is serious underemployment. When the Commission opened the Article 93 (2) procedure against the Tenth General Plan of the Joint Federal Government/*Länder* Aid Programme, it took the view that the economic and social situation in the Federal Republic, whether nationally or locally, did not justify application of Article 92 (3) (a). The Commission stated this position in the Annex to its letter to the Federal Government of 6 November 1981. This view was confirmed by the further study which the Commission carried out before opening the Article 93 (2) procedure against the regional aid schemes of the states of Baden-Württemberg, Bavaria, Hessen, Lower Saxony, Rheinland-Pfalz and Schleswig-Holstein, and was restated in the Annex to the Commission's letter to the Federal Government of 10 August 1984. The Commission would expressly refer to both these statements.

The Commission's latest review of the situation confirms its impression that neither in the Federal Republic as a whole nor in the particular area concerned by this Decision is the standard of living abnormally low or is there serious underemployment, so that the exemption specified in Article 92 (3) (a) is not applicable.

The exception provided for in Article 92 (3) (a) is applicable to aid which facilitates the development of certain economic areas, but which does not adversely affect trading conditions to an extent contrary to the common interest.

The sectoral effects of regional aid to the industry in quesiton in this case need to be examined even for the most underdeveloped areas — to which Deggendorf does not even belong. For this reason, the Commission must undertake its analysis of the economic and social situation in the frame-work of the Community interest which, in this sector, is to reduce capacities.

In the synthetic-fibre and yarn aid code there manifests itself a Community policy which has the explicit support of all Member States. Under this policy, and in the situation in which the industry concerned presently finds itself, aided investments for the purpose of increasing capacity, or in order to modernize and rationalize production without effecting any of the

changes required under the synthetic-fibre aid discipline, do not facilitate the development of certain economic areas as they cannot make a production plant financially and economically more viable and would not secure the jobs in question, so that the objectives set out in Article 93 (3) (c) would not be attained.

Therefore, the aid in question in this case did not promote the economic development of the Deggendorf area within the meaning of Article 92 (3) (c), as it did not bring to the area any lasting increase in income or reduction in unemployment, but is liable to distort competition in intra-Community trade without making the necessary contribution to regional development. It should be noted in this respect that the Commission for the same reasons had to prohibit State aid to other fibre and/or yarn producers situated in regions of the Community which face much greater problems of unemployment, and where the standard of living is much lower, than in the Deggendorf area.

Article 92 (2) (c) of the Treaty sets out that aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany, in so far as such aid is required in order to compensate for the economic disadvantages caused by that division, shall be compatible with the common market.

Article 92 (2) (c) makes its exception from the prohibition of aid contained in Article 92 (1) conditional on clearly specified exceptional circumstances. The Commission, therefore, has a duty to examine whether an aid fulfills the conditions set out in Article 92 (2) (c).

In the case in quesiton, it need not concern the Commission whether the disadvantages originally caused by partition have decreased in view of the increasing lapse of time since that division and of the growing unity of the common market.

In the industry in issue in the present case, sectoral considerations, as expressed in the synthetic-fibre and yarn aid code, which prohibits any aid for the kind of investment in question, and to which the German Government has explicitly given its agreement, namely by letters of 9 September 1981 and 5 September 1983, and as described in detail above, force the Commission to conclude that the aided investment in the present case was not appropriate to compensate any economic disadvantages in the Deggendorf area, as no lasting economic development was being initiated.

The Commission never considered the Zonal Border Areas of the Federal Republic of Germany to be automatically exempt from the monitoring of State aid to industrial sectors that are subject to a specific aid code established in order to combat a serious crisis. In particular, in its letter of 6 November 1981 concerning the tenth joint Federal Government/*Länder* aid plan, it had informed the Federal German Government of such sectoral proviso clauses. The latter never contested them.

Moreover, this policy manifested itself when the Commission prohibited in 1985 the granting of State aid to a synthetic-yarn producer situated in Neumünster (Zonal Border Area) and, as in this case, merely wishing to modernize and rationalize production without effecting any of the basic changes required under the relevant discipline [1].

Thus, it has to be concluded that the aid granted to the company in Deggendorf cannot benefit from the exemption provided for in Article 92 (2) (c) of the EEC Treaty.

In view of all the foregoing considerations, the aid in question is illegal because the Federal German Government did not fulfil its obligations under Article 93 (3) of the EEC Treaty. It does not meet the conditions which must be fulfilled in order for one of the exceptions of Article 92 (2) and (3) of the EEC Treaty to apply. The aid, therefore, must be withdrawn by recovery,

HAS ADOPTED THIS DECISION:

Article 1

The aid amounting to a grant of DM 6,12 million under the joint Federal Government/*Länder* regional aid scheme *(Gemeinschaftsaufgabe)*, and to a loan of DM 11 million at an interest rate of 5 % and running for 8 years under the Bavarian regional aid programme, both granted to a producer of polyamide and polyester yarn situated at Deggendorf during the period between 1981 and the end of 1983, and of which the Federal Government belatedly informed the Commission by letters of 22 March and 25 July 1985, is illegal as it was provided in violation of the provisions of Article 93 (3) of the EEC Treaty. Moreover, it is incompatible with the common market within the meaning of Article 92 of the Treaty.

Article 2

The aid referred to in Article 1 shall be drawn by recovery and the Federal Republic of Germany shall inform the Commission within two months of the date of notification of this Decision of the measures taken to comply herewith.

[1] OJ No L 181, 13. 7. 1985, p. 42.

Article 3

This Decision is addressd to the Federal Republic of Germany.

Done at Brussels, 21 May 1986.

For the Commission
Peter SUTHERLAND
Member of the Commission