II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 21 December 1988

concerning aid from the French Government to an undertaking in the motor vehicle sector — Peugeot SA

(Only the French text is authentic)

(89/305/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 the parties concerned notice to submit their comments, in accordance with the above Article, and having regard to those comments,

Whereas :

I

By two letters dated 30 April 1985, received on the same date, the French Government notified the Commission of aid grants to the Peugeot SA-Citroën Group.

The aid was granted in the form of three loans from the Industrial Modernization Fund (FIM) :

— a loan of FF 200 million at 9,75 % granted on 5 July 1984 to the Société Mécanique Automobile de l'Est (SMAE) for the manufacture at Caen of a completely new gearbox, 20 % lighter than existing gearboxes. The investment taken into account for the FIM loan was FF 1 016 million,

— a loan of FF 500 million at 9,75 % granted on 30 May 1984 to the Société Automobile Peugeot for the construction of a fully automated, polyvalent body assembly unit and automated assembly and sub-assembly lines at Poissy, and the introduction of advanced process technology for the manufacture of the front and rear axles. The investment taken into account for the FIM loan was FF 1 167 000 million,

— a loan of FF 500 million at 8,75 % granted on 12 July 1985 to the Société Automobile Citroën to develop, for a new, small car with low fuel consumption, optimized industrial plant, over 60 % of which uses high-technology materials, and computer-assisted production control techniques ; a considerable degree of flexibility is obtained resulting in productivity gains. The investment taken into account for the FIM loan was FF 1 150 million.

In Decision 85/378/EEC [1], the Commission specified that FIM loans were aid within the meaning of Article 92 (1) of the EEC Treaty and that they could be awarded provided that all significant cases were notified to it in advance.

The loans were initially awarded at various rates of interest for a maximum of 10 years with a grace period of up to two years. Their purpose is to assist innovatory investment especially in the installation of high-technology machinery and equipment, the development of office automation and biotechnology.

[1] OJ No L 216, 13. 8. 1985, p. 12.

The Commission therefore considered that the three loans totalling FF 1 200 million comprised aid elements within the meaning of Article 92 (1) and did not *prima facie* satisfy the conditions for exemption under Article 92 (3). It therefore opened the procedure provided for in Article 93 (2) in respect of the aid.

The main reason for initiating the procedure was the lack of information on the extent to which the FIM loans contributed to the development of genuinely innovative products.

By letter dated 29 January 1986, the Commission gave the French Government notice to submit its comments. Comments were also invited from other Member States by letter dated 15 May 1986 and from other interested parties by a notice in the *Official Journal of the European Communities* [1].

At the Commission's request, the French Government informed it by letter dated 9 September 1987 that an FIM loan of FF 500 million had been awarded on 12 March 1986 to the Société Automobile Citroën. This loan should be seen in the same context as the FF 500 million FIM loan awarded to the Société Automobile Citroën in 1985. It concerned the same programme, had the same objectives and duration and was allocated at identical rates (8,75 %). The investment taken into account for the FIM loan was FF 1 136 million.

The Commission considered that the loan of FF 500 million comprised aid elements within the meaning of Article 92 (1) and was not likely to satisfy the conditions for exemption under Article 92 (3). It therefore initiated the procedure provided for in Article 93 (2) in respect of the aid.

The principal reason for initiating the procedure was lack of information concerning the extent to which the FIM loan contributed to the development of genuinely innovative products.

By letter dated 11 December 1987, the Commission gave the French Government notice to submit its comments. Comments were also invited from other Member States by letter dated 29 February 1988 and from other interested parties by a notice in the *Official Journal of the European Communities* [2].

By letter dated 31 March 1987, the Commission asked the French authorities for further information to enable it to assess the technological content of the investments in question.

[1] OJ No C 144, 11. 6. 1986, p. 3.
[2] OJ No C 60, 4. 3. 1988, p. 2.

II

The French authorities presented their observations by letters dated 12 August 1986, 14 August and 9 September 1987 and 2 March, 4 July and 1 December 1988.

According to the French authorities, all the investments by the PSA group should be viewed in the context of the reorganization and restructuring of the group's industrial assets. After the takeover in 1978 of Chrysler Europe, followed by a depressed motor vehicle market in 1979, the poliy adopted by the PSA group was to reduce surplus production capacity to the level of demand for its products. This led to the closure of factories and therefore to redundancies and violent social disruption in 1982 and 1983, especially at Poissy and Aulnay. Only innovative investment could enable the PSA group to improve productivity and return to a level of profitability in 1985 which is still precarious.

As regards the innovatory nature of the investment financed by the FIM loans, the French authorities regard the loans as supporting investment that is genuinely innovatory and the introduction of manufacturing processes and techniques enabling completely new products to be developed.

As regards the loan to SMAE, the French authorities contended that the innovatory nature of the investment lay in the size of the technological leap taken by SMAE in the design and development of the MA gearbox and also the fact that the gearbox is manufactured under licence by another car manufacturer.

The innovatory nature of the investment financed by the FIM in 1985 and 1986 at the Peugeot and Citroën plants for the launch of two completely redesigned vehicles (the Peugeot 309 and Citroën AX) is, in the view of the French authorities, demonstrated by the fact that the technology was unquestionably among the most advanced at that time, both in Europe and worldwide. The investment in truly innovative technical processes both upstream and downstream of the manufacturing cycle entailed a certain risk for the company which it nevertheless took on with a view to making considerable gains in terms of quality, safety and production management.

The French authorities consider that these investments, which do not involve any increases in capacity, actively helped to improve the competitive position of the European car industry.

They therefore consider that the award of the loans in question to the Peugeot group is compatible with the common market and does not distort competition between undertakings in the other Member States.

In 1984 and 1985, the Peugeot group invested a total of FF 9 300 million. Thus the three loans obtained from the FIM in these two years represented 13 % of investment. In order to finance the programme, the firm would have had to rely largely on internally generated funds. It would also have received contributions from its shareholders and obtained various long- and medium-term loans from French banks or on the financial market at various rates, depending on the method of financing.

According to the French authorities, it is necessary, in order to assess objectively the existence, if any, of real difference between the cost of an investment financed on the open market and the cost of an investment financed by the FIM, to take into account all the financing arranged by the group over at least one financial year.

Thus the rates for the FIM loans granted to PLA in 1984, 1985 and 1986 do not appear to differ substantially from the average rates at which PSA obtained, or could have obtained, loans on the national and international markets in the same years. In June 1986, for example, PSA obtained an international loan of FF 1 000 million at 8 % per annum for 10 years, i. e., at a lower rate than the FIM loan obtained the same year. Similarly, PSA had envisaged a variable-rate share issue in autumn 1986 for a period of seven years and at an actuarial cost of under 9 % per annum.

Within the framework of the consultation procedures, the governments of two other Member States submitted observations.

III

On the basis of Decision 85/378/EEC, all FIM loans constitute aid within the meaning of Article 92 (1) of the EEC Treaty to the extent that it affects trade between Member States and distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods.

The four FIM loans totalling FF 1 700 million which the French Government granted to PSA are aids which enabled the recipient to make investments without bearing all the costs. The aid affects trade between Member States since there is considerable intra-Community trade in the products manufactured by PSA. Trade in passenger vehicles in 1986 between Member States accounted for 5 030 402 vehicles, of which 17,4 % (878 927 units) was exported from France to other Member States. In 1986, Peugeot and Citroën exported 688 996 vehicles to other Community countries, i. e. 45 % of their total car production in France.

It should be noted that the aid elements of the FIM loans are constituted by the two-year grace period and the difference between the interest rate applied by the Crédit National rate to determine the aid element of low-interest loans in connection with the principles for the coordination of regional aid schemes.

The four FIM loans in question, however, were granted at 9,75 % for the FF 200 million loan to the SMAE and the FF 500 million loan to Peugeot, and at 8,75 % for the two FF 500 million loans to Citroën in 1985 and 1986. The reference rates on the dates the loans were granted were 14,75 % for the SMAE loan and the loan to Peugeot, 13 % for the loan to Citroën in 1985 and 11 % for the loan to Citroën in 1986. The interest subsidy is thus 5 % for the loans to SMAE and Peugeot, 4,25 % for the loan to Citroën and 2,25 % for the loan to Citroën in 1986.

As regards 1986, the year for which the French authorities provided examples to illustrate the lack of any aid element, it is necessary to take into account that the reference rate fell sharply in the first half of the year from 13 % on 1 January 1986 to 9,25 % on 27 May 1986. As a result, it would not be appropriate to compare loans obtained after 27 May 1986 with the FIM loan of 12 March 1986.

IV

Article 93 (3) provides that aid must be notified at the planning stage and granted only after the Commission has reached a final decision (suspensory effect). As the aid in question has already been granted, it is therefore unlawful for breach of the provisions of Article 93 (3).

In view of the mandatory nature of the rules of procedure laid down by Article 93 (3) (see Court of Justice Judgments of 11 December 1973 in Case 120/73 — Lorenz, and 22 March 1977 in Case 78/76 — Steinike), the unlawful nature of the aid may not be rectified *a posteriori*. In addition, the Commission can also require the Member States to recover the aid from the recipients (see Judgment of 12 July 1973 in Case 70/72 — Kohlegesetz).

V

The PSA Group was formed in 1980 as a result of the takeover by Peugeot of Citroën and the car production interests of Chrysler Europe. The new divisions suffered to varying degrees from lack of investment and a dated product range. An attempt to relaunch the Chrysler range by reviving the historic name Talbot, inherited via Simca, was eventually considered unsuccessful and was dropped after full integration into Peugeot. In spite of this, the PSA Group has retained three different traditions, which considerably hampers the organization of production.

The PSA Group has succeeded in overcoming this complication in production organization. This is reflected in the financial recovery of the group which in 1985 started to become increasingly profitable. In 1987, its consolidated cashflow position exceeded investment for the first time for many years. Taken in conjunction with the capital increase carried out the same year and the effect of the steady decline in working capital requirements, it therefore contributed to a remakable reduction in the group's debts by more than one-third or FF 11 000 million, Its net financial debts were slightly less than own capital in 1987. The recovery was due to the combined efforts of Portugal and Citroën. The group's net results for 1987 after tax, which is still only partial, represented 4,2 % of turnover. These results would place it ahead of Japanese or German manufacturers, but still below other European and American firms.

The group's recovery is also evident in the steady rise from 1985 in passenger and utility car sales in the European market. The upswing was even stronger than that experienced by any other manufacturer. The group thus increased its share of the European market in 1987 and 1988 (eight months) to 12,2 % and 12,7 % respectively, as against 1986 when it held 11,4 % of the market. In 1981, before the restructuring and integration operations, PSA's share of the European market was 13,1 %. The group currently ocuples third place on the European market and is gradually reaching its objective : to become market leader in Europe.

VI

Article 92 (1) of the Treaty provides that aid meeting the criteria laid down therein is in principle incompatible with the common market. The exceptions provided for in Article 92 (2) are not applicable in this case because of the nature of the proposed assistance, which is not directed towards atainment of such objectives.

Article 92 (3) of the Treaty lists aid which may be compatible with the common market. Compatibility with the Treaty must be determined in the context of the Community as a whole and not in that of a single Member State. In order to ensure the proper functioning of the common market, and having regard to the principles embodied in Article 3 (f) of the Treaty, the exceptions provided for in Article 92 (3) must be construed narrowly when any aid scheme or any individual aid award is scrutinized.

In particular, they may be invoked only when the Commission is satisfied that, without the aid, market forces alone would be insufficient to guide the recipients towards patterns of behaviour that would serve one of the objectives of the said exceptions.

To invoke the exceptions in the case of aid that did not serve such an objective would be to give unfair advantages to certain Member States by affecting trading conditions between Member States to an extent contrary to the common interest.

With regard to the exceptions provided for in Article 92 (3) (a) for aid that promotes the development of certain regions, the regions in which the said PSA investments took place do not suffer from an abnormally low standard of living or from serious under-employment within the meaning of those exceptions.

As to the exceptions provided for in Article 92 (3) (b), the facts of the case provide no grounds whatsoever for considering that the aid in question is intended to promote a project of common European interest (see Judgment of 8 March 1988 in Cases 62 and 72/87) or to remedy a serious disturbance in the French economy. Furthermore, the French Government has not presented any such arguments to justify the aid in question.

The aid does not satisfy the conditions of paragraph 3 (c) as regards the regional aspect. FIM loans are not generally granted to firms located in regions identified in advance, Their aim is not therefore to facilitate the development of certain economic areas, nor has the French Government given any such justification for granting loans to the PSA Group. The aid does not therefore qualify for the exemption in question.

Finally, as regards the exception in Article 92 (3) (c) in respect of aid to facilitate the development of certain economic activities, according to Decision 85/378/EEC the only investments eligible for FIM loans are those of an innovatory nature at Community level.

In its Decision concerning the authorization of FIM loan schemes, the Commission concluded that neither furtherance of the priority industrial interest of France nor industrial modernization as such can be said to be sufficiently in the Community interest to justify application of one of the exceptions in Article 92 (3). On the contrary, such aid was liable to affect trading conditions to an extent contrary to the common interest by strengthening the position of the aided firms in relation to their competitors in the Community. The Court of Justice confirmed the validity of this approach in its Judgment of 13 July 1988 in Case 102/87 — French Republic v. Commission.

The French Government attached to its letters dated 16 June 1987, 2 March and 4 July 1988 and 1 December 1988, technical notes describing the investments partially financed by the FIM loans.

The Commission carried out an exhaustive technical examination of the information in order to determine the extent to which the investment being aided gave rise to genuine innovations at Community level and, as regards the two loans granted to Citroën (totalling FF 1 000 million) and the loan to SMAE (FF 200 million), it has reached the following conclusions :

In the bodybuild area, the traditional concept of panel shops specifically intended for a given vehicle has been abandoned. The aim was to achieve the simultaneous construction in a single body shop of three families of such different products as the Citroën AX, Peugeot 205, Peugeot 309, Citroën BX and Peugeot 405.

The polyvalent system introduced at Poissy in 1985 was considerably improved at the Aulnay plant in 1986 and 1987. At Poissy, the system was achieved by placing manual rectification stations in the middle of the process to cope with any breakdowns in the automation and robotization procedures. This polyvalent (flexible) system, which was only partly successful, had already been introduced by another Community car manufacturer before 1985. At Aulnay, however, the polyvalent system was combined with an audacious process known as 'flux rapide'. This system does away with all manual rectification stations. Welding by robots takes place without back-up and with breakdowns reduced to a minimum. This greatly reduces production time and buffer stocks and improves quality all along the line. Because the slightest breakdown, even well upstream, resulted in production losses. Citroën had to instal an extra manual line at Rennes. The investment in the polyvalent body assembly line with 'flux rapide' totalled FF 747 800 million. It also had high start-up costs, and considerable training costs connected with the 'flux rapide' system. The rapid flow system of flexible bodybuild, based on a Toyota system in Japan, thus proved a costly experiment. It probably constitutes an innovation at European level despite the fact that the body shop at Aulnay is building only one model at present.

As regards the assembly of the AX at Aulnay, PSA decided not to adopt the high-automation approach with which various competitors have experimented (e.g. Volkswagen in their Hall 54 plant). Instead, PSA attempted to avoid the high cost of such an approach by introducing a much greater manual input to achieve flexibility at relatively low investment (FF 82,6 million or 2,5 % of total amount). The flexibility was necessary in view of the huge number of model variants (at least 15 000) of the AX model.

Certain assembly operations were robotized by introducing significant innovations, especially at the stations for fitting roof-linings and windscreens. The alternating manual zones where the car moves along in front of fixed stations at constant speed and automatic assembly zones where the car stops and is released from the body carrier and geometrically aligned called for the development of a new, fully automated body carrier. The carrier, equipped with a microcomputer, is capable of compensating for halts at the automated stations and of using several speeds, including reversing, to give access to the vehicle at certain stations. The development and construction of the carrier system was carried out by an outside sub-contractor at a total cost of FF 150,4 million. This system of automotive carriers is a basic innovation : it has since been used as such or with modifications by other European car manufacturers. Intangible investment by PSA in the innovative concepts of a rapid flow polyvalent body assembly unit and semi-manual assembly unit at the Aulnay factory totalled FF 268 million

The Caen plant supplies the Aulnay assembly unit with two assembled arms and two vertical link assemblies for the front axle, and a complete rear axle assembly. The technical specifications for the AX called for a radically new design for the production lines for the front and rear suspension. Because of the particularly stringent requirements of the specifications, highly automated production and assembly lines were necessary. The techniques employed rely on the systematic use of robots and similar equipment, e.g. automatic supply, identification and loading of components and electronic conformity control by laser and video prior to designation of sub-assemblies.

Automation of the lines was accompanied by the introduction of just-in-time production, characterized by increased flow, improved production processes and greater availability of resources. The investment in these production and assembly lines was FF 435 million. Certain features of these ultra-modern installations constitute innovations at Community level and represent approximately half of the total investment.

Thus, the above innovations introduced by Citroën with the two FIM loans correspond to approximately two-thirds of the total investment (FF 1 470 million out of FF 2 288 million). Consequently, the Commission considers that most of the investments by Citroën, assisted by the two FIM loans, are not modernization investments proper but investments aimed at developing products and processes which were genuinely innovative at Community level at the time of their implementation.

As regards the investment of FF 895,3 million at the SMAE plant at Borny (a Citroën subsidiary), a technical examination by the Commission concluded that it concerned innovatory products and production processes at Community level. The SMAE programme involved the manufacture of a completely new gearbox which is 20 % lighter than existing ones. All the lines involved in the machining of the gearbox components (shafts, gear train, crown gear), i.e. turning, cutting, drifting, grinding, milling, are automated, each part being transferred from station to station by conveyor belt. The assembly operations are also fully automated, which has enabled productivity to reach levels similar to current Japanese performances.

The importance of the technological advance achieved by SMAE in the design and production of the MA gearbox is further emphasized by the fact that another car manufacturer has purchased the licence to manufacture the gearbox.

Consequently, the aid arising out of the FIM loans granted to Citroën totalling FF 1 000 million and to its subsidiary SMAE amounting to FF 200 million which enabled the above innovations to be introduced are compatible with the common market because they satisfy the conditions laid down by the Commission in its decision of 19 December 1984.

In view of the foregoing considerations, the aid elements within the meaning of Article 92 (1) of the EEC Treaty in the form of interest subsidies and a two-year grace period contained in the three FIM loans of FF 1 200 million can, although awarded illegally in breach of Article 93 (3) of the EEC Treaty, be regarded as aid likely to promote the development of certain economic activities within the meaning of Article 92 (3) (c) of the EEC Treaty without altering trading conditions to an extent contrary to the common interest, and are therefore compatible with the common market.

VII

On the other hand, it emerged from the technical examination that the investments financed by the FIM loan to Peugeot of FF 500 million contributed to the modernization of plant and the rejuvenation of products, but could not be considered innovatory at Community level at the time they were introduced. This concerns investments in :

— press shop at Poissy (FF 280,2 million),

— polyvalent body shop at Poissy (FF 505,7 million),

— upholstery and paint shop at Poissy (FF 55,3 million),

— manufacture of front and rear axle assemblies and shock-absorbers at Mulhouse and Bart and their assembly at Poissy (FF 317,2 million),

— stering and engine modifications at Dijon (FF 8,7 million).

The abovementioned investments amount to a total of FF 1 167,1 million.

In particular, the presses, polyvalent bodybuild, upholstery and paint shops and front and rear axle assembly have been automated and modernized to an average technological level in the sector. The presses and assembly units are, however, conventional, whilst the old machinery is partially outdated. As stated above, the polyvalent bodybuild system applied at Poissy had already been used by a Community competitor before 1985 and does not therefore qualify as an innovation as required for an FIM loan. As regards the investment in steering and engine modifcations and the manufacture of front and rear axles, the French authorities have not, despite the Commission's letter dated 31 March 1987, provided the supplementary information requested concerning the innovatory nature of these investments.

In short, the Peugeot investments assisted by the FIM loan concern modernizations, Peugeot's competitors also had to cope with the demands of new technology and covered their costs without assistance from the State. It is quite normal and in the interest of the producer to use the most efficient techniques and materials enabling production and management costs to be cut whilst modernizing the range of products (see Court of Justice in Cases 102/87 (SEB) of 13 July 1988 and 62/87—72/87 (Glaverbel) of 8 March 1988, and the Commission decisions on FIM loans to Renault of 29 March 1988, and to Valeo, of 23 November 1988).

Consequently, the aid resulting from the FIM loan to Peugeot in support of investment in the abovementioned fields is not compatible with the common market because it does not fulfil the conditions of Article 92 (3) (c) and those laid down by the Commission in its Decision of 19 December 1984. The FIM loan of FF 500 million to Peugeot is thus an aid that is incompatible with the common market under Article 92 of the Treaty and should be recovered.

To this end, it is necessary to withdraw the incompatible aid element contained in the FIM loan to Peugeot by ordering the loan to be recovered or by attaching normal market conditions to it and, in any event, by ordering the recovery of the incompatible interest subsidy from which Peugeot benefited until the abovementioned change in the terms of the loan. The Commission quantified the aid element of the loan by calculating the difference between the market reference rate at the time the loan was granted (14,75 % on 30 May 1984) and the interest rate actually granted (9,75 %); the interest subsidy on the loan in question amounts to FF 107,81 million at the date of this Decision.

This amount should be added to the interest subsidy from which the PSA Group could subsequently benefit in the event of a delay in the implementation of this Decision during the period between the date referred to in Article 3 of this Decision and the actual date of reimbursement or modification of the terms of the incompatible loan in question,

HAS ADOPTED THIS DECISION:

Article 1

The aid in the form of an interest subsidy on the FIM loan of FF 500 million in support of investments totalling FF 1 167,1 million granted to Peugeot SA and notified to the Commission on 30 April 1985 is unlawfull for breach of Article 93 (3) of the EEC Treaty. In addition, the aid is incompatible with the common market pursuant to Article 92 (1).

Article 2

The French Government is hereby required to withdraw the aid element contained in the FIM loan referred to in Article 1, either by recovering the loan or by applying market interest rates to it; the rate shall correspond to the Crédit national rate for equipment loans applicable on the date the FIM loan was granted (14,75 %). The French Government shall in any event recover the interest subsidy, amounting to FF 107,81 million, which was granted on the loan and from which PSA has benefited up to the date of adoption of this Decision.

Article 3

The French Government shall inform the Commission of the measures taken to comply with this Decision within two months from its notification.

Article 4

This Decision is addressed to the French Republic.

Done at Brussels, 21 December 1988.

For the Commission

Peter SUTHERLAND

Member of the Commission