II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 25 March 1992

concerning aid awarded by Spain to Intelhorce SA (ex Industrias Textiles de Guadalhorce, SA), now called GTE General Textil España, SA, a State-owned producer of cotton textiles

(Only the Spanish text is authentic)

(92/321/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 in accordance with the above Article to interested parties to submit their comments and having regard to those comments,

Whereas :

I

Industrias Textiles de Guadalhorce, SA — now called GTE General Textil España, SA — was established in 1957 by the 'Instituto Nacional de Industria (INI)', a Spanish State-owned holding agency. The company's authorized activities consist of the production and marketing of cotton products. The firm owns a sole production plant situated in a suburb at 5 km from the town of Malaga (Andalusia). Its production activities integrate vertically : spinning, weaving, finishing and clothing of cotton goods. The company's head office is annexed to the plant. The company has also a commercial delegation in Barcelona.

In 1965 the Spanish authorities decided to suspend the ordinary process of investment in the company as a result of exceptional political and economic circumstances. This fact along with a bad industrial planning made it suffer from serious financial instabilities that kept the company in the red until 1971. In 1972, taking advantage of the favourable situation in the cotton textiles sector, the company was privatized. The new owners initiated a restructuring programme with replacements of weaving equipment and an increase in workforce that reached 3 277 people. During 1972 and 1973 the company made profits. After 1974 the deterioration of the general economic situation and, notably, the crisis in the cotton textiles industry broke off the firm's recovery. The company's competitive position worsened and its negative results accelerated as a consequence of an inadequate policy of modernization. In 1975 Industrias Textiles de Guadalhorce changed its name to Intelhorce, SA.

At that time, Spain was in the midst of a delicate period of political transition and this, together with the economic and social situation in the area and the large number of jobs provided by the company, meant that, in 1980, the State had to take control of it once more through the State-owned holding agency, 'Patrimonio del Estado'. The Spanish Government since launched a restructuring plan designed to secure the company's viability. Thus, between 1980 and 1985 the company carried out considerable fixed investment totalling over Pta 6 000 million, the workforce was gradually reduced from 2 785 people in 1980 to 2 094 by the end of 1985 and sales increased to a top in 1985 of over Pta 9 400 million. Despite these efforts, Intelhorce continued making losses.

During the same period, the State provided over Pta 17 000 million in capital contributions to Intelhorce that served to finance the abovementioned restructuring and to recapitalize the company.

In 1985 Intelhorce turned over Pta 9 400 million with final losses of Pta 1 300 million. Its annual production capacities by industrial activity were : 8 700 tonnes of spun products ; 33 000 km of woven products and 16 600 km of finished products. For its part, the respective effective productions were : 7 327 tonnes ; 27 176 km and 14 192 km.

II

Following a complaint, the Commission requested the Spanish authorities, by letter dated 4 April 1989, to send it all relevant information on alleged capital contributions that the State had made to cover operating losses of Intelhorce, SA after the accession of Spain to the Communities.

By letter dated 18 August 1989, the Spanish authorities provided first information. This reply being insufficient to assess the compatibility of the State intervention with the provisions of Articles 92 and 93 of the Treaty, the Commission requested further information by letter of 28 August 1989. This information was partially submitted by letter of 15 November 1989.

At the request of the Spanish authorities, on 30 May 1990 a meeting took place between representatives of the Spanish administration and the Commission department concerned. By letter dated 31 May 1990, the Spanish authorities completed the information requested.

According to this information, after the accession of Spain to the Communities in January 1986, the State had provided Pta 7 820 million to Intelhorce through five capital increases wholly subscribed by the company's owner, the State-owned holding agency 'Patrimonio del Estado'. The dates on which these capital increases were paid up and their corresponding values are the following :

(Pta)

Date	Amount
25 June 1986 :	2 000 million
26 November 1986 :	1 975 million
30 October 1987 :	1 511 million
13 February 1989 :	607 million
23 May 1989 :	1 727 million
Total	7 820 million

These capital contributions were mainly utilized to finance both equipment replacements and the costs of workforce cut-back operations. In this respect, it should be noted that, over the period 1986 to mid 1989 Intelhorce spent some Pta 5 000 million in investments and over Pta 1 100 million towards redundancies costs, its workforce passing from 1 883 people by the end of 1986 to 1 617 by June 1989.

During the same period, Intelhorce's turnover went down from Pta 8 638 million in 1986 to Pta 6 684 million in 1988, recording final losses of Pta 2 093 million and Pta 2 413 million, respectively. For the same years, its exports to Community countries amounted to 2,7 % and 4,2 % of the abovementioned respective turnovers.

The Spanish authorities also informed the Commission that, after having examined potential alternatives to restore the firm's viability, they had concluded that it was imperative to sell Intelhorce to a private company with an adequate position in the market. With a view to privatizing Intelhorce, in January 1988, the Spanish authorities made approaches to 106 companies thought likely to be interested in the deal, by sending them a promotional brochure on the company. Later on, more detailed information was furnished to those that made known their interest. After negotiations with potential bidders, three final purchase bids were received. Finally, from amongst them, the Spanish authorities selected that offering the highest price in economic terms.

The preferred bid was presented by the companies Benorbe SA and Benservice SA — two agent companies of the Benetton group running its franchising business in Spain — on the following terms :

— before concluding the sale, the State would provide Pta 5 869 million to Intelhorce in the form of additional capital subscribed by 'Patrimonio del Estado',

— the bidders would buy Intelhorce's capital for Pta 2 000 million according to the following proportions : Benorbe (70 %), Benservice (30 %) ; the price would be paid in three instalments of Pta 700 million, Pta 700 million and Pta 600 million, due on 1 June of the years 1991, 1992 and 1993,

— the new owners would subscribe a capital increase of Intelhorce of Pta 2 000 million, 25 % of which will be paid up at the moment of the sale.

The capital contribution committed by the State under the terms of the sale was provided by 'Patrimonio del Estado' in two stages : on 1 June 1989, Pta 1 727 million, the remaining Pta 4 142 million being provided on 4 August 1989, just before the signing of the sale contract on the abovementioned terms.

It should be noted that the sale contract contained a conditional clause imposed by the State :

— the new owners will commit themselves not to apply to the State for authorization of temporary lay-offs in Intelhorce, nor to sell the shareholding acquired without previous authorization of the State, respectively, during three and four years after the moment of the purchase.

The Spanish authorities made known to the Commission that the other two final bids rejected were costlier in monetary terms. Both required from the State higher disbursements before the sale — one of them Pta 10 500 million in capital contribution; the other Pta 8 400 million in capital contribution plus public loans of Pta 4 200 million — whilst offering a symbolic price for Interhorce's shareholding. Furthermore, in the Spanish authorities' view, the selected offer was that presenting the greatest probability of success in terms of industrial viability in the light of the characteristics of the five-years restructuring programme for Intelhorce presented by the buyers (see part IV below).

Finally, the Spanish authorities indicated that the alternative for the State to wind up Intelhorce would have been costlier for the State than the preferred option to sell the company on the abovementioned terms, since the payment for dismissal of the whole workforce would have amounted to Pta 11 400 million (Pta 6,8 million for each of the 1 671 workers approximately) and the proceeds from liquidating the company's assets would only have brought in Pta 5 400 million according to their estimates. In addition, the State should have borne subsidies for reindustrialization and creation of employment in the region of Pta 5 000 million and costs of unemployment benefits estimated at Pta 3 000 million for the workers dismissed.

After having examined the foregoing information, on 25 July 1990 the Commission decided to initiate the Article 93 (2) procedure in respect of the Pta 13 689 million capital contributions provided by the State to Intelhorce between the moment of the accession of Spain to the Communities in January 1986 and the effective privatization of the company in August 1989. The Commission considered that those financial interventions constituted an aid within the meaning of Article 92 (1) of the EEC Treaty, and that this aid did not qualify in principle for any of the exemptions to incompatibility provided for in Article 92 (2) and (3). The Article 93 (2) procedure initiated also covered the potential additional aid the State could have granted in accepting the purchase bid of Pta 2 000 million for its shareholding in Intelhorce, in view that the firm's net worth was of Pta 12 500 million before the State's providing the Pta 5 869 million capital contribution under the sale terms.

III

The Commission decision to initiate the Article 93 (2) procedure was notified to the Spanish Government by letter of 18 September 1990. This letter invited the Spanish Government to submit its observations and to provide the detailed information requested therein, as well as any other information it might consider relevant for the Commission to assess the compatibility of the aid.

The other Member States and third interested parties were informed of the Commission decision by publication in the *Official Journal of the European Communities* [1] of the text of the letter sent to the Spanish Government.

The Spanish Government submitted its observations by letter dated 22 November 1990. Afterwards, by letter of 5 December 1990 the Spanish Government provided the additional information requested by the Commission.

First of all, the Spanish Government stated that it disagreed with the provisional conclusion of the Commission that the increases in capital in 1986 to May 1989 of Pta 7 820 million and the capital contribution of Pta 5 869 million before Intelhorce's sale constitute State aid which does not qualify for exemption under the EEC Treaty.

Concerning the capital increases in 1986 to May 1989, the Spanish Government stressed that they had formed part of a restructuring plan designed to secure the company's viability and that the investments carried out by the Government were based on sound criteria which would equally have been applied by a private investor. In its opinion, this produced good results until 1988 when there was a downturn on the market. Furthermore, the Spanish Government considered that the public interventions in question could not be said to have adversely affected competition in the common market, since the market presence of the firm declined in terms both of production capacity and actual output during that period.

Particularly in respect of the capital contributions in 1986 and 1987, the Spanish authorities stated that they took place in response to circumstances which developed prior to Spain's accession to the Communities.

As regards the terms of the sale, the Spanish Government stated that the sale of Intelhorce did not involve State aid either. This was substantiated, in its opinion, by the fact that Intelhorce was sold to the highest bidder, after being openly put up for sale on the international market. In addition, it emphasized that a going concern could not normally be valued on the basis of its net worth, as the Commission did, but in the light of the present value of the anticipated returns of the firm purchased. In this respect, the Spanish Government stressed that Intelhorce's losses in 1986 and 1989 amounted to Pta 2 413 million and Pta 2 145 million respectively, and that reducing the workforce of Intelhorce by 650 jobs under the restructuring programme of the buyers could cost as much as Pta 3 600 million.

[1] OJ No C 320, 20. 12. 1990, p. 16.

Afterwards, the Spanish Government pointed out that even if the terms of the sale did involve aid, the sale of Intelhorce was more than just putting the company into private hands. It meant implementing a recovery plan drawn up by the buyers, that would participate in its financing with a capital contribution of Pta 2 000 million and would incorporate their know-how into the company's assets. Consequently, in its opinion, the sale was not at all designed to keep simply the company in business, but to ensure its economic, technical and financial recovery, for which reason, the public interventions in question complied with the provisions applicable under Community law. Lastly, the Spanish authorities indicated that the firm's location in Malaga, an area classified by the Commission as eligible for regional economic aid, suggested that the exemption provided for in Article 92 (3) (a) of the EEC Treaty would in any case be applicable.

The Commission was also informed that, on 29 December 1989, Intelhorce changed its name to GTE General Textil España, S.A.

As part of the procedure, by telefax dated 18 January 1991 the German federation of textiles producers submitted its comments. This federation stressed the risk of distortion of competition that the aid to Intelhorce could generate in view of the intense competition existing between Community textile producers and the market importance of the company. These comments were communicated to the Spanish Government by letter dated 6 February 1991.

The Spanish Government answered to these comments by letter of 27 March 1991. Concerning the market importance of Intelhorce, the Spanish Government indicated that its rate of participation in the Community production of spun goods was only 0,8 %, and that its corresponding market shares in the production of woven and finished goods were not significant either. In addition, the Spanish Government indicated that Intelhorce's production forecasts for the period 1991 to 1993 show a 21 % reduction in spun goods, and 50 % in woven products. Finally, it was mentioned that in 1988 and 1989 Intelhorce's exports to Germany amounted to Pta 13,6 million and Pta 3,3 million, respectively; in 1990 there was no export to that country, nor was any planned in 1991 either.

IV

Apart from the fact that the selected purchase bid for Intelhorce was the highest one in economic terms, the Spanish authorities have also claimed to justify this choice that, in their opinion, the restructuring programme presented by Benorbe and Benservice was also that showing the highest probability of success in terms of industrial viability.

An initial restructuring programme for Intelhorce, drawn up by the new owners, was submitted by the Spanish authorities in their communication to the Commission of 15 November 1989. At first, that programme made a diagnosis of the company's situation. It identified as a strong point the recapitalization policy carried out before its sale that had improved notably its financial structure, ensuring a negligible debt/equity ratio and an excellent level of working capital. However, despite this high level of financial independence, the company showed a very low internal rate of return with the existing production and marketing structures, that made very unstable and risky its financial balance. The conclusion was that a radical change of strategy was required to ensure the company's viability. The key objective of the new strategy was placed on the attainment of a considerable strengthening of the marketing structure, by means of the creation of a double network of shops selling own-produced finished articles in the range of both household linen and clothing, with innovative design and a new promotional registered mark.

According to this strategy, over 1990 to 1992 Intelhorce planned to open 15 of its own shops in Spain for household linen, and in 1993 to 1994 22 others under franchising contracts. In respect of clothing, it planned to open 14 of its own shops in Spain over 1991 to 1992, and 50 others under franchising contracts in the period 1993 to 1994.

In terms of turnover, that strategy meant that Intelhorce would increase its sales of traditional products from Pta 7 614 million in 1990 to Pta 9 254 million in 1994, whilst its sales through the shops network increasing from Pta 140 million in 1990 to Pta 5 583 million in 1994. The corresponding final result for its traditional activities and the margin generated in the shops network would pass from losses of Pta 2 547 million and profits of Pta 56 million in 1990, respectively, to losses of Pta 697 million and profits of Pta 1 741 million in 1994. These figures would make Intelhorce's global result pass from losses of Pta 2 491 million in 1990 to profits of Pta 1 044 million in 1994, this being the first year of positive surplus in the five-years planning covered by the initial restructuring programme.

It should be remarked here that the capital contribution of Pta 5 869 million provided by the State before the sale, plays an outstanding role in the restructuring programme. This contribution was deposited by the State in a blocked bank account, and Intelhorce's managers can only make use of it gradually, if they show to the State as much investment in tangible or intangible fixed assets as the amount they had previously withdrawn. The availability of the blocked account was also limited in time according to the following schedule:

— a first section of Pta 1 869 million available just after the sale without justification, and can also be used for expenses other than investments,

— two successive sections of Pta 1 500 million each available not before 1 July of 1991 and 1992, respectively,

— a last section of Pta 1 000 million not before 1 July 1993.

For the purpose of investment computation, Intelhorce's expenses in marketing, advertising and design would be considered as investments up to a maximum of 20 % of the value of each one of the last three sections.

It should finally be mentioned that this initial restructuring programme did not consider necessary any further reduction in workforce from the 1 650 people employed at the time of the sale.

As a result of the floods suffered by the province of Malaga in November to December 1989, that affected the production structure of Intelhorce, and given the proved lack of capabilities in the company to undertake the launching of the strategy for clothing products, the initial restructuring programme had to be revised. The revised programme was submitted to the Commission in the course of the meeting that took place on 30 May 1990. It redefined the company's objectives for at least the three-year period to come according to the following guidelines: postponement for an indefinite time of the clothing line and its corresponding shops network; reduction in production levels, mainly in those activities with lower value-added proportion; and further reduction in workforce.

Concerning the workforce reduction, the revised programme provided for a further cut of about 40 % to attain a level of 1 000 people by the end of 1992. These dismissals would be mainly financed with the resources initially set aside for investments in the clothing line. Under the revised strategy, Intelhorce's sales of its traditional products would decrease from Pta 7 000 million in 1990 to Pta 5 670 million in 1992. For its part, the shops network for household linen was to turn over Pta 200 million and Pta 1 062 million, respectively, in 1990 and 1992. This meant that Intelhorce's global turnover would decrease from Pta 7 200 million in 1990 to Pta 6 732 million in 1992.

As regards company results, inclusive of planned redundancies costs, Intelhorce was to record losses in its traditional activities amounting to Pta 1 994 million and Pta 2 245 million, respectively, in 1990 and 1992. The household linen shops would contribute profits in those years of Pta 100 million and Pta 533 million. Consequently, Intelhorce's final results would pass from Pta 1 894 million losses in 1990 to Pta 1 712 million losses in 1992. After this latter year results would improve in Pta 1 200 million, which is the estimated annual cost of the further workforce reduction to be completed by the end of the three-year period covered by the revised programme. It should finally be noted that, even though the company's turnover would decline during that period, the export rate was expected to increase from 7 % in 1990 to 20 % in 1992, Europe being the main destination.

The revised restructuring programme does not exclude the initially planned strategy for clothing products being implemented before 1993, if the necessary reorganization to launch that line is carried out meanwhile.

V

On its examination of the capital contributions of Patrimonio del Estado to Intelhorce both in 1986 to May 1989 and under its sale contract, as well as of the other terms of the sale contract with Benorbe and Benservice, the Commission has verified to what extent these public interventions contain State aid elements within the meaning of Article 92 (1) of the EEC Treaty.

It should be remarked here that Patrimonio del Estado is an intrinsic part of the Spanish State with status of Directorate-General within the Spanish Ministry of Economic Affairs. Its financial requirements are wholly covered by the State on the basis of budgetary appropriations. Accordingly, the financial resources of Patrimonio del Estado are to be considered as resources of the State and, consequently, the capital contributions provided to Intelhorce constitute public interventions.

The provision of public funds to companies in the form of capital contribution may involve elements of State aid if those funds are provided in circumstances that would not be acceptable to a private investor operating under normal market conditions. This is the case, amongst others, where the financial position of the company, and particularly the structure and volume of its debt, is such that a normal return — in dividends or capital gains — cannot be expected within a reasonable time from the capital invested, or where, because of its inadequate cash flow if for no other reason, the company would be unable to raise the funds needed for an investment programme on the capital market. This position was made known by the Commission in its letter to the Member States of 17 September 1984 on the application of Articles 92 and 93 of the EEC Treaty to public authorities' holdings. In this respect, it should also be noted that, recently, in its communication of 24 July 1991 [1] introducing a new reporting system to identify when aid is present in financial flows between public authorities and publicly-owned companies, the Commission has reminded Member States of the principles it will use in determining whether aid is involved in such State interventions (see Part III of the communication).

[1] OJ No C 273, 18. 10. 1991, p. 2.

In addition, the Court of Justice has clarified the application of Article 92 (1) of the EEC Treaty in respect of public holdings (see judgments in Cases 323/82 (intermills) [1], 234/84 (Meura) [2] and 40/85 (Boch) [3]). In order to determine whether a capital contribution is State aid, the Court held that it is necessary to see whether the company in question could have obtained the finance on the private capital market. Where the evidence suggests that the beneficiary could not have survived without public funds because it could not have raised the capital required on the open market from a private investor, it is right to conclude that the payment constitutes State aid.

Taking into account that at the time of the first provision of capital by Patrimonio del Estado in 1986, Intelhorce had made losses for two decades with the exception of two years, and considering that the State had already been obliged in the past to recapitalize the company substantially on repeated occasions to keep it in business, without getting any result in terms of capital return for its investments, it is unlikely that a private investor, basing his decision on the foreseeable probability of profit, and disregarding any social consideration or considerations of regional or sectoral policy, would have provided Intelhorce over the period 1986 to May 1989 with successive capital increases totalling Pta 7 820 million.

As regards the terms of the sale of Intelhorce to Benorbe and Benservice, the Commission considers proven that Intelhorce went to the highest bidder. Nevertheless, this fact is not sufficient to assure that no State aid element is involved in the sale of the company. In order to arrive at this conclusion, it has to be proved that the sale took place in an unconditional open bid, that is to say, through a tendering process where any potential buyer is invited to bid for the company and where the State does not impose any condition for settling the sale. In this respect, the information provided by the Spanish authorities indicates that the State imposed certain conditions to the buyers, limiting temporarily the disposal of the shareholding acquired and the company's right to apply to the State for authorization of temporary lay-offs. In addition, given that the State provided financial resources to the company just before its privatization, it is necessary to verify the rationality of the State behaviour as a private investor in respect of its capital contribution of Pta 5 869 million before concluding the sale, and of its accepting a price of Pta 2 000 million for the 100 % capital shareholding held by Patrimonio del Estado in Intelhorce.

In respect of the former question, a private investor operating under normal market economic conditions would intend to maximize the profitability of its investment and would only have made that capital contribution if, later on, such contribution would place him better off in economic terms once considered the sale operation as a whole. The capital contribution provided by the State within the framework of the sale contract of Intelhorce could only have as expected monetary return the offer presented by the bidders for the company's shareholding. Both the capital contribution from the State and the price to be paid by the buyers were thus interrelated, since, under the terms of the sale contract, the buyers would not have paid Pta 2 000 million for Intelhorce's capital, should the State not have previously provided the Pta 5 869 million capital contribution.

In the light of the foregoing considerations, given that the State will recover an amount equivalent to the present value of the instalments to be paid by Benorbe and Benservice for Intelhorce's capital, and considering that in the absence of the Pta 5 869 million capital contribution, the State would not have obtained any money, since the purchaser's bid was conditional on the provision by the State of that capital, the aid element contained therein amounts to Pta 4 405 million, that is to say, the difference between Pta 5 869 and Pta 1 464 million, this latter being the present value at the moment of the sale of the three instalments totalling Pta 2 000 million in nominal terms to be paid by Intelhorce's buyers. (Actualization rate : 12,1 %, which corresponds to the interest rate fixed by the Spanish State for the ICO bonds issued in June 1989).

Concerning the other State aid element potentially involved in the acceptance by the State of a Pta 2 000 million nominal price for Intelhorce's shareholding, the Commission cannot conclude that an additional aid element exists in connection with this behaviour. This is substantiated by the fact that the capital shareholding in Intelhorce cannot be considered as having a value for the State higher than the abovementioned price, in view of the fact that the company's past financial record, as well as the anticipated final results of the company, indicated to the State that no positive return could be expected from its capital shareholding in Intelhorce without a radical change in the company's marketing and production structure that the State did not attempt to undertake.

It should also be noted that in the light of the information available to the Commission, the behaviour of the Spanish Government in selling Intelhorce on the communicated terms does not reveal any State aid element additional to the Pta 4 405 million previously identified, when the chosen option of selling the company as a going concern is compared to the alternative of liquidating the company. In this respect, according to the information submitted by the Spanish authorities the estimated adjusted value of the proceeds from the sale of Intelhorce's assets — previous to the last provision of capital by the State of Pta 5 869 million — was of Pta 5 400 million. In case of liquidation of the company this amount should have been offset against the company's

[1] [1984] ECR 3809.
[2] [1986] ECR 2263.
[3] [1986] ECR 2321.

outstanding liabilities of about Pta 1 000 million, as well as against the payments for dismissal of the whole workforce, estimated at about Pta 11 400 million. In these circumstances, the State would not have drawn any net positive surplus from the liquidation alternative for Intelhorce. Consequently, the identified State aid element under the sale terms continues to be the net disbursement by the State of Pta 4 405 million in the form of capital contribution previous to the company's sale.

Finally, it should be noted that, contrary to the observation of the Spanish authorities, the option to wind up Intelhorce does not appear costlier for the State than the preferred option to sell the company on the accpeted terms. On this score, the State, as owner of the company, would not have been obliged to cover the balance between the proceeds from the liquidation of the assets and the liabilities linked to winding up Intelhorce, given that a joint-stock company such as Intelhorce does limit its responsibility to honour debts up to the value of liquidation of its assets and, in normal circumstances, the owner of the company does not take on any responsibility for any potential deficit.

In assessing the behaviour of the State against that of a market economy private investor, the Commission must take into consideration that 'the test is, in particular, whether in similar circumstances a private shareholder, having regard to the foreseeability of obtaining a return and leaving aside all social, regional-policy and sectoral considerations, would have subscribed the capital in question' (Case 234/84 (Meura), ground 14). If these costs were considered by the Commission, it would amount to granting Member States the power to rescue companies in difficulties on the basis of pure national interest. This situation, that could create serious distortions of competition contrary to the common interest, would be in contradiction with the principles of the EEC Treaty empowering to the Commission to determine the compatibility of State assistance in the context of the Community as a whole and not in that of a single Member State. Putting the abovementioned costs together with those corresponding to the behaviour of the State as owner/shareholder of a company would amount to emptying the market-economy private-investor principle of its meaning.

Therefore, in summary, after detailed examination, the Commission has reached the conclusion that the State aid granted to Intelhorce is made up of the Pta 7 820 million corresponding to the capital contributions from Património del Estado within the period 1986 to May 1989, and the aid element of Pta 4 405 million involved in the last capital contribution from Patrimonio del Estado before the company's privatization, both interventions having artificially strengthened Intelhorce's financial position.

This aid to Intelhorce affects trade between Member States and distorts or threatens to distort competition in the common market within the meaning of Article 92 (1) of the EEC Treaty.

In fact, where financial assistance from the State strengthens the position of certain enterprises compared with that of others competing with them in the Community, it must be deemed to affect those other enterprises (Judgment of the Court of Justice in Case 730/79 (Philip Morris) [1]).

In this respect, it should be noted that the goods produced and marketed by Intelhorce (now named GTE General Textil España SA) are traded between Member States and there is competition among producers. In 1988 the Community global production of textiles amounted to ECU 86 691 million of which over 20 % corresponded to the cotton industry. The Spanish production represents around 11 % of the Community output of spun yarns (category 1) and 13 % of fabrics (category 2), no statistics are available for finished fabrics. Community production amounts to 1 million and to 700 000 tonnes respectively, as the Commission stated in initiating the procedure (Official Journal of 20 December 1990; see note 1 at bottom of page). Indeed, intra-Community trade in cotton textiles is very substantial, showing intra-Community exports rates of 22, 34 and 63 % of the respective Community productions of spun, woven and finished goods. On the other hand, Intelhorce participates in that trade and holds an important position in the Spanish market, as recognized by the Spanish authorities.

It should be recalled that, as the Multi Fibre Agreement states, the market for cotton textiles, in its categories of both yarns and fabrics, is one of those occupying the highest positions in the scale of sensitivity because of stagnation on the demand side and an increasing pressure of imports from third countries that provoke depressed prices and large proportions of idle capacity. In these circumstances, any aid granted to a particular competitor is liable to produce serious distortions of competition.

VI

Concerning the legal status of the aid to Intelhorce under Community law, it has to be calculated that it is illegal, since the Spanish Government failed to notify it in advance to the Commission as provided for by Article 93 (3) of the EEC Treaty.

[1] [1980] ECR 2688.

The situation produced by this breach of the Treaty provisions is particularly serious since the aid in question has already been paid to the recipient. In this respect, it has to be recalled that, in view of the imperative character of the rules of procedure laid down in Article 93 (3) of the EEC Treaty which also are of importance as regards public policy — the direct effect of which the Court of Justice has recognized in its rulings in Cases 77/72 (Capolongo) (1), 120/73 (Lorenz) (2) and 78/76 (Steinicke) (3) —, the illegality of the aid at issue here cannot be remedied a posteriori.

Nevertheless, it should be noted that the Commission is obliged to carry out its due procedures in relation to Article 93 (2) as recognized in the Court of Justice ruling in Case 301/87 (Boussac Saint Frères) (4).

VII

Article 92 (1) of the EEC Treaty provides that aid of the type described therein is in principle incompatible with the common market.

The exceptions provided for in Article 92 (2) of the EEC Treaty are not applicable in this case because of the nature of the aid, not directed towards the attainment of such objectives.

Article 92 (3) of the EEC 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 the single Member State. In order to ensure the proper functioning of the common market, and having regard to the principle embodied in Article 3 (f), the exceptions provided for in Article 92 (3) must be construed narrowly when any aid scheme or 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 recipients towards patterns of behaviour that would serve one of the objectives of the said exceptions.

Applying the exceptions to cases which do not contribute to such objectives or where the aid is not necessary for those purposes would amount to conferring advantages on the industries or firms of certain Member States, whose financial position would be artificially strengthened, thereby affecting trade between Member States and distorting competition without any justification based on the common interest, as referred to in Article 92 (3) of the EEC Treaty.

(1) [1973] ECR 611.
(2) [1973] ECR 1471.
(3) [1977] ECR 595.
(4) [1990] ECR I-307.

The aid to Intelhorce in the form of capital contributions of Pta 7 820 million over the period 1986 to May 1989 represented a big effort to create the basis for a definitive viable restructuring of the company. This is proved by the fact that it was mainly used in practice during that period for investments in rationalization of some Pta 5 000 million, as well as for a cut of 212 in workforce costing over Pta 1 100 million. It should also be noted that the actual production levels of Intelhorce remained for the period in question well below the capacity ceilings previous to the rationalization ; this fact confirms that this aid was not used to relaunch artificially the activities of the company, which would have produced an unacceptable negative externality for the sector. On the other hand, the Commission can also share the Spanish authorities' view that the capital contributions in 1986 and 1987 were in response to circumstances which developed prior to Spain's accession to the Communities. The Commission considers that this judgment can also be extended to those contributions that took place in 1989 without a direct link to the arrangements for the sale of the company. Preaccession industrial policy in Spain in respect of public companies was sometimes based on principles radically different from those inspiring the competition policy under the EEC Treaty. At that time, certain loss-making public companies were run according to decisions opposed to sound managerial principles and were kept artificially in business thanks to the financial assistance of the State. After the accession of Spain to the Communities, these companies have been forced to adapt themselves to an environment of fair competition. The aid to Intelhorce here in question was mainly aiming at facilitating that adaptation. In the light of the foregoing considerations, the Commission has arrived at the conclusion that the capital contributions of Pta 7 820 million in the period 1986 to May 1989 can be considered as compatible with the common market pursuant to the exception provided for in Article 92 (3) (c) of the EEC Treaty, for they contributed to implement a genuine restructuring for the activities of Intelhorce without having unacceptable effects contrary to the common interest.

In respect of the State aid element to Intelhorce of Pta 4 405 million contained in the capital contribution made just before the company's sale, Article 92 (3) (a) lays down an execution for aid that promotes the development of areas where the standard of living is abnormally low or where there is serious underemployment. In this respect, although Intelhorce is situated in Malaga, which is an assisted area pursuant to Article 92 (3) (a) qualifying for regional aid, the aid measure to Intelhorce in question was not granted under the corresponding regional aid schemes but on the bais of ad hoc decisions of the Spanish Government, taking the form of discretionary capital contributions.

Even if the aid in question here were to be considered as regional, it would not however be eligible for compatibility under Article 92 (3) (a), because aid granted pursuant

to the provisions of that Article must contribute to the long-term development of the region — this notably means in this case that the aid must at least serve for restoring the company's viability, objective not attained for Intelhorce in the light of the information submitted so far to the Commission (this aspect is discussed further below) — without having unacceptable negative effects on competition conditions within the Community.

On the other hand, even though the Pta 4 405 million aid element was explicity granted by the State on the condition that at least Pta 3 200 million (80 % of the last three sections of the capital contributions — see Part IV above) be used by Intelhorce in investments — a requisite feature for aid to facilitate the development of certain economic areas as established in the 1979 Commission communication (1), on the principles of coordination of regional aid systems — this aid to Intelhorce cannot be considered automatically as compatible since, in view that its grant was made outside the scope of aid regimes approved by the Commission, the Commission must assess its compatibility on its own merits verifying, amongst other aspects, both that the aided investment projects are in line with the interest of the Community for the sector concerned and that they contribute to a sound restructuring of the company (both aspects are also discussed further below).

In any case, the aid of Pta 4 405 million largely surpasses the level of investments of Pta 3 200 million committed by the company, situation which is in any case unacceptable for investment aid.

As regards the exceptions provided for in Article 92 (3) (b) the aid measures in question were not intended to nor have the features of a project of common interest or of a project likely to remedy a serious disturbance in the Spanish economy, Moreover, the Spanish authorities have not invoked this exception in their observations to the Commission.

As regards the exception provided for in Article 92 (3) (c) of the EEC Treaty, for aid to facilitate the development of certain economic activities, where such aid does not adversely affect trading conditions to an extent contrary to the common interest, it should firstly be noted that the aid to Intelhorce falls under the category of aid to companies in difficulties, as both the company's financial position and financial record have ever been precarious.

(1) OJ No C 31, 3. 2. 1979, p. 9.

Aid to firms in difficulties carries the greatest risk of transferring unemployment and industrial problems from one Member State to another; it acts as a means of preserving the status quo by preventing forces at work in the market economy from their normal consequences in terms of disappearance of uncompetitive firms in their process of adaptation to changing conditions in competition. For this reason the Commission takes a strict approach in assessing the compatibility of aid for restructuring firms in difficulty. In particular, the Commission requires that such public intervention be strictly conditional on the implementation of a sound restructuring or conversion programme capable of restoring the long-term viability of the beneficiary, that must also contain a compensatory justification for the aid in the form of a contribution by the beneficiary over and above the normal play of market forces altered by the aid to the achievement of Community objectives as established in Article 92 (3) of the EEC Treaty.

In this respect, as regards aid in the textile sector, the Commission worked out with the help of national experts a number of criteria to guide the Governments of the Member States on the interventions they might possibly wish to make therein. These criteria were defined in the Community guidelines of 1971 and 1977 on aid to the textile and clothing sectors which are still in force. The major principles set out therein are that aid should be such as to assist the adaptation of the industry by eliminating excess capacity, by facilitating joint R&D activities and by assisting structural changes. Genuine restructuring and adaptation is a prerequisite under the guidelines for the granting of any specific funds for investment purposes. In any case, aid should not simply seek to maintain uncompetitive position.

In the light of the foregoing considerations, it should be noted that the State aid element to Intelhorce of Pta 4 405 million will produce its effect on competition mainly in future, as the disposal of at least Pta 3 200 million is linked to the realization by the company of future investments within the framework of the restructuring plan presented by the buyers. In these circumstances the Commission must verify carefully the characteristics of the planned restructuring programme. In connection with this, it should be remarked that the Commission is suitably placed not only to anticipate and adjust the potential negative effects that this aid element could have on competition, but also to correct the negative effects that the increase in capacity caused by the aid in the period 1986 to May 1989 could have in future if Intelhorce relaunches artificially its activities.

In this respect, after detailed examination of the initial restructuring programme for Intelhorce and of its revised version, the Commission noted that none of them envisaged a commitment for reducing production capacities that could be considered as a compensatory justification for the aid. On the contrary, the initial programme even foresaw a relaunching of the company's activities by a substantial increase in its global sales, both in traditional products and in the shops network, by 91 %, from Pta 7 754 million in 1990 to Pta 14 787 million in 1994. This relaunching was abandoned as hypothesis in the revised programme, which, in a more realistic estimate, foresaw a slight sales reduction by 6,5 % from Pta 7 200 million in 1990 to Pta 6 732 million in 1992. Nevertheless, even in this case, nothing prevented Intelhorce from expanding its activities after 1992 to take advantage of the idle capacity it still owns, with the corresponding highly distorting effects this strategy could cause on competition. In this respect, it should be noted that in 1988 and 1989 the idle capacity rates of Intelhorce in spun, woven and finished products were, respectively: 21, 25 and 35 %; and 18, 25 and 31 %.

Taking this into consideration, in the course of a meeting held on 18 March 1991, the Commission officially requested the Spanish authorities to present, by 10 May 1991, a newly-revised restructuring plan for Intelhorce involving reductions in both production capacity and market share, whilst also ensuring the company's viability. Concerning the last requirement, it should be remarked that the Commission had also serious doubts as to the possibilities of the restructuring programme presented to secure Intelhorce's viability, as in both its initial and revised versions, the company recorded persistent negative financial results.

Having received no reply, by letter of 27 May 1991, the Commission reminded the Spanish authorities of its request, warning them that in the absence of an alternative restructuring plan by 31 May 1991, the Commission would be obliged to take a final position on the basis of the information available to that date. By letter of 27 May 1991, the Spanish authorities submitted further financial data on the past industrial activities of Intelhorce.

By letters dated 12 June and 18 July 1991, the Spanish authorities requested the Commission to postpone any decision on the case until they could submit an alternative restructuring plan that was currently being negotiated with the new owners.

By letter dated 6 August 1991, the Commission informed the Spanish authorities that, in view that even two additional months had already elapsed since the expiration on 31 May 1991 of the last deadline for the submission of an alternative restructuring plan, it could not delay further its taking a final decision.

The Spanish authorities not having submitted to date a revised restructuring plan, the Commission is obliged to conclude that the State aid element to Intelhorce of Pta 4 405 million involved in the capital contribution before the company's sale has to be considered as incompatible with the common market, as it affects trading conditions within the Community to an extent contrary to the common interest, for it does not contribute to a genuine restructuring fully ensuring the viability of the company.

VIII

In case of aid which is incompatible with the common market, the Commission, making use of a possibility given to it by the Court of Justice in its judgment in Case 70/72 (Kohlegesetz) [1], confirmed in Case 310/85 (Deufil) [2], can require Member States to recover from recipients aid granted illegally.

Consequently, Intelhorce must repay the Pta 4 405 million illegally received.

Repayment must be made in accordance with the procedures and provisions of Spanish law, in particular those relating to interest on arrears on State liabilities, with interest starting to run on the date on which the illegal aid was granted. This measure is necessary in order to restore the status quo by removing all the financial benefit which the firm receiving the unlawful aid has improperly enjoyed since the date on which the aid was paid (see judgment in Case 142/87 (Tubemeuse [3]),

HAS ADOPTED THIS DECISION:

Article 1

The aid to Intelhorce in the form of capital contributions of Pta 7 820 million over the period 1986 to May 1989 was granted illegally, since it was granted by the Spanish Government in breach of the procedural rules established in Article 93 (3) of the EEC Treaty.

[1] [1973] ECR 813.
[2] [1987] ECR 901.
[3] [1990] ECR I-959.

Nevertheless, the said aid meets the conditions which must be fulfilled in order for the Article 92 (3) (c) exception to apply, for which reason it is compatible with the common market.

Article 2

The State aid element of Pta 4 405 million contained in the capital contribution provided by Patrimonio del Estado to Intelhorce before its privatization in August 1989 is illegal, since it was awarded by the Spanish Government in violation of the provisions of Article 93 (3).

Furthermore, the said aid element does not meet any of the conditions which must be fulfilled in order for one of the exceptions of Article 92 (2) and (3) to apply, for which reason it is incompatible with the common market.

Article 3

The incompatible State aid element shall be withdrawn by way of recovery. Accordingly, Patrimonio del Estado shall recover Pta 4 405 million referred to in Article 2 from GTE General Textil España, SA (ex Intelhorce, SA).

The aid element shall be recovered in accordance with the procedures and provisions of national law, in particular those relating to interest on arrears payable on State liabilities, with interest starting to run on the date on which the illegal aid was granted.

Article 4

The Spanish Government shall inform the Commission within two months of the date of notification of this Decision of the measures taken to comply herewith.

Article 5

The Decision is addressed to the Kingdom of Spain.

Done at Brussels, 25 March 1992.

For the Commission

Leon BRITTAN

Vice-President