II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 22 December 1998

on aid granted by the Republic of Austria to Ergee Textilwerk GmbH

(notified under document number C(1998) 4568)

(Only the German text is authentic)

(Text with EEA relevance)

(1999/589/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

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

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

Having given notice to the parties concerned, in accordance with Article 93(2) of the EC Treaty, to submit their comments, and having regard to those comments,

Whereas:

1. PROCEDURE

By letter dated 30 June 1997, the Austrian authorities notified the Commission of rescue aid for Ergee Textilwerk GmbH, Schrems, Austria ('Ergee'). The proposed aid was in the form of a guarantee from the Federal Government and the Province of Lower Austria for an operating loan of up to ATS 150 million (ECU 10,8 million). By letter dated 18 November 1997, Austria also notified a capital injection by a new shareholder of ATS 25 million (ECU 1,8 million) which was to be converted into equity capital. The new shareholder is the State-owned Gesellschaft des Bundes für Industriepolitische Maßnahmen GmbH, Vienna ('GBI'). Since GBI carried out the capital injection before the Commission had taken a decision, and the Commission first took the view that the capital injection possibly constituted State aid, since there was no restructuring plan, the case was classified as unnotified aid. On 17 December 1997, the Commission approved the rescue aid under number NN 181/97 (ex N 455/97) for the period from July 1997 to the end of 1997. The Austrian Government was informed of the Commission's decision by letter dated 22 January 1998. A notice to that effect was published in the *Official Journal of the European Communities* [1].

By letter dated 19 December 1997, the Austrian authorities notified restructuring aid. By letter dated 26 January 1998, the Commission requested additional information, which the Austrian authorities provided by letter dated 10 March 1998. By letter dated 20 April 1998, the Commission again requested information, which it should have received within the usual period of 20 working days. On 9 June 1998, Commission officials discussed the matter in Brussels with representatives of the Austrian authorities. By letter dated 23 June, the Austrian authorities provided background information on the GBI. However, the additional information which was requested on 20 April 1998 has not been received. Instead, Austria informed the Commission by fax on 3 July 1998 of some changes to the notification.

By letter dated 4 August 1998 the Commission informed Austria of its decision to initiate proceedings under Article 93(2) of the EC Treaty. It had reached the conclusion that to date Austria had not proved that all the restructuring measures were absolutely necessary or that the State aid was limited to the strict minimum required. The Commission also wanted to know whether Ergee had already received restructuring aid in 1994. Moreover, it found that the GBI capital injection of ATS 25 million (ECU 1,8 million) during the six months' duration of the rescue measures possibly constituted an extension of rescue aid and that perhaps other GBI measures needed to be examined more closely.

[1] OJ C 70, 6.3.1998, p. 8.

In accordance with the judgment of the Court of Justice of the European Communities of 13 April 1994 in Joined Cases C-324/90 and C-342/90 (*Federal Republic of Germany and Pleuger Worthington* v. *Commission*) ([2]), the Commission issued an interim decision requiring Austria to provide all such documentation, information and data as are necessary in order to examine the compatibility of the aid with the common market.

The Commission decision was published in the *Official Journal of the European Communities* ([3]). It requested all interested parties to submit their comments. One comment was received.

2. DETAILED DESCRIPTION OF THE AID MEASURES

The following restructuring measures were notified by the Austrian authorities:

(1) the Federal Government and the Province of Lower Austria are planning to provide, from 1998 to the end of the year 2000, a guarantee for an operating loan of up to ATS 90 million (ECU 6,5 million). The Federal Government and the Provincc of Lower Austria intend to share this guarantee in the proportion two thirds/one third. The guarantee is free of charge to Ergee;

(2) the Federal Government and the Province of Lower Austria are planning to provide a loan of ATS 40 million (ECU 2,9 million), which they are sharing in the proportion of two thirds/one third. The loan has an interest- and redemption-free grace period of one year; that is followed by a period of six years in which the loan is repaid. The repayment terms and conditions and the interest rate are in line with the ERP Fund guidelines for 1996/97;

(3) As regards the loan of ATS 42 million (ECU 3,0 million) granted to Ergee on 30 December 1994, both the Ministry of Labour, Health and Social Affairs and the Province of Lower Austria intend to waive interest payments. If the firm can prove a workforce of at least 370 employees in the period 1997 to 1999, they will also waive repayment of one third of the amount of the loan annually, i.e. ATS 14 million (ECU 1,0 million) per annum.

Austria confirmed that no other firms within the group have received any aid.

Austria also informed the Commission that the GBI wished to increase the payment on account in respect of a subsequent equity capital increase from ATS 25 million (ECU 1,8 million) to ATS 50 million (ECU 3,6 million). Austria did not notify this measure pursuant to Article 93(3) of the EC Treaty, since in its view the activities of the GBI were not caught by Article 92 of the EC Treaty.

([2]) [1994] ECR I p. 1173.
([3]) OJ C 298, 26.9.1998, p. 2.

3. OPINION OF INTERESTED PARTIES

By letter dated 20 October 1998, the British Apparel & Textile Confederation fully agreed with the Commission's measures.

4. AUSTRIA'S POSITION

By letter dated 17 September 1998, Austria communicated the information on the restructuring measures in question which had been requested in the Commission decision initiating proceedings.

Austria supplemented the restructuring plan which had already been sent.

Austria provided information on the equity capital and the other liabilities in 1997 and the balance sheet forecast for 1998 to 2000. This information was explained in detail.

Austria also provided information on the investment carried out in 1997 and planned from 1998 to 2000. The individual investment projects were described in detail and were related to the development of the fixed assets and to Ergee's production capacity. Austria took the view that the individual investment projects were necessary to restore the firm's viability.

Austria provided an up-to-date list of all restructuring costs, including the operational and financial restructuring measures, and an updated list of all restructuring measures.

Austria also presented cash flow calculations which in its view showed that the total amount of aid was 1imited to the amount necessary to restore Ergee's viability.

Austria provided evidence that the 1994 subsidised loan of ATS 42 million (ECU 3 million) from the Federal Ministry of Labour, Health and Social Affairs and the Province of Lower Austria had been planned as investment aid. The investment costs were substantiated in detail.

Austria described the measures of the GBI in the present case and its general approach. It took the view that the GBI was acting in the same way as a private investor and its activities therefore did not constitute State aid within the meaning of Article 92 of the EC Treaty.

Lastly, Austria communicated the calculations on which the GBI based its decision to take over Ergee. In Austria's view these calculations, which took into account the high risk of the participation concerned, proved that the GBI could expect huge advantages from this investment.

5. **ASSESSMENT**

The Commission examined the case on the basis of the information provided by Austria by letter of 17 September 1998.

5.1. **The aid recipient**

The Ergee group was established in 1960 by Edwin E. Rössler KG, Sonthofen, Germany. Ergee is located in the Waldviertel Region which, in accordance with a decision by the EFTA Surveillance Authority [4], is an assisted area within the meaning of Article 92(3)(c) of the EC Treaty.

On 1 September 1994, Rössler KG applied for the intiation of bankruptcy proceedings. Ergee was not involved in any insolvency proceedings. Subsequently, the managing director of Ergee Textilwerk GmbH took over the German parent company's shares and part of its assets. The management buy out, which was largely financed with borrowed funds, was unsuccessful. In July 1997, the State-owned GBI took over the Ergee shares for ATS 1.

In 1997 Ergee employed on average 417 persons, its turnover was ATS 495,8 million (ECU 35,8 million) and its balance-sheet total was ATS 428 million (ECU 30,9 million). The firm has a 69,7 % stake in Loana a.s., Roznov, Czech Republic, which operates at four different sites with a workforce of 926 (1997 figures). Ergee also holds 100 % of the shares in the marketing company Ergee GmbH, Germany (190 employees) and in Ergee AG, Kronbühl, Switzerland (seven employees). According to the Commission recommendation of 3 April 1996 concerning the definition of small and medium-sized enterprises (SMEs) [5], Ergee is a large enterprise which cannot be classified as an SME.

Ergee and its subsidiaries operate in the textile industry. In Austria, Ergee produces stockings and knitwear. The Czech subsidiary produces socks, stockings, medical rubberised stockings and children's clothing.

In 1996, Ergee registered a loss on normal business activity of ATS 214,2 million (ECU 15,5 million) with a turnover of ATS 600,1 million (ECU 43,3 million). At the end of 1996, the negative equity capital amounted to ATS 168,3 million (ECU 12,2 million). At the time when Austria notified the restructuring and rescue aid, Ergee was a company in difficulties.

5.2. **The activities of GBI**

The GBI was established in 1983 by the Federal Government with public money and therefore operates with State resources. Under the terms of the Austrian Law on companies with limited liability, the acquisition of subsidiaries, e.g. the acquisition of Ergee, requires the agreement of the GBI's supervisory board. As the owner of the GBI, the Federal Government appointed the members of the supervisory board. There is therefore a clear influence on the part of the State on the GBI's decision-making. Furthermore, Ergee operates on a market which apparently suffers from overcapacity. Lastly, the GBI participation in Ergee was accompanied by notified rescue and reconstruction aid. In accordance with its many years of investigation practice, the Commission must therefore examine whether the GBI's activities constitute State aid [6].

The GBI's main task is to take over ailing firms, restore them to long-term viability and then sell them. The GBI emphasised that projects were examined in the greatest detail not only by its restructuring experts, but also by recognised audit firms and independent consultancies. According to the information provided by Austria, the GBI only takes over a firm if it can expect to turn it round within two to three years. Since 1983 the GBI has examined some 90 firms and has taken a participation in only nine cases.

Up to now, the GBI has been extremely successful in restoring ailing companies to health. In 1983 it acquired four companies. It took over Austria Haustechnik GmbH, Rottenmann, Glanzstoff Austria GmbH, St. Pölten, Austria Antriebstechnik G. Bauknecht GmbH, Spielberg, and IFE Industrieeinrichtungen Fertigungs AG, Waidhofen/Ybbs. The GBI sold all these firms at a profit in 1988 and 1989 after successful restructuring. In 1993, the GBI took over the Austrian firms Schmid Schrauben Hainfeld GmbH and Assmann Ladenbau Leibnitz GmbH. In both cases, recipient companies were established which bought up the stocks of the ailing companies and leased their fixed assets. The fixed assets were not bought until the success of the restructuring measures was assured. Schmid Schrauben Hainfeld GmbH was sold at a profit in 1996. For Assmann Ladenbau Leibnitz GmbH a stock exchange launch is being considered. In 1997 the GBI acquired Ergee, ATB Austria Antriebstechnik AG, Spielberg, and ATB Antriebstechnik AG, Weinheim, Germany.

The Commission has examined the GBI's financial situation and established that this is an extremely profitable company. Its revenue sources include fees for consultancy services for subsidiaries, dividends paid and profits transferred from such subsidiaries, returns on investment and proceeds from the sale of firms. In 1983 the GBI was provided with equity capital of ATS 44 million (ECU 3,2 million), which it increased to ATS 241 million (ECU 17,4 million) by 1996 from profits and without any further State participation.

As regards Ergee, Austria stated that it was not until the GBI had carried out a due diligence examination that the supervisory board decided to take over the firm in difficulties. Production at Ergee was continued on the basis of the result of this examination. According to this, Ergee was an extremely well-known brand in central Europe (Germany, the Czech Republic, Switzerland, Slovakia and Austria). The firm possessed considerable restructuring potential not only in terms of staff, organisation, logistics, and reduction in the number of company locations, but also in terms of an optimum division of labour in the remaining production plants and of the reorganisation of the operating network. According to the information provided by Austria, the GBI

[4] OJ C 199, 11.5.1994, p. 7.
[5] OJ L 107, 30.4.1996, p. 4.
[6] Bull. EC 9–1984.

was also interested in another of Ergee's Austrian competitors, but decided against its takeover. Following this, the GBI injected capital amounting to ATS 25 million (ECU 1,8 million) into Ergee and incorporated it into the cash management of the group, in order to bridge Ergee's short-term need for finance. In 1998 the GBI will provide Ergee with a further capital injection of ATS 25 million (ECU 1,8 million). It also sent Ergee two of its marketing and financial control experts to strengthen its management.

Austria submitted a detailed calculation of the return on investment. The GBI wishes to maintain its holding in Ergee until 2003.[…](*).

Taking into account all the facts mentioned above, the Commission reaches the conclusion that the GBI's activities are to be equated with those of a private investor and therefore do not constitute State aid within the meaning of Article 92 of the EC Treaty.

5.3. **The notified State aid measures**

The guarantee, the new State loan and the waiving of interest and possibly of repayment of the earlier loan are measures by State bodies. The notified measures are therefore granted from State resources. The purpose of these measures was to enable the ailing Ergee to continue in business and to restore its viability. In this way Ergee was favoured in relation to its competitors. Furthermore, the company is active in the textiles sector on which several competitors are present within the EEA. The firm's main competitors are the two Austrian companies, Palmers Textil AG and Wolford AG, and the two German businesses, Falke Group and Kunert VertriebsgmbH, all of which operate internationally. The notified measures are therefore capable of affecting the business position of these competitors in other Member States. Accordingly, these measures distort or threaten to distort trade between Member States and constitute State aid within the meaning of Article 92(1) of the EC Treaty and Article 61(1) of the EEA Agreement.

The abovementioned aid does not fall under any other approved or already existing system of aid and must therefore be notified individually under Article 93(3) of the EC Treaty. Austria complied with this notification requirement.

5.4. **Derogations**

Article 92(1) of the EC Treaty and Article 61(1) of the EEA Agreement established the principle that aid having the characteristics set out therein are incompatible with the common market. Article 92(2) and (3) of the EC Treaty and Article 61(2) and (3) of the EEA Agreement specify which types of aid may exceptionally be considered to be compatible with the common market.

The Commission has examined whether the measures notified fall within one of these derogations from the aid prohibition.

The derogations provided for in Article 92(2) of the EC Treaty and Article 61(2) of the EEA Agreement are not applicable here, because the aid in question is neither aid having a social character, aid granted to individual consumers, nor aid to make good the damage caused by natural disasters nor aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany.

The derogations provided for in Article 92(3)(a) of the EC Treaty and Article 61 (3)(a) of the EEA Agreement as well as the regional aspect of the derogation in Article 92(3)(c) of the EC Treaty and Article 61(3)(c) of the EEA Agreement are not relevant, since the aid is not granted to promote the economic development of areas where the standard of living is abnormally low or to facilitate the development of certain economic areas.

As regards the derogations provided for in Article 92(3)(b) of the EC Treaty and Article 61(3)(b) of the EEA Agreement, the Commission was compelled to etablish that the project concerned did not fulfil the criteria which usually apply for 'projects of common European interest', nor does it serve to remedy a serious disturbance in the economy of a Member State.

The derogations provided for in Article 92(3)(d) of the EC Treaty and Article 61(3)(d) of the EEA Agreement are not applicable either, because the aid is not intended to promote culture or heritage conservation.

Accordingly, only the first part of the derogation provided for in Article 92(3)(c) of the EC Treaty and Article 61(3)(c) of the EEA Agreement could be applicable, if the aid facilitates the development of certain economic activities and at the same time does not adversely affect trading conditions to an extent contrary to the common interest.

5.5. **Community guidelines**

Ergee is a firm in difficulties. The notified measures represent restructuring aid. The Community guidelines on State aid for rescuing and restructuring firms in difficulty [7] (hereinafter referred to as 'the guidelines') set out the conditions in which restructuring aid may be considered to be compatible with the common market.

According to the guidelines, restructuring must form part of a realistic, coherent and far-reaching plan that will restore the

(*) Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

[7] OJ C 368, 23.12.1994, p. 12.

long-term viability and health of the firm within a reasonable time scale and on the basis of realistic assumptions as to its future operating conditions. The restructuring plan must take account of the circumstances which led to the firm's difficulties, the supply and demand situation on the relevant product markets and the way it is likely to develop, and the specific strengths and weaknesses of the firm. The plan should enable the firm to make a smooth transition to a new structure that is viable in the long term and will enable it to remain in existence on its own merits without any further State support.

Restructuring is normally accompanied by reorganisation and rationalisation of the firm's activities so as to create a more efficient base. This usually means giving up activities that are no longer profitable or are already loss-making, the restructuring of activities that can be made competitive again and possibly the development of, or diversification into, new profitable activities. Such physical restructuring must normally be paralleled by financial restructuring.

Under section 3 of the guidelines, the Commission must in particular examine whether the restructuring satisfies the following conditions: first, restructuring must restore the viability of the firm within a reasonable time scale; secondly, the aid must avoid undue distortion of competition; and thirdly, the aid must be in proportion to the restructuring costs and benefits.

The guidelines also provide that the firm must fully implement the restructuring plan that was submitted to and accepted by the Commission and must discharge any other obligations laid down by the Commission decision.

The Community guidelines also require the Commission to monitor the implementation, progress and success of the restructuring plan.

5.6. **Restoration of long-term viability**

Austria has submitted a realistic, coherent and far-reaching restructuring plan. To begin with, the Commission establishes that the firm is obliged to implement the restructuring plan.

The restructuring plan takes account of the circumstances which led to the firm's difficulties. These difficulties can be attributed to three main areas.

First, Ergee suffered from a bad financial structure. At the end of 1996, the group showed negative equity capital of ATS 122 million (ECU 8,8 million).

Secondly, it is clear that insufficient control was exercised over the group's manufacturing plants in Austria and in the Czech Republic, there was no proper cost management and the group had clearly not adapted its production process to the changing market conditions. In addition, the firm did not pursue a proper brand and product strategy.

The third problem area arises from Ergee's inadequate investment in recent years.

Accordingly the Ergee restructuring measures, which are summarised in the following table, concentrate on these three main areas.

Restructuring costs	ATS (million)	ECU (million)	%
Making good negative equity capital	121,0	8,8	18,7
Injection of sufficient equity capital	165,0	12,0	25,3
Operating losses 1997 and 1998	148,0	10,7	22,7
Extraordinary depreciation of stocks and receivables	56,0	4,1	8,9
Total financial restructuring costs	491,0	35,6	75,4
Redundancy programme	[…] (*)	[…] (*)	[…] (*)
Transfer of storage facilities and offices	[…] (*)	[…] (*)	[…] (*)
Organisational changes	[…] (*)	[…] (*)	[…] (*)
Consultants	[…] (*)	[…] (*)	[…] (*)
Extraordinary marketing measures	[…] (*)	[…] (*)	[…] (*)
Total operational restructuring costs	84,1	6,1	12,9
Investment 1997 to 1999	76,0	5,5	11,7
Total restructuring costs	651,1	47,2	100,0

5.6.1. *Financial restructuring measures*

The total cost of financial restructuring is some ATS 491 million (ECU 35,6 million). In order to restore the group's finances, it was necessary to offset its negative capital of ATS 121 million (ECU 8,8 million) to provide the group with sufficient equity capital of some ATS 165 million (ECU 12,0 million), equivalent to around 25% of the group's balance-sheet total, to cover the losses of ATS 148 million (ECU 10,7 million) forecast for 1997 and 1998 and to make good an extraordinary depreciation of stocks and receivables of ATS 56 million (ECU 4,1 million).

The Commission takes the view that the financial restructuring measures are necessary in order to restore Ergee's financial situation.

The main element in bringing the group's financial situation back to health was the waiver by Ergee's house banks of unsecured loans of ATS 338 million (ECU 24,5 million) in 1997. The following Austrian banks were involved: Bank Austria AG, the Erste Bank der österreichischen Sparkassen AG and the Raiffeisenbank Oberes Waldviertel registrierte Genossenschaft mit beschränkter Haftung. By letters dated 28 May 1998 and 8 June 1998, these banks confirmed that they had agreed to the waiver, since their losses would be far higher if Ergee were to go bankrupt. The Commission takes the view that Bank Austria AG is a public enterprise, although more than 50% of the shares are held by private investors, since it is controlled by the State as largest individual shareholder. The other two banks are private banks. By far, the largest contribution was made by the private Erste Bank der österreichischen Sparkassen AG. The banks established a consortium and took decisions unanimously. The Commission concludes from this that the public Bank Austria AG acted as a private investor.

The GBI provided funds amounting to ATS 25 million (ECU 1,8 million) to increase the capital and undertook to make available a further ATS 25 million, as soon as the Commission adopted a decision on the case.

The State wishes to waive the existing unsecured loan of ATS 42 million (ECU 3,0 million) if the Commission approves this and Ergee satisfies the conditions regarding the number of persons employed in production plants in Austria. In addition, the firm itself intends to make a contribution with the sale of assets[…] (*) and with profits […] (*) expected for 1999 and 2000.

Altogether, funds total ATS 494 million (ECU 35,8 million) and so ensure that the firm will return to a healthy financial situation.

5.6.2. *Operational restructuring measures*

The total cost of the operational restructuring measures is ATS 84,1 million (ECU 6,1 million). The group's main task is to shed labour, in order to improve its cost structure. This is why numbers employed had already been cut from 1 966 in 1996 to 1 397 in 1998. This is equivalent to a 29% reduction. The necessary redundancy programme (mainly for Germany) will cost ATS 55,5 million (ECU 4,0 million).

The following table gives the employment figures.

Reduction in numbers employed	1996	1997	1998
Austria	521	417	390
Czech Republic	1 215	926	921
Germany	225	197	78
Switzerland	5	8	8
Total	1 966	1 548	1 397
Total percentage compared with 1996	100,0	78,7	71,1

Labour shedding is chiefly the result of organisational changes within the group. The group will exercise better control over its production plants in Austria and the Czech Republic. It will also relinquish its storage facilities in Germany and concentrate its storage activity on the Austrian location. The German subsidiary will be converted into a marketing company. […] (*)The organisational changes at the Austrian location will cost ATS 1 million (ECU 0,1 million).

After GBI's takeover of Ergee, the Ergee and Loana a.s., board members were replaced by experienced reorganisation managers. The GBI also sent Ergee two of its marketing and financial control experts to strengthen the firm's management capacity. The Ergee supervisory board was also replaced by experienced reorganisation managers and textile experts. The changes at management level were necessary in order to achieve cost-cutting measures so as to make production more efficient and shorten product throughput times in the factories in Austria and the Czech Republic. Consultants are also responsible for implementing the restructuring measures.[…] (*).

In order to guarantee long-term profitability, the group must also redefine its market position and improve its brand and product strategy.[…] (*).

The operational restructuring measures are to be financed mainly by a State-guaranteed operating loan of up to ATS 90 million (ECU 6,5 million).

5.6.3. *Restructuring measures associated with investment*

Austria has indicated that the group must invest in order to return to long-term profitability. The group is planning investment of ATS 76 million (ECU 5,5 million) for the period 1997 to 1999, which an average is equivalent to […] (*) of turnover.

The bulk of the investment will be devoted to the expansion and technical modernisation of the central storage facilities at the Austrian location — since the central storage facilities in Germany are to be closed — and the provision of software and hardware or its adaptation to the state of the art.

A smaller proportion of investment will be devoted to the stock of machinery: old, written-off machines are to be replaced so that a high standard of quality can be maintained, new fibres and more ambitious designs can be processed and material costs can be cut substantially. Austria has stated that in recent years the group had reduced its tangible assets.

The following figures show that the value of the machinery newly acquired — either by purchase or by leasing — was lower than the depreciation and leasing costs of the machinery used by the group, although much of it had already been completely written off.

Changes in the value of machinery	1996		1997		1998	
	ATS (million)	ECU (million)	ATS (million)	ECU (million)	ATS (million)	ECU (million)
Acquisition of new machines (purchase and leasing)	24,0	1,7	19,3	1,4	15,6	1,1
Depreciation and leasing costs	– 30,7	– 2,2	– 31,6	– 2,3	– 21,4	– 1,6
New acquisitions as percentage of depreciation and leasing costs	78 %		61 %		73 %	

The investment is to be financed by the new ATS 40 million (ECU 2,9 million) State loan and further bank loans.

The Commission takes the view that the investment is limited to the minimum necessary to permit the restructuring of the group.

5.6.4. *Estimated accounts*

The Commission has examined the estimated balance sheets, profit and loss accounts and cash flow figures up to the year 2000 in order to determine whether the restructuring measures will restore the firm's viability. It finds that the estimated accounts were presented in full and the underlying assumptions were explained in detail.

As a result of the strategy of reducing the product range, shedding labour and trimming production capacity, the group will reduce its output. In the year 2000 this will still be below the l997 figures.

The Commission notes that — despite a considerable decrease in output in 1998 as compared with the previous year (– 6 %) — the operating result will be positive as early as 1998. This improvement will be achieved mainly by a substantial cut in employee expenditure as a proportion of output from 41,7 % in 1997 to 34,0 % in 1998. Because of the continuing high expenditure on interest the result for usual business activity will, however, remain in the negative area. According to the plan the group will make a profit in 1999. […](*). The improvement is based on further cost-cutting measures and a more efficient production process. According to the estimated accounts, in the year 2000, the group will increase its profits to […](*), i.e. […](*) % of output. This figure makes it clear that although the group must continue to manage its costs, it is quite capable of being restored to viability.

Mainly as a result of the waived repayment of the bank loan and the capital injection from the GBI, the group registered positive capital of l5,2 % of the balance-sheet total as early as 1997. With the help of a further capital injection from GBI and retained profits for 1999 and 2000, equity capital will amount to 27,8 % of the balance-sheet total in the year 2000. In the Commission's judgment, the group will be in a healthy financial situation in the year 2000.

Therefore, the Commission feels that the projections prove that the group has the prospect of long-term viability and is in a position to operate on its own merits and without further State support.

The following table summarises the most important figures of the Commission's analysis:

Profit and loss account (Group)	1997		1998		1999		2000	
	ATS (million)	ECU (million)	ATS (million)	ECU (million)	ATS (million)	ECU (million)	ATS (million)	ECU (million)
Output	949,8	68,8	893,7	64,8	[…] (*)	[…] (*)	[…] (*)	[…] (*)
Operating result	– 97,2	– 7,0	6,2	0,4	[…] (*)	[…] (*)	[…] (*)	[…] (*)
Financial result	– 37,4	– 2,7	– 19,7	– 1,4	[…] (*)	[…] (*)	[…] (*)	[…] (*)
Result for usual business activity	– 134,6	– 9,8	– 13,5	– 1,0	[…] (*)	[…] (*)	[…] (*)	[…] (*)
Balance sheet (Group)	1997		1998		1999		2000	
	ATS (million)	ECU (million)	ATS (million)	ECU (million)	ATS (million)	ECU (million)	ATS (million)	ECU (million)
Equity capital	113,0	8,2	117,3	8,5	149,9	10,9	185,0	13,4
Liabilities	550,8	39,9	506,0	36,7	476,2	34,5	440,5	31,9
Balance-sheet total	663,8	48,1	623,3	45,2	624,1	45,2	625,5	45,3

5.7. **Avoidance of undue distortions of competition through the aid**

The Commission has examined whether measures have been taken to offset adverse effects of the restructuring aid on competitors.

5.7.1. *Reduction of production capacity*

The Commission notes that external factors have also contributed to the group's difficulties. According to the results of a survey ([8]), 40 % of consumers wishing to cut back on their expenditure do so by reducing their expenditure on purchases of clothing. In addition, textile demand is declining by 5 % to 7 % annually in Europe. At the same time, imports from the Far East are increasing. These factors resulted in downward pressure on prices, predatory competition and structural overcapacity. The Commission also notes that Austria does not dispute the existence of structural overcapacity on the relevant market.

In accordance with point 3.2.2 (ii) of the guidelines, the restructuring plan must make a contribution, proportionate to the amount of aid received, to the restructuring of the industry serving the relevant market in the Community by irreversibly reducing or closing capacity. A reduction or closure is irreversible when the relevant assets are scrapped, rendered permanently incapable of producing at the previous rate, or permanently converted to another use.

The Commission notes that the firm must replace old written-off machines as part of the restructuring measures, in order to be able to maintain a high standard of quality, to process new fibres and more ambitious designs and to improve its efficiency, so that the group's long-term viability is secured. The replacement of machines does not, however, lead to any increase in total machinery or in capacity. Austria has proved that at group level and taking into account not only its own machines, but those which have been leased, not only is the number of machines diminished, but also potential production capacity, expressed in units per day, is irrevocably reduced. Thus, the group will reduce knitting capacity by 11 %, the toe-closing capacity by 23,9 % and flat-knitting capacity by 51,2 %. These are the relevant capacities for the manufacture of the group's products. The proportion of leased machines in relation to own machines is small.

The following table gives an overview of changes in the group's production capacities.

… (*)

([8]) Carried out by the magazine 'TV Hören und Sehen', March 1995.

The Commission also notes that the reduction of production capacities was accompanied by a 28,9% cut in the workforce, together with a reduction in the group's storage area from 24 000 m^2 to 13 000 m^2 and a 15% reduction in the product range. In addition the Commission again points out that the group will not have increased its output above the 1997 level by the year 2000.

According to the information provided by Austria, Ergee has a market share of 10,9% and 6% in the largest markets, Austria and Germany. Ergee's market shares are not significant in the other EEA countries. Ergee is therefore a comparatively small competitor on the EEA market.

5.7.2. *The competition-distorting effect of State aid measures*

As regards the planned waiver of the existing, unsecured State loan of ATS 42 million (ECU 3,0 million), the Commission takes the view that this contribution is necessary to ensure that the group has sufficient liquid funds. The Commission has also borne in mind that, according to the information provided by Austria, the State would lose the entire amount if Ergee were to go bankrupt. Furthermore, the State is acting in the same way as Ergee's banks, which are also waiving 100% of their unsecured loans. Also, the waiver of the loan is conditional on the number of employees which are employed by Ergee by the year 2000.

As regards the new State loan of ATS 40 million (ECU 2,9 million), the Commission has reached the conclusion that the loan is necessary to guarantee the financing of the necessary investment. The Commission has also taken into account the fact that in accordance with the EFTA Surveillance Authority decision of 11 May 1994, the firm is situated in an assisted area under Article 92(3)(c) of the EC Treaty with a permissible maximum aid intensity of 20% net.

With the help of the guarantee of ATS 90 million (ECU 6,5 million), Ergee can procure enough liquid funds to finance its restructuring measures.

The Commission points out, however, that Ergee does not have to make any payment for this guarantee. Since the group has the prospect of long-term viability and its financial position has already been corrected, it is not necessary to waive the guarantee charge in order to restore the firm's viability. In addition the group's financial expenditure is only some 2% of output. So it can be shown that a free-of-charge guarantee is not justified. Failure to make a charge would reduce the firm's financial burden up to the year 2000 to an unjustified extent. The Commission consequently takes the view that the guarantee constitutes State aid, since Ergee does not have to pay for it on normal market terms, and as such is not compatible with the common market.

5.8. **Aid in proportion to the restructuring costs and benefits**

The Commission has examined whether the aid is limited to the strict minimum needed for the restructuring of the firm.

In the following table the contributions to the group's restructuring are again summarised.

Contributions to restructuring	ATS (million)	ECU (million)	%
Waiving of State loan	42,0	3,0	6,5
New loan	40,0	2,9	6,1
State-guaranteed loans	90,0	6,5	13,8
Total State aid	172,0	12,5	26,4
Contribution by parent company	50,0	3,6	7,7
Retained profits in 1999 and 2000	[…] (*)	[…] (*)	[…] (*)
Sale of capital assets	[…] (*)	[…] (*)	[…] (*)
Total company contribution	63,5	4,6	9,8
Waiving of bank loans	338,0	24,5	51,9
Further necessary bank financing	23,8	1,7	4,2
Total bank contribution	365,6	26,5	56,2
Total of all contributions	651,1	47,2	100,0

The table shows that the restructuring of the firm is mainly financed by the banks (56,2%). The State contribution amounts to 26,4% of restructuring costs, the firm's contribution to 9,8% and that of the parent company, GBI, to 7,7%.

The above percentages show that State aid is in an appropriate proportion to the restructuring costs and to the contributions of the other parties involved. The Commission, however, again points out that provision of the guarantee without charge is not necessary to restore the viability of the firm. This guarantee is therefore not compatible with the common market.

5.9. **The nature of the existing State loan**

Austria has established that the existing loan of ATS 42 million (ECU 3,0 million) was intended for investment of ATS 92,7 million (ECU 6,7 million) in 1994 and 1995. A detailed breakdown of the investment costs was provided.

The existing loan was provided in accordance with Article 35a of the Law to promote the labour market; this Law was entered by the EFTA Surveillance Authority as number 93-359 in the list of existing regional aid schemes. The Commission therefore takes the view that this aid is covered by an existing aid scheme.

The Commission also finds that according to the information provided by Austria, Ergee was not involved in the bankruptcy proceedings of the German parent company and was not in difficulties when the loan was granted.

The Commission has therefore reached the conclusion that this loan is an investment aid.

The Commission finds that Ergee is applying for restructuring aid for the first time.

5.10. **No extension of rescue aid**

On 17 December 1997 the Commission approved rescue aid in the form of a guarantee and a payment on account by GBI in respect of a subsequent increase in equity capital for the period July 1997 to the end of 1997. According to the information provided by Austria, the guarantee was granted only until the end of 1997. However, Ergee still has the funds of ATS 25 million (ECU 1,8 million) made available by the GBI.

In its decision on the rescue aid, the Commission ruled that without a soundly based restructuring plan it could be neither proved nor expected that a normal return on investment could be achieved within an appropriate period of time. The Commission therefore reached the conclusion that the measures of the GBI, at the time when the rescue measures were carried out, may have comprised State aid. But since the Commission has already found that the measures of the GBI since the restructuring phase are based on business principles and do not constitute State aid within the meaning of Article 92 of the EC Treaty, there is in fact no reason to regard the capital injection from GBI as an extension of rescue aid.

6. **CONCLUSIONS**

The Commission concludes that the activities of the GBI are to be equated with those of a private investor and do not constitute State aid within the meaning of Article 92 of the EC Treaty.

The Commission takes the view that Austria has submitted a realistic, coherent and far-ranging restructuring plan and has shown that the group has the potential for long-term viability and is in a position to operate on its own merits without further State support. The reduction in production capacity is considerable and is sufficient to prevent unjustified market distortions. The State aid is in an appropriate proportion to the restructuring costs and the contributions of the other parties involved. The Commission also takes the view that Ergee has applied for restructuring aid for the first time. Lastly, there is in fact no longer any reason to regard the capital injection from GBI as an extension of rescue aid. The Commission does, however, take the view that the provision of the guarantee without charge is not necessary to restore the firm's viability. This would give the group an unjustified advantage.

The Commission therefore approves only the provision of a new State loan of ATS 40 million (ECU 2,9 million) and the waiving of the interest on and repayment of the existing State loan of ATS 42 million (ECU 3,0 million).

The Commission, however, takes the view that State aid in the form of a guarantee of ATS 90 million (ECU 6,5 million) to Ergee free of charge is not compatible with the common market.

The Commission has therefore reached the conclusion that the provision of a new State loan of ATS 40 million (ECU 2,9 million) and the waiving of the interest on and repayment of the existing State loan of ATS 42 million (ECU 3,0 million) contributes to the development of certain economic activities without adversely affecting trading conditions to an extent contrary to the common interest. The Commission therefore decides that the State aid measures can be considered to be compatible with the common market in accordance with the first part of Article 92(3)(c) of the EC Treaty and Article 61(3)(c) of the EEA Agreement. However, the State aid in the form of a guarantee of ATS 90 million (ECU 6,5 million), free of charge, does adversely affect trading conditions to an extent contrary to the common interest and is therefore not compatible with the common market.

The Commission requests Austria to inform it within two months of publication of this decision of the measures it has taken to comply with it.

In accordance with section 3 of the Commission guidelines, the Commission requests Austria to submit detailed annual reports in order to prove that the restructuring plan is being properly implemented,

HAS ADOPTED THIS DECISION:

Article 1

The State aid which Austria wishes to grant the Ergee Textilwerk GmbH, Schrems, in the form of a waiver of interest on and repayment of a State loan of ATS 42 million (ECU 3,0 million) and of a new State loan of ATS 40 million (ECU 2,9 million), is compatible with the common market.

The State aid which Austria wishes to grant the Ergee Textilwerk GmbH, Schrems, in the form of a guarantee of up to ATS 90 million (ECU 6,5 million), free of charge, is not compatible with the common market. This aid must not therefore be granted.

Article 2

Austria shall submit detailed annual reports in order to prove that the restructuring plan is being properly implemented.

Article 3

Austria shall inform the Commission within two months of notification of this Decision of the measures it has taken to comply with it.

Article 4

This Decision is addressed to the Republic of Austria.

Done at Brussels, 22 December 1998.

For the Commission
Karel VAN MIERT
Member of the Commission