STATE AID

GERMANY

(98/C 171/04)

(Text with EEA relevance)

(Articles 92 to 94 of the Treaty establishing the European Community)

Commission notice pursuant to Article 93(2) of the EC Treaty to other Member States and interested parties regarding Germany’s refusal to accept the introduction of the multisectoral framework on regional aid for large investment projects

By the letter reproduced below, the Commission informed the German Government of its decision to open the procedure provided for pursuant to Article 93(2) of the EC Treaty.

‘Over a period of several years, the Commission worked on the formulation of new rules to apply to the control of regional aid to large investment projects. The Commission’s intention to consider the adoption of a horizontal approach to State aid control to such projects was first signalled in its Communication to the Council, the Parliament, the Economic & Social Committee and the Committee of the Regions called “An industrial competitiveness policy for the European Union” (1). Subsequently, the Council Resolution of 23 November 1994 on the strengthening of the competitiveness of Community industry explicitly referred to the need for consideration of a horizontal approach.

Periodic discussions on the provisions of a new framework took place between the Commission and Member States. As a result of these discussions, the Commission tabled revised draft rules entitled “The multisectoral framework on the control of regional aid to large investment projects” on the occasion of the multilateral meeting of Member States’ State aid experts held in Brussels on 15 January 1997. Following that meeting, at which a large majority of Member States responded positively to the Commission’s revised proposal, the Commission consulted Member States on the technical details of the proposal by letter dated 25 February 1997 and had a number of bilateral discussions with Member States, including Germany. The introduction of the multisectoral framework also constituted a specific priority under the Commission’s action plan for the single market which the European Council welcomed at its meeting on 16 and 17 June held in Amsterdam.

By letter dated 5 March 1998, the Commission informed all Member States of its decision adopted on 16 December 1997 to propose the introduction of a new Community State aid framework in the area of regional aid to large investment projects in the form of an appropriate measure within the meaning of Article 93(1) of the EC Treaty. The Commission invited Member States to signify their consent within 20 working days to the introduction of the multisectoral framework in so far as it related to the notification procedure. The letter stated that if any Member State did not signify its agreement within that time period the Commission would, if necessary, immediately open proceedings under Article 93(2) of the EC Treaty with regard to all schemes in operation in the Member State concerned under which aid coming within the scope of the new measures might be provided.

Under the framework Member States are required to notify pursuant to Article 93(3) of the EC Treaty any proposal to award regional investment aid (2) within the scope of an approved scheme (3), where either of the following two criteria are met:

(i) a total project cost of at least ECU 50 million (4), plus a cumulated aid intensity (5) expressed as a percentage of the eligible investment costs of at least 50 % of the regional aid ceiling for large companies in the area concerned plus aid per job created or safeguarded amounting to at least ECU 40 000 (6) or

(ii) at least ECU 50 million total aid.

(1) COM(94) 319 final.

(2) Regional investment aid awarded solely for the creation of jobs as described in the Community regional aid guidelines is not covered by this framework.

(3) The notification requirement also applies of course to proposals to award ad hoc aid.

(4) ECU 15 million in the case of projects carried out in the textile and clothing sector.

(5) Including any co-financing from the Structural Funds.

(6) ECU 30 000 in the case of projects carried out in the textile and clothing sector.
14 Member States have communicated their written agreement with regard to the introduction of the multi-sectoral framework. By letter dated 31 March 1998, the Government informed the Commission that it did not agree with its introduction. The arguments put forward in that letter are detailed and evaluated below.

1. In general terms, the Government states that it still supports the Commission's objective of replacing sector-specific rules by a horizontal approach. It has a number of serious objections however to the formulation of the multi-sectoral framework which it previously expounded to the Commission but which the latter has not taken up.

The Commission notes that it made considerable efforts during the course of 1997 to take account of Germany's reservations on the draft text of the framework, despite the fact that Germany failed to reply in writing to the Commission's letter dated 25 February 1997 in which all Member States were invited to comment on specific elements of the text. Several subsequent bilateral discussions between the Commission and the authorities took place as a result of which the Commission made certain modifications to the draft text. These bilateral exchanges included a meeting held on 15 July 1997, following which there were exchanges of correspondence (Commission letters dated 28 July 1997 and 15 December 1997 and a letter from the authorities to the Commission dated 24 November 1997).

During these bilateral and multilateral discussions, and in recognition of the compromises that most if not all Member States had to make in order to arrive at a consensus, the Commission made clear that the multi-sectoral framework would be introduced on a trial basis only for three years and that before the end of that period the Commission would carry out a thorough review of the utility and scope of the framework, which would, inter alia, consider the question of whether it should be renewed, revised or abolished.

2. The authorities state that the three assessment factors and the calculation formula linked to them could lead in individual cases to the Commission decision not being predictable and investors not having the necessary legal certainty.

The Commission therefore considers that the degree of predictability and legal certainty offered by the multi-sectoral framework is sufficient. It should be borne in mind at the same time that the margin of appreciation available to the Commission for the application of Article 93(3) of the EC Treaty has been confirmed by the Court of Justice (†).

3. The authorities state that the three assessment factors proposed by the Commission in examining individual cases would lead to Commission interference in assessing the merits of supporting a particular aid proposal, especially since the Commission reserves the right to request details concerning the viability of a project. The authorities wonder whether this type of assessment is necessary for State aid control and whether it respects the division of competences between the European Commission and Member States.

The Commission reiterates, as stated in paragraph 1.5 of the framework, that it has no intention of

(†) See case C-225/91 Matra v. Commission for example.
seeking unnecessarily to interfere with the discretion of Member States in the field of regional policy. Nor does it seek to weaken the application of Article 92(3)(a) and (c) of the EC Treaty, which aims to encourage companies to invest in disadvantaged areas, despite the structural handicaps that they face there. On the contrary, the intention is strictly to limit the scope of the new rules to those large-scale projects, often capital intensive in nature, which could have a serious impact on unaided competitors located elsewhere in the EEA, and to examine more critically the planned levels of aid for those projects which do not have a significant impact on the region concerned in terms of employment, directly or indirectly, which is an important objective of regional policy. By helping to restore a balance with regard to aid which supports the creation of jobs, the framework is fully consistent with the conclusions of the Luxembourg Summit on Jobs held on 20 and 21 November 1997. Member States will continue to be able to decide freely on the aid intensity in the vast majority of cases, within the terms of the approved regional aid schemes. The Commission considers that it is vital for the effective functioning of the single market to maintain strict control on State aid to such projects. The fifth State aid survey for the years 1992 to 1994 (\(^\text{(*)}\)), which showed no diminution in the overall levels of aid, underlined the necessity for concrete action.

As regards the assessment of the potential viability of a project, the Commission stresses that it has no intention of assuming the responsibility of investigating this aspect. On the contrary, the text of the framework explicitly states in paragraph 3.1 that "the question of the viability of an individual project will be for Member States themselves to determine". While the Commission would not usually expect to need to request data from Member States on this point, it nevertheless considers that there may be certain circumstances in which such information, which should be readily available, could facilitate its analysis of a case.

4. The authorities argue that as a result of the possible reduction in the permissible aid intensity by up to 85% of the regional aid ceiling there would no longer be a sufficient incentive to attract firms to invest in assisted regions and that aid would simply be given to those firms which would have invested in them irrespective of the possibility of aid. The framework could therefore lead not simply to a reduction in aid but actually prevent the granting of incentives to large projects in structurally weak regions. The authorities state that in view of the support which such regions deserve, such an approach would not be justified, since a minimum investment incentive is indispensable.

The Commission notes firstly that the authorities do not state the level at which the minimum incentive level should be set. The Commission stresses that the framework is not concerned with banning aid to the projects coming within the scope of control of the framework but avoiding excessive levels of aid in a small minority of regional aid cases. It should be recalled that the application of the framework does not a priori mean the reduction in the permissible aid intensity below the regional aid ceiling in all, or even in most cases. Even in those cases where the Commission may foresee a reduction in the proposed aid intensity below the regional aid ceiling as a result of the application of either or both of the first two assessment factors, namely the capital-labour ratio factor and the competition factor, a "bonus" would be possible under the third regional impact factor, the effect of which would be at least, in part, to restore the cuts made under the first two factors. Finally, the hypothetical example quoted by the authorities of a cut of 85% in the permissible aid intensity is an extreme one. It would involve a project in which the amount of proposed capital invested per job created would be at least ECU 1 million, in which the aided project would result in a capacity expansion in a sector facing serious structural overcapacity and/or an absolute decline in demand and one which created few indirect jobs in the assisted regions concerned in relation to the direct jobs created. Even in such circumstances, the permissible amount of aid in absolute terms would probably be substantial given the size of the projects covered by the framework.

5. The authorities state that the application of the capital-labour factor could lead to a reduction of up to 60% of the original amount and thereby discriminate against capital-intensive investments in favour of labour-intensive investments and contribute to the preservation of labour-intensive economic structures which are not sufficiently competitive. The result would be to hamper the competitiveness of European enterprises.

\(^\text{(*)}\) COM(97) 170 final, 16.4.1997.
The Commission rejects this argument. Since regional aid is usually granted in the form of capital subsidies, there is an apparent tendency for such aid measures to encourage capital-intensive projects to locate in assisted areas. While this is a positive development, such a policy does not necessarily contribute to the creation of significant job creation in less favoured regions which is an important objective of regional policy. The application of the capital-labour factor will only affect those projects, on the basis of a sliding scale, where the level of proposed aid per job created or safeguarded is very high (above ECU 200,000). As for the hypothetical case cited by the authorities, a reduction of 40% below the regional ceiling would only affect projects where the aid per job created or safeguarded is at least ECU 1 million. Moreover, as mentioned above, any reduction made under the capital-labour ratio factor could be mitigated or offset by the application of the regional impact factor, i.e. where the forecast indirect jobs created would be significant in relation to direct jobs. The framework leaves to the entrepreneur all decisions concerning the appropriate structure and staffing of his investment. It does not seek to preserve insufficiently competitive operations which the authorities consider, without evidence, to be the case.

6. The authorities maintain that the formulation of the competition assessment factor does not take account of the problem of the "relevant market" and that it does not differentiate between the general market situation and the special development of particular market segments (market niches). This gives rise to doubts about the required predictability and the material correctness of the Commission decision. Even investment projects, which contain innovative elements and would secure the longer-term competitiveness of the enterprise and thereby the location (Standort) of Europe, would have to reckon with a large reduction in the aid intensity in case of doubts about a capacity expansion or a declining market.

The Commission cannot accept these arguments. Firstly, the prime consideration in the competition assessment factor is not the "relevant market" but the relevant sector or sub-sector. This is in line with the constant Commission practice of focusing in State aid cases (as distinct from other areas of competition policy) on the recipient of the aid and on the industry in which those firms operate rather than the identification of competitive constraints faced by the products of the aid recipient. This practice is confirmed in the Commission notice on the definition of the relevant market for the purposes of Community competition law (footnote 1). As regards the sector to be taken into consideration, the framework makes clear (in the section on definitions) that this will be established at the lowest available segmentation of the NACE classification.

The framework states in the section on definitions that the relevant product market for determining market share comprises the products envisaged by the investment project and, where appropriate, their substitutes considered by the consumer or by the producer. The relevant geographic market usually comprises the EEA or, alternatively, any significant part of it.

As regards the assessment of projects undertaken by companies possessing more than 40% market share for the producer(s) concerned, the framework expressly states in paragraph 3.6 that there could be exceptions to the general rule of imposing a reduction in the permissible aid intensity, "for example where the company creates, through genuine innovation, a new product market".

As to whether or not a declining market exists, the framework also states in the section on definitions that this will be assessed on the basis of the average annual growth rate of apparent consumption of the product(s) over the previous five years in relation to the annual average of the EEA manufacturing industry as a whole. A declining market would not be deemed to exist where there was a strong upward trend in the relative growth rate of demand for the product(s).

7. The authorities assert that the application of the regional impact factor may conflict with the operation of free competition in the Community, since an investor will seek suppliers/purchasers where it makes commercial sense for it to do so. If the investing firm were to make its suppliers/purchasers dependent on

the extent of the aid available, this would lead to an overall misallocation of resources. The authorities also have doubts about how a company can state \textit{ex-ante} what suppliers/customers it will deal with and the number of jobs a project will create. An investment project is not a static operation but has to react to changing market circumstances. Finally, the promotion of regional development by means of encouraging export-oriented companies to locate in an assisted region by means of aid measures, would be counteracted by this assessment factor.

In the Commission’s view job creation can be used as an indicator of a project’s contribution to the development of a region. As mentioned above, this approach is fully consistent with the conclusions of the Luxembourg Summit on Jobs held on 20 and 21 November 1997 which stated that “the European Council believes that it is important to focus on aid arrangements which favour economic efficiency and employment without causing distortions of competition”. It accepts that it will not necessarily be possible to state \textit{ex-ante} the precise effects of a project in terms of direct and indirect job creation. It is mainly for this reason that the framework contains specific \textit{ex-post} monitoring provisions in order to assess implementation of the project against the estimates made at the time of notification of the project.

The Commission agrees that companies will of course seek suppliers/purchasers where it makes commercial sense for them to do so. The framework is not intended to nor does the Commission believe it will influence companies in this regard. It should also be stressed that no reductions in aid will be made under this assessment factor (unlike potentially under the other two factors) because its minimum value is equal to 1. This prevents the factor from having a counteracting effect on policies encouraging export-oriented companies to locate in an assisted region. On the other hand, the Commission believes it is reasonable to offer a bonus to those projects which generate a relatively high number of indirect jobs in the assisted regions concerned.

On the question of the bureaucratic burden involved, the Commission reiterates that this framework is intended, through setting the notification thresholds at a high level, only to capture a small number of projects each year which, by virtue of their size, pose particular concerns from the point of view of distortion of competition. This is fully in line with the Commission’s policy, shared by Member States, of concentrating resources on the most important cases. In order to limit the scope for misunderstanding about the information required by the Commission and speed up the decision-making process, the framework contains a detailed standard notification form as an annex.

Conclusion

The authorities conclude in their letter dated 31 March 1998 that they cannot accept the new framework.

The notification requirement in the multisectoral framework is an appropriate measure in the sense of Article 93(1) of the EC Treaty. In the light of the reasons detailed above, the Commission considers that
there is no justification for the Commission to modify the appropriate measure proposed to Member States by letter dated 5 March 1998.

14 Member States have accepted unconditionally the notification requirement contained in the multi-sectoral framework. Thus Germany is the only Member State not to have approved it. Consequently, in order to apply the framework and ensure an equality of treatment in the whole of the Community, the Commission needs to open the Article 93(2) procedure with regard to all the aid schemes in Germany under which aid could be awarded covered by the notification requirement of the multi-sectoral framework on regional aid for large investment projects. These include all approved aid schemes under which aid can be awarded at a level which meets either of the two notification thresholds plus any aid scheme under which aid can be cumulated with aid from another aid scheme to reach the same level: notably the principle German regional aid scheme, the programme for the improvement of regional economic structures (26. Rahmenplan der Gemeinschaftsaufgabe Verbesserung der regionalen Wirtschaftsstruktur (\(\text{\textsuperscript{26}}\)) and the fiscal aid scheme the Investitionszulagenengesetz (\(\text{\textsuperscript{15}}\)).

In the context of this procedure, the Commission hereby gives the German Government the opportunity to present, within two weeks of receipt of this letter, any observations and supplementary information required for the Commission assessment.

The Commission hereby informs the German Government that it will publish this letter as a notice in the *Official Journal of the European Communities*, giving other Member States and interested parties notice to submit comments, and in the EEA supplement to the *Official Journal*, giving interested parties in the EFTA States similar notice to submit comments. *

The Commission invites the Member States and other interested parties to submit their comments on the aid measures in question within a period of two weeks following the date of publication, to the following address:

European Commission,  
Directorate-General for Competition (DG IV),  
State Aid Directorate,  
Rue de la Loi/Wetstraat 200,  
B-1049 Brussels,  
Fax (32-2) 296 95 79.

These comments will be communicated to the German Government.

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\(\text{\textsuperscript{26}}\) Case N 123/97.  
\(\text{\textsuperscript{15}}\) Case N 494/A/95.