

II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 20 May 1998

concerning State aid for the processing and marketing of German agricultural products which might be granted on the basis of existing regional aid schemes

(notified under document number C(1998) 1712)

(Only the German text is authentic)

(1999/183/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 given the parties concerned the opportunity to submit their comments, in accordance with the above-mentioned Article,

Whereas:

I. PROCEDURE

(1) By letter SG(95) D/13086 of 20 October 1995, the Commission proposed to the Member States, pursuant to Article 93(1) of the Treaty, guidelines and appropriate measures for State aid in connection with investments in the processing and marketing of agricultural products⁽¹⁾ (hereinafter referred to as the 'guidelines and appropriate measures').

(2) By the same letter, the Commission informed the German authorities (and the other Member States) that it would authorize no further aid measure for investment in the processing and marketing of agricultural products notified to it under Article 93(3) of the Treaty which did not comply with these guidelines and appropriate measures and

which applied or would continue to apply after 1 January 1996.

(3) The Commission also requested the German authorities (and the other Member States) pursuant to Article 93(1) to confirm within two months of the date of the said letter that they would comply no later than 1 January 1996 with the guidelines and appropriate measures in question by amending their existing aids, where such aids did not comply with the guidelines and appropriate measures. The Commission indicated that if it did not receive such confirmation, it would reserve the right to commence the procedure under Article 93(2) of the Treaty.

(4) In reply to the Commission letter of 20 October 1995, the German authorities, by letters of 11 January and 14 February 1996:

(a) confirmed that with regard to sectoral aid, they would comply with the appropriate measures in question as from 1 January 1996, amending existing aid schemes if necessary;

(b) stated that with regard to regional aid, more flexibility was needed on the appropriate measures, given that conditions and agricultural structures in the Community varied from one region to another.

⁽¹⁾ OJ C 29, 2. 2. 1996, p. 4.

- (5) By letter dated 1 July 1996 (SG(96) D/6026) the Commission informed Germany of its decision of 12 June 1996 to initiate the procedure provided for in Article 93(2) of the Treaty in respect of State aid for the processing and marketing of agricultural products which might be granted in Germany on the basis of existing regional aid schemes ⁽¹⁾.
- (6) In the course of the procedure, the Commission examined the arguments submitted by Germany to justify its refusal to agree to the application to regional aid schemes of the guidelines proposed by the Commission in its letter of 20 October 1995. After examining those comments, the Commission concluded at that stage that there were no grounds for accepting Germany's refusal.
- (7) By the abovementioned letter, the Commission gave the German Government notice to submit its comments within one month of the date of the letter. In accordance with Article 93(2), the other Member States and interested parties were informed by publication of the letter in the *Official Journal of the European Communities* and were requested to submit their comments.
- (8) The German Government communicated its comments to the Commission under the procedure by letter dated 31 July 1996. In that letter the German Government also referred to further comments which had been transmitted to the Commission by letter of 24 May 1996. For technical reasons, these latter comments had not been taken into consideration by the Commission in its decision of 12 June 1996 to open the procedure under Article 93(2) of the Treaty.
- (9) No comments were submitted by the other Member States or from interested parties.

II. GERMANY'S OBSERVATIONS

- (10) In their communications of 24 May 1996 and 31 July 1996, the German Government has raised two series of objections to the application of the guidelines and appropriate measures to regional aid schemes. The first series of objections concerns legal considerations arising from the manner in which the guidelines and appropriate measures were adopted. The second is based on the argument

that the application of the guidelines and appropriate measures 'would entail a restriction on State regional aid which would appreciably impair the development opportunities for rural areas'.

1. Observations of a legal nature

- (11) In its letter of 24 May 1996, the German Government expresses the opinion that existing Community rules, read in conjunction with the various communications of the Commission, and the letter approving the 23rd Federal framework plan for the improvement of regional economic structures (SG(94) D/11038 of 1 August 1994), entail neither an indirect nor a direct restriction on possible State aid measures in favour of the processing or marketing of agricultural products in connection with eligible investment projects under the joint scheme 'Improving the regional economic structure'.
- (12) According to the German authorities, Council Regulation (EEC) No 866/90 of 29 March 1990 on improving the processing and marketing conditions for agricultural products ⁽²⁾ cannot be used to justify a restriction on State aid measures on processing or marketing Annex II products under the joint scheme. That Regulation merely stipulates how and under what conditions the Guidance Section of the European Agricultural Guidance and Guarantee Fund can contribute to measures for improving the processing and marketing conditions for agricultural products. The Council states in the preamble to the Regulation that 'the types of investments eligible for a contribution from the EAGGF Guidance Section (hereinafter referred to as the "Fund") should be defined, taking account of the current situation both on the agricultural markets and in the agriculture and food sector, as well as the prospects for developing outlets for agricultural products'. Thus Germany contends that the Regulation seeks no more than, first, to guarantee consistency between Community intervention and the common agricultural policy and, secondly, to coordinate the interventions of the different Structural Funds between themselves, on the one hand, and, on the other, to balance those interventions with those of the European Investment Bank and other existing financial instruments.
- (13) According to the German authorities, it follows that the power given to the Commission by the Council by way of Article 8(3) of the above Regulation only permits the Commission to determine the selection criteria for designating those investments in which the Community Fund may participate. The Commission made use of that power in

⁽¹⁾ OJ C 36, 5. 2. 1997, p. 13.

⁽²⁾ OJ L 91, 6. 4. 1990, p. 1; this Regulation has subsequently been replaced by Council Regulation (EC) No 951/97 of 20 May 1997 on improving the processing and marketing conditions for agricultural products; OJ L 142, 2. 6. 1997, p. 22.

Decision 94/173/EC of 22 March 1994 on the selection criteria to be adopted for investments for improving the processing and marketing conditions for agricultural and forestry products and repealing Decision 90/342/EEC⁽¹⁾. That Decision seems to have no restrictive effect on national aid schemes and in favour of financing from the Fund.

(14) The German authorities also take the view that the 1994 Commission Communication to the Member States regarding State aid for investments in the processing and marketing of agricultural products⁽²⁾ does not bar the granting of State aid to sectors which are excluded from Community co-financing by virtue of the abovementioned decisions. Paragraph 1 of that Communication states that the Commission generally applies sectoral restrictions governing the part-financing by the Community of investments at processing and marketing level 'by analogy [...] when assessing State aid for such investments'. The Communication is not an 'appropriate measure' within the meaning of the second sentence of Article 93(1) of the Treaty because extension of the restrictive effect to State aid by analogy was not carried out using the procedure laid down by the second sentence of Article 93(1) of the Treaty (proposal for an appropriate measure). In terms of the legislative forms laid down in Article 189 of the Treaty, that Communication is neither a regulation, a directive nor a decision; it can only be regarded as a recommendation, and as such is not binding.

(15) Moreover, the German Government argues that the analogy drawn in the Communication runs up against substantial legal objections with regard to the basic Regulation (EEC) No 866/90. It is the wish of the legislature, as expressed in Article 16(5) of that Regulation, (now Article 16(5) of Regulation (EC) No 951/97) that national aid measures should be expressly permitted on condition that they comply with Articles 92 and 94 of the Treaty. The Commission Communication places a sectoral restriction on the scope of Article 92(3) of the Treaty, against the wishes of the legislature. Furthermore, according to Article 1(1) of Regulation (EEC) No 866/90 the measures laid down in the Regulation should serve the implementation of regional policy objectives. The Federal German Government therefore claims that the Commun-

ication cannot result in a legally binding restriction on the possibility of State aid measures.

(16) The German Government believes that no preclusion of State aid measures for the processing and marketing of Annex II products may be inferred from the Commission letter approving the 23rd framework plan for the joint scheme (SG(94) D/11038 of 1 August 1994). The end of that letter contains a passage whereby the Commission draws the Federal Government's attention to the need to take account of Community law provisions and conditions and the resultant obligations when applying the intended measures, particularly with regard to the prior notification of individual cases which apply (a) to the cumulation of aid under different Objectives, (b) in certain sectors of industry (including the provisions of the ECSC Treaty), agriculture and fisheries, and (c) for agricultural undertakings operating on an industrial scale.

(17) The German Government stresses that the approval letter requires that Community law shall contain an obligation not to grant unrestricted State aid in certain sectors. However, in its opinion, neither Regulation (EEC) No 866/90 nor the establishment of the selection criteria by the Commission pursuant to Article 8(3) of that Regulation, nor the content of the 1994 Commission Communication entail an obligation not to apply State aid measures to the processing and marketing of agricultural products.

(18) Moreover, the German Government maintains that no restrictive effect may be found in the rules adopted by the national legislators themselves under the joint scheme. They concede that Part 1, point 10.3 of the 23rd plan refers to the Commission's determination of the selection criteria for investments in improving the processing and marketing conditions for agricultural and forestry products. However, they emphasize that that does not mean that the Commission's position at that time had been communicated to the German authorities or that it had been accepted in some kind of voluntarily binding form. The German authorities point out that the determination of the selection criteria by the Commission is only referred to in Part 1 of the framework plan. That Part, however, contains only non-binding general references to the structure and objectives of the plan and to various secondary aspects, including the monitoring of aid by the Commission. The

⁽¹⁾ OJ L 79, 23. 3. 1994, p. 29.

⁽²⁾ OJ C 189, 12. 7. 1994, p. 5.

Federal Government also stresses that the listing of various regulations, communications and Community guidelines does not automatically signify that aid is expressly excluded in those sectors. Rather, Part 2 states that the following rules are to be taken into account in decisions on aid applications. The list therefore only serves to alert the approval authorities responsible for implementing the joint scheme in the Länder to the various rules that might play a role in a decision on a specific aid application. The German authorities therefore hold the view that mentioning the determination of selection criteria represents only a non-binding reference to coordination with the Commission's agricultural policy.

2. Observations concerning the effect of the guidelines on regional aid schemes

- (19) In their Communications of 24 May 1996 and 31 July 1996, the German Government has, in substance, maintained the same position as that previously expressed in their letters of 11 January 1996 and 14 February 1996. According to Germany, the Community provisions may not result in excessive restrictions on national aids for regions, which might jeopardise the chances of developing the rural environment. 'In the rural environment, it is the industrial sectors handling agricultural products which are best suited for the redeployment of farmers who have had to quit their profession in the course of structural change. If large areas of the agricultural processing and marketing sector were to be systematically excluded from national aid, the scope of regional measures, particularly in connection with the joint scheme for improving regional economic structures, could be reduced in rural areas to an unacceptable level'.
- (20) In its letter of 24 May 1996, the German Government argues that employment opportunities in rural areas for farmers forced to give up their profession because of structural conversion can best be created in agriculture-related industrial sectors. The current Commission proposal to adopt Community guidelines regarding the processing and marketing of Annex II products is considered to result in an unjustifiable reduction in regional aid to rural areas. Points 3(a)(iii) and (iv) of the guidelines and appropriate measures contain very wide-ranging definitions of processing and marketing. Processing, for instance, covers any actual operation affecting an agricultural product falling within Annex II of the Treaty and marketing covers, for example, the packaging of
- shipping devices. Decision 94/173/EC and its implementation through the guidelines provides broad categories of exclusion. In the cereals and rice sectors, all investments relating to cereal-starch plants, mills, maltings and semolina mills and to the secondary products of that industry are excluded, apart from products for innovative non-food applications. The list of exclusions also lays down that in some Objective 1 regions aid can only be granted if there is a demonstrable lack of capacity. The questions as to (a) when such a lack of capacity is to be assumed, and (b) what evidence for it is required are not answered either in the Community proposal or in the above Commission Decision. The positions on the proposed Community measure received to date from the Länder responsible for implementing the joint scheme all ask the Government to reject the proposal for an appropriate measure regarding regional aid. All the positions state that the grant of regional aid for the processing and marketing of agricultural products by commercial companies (industry, services) is an indispensable tool for assisting rural regions with inadequate structures.
- (21) In their letter of 31 July 1996, the German Government contests the premise that the introduction of Community guidelines would improve consistency with the common organisation of agricultural markets. It argues that the Community guidelines do not cover the production of agricultural products but rather the industrial processing and commercial marketing of existing Annex II products. Germany therefore contends that the way in which price and quantity are regulated under the common market organisation cannot be influenced by restrictions on industrial processing or marketing. Agricultural surpluses are not encouraged by the maintenance of competitive processing capacities but by production incentives under the agricultural market organisations in question. Employment policy considerations provide a legitimate interest in a competitive industry processing agricultural products in less-favoured rural areas, irrespective of whether or not the primary agricultural products used are produced by the domestic agricultural sector or are imported.
- (22) In addition, the German authorities refer to the text of the Community Support Framework 1994-1999 on Objective 1 Structural Fund assistance, emphasizing the following:
- 'A competitive processing industry is essential to give an economic boost to the agricultural sector and the countryside as a whole. The EAGGF

Guidance Section will therefore have a share in investment aid benefiting companies in the processing and marketing sector on the basis of Regulations (EEC) Nos 866/90 and 867/90.' (Point 198, p. 2 and p. 3)

'With respect to the processing and marketing of animal products the Fund will complement the value-added chains above all. The aim of this strategy is to produce high value, high-quality products. The Commission believes this is the only way to safeguard the agricultural sector in eastern Germany in the long term.' (Point 199, *in fine*).

(23) In the light of those statements highlighting the need for Community-scale financial participation in competitive industrial companies employed in the processing and marketing of agricultural products, the German Government cannot understand why national measures promoting competitive processing industries have been prohibited completely in some cases. Moreover, current German legislation prohibits the granting of aid to companies which are not competitive in the long term.

(24) At the request of the Commission, the German Government provided a number of examples to demonstrate the specific impact of the appropriate measures in the sector of the processing and marketing of agricultural products:

— in Schleswig-Holstein, two projects will safeguard a total of almost 500 permanent jobs in the Bockling and Großenbrode rural areas,

— in Saxony an aid scheme is about to be implemented in the processing sector involving around 40 rural jobs. Since 1990 around 300 permanent jobs have been created or safeguarded through 20 rural projects,

— in Lower Saxony more than DEM 560 million has been invested in the processing and marketing of agricultural products since 1993, with financial aid accounting for around DEM 62 million. Lower Saxony therefore has a share of around 12 % of the total volume of investment in receipt of financial aid. These measures have created more than 1 240 new permanent jobs and safeguarded 606 jobs,

— in North Rhine-Westphalia, 86 investment projects are set to create 2 474 new jobs and safeguard 599 permanent jobs. An additional three projects are currently in receipt of aid; these are set to create 168 new jobs,

— in Rhineland-Palatinate, since 1994 alone around 200 permanent jobs have been created through regional support for a total of seven companies,

— in Saxony-Anhalt, 28 applications for assistance under the Joint Scheme involving investment of around DEM 220 million plan to safeguard and create around 1 150 jobs in total. There is a clear shift in investment away from large-scale concerns towards small and medium-sized enterprises, which generally concentrate on investments in processing products typical of or specific to the region,

— in Mecklenburg-Western Pomerania the food industry is the main source of employment, accounting for 21,8 % of all those employed in processing and 23,8 % of processing enterprises. The continuing importance of the food processing industry in Mecklenburg-Western Pomerania in the future can be seen from the number of applications for funding under the Joint Scheme. In July 1996, 55 applications were pending, involving total investment of DEM 354 million for creating or safeguarding a total of around 2 400 permanent jobs. Again, it is particularly important from the regional policy viewpoint that much of the planned investment is intended for severely disadvantaged rural areas, with a focus on creating employment opportunities for women. Investment could therefore also help resolve qualitative structural deficits.

(25) In conclusion, the German Government emphasises that the possibility of providing purely national aid to support a competitive processing industry and a competitive marketing sector must be retained both for legal reasons and in order to support regional policy.

III. ASSESSMENT OF THE OBSERVATIONS AND COMMENTS RECEIVED

1. General

(26) Article 93(1) of the EC Treaty provides that the Commission shall, in cooperation with Member States, keep under constant review all systems of aid existing in those States. It shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the common market.

(27) By letter SG(95) D/13086 of 20 October 1995, the Commission proposed to Germany, pursuant to Article 93(1) of the Treaty, guidelines and appropriate measures for State aid in connection with investments in the processing and marketing of agricultural products. In the same letter, the Commission informed the German authorities that it would authorise no new aid scheme which did not comply with these guidelines and appropriate measures which applied or would continue to apply after 1 January 1996. It also requested Germany and the other Member States to confirm, within two months of the date of the said letter, that they would comply with the guidelines and appropriate measures by amending their existing aid schemes.

(28) At no stage during the procedure have the German authorities contested the right of the Commission to make such a proposal. Indeed, they have indicated to the Commission that they are prepared to accept the proposal for sectoral aid schemes while insisting on the need for greater flexibility in respect of regional aid schemes. It is the refusal of the German authorities to accept the application of the guidelines and appropriate measures in respect of State aid granted in the framework of regional aid schemes, and the refusal of the German authorities to amend existing regional aid schemes to bring them into line with the guidelines and appropriate measures, which are the subject of this procedure.

2. Examination of the legal objections put forward by Germany

(29) The German authorities argue that the provisions of Council Regulation (EEC) No 866/90 cannot be used to justify restrictions on State aid measures, since that Regulation is solely concerned with whether, and under what conditions, the EAGGF can contribute to measures for improving the processing and marketing of agricultural products. Moreover, Article 16(5) of the Regulation expressly permits the granting of State aid which are subject to conditions or rules which differ from those provided for in the Regulation, or where the amounts of aid exceed the ceilings specified therein, on condition that these measures comply with Articles 92, 93 and 94 of the Treaty. There-

fore, while Commission Decision 90/342/EEC of 7 June 1990 on the selection criteria to be adopted for investments for improving the processing and marketing conditions for agricultural and forestry products ⁽¹⁾, and subsequently Decision 94/173/EC, may restrict the range of investments which are eligible for support from the Community's structural funds, they have no effect on the range of investments which are eligible for regional State aid funded by the Member States alone.

(30) The Commission cannot accept this argument. It is correct that Article 16(5) of Regulation (EEC) No 866/90 permits the granting of State aid which are subject to conditions or rules which differ from those provided for in the Regulation, or where the amounts of aid exceed the ceilings specified therein. However, this possibility is expressly stated to be subject to the condition that the aids comply with Articles 92, 93 and 94 of the Treaty. Article 42 of the Treaty, which constitutes one of the legal bases of Regulation (EEC) No 866/90, provides that the provisions of the Chapter on competition shall apply to production of and trade in agricultural products only to the extent determined by the Council. The Council therefore has the option of limiting the application of State aid rules in the sector of the processing and marketing of agricultural products ⁽²⁾. However, instead of availing itself of that option, the Council has expressly stated in Article 16(5) of the Regulation that Articles 92, 93 and 94 of the Treaty shall apply to such measures. It must therefore be concluded that Regulation (EEC) No 866/90 does not contain any express or implied restriction on the discretionary powers which are conferred on the Commission by Article 92(3) of the Treaty to determine whether aid may be considered compatible with the common market. The question which remains outstanding therefore, is whether the Commission is entitled, when considering the compatibility of State aid for the processing and marketing of agricultural products with Article 92 of the Treaty, granted under regional development schemes, to apply by analogy the same sectoral limitations which it uses for Community funded measures in accordance with Regulation (EEC) No 866/90. This question is considered in recitals 35 to 56 below.

(31) Secondly, the German authorities argue that the 1994 Commission communication to the Member States regarding State aid for investments in the processing and marketing of agricultural products

⁽¹⁾ OJ L 163, 29. 6. 1990, p. 71.

⁽²⁾ See, in particular, Regulation 26 of 4 April 1962 on the production and marketing of agricultural products (OJ 30, 20. 4. 1962, p. 993/62).

does not rule out the granting of State aid to sectors which are excluded from Community co-financing, since that Communication did not observe the forms laid down in Article 93(1) of the Treaty.

(32) The Commission considers that this argument is not relevant for the purposes of the present decision, which is exclusively concerned with the refusal of Germany to implement the proposal for appropriate measures which was addressed to that country by letter SG(95) D/13086 of 20 October 1995. At no stage in the procedure has Germany suggested that the Commission failed to respect the procedures laid down in the Treaty when making that proposal.

(33) Thirdly, the German Government argues that no exclusion of the possibility of State aid measures for the processing and marketing of Annex II products is apparent from the Commission letter approving the 23rd framework plan for the joint scheme (SG(94) D/11038 of 1 August 1994). In particular, Germany argues that the passage at the end of that letter whereby the Commission draws the German Government's attention to the need to take account of the provisions of Community law relating to certain sectors of industry (including agriculture) and industrially organised agribusinesses in implementing the framework plan has no legal effect, since, at the relevant time, Community law did not contain an obligation not to apply State aid measures to the processing and marketing of agricultural products.

(34) However, the Commission would point out that this argument cannot be put forward for the purposes of this Decision, since the matters referred to took place before the date of the Commission's proposal for appropriate measures. Nevertheless, the Commission reserves the right to open the procedure provided for in Article 93(2) of the Treaty should it appear that aids have been paid out for the processing and marketing of Annex II products in contravention of Community law within the framework of the 23rd framework plan for the joint scheme, or within the framework of any other regional aid scheme in Germany.

3. The development of Commission policy on State aid for investments in the processing and marketing of agricultural products

(35) In the guidelines and appropriate measures for State aid in connection with investments in the processing and marketing of agricultural products, the Commission explained the philosophy underlying its policy to State aid in this sector in the following terms.

'To the extent that State aid granted in connection with investments in the processing and marketing of agricultural products distorts or threatens to distort competition by favouring certain undertakings or certain types of production, it is, in so far as it affects trade between the Member States, incompatible with the common market under Article 92(1) of the EC Treaty.

While State aid in connection with investments in the processing and marketing of agricultural products may of course benefit from one of the exceptions provided for in Article 92(3), it is established Commission policy to ensure that in certain specific sectors of agricultural production, State aid may not enjoy one of these exceptions and that in other sectors it may enjoy such an exception only where certain strict conditions are met.

These sectoral restrictions, introduced following analysis of representative markets at Community level, are applied by the Commission in assessing whether any public aid in connection with investment in this field, whether at Community or national level, is in the Community interest. In this way, the Commission seeks to ensure consistency between the common agricultural policy and State aid policy so that investment is not encouraged where, for structural reasons, it is contrary to the Community interest.

This basic philosophy remains valid and is thus applied in the context of these guidelines and appropriate measures.'

(36) The new guidelines and appropriate measures which were communicated to the Member States by the Commission's letter of 20 October 1995 do not constitute a major change from previous Commission policy, but rather the adjustment of an existing policy to changed market conditions. In fact, it has been established Commission policy for many years to exclude or restrict State aid for investments for the processing and marketing of agricultural products in sectors which are suffering from over-capacity. The reason for this policy is

that State aid for investments in such sectors are likely to have an unfavourable impact on economic operators who are not in receipt of such aids. Moreover such aids are unlikely to bring about a lasting structural improvement to the sector concerned, but are likely to have a deleterious effect on trade, and are likely to cancel each other out by counteracting the efforts made by both national and Community authorities to remedy the structural difficulties in the sectors concerned. Thus, these aids will affect trading conditions to an extent which is contrary to the common interest. Such aids therefore cannot be considered to be compatible with the common market either within the meaning of Article 92(3)(a) or within the meaning of Article 92(3)(c).

In this context, the Commission also refers to the judgment of the Court of Justice of 14 January 1997 in Case C-169/95 (Spain v. Commission) ⁽¹⁾. After reviewing the difference in wording between Article 92(3)(a) and Article 92(3)(c), the Court went on to conclude that 'that difference in wording cannot lead to the conclusion that the Commission should take no account of the Community interest when applying Article 92(3)(a), and that it must confine itself to verifying the regional specificity of the measures involved, without assessing their impact on the relevant market or markets in the Community as a whole. It has consistently been held that Article 92(3) gives the Commission a discretion the exercise of which involves economic and social assessments which must be made in a Community context... The Commission has on a number of occasions informed the Member States of the policy which, in accordance with the powers thus vested in it by Article 92 *et seq.* of the Treaty, it intended to apply with respect to regional aid schemes — *inter alia*, in its 1988 communication on the method for the application of Article 92(3)(a) and (c) to regional aid. It is clear from that policy that the application of both Article 92(3)(a) and Article 92(3)(c) presupposes the need to take into consideration not only the regional implications of the aid covered by those provisions but also, in the light of Article 92(1), its impact on trade between Member States and thus the sectoral repercussions to which it might give rise at Community level.' (recitals 17 to 20).

- (37) In order to ensure a coherent approach to measures to support the development of the sector of the processing and marketing of agricultural products, the Commission considers that the same limitations of a sectoral nature which are placed on the

granting of such aids must apply both to investment aids which are financed by the Community and to measures which are solely financed by Member States. In this way, the Commission endeavours to guarantee compatibility between the common agricultural policy and policy on State aid so that an investment is not encouraged where, for structural reasons, it is contrary to the Community interest. Clearly, efforts at Community level to reduce or eliminate structural over-capacity would be undermined if Member States were free to give aid at the national level.

- (38) At first, the Commission applied such sectoral limitations on the basis of specific measures taken in respect of the individual sectors concerned (sugar, iso-glucose, dairy products). However, following the adoption of Decision 90/342/EEC, the Commission began to apply the Decision by analogy to new State aid in order to ensure that the categories of investment excluded from Community aid were also excluded from State aid.
- (39) This development of Commission policy through the introduction of sectoral limitations to aids for investment for the processing and marketing of agricultural products is clearly outlined in the Annual Commission Reports on Competition Policy. Both the XXth Report (1990) ⁽²⁾ and the XXIst Report (1991) ⁽³⁾ refer to the application of individual product sector limits. The XXIIInd Report (1992) explicitly states ⁽⁴⁾:

'In structures policy for investments at processing and marketing level, Council Regulation (EEC) No 866/90 allows Member States in principle to introduce unilateral measures, under the terms of Articles 92 and 93, in all areas covered by the Regulation.

In practice, this freedom is circumscribed by the Commission policy of excluding from State aid the same investments which are excluded from Community co-financing under point 2 of the Annex to Commission Decision 90/342/EEC of 7 June 1990.'

This position was restated in similar terms in the XXIIIrd Report (1993) ⁽⁵⁾ and in the XXIVth Report (1994) ⁽⁶⁾.

⁽²⁾ Paragraph 337.

⁽³⁾ Paragraph 317.

⁽⁴⁾ Paragraph 506.

⁽⁵⁾ Paragraph 550.

⁽⁶⁾ Paragraph 371.

⁽¹⁾ [1997] ECR I-135.

(40) Furthermore, this policy was explicitly communicated to the German Government in the context of specific decisions on individual aid schemes which had been notified to the Commission. For example, by letter of 30 March 1993 (SG(93) D/5076) the Commission informed the German Government of its decision to open the procedure laid down in Article 93(2) of the Treaty in respect of aids which Germany has decided to grant for the modernisation of a grain mill in Dresden (C 6/93). In that letter, the Commission wrote:

‘In assessing State aid to investments for processing and marketing, it is established Commission policy to apply the sector specific selection criteria in point 2 of the Annex of the Commission Decision [90/342/EEC] (“sector limits”) by analogy, given that they are designed to take account of the Community market situation.’

A statement in identical terms was included in the Commission’s letter of 28 June 1993 (SG(93) D/10681) opening the procedure in respect of aid to modernize grain mills in Saxony (C 15/93).

(41) Following the adoption of Decision 94/173/EC which updated the selection criteria and the categories of investment excluded from Community aid to current market conditions, in particular as a result of the reform of the common agricultural policy, it was clear that the Commission had to amend its State aid policy. In a Communication to Member States of 1 July 1994, the Commission announced that it intended to review its practice in this area as soon as the necessary preparatory work with the Member States had been completed. However, for reasons of legal certainty, the Commission would continue to apply the sectoral limitations as set out in Decision 90/342/EEC until the preparatory work was completed. In the same communication, the Commission restated its basic philosophy of applying the same sectoral limitations to measures which are funded by the Community and to measures which are exclusively funded from State aid.

(42) The Commission embarked on its review by approving, on 30 November 1994, a first draft of the guidelines for this type of aid, which was sent to the Member States by letter of 13 February 1995. After consulting the Member States within the Working Group on Conditions of Competition in

Agriculture at a meeting on 3 May 1995, the Commission approved the guidelines and appropriate measures in question by decision of 19 July 1995.

(43) While confirming its established practice of applying by analogy the sectoral restrictions on Community part-financing of such investments under Regulation (EEC) No 866/90, the following amendments were introduced as compared with the provisions applicable up to 31 December 1995:

- application of the sectoral restrictions laid down in points 1.2. (second and third indents) and 2 of the Annex to Decision 94/173/EC instead of those referred to in point 2 of the Annex to Decision 90/342/EEC,
- the automatic adjustment of the guidelines and appropriate measures to take account of future amendments to Commission Decision 94/173/EC,
- fixing of maximum levels for public aid in terms of gross rates,
- application of the guidelines and appropriate measures also to aids for investment in the processing and marketing of agricultural products at farm level,
- where a State aid subject to the special conditions referred to in point 2 of the Annex to Decision 94/173/EC is granted under a general regional or sectoral aid scheme to which the Commission has raised no objection under Articles 92 and 93 of the EC Treaty, possible requirement that an annual report be submitted to the Commission enabling it to check that each of the conditions for the grant of such an aid referred to in point 2 of the Annex to Decision 94/173/EC has been met,
- repeal of certain instruments whose provisions have been incorporated into the guidelines and appropriate measures in question.

4. Application of the guidelines and appropriate measures to regional aid schemes

(44) In the course of the procedure, the German Government has in substance contested the application of the guidelines to regional aid schemes. In the first instance, it argues that if large areas of the agricultural processing and marketing

sector were to be systematically excluded from national aid, the scope of regional measures for improving regional economic structures could be reduced in rural areas to an unacceptable level. In other words, Germany argues that the application of national regional aid schemes should be given priority over the specific requirements of the common agricultural policy.

The Commission cannot accept this position. The common agricultural policy, the establishment of which is required under Article 3(e) of the EC Treaty, is based on the development, through the common organisations of the market and through structural measures, of specific support mechanisms which take account of the needs of the particular sectors concerned and which therefore differ considerably from one sector to another. This policy has been developed at the Community level, in accordance with the procedures laid down in Article 43 of the Treaty, and it is managed and implemented at Community level. It follows that when designing and implementing their national aid schemes, Member States must take account of the objectives of the common agricultural policy, and in particular of the specific restrictions which have been placed on the granting of financial support for certain sectors, whether at the stage of primary production, or at the stage of processing and marketing of agricultural products. It is for this reason that the Commission has always insisted that national regional aid schemes must take account of the specific rules applicable to the agricultural sector.

(45) Furthermore, the Commission cannot accept the distinction made by the German Government between sectoral and regional aid schemes. In assessing the compatibility of national aid measures with Article 92(3) of the Treaty, the Commission must consider the economic effects of the measure, and in particular the extent to which it is likely to adversely affect trading conditions to an extent contrary to the common interest. The classification which is given by the Member State to the aid is, at best, of secondary importance. Otherwise, it would be easy for a Member State to escape the application of a restrictive policy in respect of certain types of aid by reclassifying a 'sectoral aid' measure as 'regional aid', or by relocating an investment from an area which is not eligible for regional aid to one which is. In such circumstances, any restrictions which are imposed by the Commission on the granting of aids to sectors with proven overcapacity would serve no purpose.

(46) The Commission accepts that the sector of the processing and marketing of agricultural products

is an important sector of the European economy. In particular, investments in this sector are likely to promote the economic development of rural areas, and the creation of employment in those areas. Investments in the processing and marketing of agricultural products are also likely to assist farmers to find new outlets for their products. For this reason, the Community provides substantial financial support for such investments through Regulation (EEC) No 866/90. The Commission has always taken a favourable approach to State aid in this sector, currently allowing aids of up to 55 %, or 75 % in Objective 1 regions (¹).

(47) Moreover, it should be noted that the Community guidelines take account of the particular needs of regional aid schemes in so far as they allow for a higher aid rate than that mentioned above, where this is the rate applicable in the regional aid scheme concerned. Point 4(b)(ii) of the guidelines and appropriate measures reads:

'Regional aid schemes which include aid for investment in the processing and marketing of agricultural products are subject to these guidelines and appropriate measures as far as such investments are concerned. The implementation of a regional aid scheme will be subject to the intensity of the aid approved under that scheme.'

(48) The German Government asserts that Decision 94/173/EC excludes large numbers of investments in the processing and marketing of agricultural products. It is true that a significant number of types of investment are excluded unconditionally by Decision 94/173/EC. However, it should be emphasised that the Commission has in fact taken account of regional diversities in the sectoral limits themselves, both in the 1990 and the 1994 versions, by providing for a whole series of derogations from the prohibitions laid down in the restrictions to assist less-developed regions, in particular Objective 1 areas. For example, the sectoral limits sometimes permit investments which would otherwise be excluded, in Objective 1 regions with a proven shortage of production capacity, or provided that there is no overall increase in production capacity. Even in sectors where there are no derogations in favour of the less favoured areas, in many cases not all investments are prohibited. In particular, investments to update production facilities to meet hygiene, animal welfare or environmental requirements are often allowed providing that there is no overall increase in production capacity, or subject to a reduction in production capacity.

(¹) Annex to the Guidelines for State aid in connection with investment in the processing and marketing of agricultural products.

- (49) Germany also objects that no guidance is given in the Commission Decision as to when such a lack of capacity is to be assumed, or what evidence is required to show it. However, the second subparagraph of point 3(b) of the guidelines states: 'Where State aid subject to the special conditions referred to in point 2 of the Annex to Decision 94/173/EC is granted in the framework of a general regional or sectoral aid scheme to which the Commission has raised no objection... an annual report is to be provided to the Commission giving details of any instance of grant of such aid during the year in question and in particular containing all information necessary to enable the Commission to conclude without recourse to additional enquiry, that each of the conditions attached to the grant of such aid referred to in point 2 of the Annex to Decision 94/173/EC has in fact been met.' It follows that the primary responsibility for determining whether the conditions set out in Decision 94/173/EC have in fact been met lies with the competent authorities of the Member States. If the competent authorities are in any doubt about the application of the criteria concerned, they can always obtain clarification from the Commission in accordance with Article 5 of the Treaty.
- (50) Furthermore, the German Government has failed to provide details of the precise manner in which the application of the sectoral limitations contained in Decision 94/173/EC interferes with its regional aid policy. In its letter of 31 July 1996, Germany has provided the Commission with a general description of the importance of State aid for the processing and marketing of agricultural products, but it has not specified in detail the nature of the investments concerned, or the extent to which the measures concerned are covered by the sectoral limitations contained in Decision 94/173/EC.
- (51) Given that 14 Member States have accepted the application of the sectoral limitations to regional aid schemes and given the absence of a detailed explanation from the German Government as to why it considers that the application of these sectoral limitations will result in an unacceptable restriction of regional aid policy, the Commission has to conclude that the position taken by Germany is not justified.
- (52) Should the German Government consider that one or more of the sectoral limitations set out in Decision 94/173/EC is unduly restrictive, it is always free to ask the Commission to review, and if necessary amend the provisions of the decision in question. This would have the advantage of allowing not only State aid, but also Community financial support through the structural funds to be granted to the activities in question, and would also enable the Commission to maintain a coherent approach between the common agricultural policy and State aid policy.
- (53) The German Government also contests the premise that the introduction of Community guidelines should improve consistency with the common organisation of agricultural markets. The guidelines and appropriate measures in question do not cover the production of agricultural products but rather the industrial processing and commercial marketing of existing Annex II products. The German authorities therefore argue that the way in which price and quantity are regulated under the common market organisation cannot be influenced by restrictions on industrial processing or marketing. Agricultural surpluses are not encouraged by the presence of competitive processing capacities but by production incentives under the agricultural market organisations in question.
- (54) The Commission does not accept the rigid distinction which the German authorities seek to draw between the primary production sectors, covered by the common market organisations, and the processing and marketing of agricultural products. The experience acquired in the operation of the common agricultural policy shows that the creation of new capacity for the processing and marketing of certain types of agricultural products will tend to encourage farmers to produce more of the products concerned. Conversely, measures which are taken to reduce primary agricultural production in certain sectors may result in over-capacity in the processing and marketing industries for the products concerned unless commensurate reductions are made in the capacity of those industries. Indeed, Regulation (EEC) No 866/90 is specifically based upon this close economic relationship between primary agricultural production and the processing and transformation of agricultural products. In particular the Regulation is based on the principle that investments should be made conditional on the inclusion of such investments in sectoral plans containing an in-depth analysis of the situation in the sector concerned and the proposed improvement. Moreover, it must be ensured that investments are viable, and that farmers have a fair share in the economic benefits of the actions undertaken. The Commission considers that it is also entitled to give consideration to the close economic relationship between primary production and the processing and marketing of agricultural products when determining whether State aid can be considered compatible with the common market in accordance with Article 92(3) of the Treaty.

(55) Furthermore, the Commission would point out that its objective in determining its policy for State aid for investments for the processing and marketing of agricultural products is to ensure coherence between competition policy and the common agricultural policy as a whole. In order to ensure consistency, the Commission seeks to ensure that the same sectoral limitations apply to all public investments in this sector, whether financed by the Member States or by the Community. However, it is important to emphasise that the sectoral limitations set out in Decision 90/342/EEC and the changes made by Decision 94/173/EC were introduced following an extensive analysis of representative markets at the level of the processing and marketing industries themselves and not at the level of primary production. For example, the exclusion of investments relating to starch production are based on the continuing existence of over-capacity in the starch production sector, not on any possible over-capacity in the production of potatoes or cereals for use as raw materials in starch production. Similarly, the restrictions on investments relating to the slaughter of cattle, pigs, sheep and poultry are based on over-capacity in the slaughterhouse sector, and not on levels of primary production. The other sectoral limitations are also based on the existence of over-capacity in the processing and marketing sectors.

(56) Lastly, the German Government argues that it should be possible to grant State aid irrespective of whether or not the primary agricultural products used are produced by the domestic agricultural sector or are imported. Pursuant to Article 13 of Regulation (EC) No 951/97⁽¹⁾, Community financing of investments in the processing or marketing of products from third countries is excluded. However, the guidelines and appropriate measures on State aid in connection with investments in the processing and marketing of agricultural products do not explicitly exclude State aid for investments for the processing and marketing of products which are imported from third countries, and the Commission would not raise objections to such aid, provided that all the other conditions laid down in the guidelines and appropriate measures are met, in particular the sectoral limitations imposed by Decision 94/173/EC. The reason for this difference of approach is that the Commission considers that it is necessary to ensure that Community funding is used to ensure the development of processing and marketing capacity for products of Community origin. On the other hand,

the Commission considers that Member States can be left with a discretion to decide whether to grant State aid for the processing and marketing of imported agricultural products, subject of course to compliance with Articles 92 and 93 of the Treaty, in order to take account of the specific situation at national level. For these reasons, this argument of the German Government is not founded.

IV. CONCLUSION

(57) In view of the foregoing, the arguments and submissions put forward by the German Government do not justify its refusal to agree to the application of the guidelines and appropriate measures to regional aid schemes as proposed by the Commission.

(58) All the other Member States have agreed unconditionally to the introduction of the guidelines and appropriate measures. Germany is the only Member State which has not done so. In the absence of a clear justification by the Member State concerned, the Commission cannot accept the non-application of the guidelines and appropriate measures to regional aid schemes in only one of the Member States.

(59) In view of Germany's refusal to comply with these guidelines and appropriate measures, the Commission, having initiated and carried out the procedure laid down in Article 93(2), is entitled by way of a decision taken pursuant to that provision and on the basis of the considerations set out in Section III, to require existing aid schemes to be altered by placing Germany under an obligation to comply with the guidelines for State aid in connection with investments in the processing and marketing of agricultural products. In order to achieve this result, it is necessary to require that Germany amend its existing aid schemes to bring them into line with Decision 94/173/EC,

HAS ADOPTED THIS DECISION:

Article 1

National regional aid schemes in Germany are incompatible with the common market within the meaning of Article 92(1) of the EC Treaty, in so far as they do not comply with the guidelines and appropriate measures for State aid in connection with investments in the processing and marketing of agricultural products which were communicated to Germany by letter SG(95) D/13086 of 20 October 1995.

⁽¹⁾ See footnote 3.

Article 2

Within two months of the date of this Decision Germany shall amend, or where necessary abolish, existing aids and existing aid schemes in order to ensure that they are compatible with the common market. In particular, in accordance with point 3(b) of the guidelines referred to in Article 1, Germany shall ensure that:

1. no State aid for investments in the processing and marketing of agricultural products shall be granted in respect of any of the investments which are referred to in the second and third indents of point 1.2 of the Annex to Decision 94/173/EC or which are excluded unconditionally by point 2 of that Annex;
2. no State aid for investments in the processing and marketing of agricultural products shall be granted in respect of the other investments referred to in point 2 of the Annex to Decision 94/173/EC unless they meet the special conditions laid down in that Annex.

Article 3

Germany shall inform the Commission of the measures taken to comply with this Decision within two months of notification thereof.

Article 4

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 20 May 1998.

For the Commission

Franz FISCHLER

Member of the Commission
