STATE AIDS (MOTOR VEHICLES): THE VOLKSWAGEN CASE

Subject: State aids

Industry: Motor vehicles (some implications for other industries)

Parties: The Free State of Saxony
Volkswagen AG and Volkswagen Sachsen GmbH
Commission of the European Communities
The Federal German Republic (Intervener)
The United Kingdom Government (Intervener)

Source: Press Release No 97/99, dated 15 December 1999, summarising the Judgment of the Court of First Instance in Joined Cases T-132/96 and T-143/96 (*Freistaat Sachsen, Volkswagen AG and Volkswagen Sachsen GmbH v Commission*)

(Note. This is a case in which the Court has upheld a Commission decision refusing to allow part of the aid granted by the German authorities to VW, notwithstanding the provisions of the EC Treaty allowing for special aid to what was formerly East Germany.)

The Commission decision of 26 June 1996 refusing to authorise part of the aid granted by Germany to the Volkswagen Group for the Mosel and Chemnitz (former Trabant) works complies with Community law.

German reunification in 1990 brought with it the collapse of demand for, and production of Trabant vehicles in Saxony. To safeguard the automobile industry in that region, the Volkswagen group entered into negotiations with the Treuhandanstalt, the public law body entrusted with restructuring the businesses of the former German Democratic Republic, which led to an agreement in October 1990.

Among other things, that agreement envisaged the reopening and restructuring of the former works at Mosel (Mosel I) and Chemnitz (Chemnitz I) with a view to their temporary operation and, subsequently, the construction of a new automobile works on the Mosel (Mosel II) and Chemnitz (Chemnitz II) sites.

By a first decision of 27 July 1994 (Decision 94/1068/EC), the Commission agreed to the ayment of DM 487m in restructuring aid for Mosel I and DM 84.8m in such aid for Chemnitz I. By a cond decision of 26 June 1996 (Decision 96/666/EC), the Commission agreed to the payment of DM 539.1m in aid by way of compensation for regional handicaps faced by Volkswagen at Mosel II and Chemnitz II. However, it disallowed the balance of the aid envisaged, namely DM 240.7m, holding that amount to be incompatible with Community law.

On 8 July 1996, the Free State of Saxony (Freistaat Sachsen) nevertheless paid /

Volkswagen DM 90.7m in the form of investment grants, even though they had been declared incompatible with the common market. (Part of that aid has since been repaid).

On 26 August and 13 September 1996, the Free State of Saxony and the Volkswagen group brought two actions before the Court of First Instance seeking partial annulment of the second Commission decision, of 26 June 1996, concerning Mosel II and Chemnitz II. Germany has intervened in support of the State of Saxony and Volkswagen, the United Kingdom in support of the Commission.

The Court of First Instance has dismissed those actions.

Article 92(2)(c) of the EC Treaty authorises as compatible with the common market "aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany, in so far as such aid is required in order to compensate for the economic disadvantages caused by that division".

[Article 92 is now Article 89, EC Treaty.]

In the judgment of the Court of First Instance, that provision does not permit wholesale compensation for the economic backwardness of the new provinces (Länder). Such an interpretation would disregard the fact that that provision is in the nature of a derogation and its context and aims. According to the Court, the words "division of Germany" refer, historically, to the partition into two zones carried out in 1948. Therefore, the "economic disadvantages caused by that division" mean only the economic disadvantages caused by the isolation resulting from the establishment or maintenance of that frontier. The differences in development between the old and new provinces (Länder) are due to causes other than the division of Germany as such, and in particular to the different political and economic systems established in each State. The Commission did not therefore err in law by refusing to apply that derogation to regional aid for new investment projects.

Moreover, under Article 92(3)(b) of the EC Treaty, aid may be considered to be compatible with the common market if it is designed to remedy a serious disturbance in the economy of a Member State.

In the Court's judgment, a "serious disturbance in the economy of a Member State" within the meaning of that provision must affect the whole of the economy of the Member State concerned and not just the economy of one of its regions or parts of its territory. In the application for the annulment of the Commission decision, no reference is made to the state of the economy of the Federal Republic of Germany. Nor have the applicants established that the Commission made an obvious error of assessment in holding that the unfavourable repercussions of German reunification on the German economy, however true, did not in themselves constitute a ground for applying that derogation from the aid system.

The Court also draws attention to the fact that the Commission has a wide discretion in monitoring State aid, which involves complex assessments of an economic and social nature. In this case, it did not make any obvious error in its assessment of the amount of aid which the Volkswagen group might enjoy for the benefit of its investments in Saxony. It took ample account in its decision of the fact that the new provinces constitute "an underdeveloped region" where "the standard of living is low" and there is extremely high unemployment which continues to grow, and therefore authorised intensive investment aid to facilitate regional economic development.

The Volkswagen group has already received significant aid for its investments at Mosel I and Chemnitz I, which allowed it to benefit from a fully operational automobile construction plant by 1994 at the latest.

The Court also points out that the Commission was entitled to refer to excess production capacity in the automobile industry, and therefore to take the Community interest into account, in disallowing payment of part of the aid in question, in so far as it exceeded compensation for the economic disadvantages affecting the new provinces by comparison with other unaided regions of the Community. ■

The Alcoa / Reynolds Case

As "second phase" investigations into concentrations are still comparatively rare, the following case has some interest. On 20 December 1999, the Commission decided to open a Second Phase investigation into the proposed merger between aluminium producers Alcoa and Reynolds which would create one of the largest integrated aluminium companies in the world. The Commission's initial investigation has identified a number of markets where the merger would raise serious doubts as to its compatibility with competition rules in the common market, but further investigation is needed. A final decision by the Commission is expected by early May, 2000.

Alcoa, the largest aluminium producer world-wide, is a US corporation involved in all aspects of the alurminium industry (bauxite mining, alumina refining, aluminium smelting, manufacturing and recycling as well as research and technology). Reynolds is a US corporation also involved in all aspects of the aluminium industry Qauxite mining, alumina refining, aluminium smelting, manufacturing and recycling, packaging, as well as research and technology). On 18 August 1999, Alcoa and Reynolds entered into a merger agreement whereby Reynolds would become a wholly owned subsidiary of Alcoa, and Alcoa would acquire sole control over Reynolds.

Having decided to open a full investigation of the merger, the Commission will now continue a detailed fact-finding operation, using as a legal test whether the merger might create or reinforce a dominant position, held either by a single entity (single dominance) or by a cluster of competitors presenting the structural characteristics of an oligopoly (collective dominance).

Source: Commission Statement IP/99/1010, dated 20 December 1999.