

Oprescu, Gheorghe; Atanasiu, Isabela; Papatulică, Mariana; Prisecaru, Petre

**Research Report**

## State aid control in the sensitive sectors: Coal, steel, shipbuilding, motor vehicles

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# **European Institute of Romania**

**Study no. 10**

## **STATE AID CONTROL IN THE SENSITIVE SECTORS - Coal, Steel, Shipbuilding, Motor Vehicles -**

**Authors:**

Gheorghe Oprescu, Professor - coordinator

Isabela Atanasiu, Ph.D.

Mariana Papatulică

Petre Prisecaru, Ph.D

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## **PART I**

### **EU RULES ON THE AWARD OF STATE AID TO THE “SENSITIVE SECTORS”**

#### **Introduction**

Starting with the 1970s, the European Commission defined its policy for the control of state aid for specific manufacturing sectors, and published numerous guidance documents on the subject. The Commission’s Communication of 1978<sup>1</sup> established the general principles of this policy, which are valid to present. The main objective is to ensure that state aid does not distort competition on the internal market, but certain state aid measures may exceptionally be considered justified when they contribute to achieving the economic and social cohesion objectives of the Community. This may happen when the rules of the free market prevent, delay or postpone beyond acceptable limits the achieving of the mentioned Community objectives.

A first step towards consolidating the various sector-specific regulations in this domain was the publication in 1998 of the *Multisectoral Framework on regional aid for large investment projects*.<sup>2</sup> Although the title suggests that this document refers only to regional aid issues, it nevertheless has important consequences for the control of state aid to the ‘sensitive sectors’. The 1998 Multisectoral Framework stipulated that the specific rules applicable to certain sectors, including agriculture, fisheries, steel, shipbuilding, synthetic fibres, motor vehicles, transport and coal, remained in place - whereas textiles and clothing, previously subject to specific rules, were brought under the scope of the Multisectoral Framework. The Multisectoral Framework was updated and amended on 1 January 2004, and the new version is also applicable to the synthetic fibres and motor vehicles sectors.

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<sup>11</sup> COM (78) 221 final – May 1978.

<sup>2</sup> OJ C 70 of 19.3.1998, pp. 8-20.

## CHAPTER 1.

### GENERAL ASPECTS OF STATE AID CONTROL IN THE EU

The ECSC Treaty expired on the 23 of July 2002. Starting with this date, the EU steel and coal sectors, which were previously covered by the state aid provisions of this Treaty, became subject to the general provisions on state aid in the EC Treaty and the secondary legislation developed in their application. However, as we will show in the following sections, the steel and coal sectors continue to be subject to a distinct and stricter policy of state aid control, established through a series of specific policy documents adopted by the European Commission in application of Art. 88 EC.

By signing the Association Agreement with the EU, Romania undertook to apply in full the EC regulation concerning the control of state aid, including both the general provisions in Arts. 87-88 EC as the secondary legislation developed in their application. On general terms, this implies that at present Romania is obliged to apply in full the EC regulation on state, as if it were already a member of the EU. BY exception from this general rule, the steel industry in Romania makes the object of special provisions comprised in Protocol 2 to the Association Agreement, which contained a five-year derogation from the EU rules on rescue and restructuring aid for this sector – this derogation has been prolonged to the end of December 2005.

This section is intended to offer to the readers who are not familiar with EC state aid control regulation an accessible introduction to the basic legal concepts relevant in this domain. Such notions are indispensable in order to understand the specific rules applicable in the control of state aid to the so-called ‘sensitive sectors’, which make the object of this report. A good understanding of the legal concept of ‘state aid’ is furthermore necessary in the Romanian context, where budgetary restraints determine the public authorities and bodies to supplement or even substitute traditional aid measures with indirect measures of support. Thus it becomes necessary to understand to what extent such indirect support measures fall under the scope of the state aid rules.

Thus, in this section we overview the main provisions of the EC Treaty on state aid, focusing in particular on the following:

- a. the legal concept of state aid as resulting from the EU legislation;
- b. the general conditions for the approval of state aid in the EU; and
- c. the procedures applied by the European Commission in the screening for approval, respectively the monitoring, of state aid given in the EU.

The specific rules relevant to the control of state aid for the so-called ‘sensitive sectors’ will be examined in detail in the following sections.

#### 1.1. The legal concept of state aid

Art. 87(1) EC prohibits to the Member States the award of financial aid to undertaking, *no matter in what form*, to the extent that such aid distorts competition by favouring certain undertakings or the production of certain goods and thus having a negative effect on intra-community trade. The prohibition laid down in Art. 81(1) EC is one *of principle*, as para. (3) of the same Article foresees a number of *exceptions* from this rule – in practice, it empowers the European Commission to approve by way of exception certain state aid measures that are considered justified in the pursuit of Community-accepted economic and social policy objectives.

Art. 87 EC does not contain an exact definition of the legal concept of state aid. This legal definition has taken shape in time, through the adoption of secondary legislation implementing Art. 87 EC and the case law of the European Commission and European courts. We underline that, in the textual formulation of Art. 87 EC, *the form in which the state intervenes to support certain undertakings or the production of certain goods is not relevant to the qualification of a state support measure as 'state aid'* (as we will show in what follows, the legal definition of state aid covers both direct support measures – such as budgetary allocations, or what is usually referred to as 'subsidies' – but also indirect forms of support, such as fiscal facilities, or regulation that favours certain undertakings or sectors). Rather, *a measure of support will be qualified as involving 'state aid' mainly in function of its effects*. This broad definition of state aid allows to the European Commission to exert control over a wide range of support measures adopted by the Member States, including those involving the participation of the EU itself (for example, the incentives to investment in assisted areas, co-funded by the Member States and the EU via the Structural Funds).

We do not intend to cover in detail the legal definition of state aid in this context,<sup>3</sup> but only provide a short overview of its main elements. A good understanding of these *cumulative* elements allows to specify the state support measures that fall under the scope of Arts. 87-88 EC and the secondary legislation developed in their application – as we already mentioned before, the specification of such measures is particularly relevant for the context of Romania and the new member States from Central and Eastern Europe, whose budgetary possibilities are tighter than those of the older member States, and which therefore often supplement or even substitute traditional forms of subsidisation with measures of indirect support.<sup>4</sup>

In practice, a state support measure will be qualified as involving state aid when the following *four cumulative conditions* are met:

1. the measure involves the *use* (directly or indirectly) *of public resources*;
2. the measure confers an *advantage* to the beneficiary/beneficiaries;
3. the scope of application of the measure is *selective*;
4. the measure implies *distortions of competition* and *negative effects on intra-community trade*.

1. Use of public resources. Art. 87(1) EC stipulates that state aid can be granted “by the state or through public resources”. Thus, first, the legal definition of state aid covers both measures of support implemented by administrative bodies (the government, the regional and local administration) and support measures that are implemented by private bodies acting on behalf of the state.<sup>5</sup> Second, the legal definition of state aid covers not only support measures involving a direct expenditure from the state's coffers (for example, direct subsidies or the subsidisation of loans) but also measures that imply a loss of state revenue (for example, the postponing or waiver of public debt, fiscal facilities involving the reduction or postponement of tax or social security contributions, etc.).<sup>6</sup> From this perspective, it is worth making a few

<sup>3</sup> For further details on this subject, see, e.g.: Carl Baudenbacher (1999): *A Brief Guide to European State Aid Law*, London: Kluwer Law International; Malcolm Ross (2000): “State aids and national courts: definitions and other problems”, *Common Market Law Review* vol. 37, pp. 401-423; European Commission (1998): *Competition Law in the European Communities, Vol. II B: Explanation of the rules applicable to State Aid*, Brussels/Luxembourg (available on DG Competition's website), Isabela Atanasiu (2001): “State Aid in Central and Eastern Europe”, *World Competition* vol. 24, pp. 257-283.

<sup>4</sup> For a detailed examination of the forms of aid and expenditure patterns in the Central and Eastern European countries, see I. Atanasiu (2001), *op. cit.*

<sup>5</sup> In this sense, see, e.g., Joint Cases C-72/91 and 73/91 *Sloman Neptun* [1993] ECR I-887, Joined Cases C-52/97 and C-54/97 *Viscido* [1998] ECR I-2629, Case C-379/98 *PreussenElektra* [2000] ECR I-2099.

<sup>6</sup> See for example *Viscido*, *supra* note.



comments on the particularities of state guarantees to loans. Although such guarantees do not always have to be honoured (in practice, the guarantees must be honoured only when the debtor is unable to pay back the contracted loan), such support measures contain an inherent element of state aid to the extent that the beneficiary obtains a more favourable interest rate on the contracted loan because of the availability of the state guarantee, and furthermore, in certain cases (firms in difficulty) the loan would not have been obtained to begin with in the absence of the state guarantee.<sup>7</sup>

In what follows we list a few practical examples of what was discussed above:

- **The DMT judgment:**<sup>8</sup> in this case, the European Commission qualified as state aid the exceptional treatment applied by the ONSS (the Belgian institution responsible for collecting social security contributions) to DMT, a firm in financial difficulty, involving the postponement for 8 years of some payment due by the latter. The ECJ upheld the European Commission's decision, showing that: "as long as social security contributions are imposed by law and administrated (by the ONSS) on its basis, such contributions must be qualified as state resources". Thus, the circumstances of the case met the first element in the legal definition of state aid, namely the involvement of state resources.
- **The PreussenElektra judgment:**<sup>9</sup> this case concerns the introduction in Germany of a law forcing private electricity suppliers on the German market to purchase German-produced electricity from 'alternative sources' (bio-energy, hydro-energy, etc.) at a pre-established minimum price.<sup>10</sup> The European Court of Justice received a request for a preliminary ruling from a German regional court, asking for guidance on the applicability of EC state aid rules to the case in question. In the course of the proceedings, the European Commission argued that the German law relevant in the case involved an element of state aid, in so far as it supported the German producers of electricity from alternative sources by offering the possibility to sell at a price above the market level. The European Court of Justice retained however that the German law in question did not fall under the scope of EC state aid rules, because it did not satisfy the condition of use of state resources. While it was undeniable that the law in question offered a financial advantage to the German producers of electricity from alternative sources, this advantage was the consequence of a re-distribution of production and sale costs among the electricity operators, without implying any use, direct or indirect, of state sources. (*PreussenElektra* is one of a series of cases where the European Court of Justice put a brake on the European Commission's tendency to expand the coverage of the state aid concept so as to extend its control over a wider range of economic policy measures adopted by the Member States.)

2. The financial advantage: This condition was defined by the case law of the European court so that the legal concept of state aid comprise "any support measure, whatever its form, that has as an effect the reduction of the expenses normally borne by the undertakings, even if it is not a subsidy, but has the same nature and effects".<sup>11</sup>

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<sup>7</sup> See M. Ross (2000), *op. cit.*, and C.-D. Ehlermann and M. Everson, ed. (2001): *European Competition Law Annual 1999: Selected Issues in the Field of State Aid*, Oxford: Hart Publishing.

<sup>8</sup> Case C-256/97 *Déménagements Manutention Transport SA (DMT)* [1999] ECR I-3913.

<sup>9</sup> Case C-379/98 *PreussenElektra* [2000] ECR I-2099.

<sup>10</sup> In the Community terminology, the notion of 'electricity produced from alternative sources' covers all types of electricity apart from what is produced from fossils - see *Community Guidelines on State aid for environmental protection*, OJ C 37 of 3.2.2001, p. 15.

<sup>11</sup> As an interesting anecdotal detail, this condition was firms defined in Case 30/59 *De Gezamenlijke Steenkolenmijnen in Limburg v. High Authority* [1961] ECR 19, a case concerning the application of the state aid provisions in the ECSC Treaty to coal extractions.

This condition is difficult to verify in the case of indirect support measures, and particularly of support measures implemented by independent bodies or private undertakings acting on behalf of the state (for example, commercial banks). The European Commission has developed an analytical tool for the assessment of such cases, the so-called “market economy investor principle” (MEIP). The test consists of comparing the behaviour of the body implementing the support measure with that of a private investor acting in similar circumstances.<sup>12</sup> Despite its apparent straightforwardness, the MEIP is often difficult to apply in practice, the main problem being to identify the hypothetical behaviour of a private investor to measure against. For example, when a public institution implements a support measure adopted in the context of a wider economic policy strategy, this behaviour must be measured against that of a holding company seeking to increase its profits in the medium or long-term.<sup>13</sup>

It is also worth mentioning that the MEIP test is useful not only for identifying support measures involving state aid, but also for quantifying the aid element in question. For example, in the case of a state guarantee for a loan from a commercial bank, the exact amount of state aid received by the beneficiary is given by the difference between the interest rate that would have been applied in normal conditions and the (lower) interest rate obtained because of the state guarantee.<sup>14</sup>

In what follows we give an example illustrating the above:

- **the DMT case:**<sup>15</sup> the ECJ explains in its judgment that the notion of state aid is broader than that of a subsidy, including not only direct support such as in the case of subsidies, but also measures that reduce in one way or another the expenses normally borne by undertakings. When a public institution entrusted with the collection of social security contributions (the Belgian ONSS in the case in question) tolerates the delayed payment of the contributions due by an undertaking, this behaviour confers a significant financial advantage to the undertaking in question. In other words, state measure allowing to the undertakings to delay the payment of public debts, whatever their form, confers a financial advantage to the beneficiaries to the extent that they would not have been able to obtain a similar treatment from a private creditor. As the ECJ explains further, the tolerating behaviour of the Belgian ONSS towards DMT must be compared to that of a private creditor acting in similar circumstances. Private creditors may also decide to allow the postponement of payments for their debtors in financial difficulty, for the purpose of allowing them to recover and thus be able to repay their debts. Thus, in such a case, the problem consists of seeking to determine whether the tolerance manifested by the Belgian ONSS towards DMT exceeds the limits that would have been considered tolerable by a rational private creditor.

3. Selectivity: Art. 87 EC applies only to support measures that “favour certain undertakings or the production of certain goods”, or in other words, are selective. Thus, EC regulation distinguishes between support measures of a general character, which are available under the same conditions to all undertakings, no matter of the economic sector in which they operate, and selective support measures, whose distorting potential is higher than in the case of the former.

First, we observe that this condition is, once again, very difficult to verify in practice. The EC case law does not offer sufficient guidance on this subject, while the European Commission

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<sup>12</sup> For details on the application of the MEIP, see e.g. G. Abbamonte (1996): “Market Economy Investor Principle: A Legal Analysis of an Economic Problem”, *European Competition Law Review* no. 4, pp. 259-268.

<sup>13</sup> Case C-305/89 *Italy v. Commission (Alfa Romeo)* [1991] ECR I-1603; Case C-303/88 *Italy v. Commission (ENI-Lanerossi)* [1991] ECR I-1433.

<sup>14</sup> See *Commission Notice on the Application of Articles 87 and 88 EC to State Aid in the Form of Guarantees*, OJ C 71 of 11.03.2000.

<sup>15</sup> See *supra* note no. 6..

and the European courts have the tendency to apply a selectivity presumption to all measures suspected of involving an element of state aid, thus leaving the burden to prove the contrary to the Member State in question (the proof involving to demonstrate that the measure has a general scope of application). Below we give two examples of support measures qualified as selective:

- in *Maribel bis/ter*, a Belgian law reducing the rate of social security contributions for manual workers was qualified as selective, in so far as favouring certain undertakings and economic sectors;<sup>16</sup>
- in *CETM*, a Spanish law that involved the subsidising by the state of loans to purchase industrial vehicles by physical persons, SMEs, public institutions and public transportation companies, was qualified as selective for the same reasons as above.<sup>17</sup>

Second (and **nota bene**) support measures that apparently have a general character will be at any rate qualified as selective if the institutions empowered to implement their provisions enjoy a certain degree of discretion in their practical application. Below a few examples in this sense:

- the *Ecotrade*<sup>18</sup> and *Piaggio*<sup>19</sup> cases both dealt with Italian Law No. 95/79, an act that established a procedure for passing certain Italian companies in difficulty under the direct administration of the Ministry of Industry. Law No. 95/79 was qualified as selective because: i) the criteria for selecting the companies to benefit from this support scheme were discretionary; ii) the Ministry of Industry could select in a discretionary way which of the companies placed under its administration could continue their activity.
- in *DMT*,<sup>20</sup> the Belgian ONSS was in the position to establish in a discretionary way the postponement of payments due to it by the undertakings.

The application of the selectivity criteria raises a number of specific issues in the case of state aid given in the form of *fiscal facilities*. In its Notice on fiscal aid, the European Commission shows that, although certain fiscal measures have a selective nature, they do not fall under the scope of EC competition rules in so far as the selectivity character is “justified by the nature of the system”.<sup>21</sup> This means that, in practice, although a general fiscal measure benefits more to certain undertakings or sectors than to other, it will not necessarily be considered to involve state aid, in so far as this differentiation is justified by the nature of the general fiscal system applicable in the Member State in question.

The Commission’s Notice on fiscal aid is undeniably insufficiently clear on the distinction between general and selective taxation measures. What is the difference between selective measures that are considered “justified by the nature of the system” and those that are not considered so? Until this distinction will be clarified, probably by case law, the legislator in the Member States should be prudent to make sure that certain fiscal facilities have a clear general scope of application - according to the same Notice, a fiscal measure will be qualified as general when the following conditions are met:<sup>22</sup> i) it is open to all undertakings under the same conditions; ii) the fiscal authorities do not have the discretion to decide under which conditions the measure applies to each undertaking. Not in the least, the Notice underlines that fiscal facilities having a regional, local or sectoral scope of application will be automatically classified

<sup>16</sup> Case C-75/97 [1999] ECR I-3671.

<sup>17</sup> T-55/99 [2000] EC II-3207.

<sup>18</sup> C-200/97 [1998] ECR I-7907.

<sup>19</sup> C-295/97 [1999] ECR I-3735.

<sup>20</sup> See *supra* note no. 6.

<sup>21</sup> *Commission Notice on the application of state aid rules to measures relating to direct business taxation*, OJ C 384 of 10.12.1998.

<sup>22</sup> Point B.12 of the Notice on fiscal aid, see above.

as selective (a typical example in this sense is that of the fiscal facilities for investment in the assisted areas).

4. Distortion of competition on a cross-border dimension: Theoretically speaking, all financial support to an undertaking or sector distorts competition (to the extent that the respective market is open to competition) because it reduces the costs incurred by the beneficiary and thus gives it a financial advantage by respect to its competitors or potential competitors. EC state aid rules apply, however, only when such distorting effects have a cross-border dimension, or in other words, when intra-community trade is distorted. In practice, this criterion is considered to be satisfied when the beneficiaries of the financial support sell on geographical markets in other Member States, or when competitors from other Member States operate on the same national market with the beneficiary. Thus, financial support offered to undertakings operating on strictly regional or local markets is excluded from the scope of application of EC state aid rules.<sup>23</sup>

## 1.2. The general conditions for the approval of state aid

As already mentioned above, Art. 87 EC contains a prohibition *of principle* of the support measures qualifying as state aid. At the same time, paragraphs (2) and (3) of the same Article stipulate a series of *exceptions* from this ban. Some of these exceptions - namely those foreseen by para. (2) - apply automatically, while others – namely those at para. (3) - are applied by the European Commission, following a scrutiny of the objectives and effects of the aid measures in question.

The exceptions from the ban on state aid that have most practical relevance are those mentioned in Art. 87(3). On the basis of this provision, the European Commission can approve:

- state aid destined to promote the economic development of certain areas where the standards of living are very low or unemployment is very high (Art. 87(3)(a) EC);
- state aid destined to facilitate the development of certain economic activities or areas, in so far as the aid does not distort to an unacceptable extent intra-community trade (Art. 87(3)(c) EC).

We do not intend to discuss in detail in this context the application of these exception provision by the European Commission. However, it is worth mentioning that:

- under Art. 87(3)(a) EC, the European Commission usually approves state aid destined to attract and/or stimulate investment in the poorer regions of the EU, where GDP per capita (PPS) is below 75% of the EU average.<sup>24</sup> EU regulation establishes the *maximum aid intensity ceilings* applicable in such regions (to be noted that the intensity ceilings applicable in each assisted region are determined individually, taking into account its specific economic and social problems and development needs), as well as the general conditions under which investment aid may be approved in such regions.<sup>25</sup> In addition, the European Commission takes a more lenient approach to the control of rescue and restructuring aid given to firms in difficulty operating in the assisted regions covered by the provisions of Art. 87(3)(a)

<sup>23</sup> Case 40/75 *Produits Bertrand v. Commission* [1976] ECR 1; Case 52/76 *Benedetti v. Munari* [1977] ECR 163.

<sup>24</sup> For details on the methodology for selecting the ‘assisted regions’ covered by the provisions of Art. 87(3)(a) EC, see *Commission Guidelines on National Regional Aid*, OJ C 74 of 10.03.1998.

<sup>25</sup> See *Commission Guidelines on Regional Aid*, OJ C 74 of 10.3.1998, pp. 3-8, and *Communication from the Commission - Multisectoral framework on regional aid for large investment projects*, OJ C 70 of 19.03.2002, pp. 8-20.

EC – for example, the conditions of reducing excessive production capacities usually imposed for the approval of such aid may be more permissive for firms in difficulty in such regions, so as to cushion the negative impact of redundancies on the regional economy.

- under Art. 87(3)(c) EC, the European Commission approves the following categories of state aid: i) investment aid granted in regions that enjoy ‘assisted area’ status under Art. 87(3)(c) EC – usually, such regions are selected among those affected by industrial decline, or displaying lower standards of living by comparison to other regions in the same Member State (although sometimes better off than regions in other Member States);<sup>26</sup> ii) rescue and restructuring aid to firms in difficulty;<sup>27</sup> iii) aid to stimulate other types of investment than in physical capital, e.g. R&D, environmental protection, employment, training, etc.

### **1.3. The control and monitoring of state aid given in the EU**

It is beyond the purposes of this report to discuss in detail the procedural rules developed in the implementation of Arts. 87-88 EC. We mention however that the basic procedural rules governing the European Commission’s state aid control and monitoring activities were codified in a Council Regulation adopted in March 1999.<sup>28</sup> In essence, the EC Treaty lays the grounds for a system of *ex ante* notification for approval by the European Commission of all support measures proposed to be implemented by the Member States (except those covered by the automatic exceptions stipulated in Art. 87(3)(b) EC, as well as those excepted from the notification obligation *via* block exemption regulations and other policy guidance documents or regulations adopted by the European Commission and Council), followed by a monitoring of their implementation by the same European Commission. The Member States are obliged to respect the “standstill clause” imposed by the Treaty and the Procedural Regulation, meaning that they cannot implement new state aid measures or bring modifications to existing (and already approved) before obtaining the Commission’s approval. The European Commission is empowered to order the suspension of state aid measures implemented in breach of the stand-still clause, and order the temporary recovery of the aid already paid on their basis until a decision on the legality of the aid measure in question is reached. Not in the least, the European Commission is empowered to order the recovery of state aid granted without respecting the conditions it imposed upon approval.

### **1.4. Recovery of illegal aid**

#### *a. Legal framework*

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<sup>26</sup> See *supra* note no. 26.

<sup>27</sup> *Community Guidelines on State aid for rescuing and restructuring Firms in Difficulty*, OJ C 288 of 9.10.1999, p. 2-; see also the *Draft Community guidelines applying Articles 87 and 88 of the Treaty to the granting of urgency and/or restructuring aid to firms in difficulty*, proposed by DG Competition, and discussed with the experts of the Member States in February 2004 – available at [http://europa.eu.int/comm/competition/state\\_aid/others/](http://europa.eu.int/comm/competition/state_aid/others/).

<sup>28</sup> *Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty*, OJ L 83 of 27.3.1999.

As already mentioned above, Art. 88 EC establishes a system of *ex ante* control for approval, and respectively *ex post* monitoring by the European Commission, of state aid given in the Member States. In particular, Art. 88(3) EC obliges the Member States to:

- notify to the European Commission, for control and approval, any plans to introduce state aid measures or modify the aid measures already approved by the Commission (the *notification obligation*);
- not to implement such measures until the Commission pronounces a decision on their legality (the *stand-still clause*).

The above-mentioned obligations are taken over in Art. 2 of Council Regulation 659/1999 (hereafter “the Procedural Regulation”),<sup>29</sup> which details the procedures relevant in the implementation of Arts. 87-88 EC. According to Art. 1(f) of the Procedural Regulation, state aid measures that are implemented by the Member States in breach of the notification and stand-still obligations will constitute “unlawful aid”. We underline again that the legal concept of “unlawful aid” also covers state aid measures previously approved by the Commission, but modified by the Member States without respecting the notification and stand-still clauses.

The rules applicable to unlawful aid are detailed in Arts. 11-14 of the Procedural Regulation. According to Art. 11, the European Commission is entitled to adopt a series of *interim measures* with respect to unlawful aid, as following:

- order the Member State to suspend the application of unlawful aid measures until the adoption of a decision on their legality (the *suspension injunction* – Art. 11(1));
- order the Member State to recover provisionally from the beneficiary/beneficiaries the aid paid so far on the basis of the unlawful measure (the *provisional recovery injunction* – Art. 11(2)); the provisional recovery order will be put to effect by the Member State in question according to national procedures, similar to the case of putting to effect decisions ordering the recovery of illegal aid (as it will be explained below); the European Commission may adopt a provisional recovery injunctions only when the following conditions are met: i) there are no doubts as to the qualification of the measure in question as involving state aid according to the provisions of Art. 87(3)(1) EC; ii) there are urgent reasons justifying the adoption of such an interim provision; iii) there is a risk that the continuation of the unlawful support measure bring substantial and irreparable damage to the competitors of the beneficiary/beneficiaries.

The Member States that fail to put to effect the interim measures mentioned above breach the obligations assumed under the EC Treaty (Art. 15 of the Procedural Regulation), and the Commission can bring before the European Court of Justice an action for breach of the Treaty obligations against them.

Art. 14 of the Procedural Regulation contains provisions regarding the Commission’s final decisions regarding unlawful aid and their implementation, as following:

- the Commission is empowered to adopt decisions ordering the recovery of illegal aid (*recovery decisions* – Art. 14(1)). **Nota bene**, the Commission cannot order the recovery of illegal aid when such recovery would contradict a principle of Community law (as we shall discuss below, this may be the case in particular circumstances where the beneficiary and/or the public authority that introduced the aid measure are in good faith as to the compatibility of their initiative with Community law);

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<sup>29</sup> See above.

- the aid to be recovered includes the sums paid and the related *interest*, calculated on the basis of a rate indicated by the Commission, covering the period of time from the payment of the illegal aid and until its effective recovery from the beneficiary/beneficiaries (Art. 14(2));
- the recovery of illegal aid is carried out according to national procedures; the Member States shall put to effect without delay the Commission's recovery decisions, according to the provisions of their own legal system, including through the use of interim measures when necessary, while national law provisions that obstacle or delay the immediate recovery of illegal aid should be disapplied.

Art. 15 of the Procedural regulation establishes a *time-limit* for ordering the recovery of illegal aid: the Commission cannot adopt recovery decisions when more than 10 years have elapsed from the date when the aid was paid to the beneficiary/beneficiaries. This time-limit is interrupted by any act of procedure undertaken by the Commission or the Member State regarding the illegal aid in question, and thereafter runs afresh.

We underline that the Commission's recovery decisions are addressed to the Member States, and not to the beneficiary/beneficiaries of illegal aid, and it is therefore for the Member States in question, as addressees of the Commission's decision, to initiate procedures under national law for the recovery of illegal aid.<sup>30</sup> The European Commission is entitled to bring action before the ECJ against Member States that do not fulfil their obligations with respect to putting into effect recovery decisions.

*b. Issues related to the recovery of illegal aid in the EU*

In spite of the availability of comprehensive and apparently effective legal provisions for the recovery of illegal aid, in reality, the recovery of illegal aid has always been one of the weakest points of the EU state aid control system. In essence, there are a number of obstacles to the effective recovery of illegal aid, some of them surging from the conflict of interests at the level of the Member States in question – which, on the one hand are the initiators of the illegal aid measures, and on the other are obliged to put to effect the Commission's recovery decision – and some related to the fact that the Commission's recovery decisions are implemented according to national law – sometimes implying the exhaustion of long internal procedures, or that the beneficiaries of illegal aid invoke principles of national law in order to delay and/or obstacle the recovery procedures.

The Procedural regulation codifies a number of principles and practices that were already established in the case law of the Commission and the ECJ, whereas there are few novelties in terms of Community instruments for removing national law obstacles to recovery. For example, the fact that the Procedural Regulation confirms (at Art. 11) the Commission's power to issue interim recovery injunctions has in practice a very limited impact, as long as the same Regulation imposes conditions that limit the Commission's possibility to adopt such injunctions (see above).<sup>31</sup> Moreover, in the Commission's initial draft of the Procedural Regulation, Art. 14 contained a provision suspending the applicability of national provisions that delayed the recovery of illegal aid. This provision was eliminated by the Member States from the final

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<sup>30</sup> In *Boussac*, the ECJ established that a Commission decision ordering the recovery of illegal aid is in itself a valid legal instrument for the actual recovery of the aid, meaning that it does not have to be transposed into a decision by a national court to the same effect (Case C-301/87 *France v Commission (Boussac)* [1990] ECR I-307).

<sup>31</sup> For a detailed analysis of the procedural Regulation and a commentary on its adoption, see Annida Sinnavee (1999): "State aid procedures: the reform project", in S. Bilal and P. Nicolaidis, eds., [\*Understanding State Aid Policy in the European Community: Perspectives on Rules and Practice\*](#), Maastricht: EIPA, pp. 209-230.

version of Art. 14 (during negotiations at the Council), for being assimilated in practice to a harmonization of national procedures. As a consequence, the only “guarantee” offered by the Procedural Regulation for the recovery of illegal aid without delay is given by Art. 14(3): “[...] recovery shall be enforced without delay and in accordance with the procedures under the national law of the Member State concerned, provided that they allow the immediate and effective execution of the Commission’s decision.” This rather indirect formulation appears to be a weaker Community law “guarantee” than, for example, a direct formulation in the sense that national law provisions impeding the immediate and effective recovery of illegal aid must be disapplied.

The record in the EU shows that, in practice, most times the timely and effective recovery of illegal aid is impeded either by the fact that the beneficiaries of illegal aid invoke as defence some principle of national law, such as *the principle of legitimate expectations*, or by the fact that the recovery of illegal aid granted to firms in difficulty is blocked by *national bankruptcy proceedings*.<sup>32</sup>

The principle of legitimate expectations is available - with different terminologies - in most national legal systems, as well as in Community law. Its purpose is to defend subjects of the law that are in good faith against the legal consequences of acts that they are not responsible for. In cases related to the recovery of illegal aid, the principle of legitimate expectations has a double applicability: it may be invoked by the beneficiaries of illegal aid as a defence against the Member State that has granted the aid in the first place, or it may be invoked by the member States themselves against the European Commission, in the course of actions before the European Court of Justice to annul the Commission’s recovery decisions.

We must mention that, even before the adoption of the Procedural Regulation, the case law of the ECJ has substantially restricted the applicability of the principle of legitimate expectations as a defence in proceedings regarding the recovery of illegal aid. The ECJ case law establishes in particular that:

- EC law obliges the Member State to annul administrative acts on the basis of which illegal aid has been granted and to recover the aid given, “even when the state authorities are responsible for the illegality of the aid in question, and the annulment of the administrative act on the basis of which the aid was granted appears to be in breach of the principle of legitimate expectations, as well as when principle of national law would exclude the recovery of the illegal aid on grounds that there is no unjustified enrichment, and the beneficiaries did not act in bad faith.”<sup>33</sup>
- Given the mandatory nature of Community rules on the notification and approval of aid, the general rule is that the beneficiaries of illegal state aid cannot have legitimate expectations with respect to the legality of the measure in question unless the notification procedure has been carried out. Moreover, according to well-established principles of Community law, a diligent behaviour by an undertaking implies verifying whether the notification procedure has been carried out with respect to the aid received.<sup>34</sup>

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<sup>32</sup> For further details on this subject, see various issues of the State Aid Scoreboard, available on DG COMP’s website ([http://europa.eu.int/comm/competition/state\\_aid/scoreboard](http://europa.eu.int/comm/competition/state_aid/scoreboard)), as well as the Report on the application of EC state aid rules by Member State courts ([http://europa.eu.int/comm/competition/state\\_aid/legislation/app\\_by\\_member\\_states](http://europa.eu.int/comm/competition/state_aid/legislation/app_by_member_states)).

<sup>33</sup> Case 24/95 *Land Rheinland Pfalz v Alcan Deutschland* [1989] ECR 175 (Alcan II).

<sup>34</sup> Case C-5/89 *Commission v Germany* [1990] ECR I-3437, Case C-24/95 *Alcan Deutschland* [1997] ECR I-1591, Case 265/85 *Van der Bergh en Jurgens BV* [1987] ECR 1115, Case T-55/99 *Confederación Española de Transporte Mercancías (CETM) v Commission* [2000] ECR II-0000.



- by derogation from the general principles mentioned above, EC case law admits that *in exceptional circumstances* the beneficiaries of illegal aid may have legitimate expectations as to the legality of the aid received.<sup>35</sup> The case law does not define very clearly what circumstances may be considered as “exceptional” in this sense. However, given that the principle of legitimate expectations cannot be invoked by the beneficiaries who have not inquired whether the notification procedures were carried out, it becomes clear that the cases where such “exceptional circumstances” will be considered to be met are quite rare. One of such examples is a case dating from 1987, when state aid was given on the basis of a scheme already approved by the Commission, successively modified by the authorities of the Member State in question, and where the modifications have also been notified to the Commission; in this case, the Commission has taken a decision on the legality of the notified modifications only 26 later, while the public authorities have in the meantime implemented them.<sup>36</sup> Another example, where circumstances are different, but still relevant to this context, is that of cases in which the Commission modifies its initial position as to the legality of a given support measure. For instance, in *Irish Corporate Tax*,<sup>37</sup> the Commission asked the Irish authorities to modify for the future the act establishing the base corporate tax rate for the manufacturing industry at 10%. This act has been notified to the Commission on two occasions, in 1980 and in 1990, and on both occasions the Commission had decided that the measure did not involve elements of state aid. However, following the publication of the Notice on fiscal aid,<sup>38</sup> the Commission re-evaluated this act and found that it had a selective nature, to the extent that the low tax rate base in question was applicable to the manufacturing industry only, and moreover, the aid granted to the manufacturing industry on its basis was qualified as (illegal) operating aid. Taking into consideration however the legitimate expectations created on the basis of the Commission’s previous decisions on the act, the case was settled with the Irish government by agreeing on a progressive future adjustment of the tax rate base to a commonly agreed level.
- We also underline that the “*exceptional circumstances*” mentioned above *may be invoked only before national courts*, in the course of proceedings related to the recovery of illegal aid (in other words, such circumstances cannot be invoked in the course of actions for the annulment of Commission recovery decisions brought by the Member States before the ECJ).<sup>39</sup> Also, the principle of legitimate expectations may be invoked only by the beneficiaries of the illegal aid, and not by the Member State in question, as a defence in the course of an action brought by the Commission before the ECJ for the breach of Community obligations resulting for not putting to effect the recovery decision.<sup>40</sup>

Bankruptcy of the aid beneficiaries. The restrictions imposed by the ECJ case law on the application of the principle of legitimate expectations in the course of procedures for the recovery of illegal aid, together with the codification of the recovery procedures through the

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<sup>35</sup> Case C-5/89 *Commission v Germany* [1990] ECR I-3437, Case C-183/91 *Commission v Greece* [1993] ECR I-3131.

<sup>36</sup> Case 223/85 *Rijn-Schelde-Berolme (RSV) Machinefabrieken en Scheepswerven NV v Commission* [1997] ECR 4618.

<sup>37</sup> European Commission, State Aid Decision E/2/1998 Ireland, OJ C 395 of 18.12.1998, pp. 0019-0023.

<sup>38</sup> European Commission (1998: *Notice on the application of the state aid rules to measures relating to direct business taxation*, OJ C 384 of 10.12.1998.

<sup>39</sup> Case T-459/93 *Siemens v Commission* [1995] ECR II-1675, Case T-67/94 *Ladbroke v Commission* [1998] ECR II-1.

<sup>40</sup> Joined Cases 205/82 to 215/82 *Deutsche Milchkontor v Germany* [1983] ECR 2633.

adoption of the Procedural Regulation, have made that, at present, the most significant obstacle to recovery be national procedures related to the bankruptcy of the aid beneficiaries. According to the latest *Scoreboard* published by the Commission,<sup>41</sup> one third of the recovery cases pending on the Commission's role is related to companies in difficulty that follow bankruptcy procedures.<sup>42</sup> In the absence of EC provisions on bankruptcy, most Member States have recently introduced bankruptcy laws inspired from the US model, which temporarily shield the companies undergoing such a procedure against the creditors, the state comprised (including when the debt is related to the recovery of aid received illegally). The legal problems that arise when recovery procedures meet bankruptcy procedures are quite complex, and furthermore, there are notable differences in this respect between the legal systems of the Member States, so that the Commission recently created a special unit at DG Competition trusted with examining them. IN what follows, we briefly mention the most important issues that have surfaced so far:

- when the recovery of illegal aid takes place in the framework of a bankruptcy procedure involving the beneficiary, the actual recovery is delayed, but the member State can argue that it has fulfilled its obligation of putting to effect the Commission's recovery decision by registering among the creditors of the bankrupt firm.
- Member States may invoke national provisions regarding bankruptcy which do not allow the recovery of interest on the illegal aid starting with the date of filing for bankruptcy.<sup>43</sup>
- Considering what has been mentioned before about the restricted applicability of the legitimate expectation principle in recovery cases, nowadays the only valid defence that a Member State may invoke in order to avoid putting into effect a recovering order from the Commission is the so-called "absolute impossibility".<sup>44</sup> ECJ case law establishes, however, that when a member State faces difficulties in carrying out a recovery order in time (meaning by the date imposed by the Commission in its decision), it must inform the Commission of these difficulties and discuss with it alternative ways to proceed. This means that the absolute impossibility defence cannot be invoked if the Member State in question cannot demonstrate that it has informed the Commission in time of the difficulties met, and sought to find acceptable alternative solutions.

We should add that, whenever the illegal aid was granted to several beneficiaries on the basis of an aid scheme, and particularly when the illegal aid was granted in the form of fiscal facilities, the problems related to the recovery of the illegal aid from the beneficiaries only multiply. One additional problem is identifying all the beneficiaries who benefited from the illegal scheme; moreover, it may happen that one and the same scheme involve illegal aid to certain beneficiaries, while the aid to others be compatible with the EC rules (for example, one could be imagine a scheme offering fiscal facilities to investors, whereby the amount of aid granted to large investment projects exceeds the maximum intensity ceilings imposed by EU regulation, whereas the aid granted to "normal" investment projects be within the permissible limits.

Finally, we need to mention that *de minimis* aid (totalling under 100 000 Euro) is deducted from the amount to be recovered from the beneficiaries of illegal aid.

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<sup>41</sup> (2004) 256 final, 20.04.2004 – see *supra* note no. 35.

<sup>42</sup> At the same time, it is also true that some companies' decision to file for bankruptcy was prompted by the carrying out of Commission orders regarding the recovery of illegal aid – see, for example, East German companies such as *Groditzter Stahlwerke*, *System Microelectronic Innovation*, *CDA Compact Disc Albrechts și Erba LAutex*.

<sup>43</sup> Case C-480/99 *Spain v Commission (Magefesa I)*, judgment of the Court of 12 october 2000.

<sup>44</sup> Case C-348/93 *Commission v Italy* [1995] ECR I-673, Case C-261/99 *Commission v France* [2001] ECR I-2537, Case C-499/99 *Commission v Spain (Magefesa II)*, judgment of 2 July 2002.

## CHAPTER 2.

### STEEL

#### 2.1. The EU legal framework for the control of state aid to the steel sector

Due to the strategic importance of this sector for the European economy, steel was subject to specific rules from the establishment of the European Communities. The ECSC Treaty laid the foundations for an European internal market of steel and coal. Indeed, although Art. 4 of the ECSC Treaty prohibited state aid to the steel and coal sectors, in whatever form, in reality these sectors were among the most subsidised throughout the early history of the European Communities.

The structural crisis that affected the steel sector in the 1970s and 1980s brought about a subsidy war among the Member States, which were facing serious economic and social problems in the attempt to restructure an industry that has traditionally been concentrated in certain regions of Europe and employed a large number of workers (hundreds of thousands at the beginning of the 1970s). In the attempt to bring under control the subsidy levels and to promote a coordinated restructuring process in the member States, the European Community adopted successively a number of special regulations on state aid to the steel sector, also known as “the Steel Aid Codes”. The first signs of success in the restructuring process showed after the implementation of the second Steel Aid Code (1981), which conditioned the approval of state aid upon reductions of excess production capacities. The latter were for the most part eliminated during the first half of the 1980s, so that, during the period 1985-1991, the Community returned to the regime originally intended for state aid to this sector – a general ban on state aid in whatever form, except for limited aid awards, destined to support R&D and environmental protection projects in the industry, the closure of production plants or investment in the disadvantaged regions of East Germany, Greece and Portugal.

In spite of the long restructuring process, at the beginning of the 1990s the European steel producers were affected by a new structural crisis, determined by the drop of prices at the international level. The European Commission proposed to the interested Member States a plan to coordinate further reductions of excessive production capacities, whose costs were proposed to be co-financed by the EC in the form of compensations for the workers who lost their jobs. This plan did not find the acceptance of the Member States, who sustained instead the ward of individual aid to companies in difficulty. In December 1993 the European Commission exceptionally approved such individual aid measures (on the basis of Art. 95 ECSC) for six steel producers from East Germany, Italy, Spain and Portugal, to be followed by an additional case involving an Irish steel company in 1995. These individual aid measures were approved upon strict conditions concerning the reduction of excess production capacities. The Commission was empowered to monitor regularly the implementation of the approved restructuring plans.

Following an analysis of the sector over the period 1993-1994,<sup>45</sup> the Commission found that the Member States’ efforts to reduce excess production capacities have been insufficient, and even proposed to suspend Community aid to some of the restructuring plans (involving aid to compensate the social costs of restructuring, and commercial protection measures towards imports from third countries). Therefore the last Steel Aid Code (1996),<sup>46</sup> covering the period

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<sup>45</sup> European Commission (1994): *Fresh Impetus for Restructuring the Steel Industry*, COM(94)265; European Commission (1994): *Restructuring the Community Steel Industry: Final Assessment and Conclusions*, COM(94)466.

<sup>46</sup> *Decision No. 2496/96/ECSC of 18 December 1996 establishing Community Rules for State Aid to the Steel Industry* (Sixth Steel Aid Code), OJ L 338 din 18.12.1996, p. 42-47.

1997-2002 (until expiry of the ECSC Treaty), introduced a tighter discipline with respect to state aid for the steel sector, allowing in practice only the granting of R&D, environmental protection and closure aid.<sup>47</sup>

Following the expiry of the ECSC Treaty (23 July 2002), the steel sector becomes subject to the general rules on state aid contained in Arts. 87-88 EC and the secondary legislation developed in their application. However, in a 1999 Communication to the Council and the European parliament on the state of competitiveness of EU steel,<sup>48</sup> the Commission stressed that it was important to maintain a strict discipline on state aid given in this sector even after the expiry of the ECSC Treaty, so as to safeguard the outcomes of the previous restructuring efforts.

In March 2002, the Commission published a Communication on aid to steel firms in difficulty,<sup>49</sup> which prohibits rescue and restructuring aid to steel companies, no matter in what form (the steel sector is defined in Annex B to the Multisectoral Framework on regional aid to large investment projects<sup>50</sup>).

The same Communication reminds that regional aid to companies in this sector is also prohibited, according to the special provisions in this sense contained in the Multisectoral Framework.<sup>51</sup> This prohibition does not apply only to regional aid for large investment projects undertaken by regular or large companies (i.e., projects whose cost exceeds 50 million Euro or totalling more than 5 million Euro), but also to large investment projects undertaken by SMEs - as defined in Art. 6 of Regulation 70/2001 on state aid to SMEs.<sup>52</sup> In other words, regional aid to SMEs in the steel sector cannot be awarded beyond the following limits imposed through EC regulation:

- when the overall cost of the investment project exceeds 25 million Euro, the intensity of the proposed aid (net grant equivalent) should respect the following conditions: i) it cannot exceed 50% of the regional aid ceiling applicable at the location of the project; ii) it cannot exceed 15% of the total cost of the investment project for small enterprises, respectively higher than 7.5% for medium-sized enterprises. Also,
- the total aid awarded to SMEs (gross) cannot exceed 15 million Euro.

We underline that, except for cases meeting the circumstances described above, SMEs operating in the steel sector can receive regional aid according to the conditions established in Regulation 270/2001, namely, up to a maximum intensity of 15% of the overall cost of the investment project for small enterprises, respectively up to 7.5% of the overall cost of the investment project for medium-sized enterprises.

The conditions discussed above apply to individual (ad hoc) state aid measures as well as to aid awarded on the basis of a scheme. In other words, translating these conditions to the case of Romania, a transposition of the conditions laid down in Regulation 70/2001 into the Romania legislation would imply that companies operating in the Romanian steel sector (except for SMEs,

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<sup>47</sup> For a historic overview of the Steel Aid Codes and their application, see Alexander Schaub (1997): "State Aid in the ECSC Steel Sector", *EC Competition Policy Newsletter* vol. 3, no. 2; European Parliament Factsheets 4.7.2. *Steel Industry*, available at [http://www.europarl.eu.int/factsheets/4\\_7\\_2\\_en.htm](http://www.europarl.eu.int/factsheets/4_7_2_en.htm); see also Communication from the Commission to the Council, the European parliament and the ECSC Consultative Committee (1999): *The State of Competitiveness of the Steel Industry in the EU*, COM(1999) 453 final.

<sup>48</sup> See *supra* note no. 50.

<sup>49</sup> European Commission (2002): *Communication on Rescue and Restructuring Aid and Closure Aid for the Steel Sector*, OJ C 70 din 19.3.2002.

<sup>50</sup> See European Commission (2002): *Multisectoral framework on regional aid to large investment projects*, OJ C 70 din 19.3.2002 (amended version).

<sup>51</sup> See Point 4 para. 27 of the Multisectoral Framework, *supra* note no. 53.

<sup>52</sup> *Commission Regulation (EC) No 70/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to State aid to small and medium-sized enterprises*, OJ L 10 din 13.01.2001.

as mentioned above) cannot benefit from the fiscal facilities available in the assisted regions, or from rescue and restructuring aid under the schemes applicable in the industrial decline areas.

The Commission's Communication of March 2002 (applicable until 31<sup>st</sup> December 2009) established the conditions for the award of closure aid to companies in the steel sector. This may take the following forms:

- i. compensations for early retirement and for workers losing their jobs may be granted if the following conditions are met:
  - o the steel company about to be closed should not have received itself aid for the same purposes;
  - o individual payments should not exceed the amounts usually paid in other sectors for the same purposes;
  - o the overall proportion of aid in the compensation awarded should not exceed 50%.
- ii. aid for steel firms permanently closing their production activity may be awarded to firms meeting the following conditions:
  - o registration as a steel company before the 1<sup>st</sup> of January 2002;
  - o proof of regular steel production before the date of application for aid;
  - o not having undertaken restructuring or the modernization of production after the 1<sup>st</sup> of January 2002;
  - o production units must be closed and disassembled in maximum 6 months from the discontinuation of production or the approval of closure aid;
  - o should not have benefited from previous closure aid;
  - o the overall closure aid awarded should not exceed the residual booking value of the production plant about to be closed
- iii. if the steel firms permanently closing their production activity (as in ii) above) are owned or controlled by other steel companies, or in their turn own or control other steel companies, the aid related to closure may be granted only if the following conditions are met:
  - o the firm about to be closed be legally and effectively separated from the firm in control or controlled by it at least 6 months before the award of aid;
  - o the books of the firm about to be closed be checked by an independent accountant appointed by the Commission
  - o closure of production at the beneficiary firm brings about a real and quantifiable benefit in terms of the overall reduction of excess production capacities at the level of the whole sector, whose effects would be lasting for at least 5 years after the award of aid.

In addition to closure aid and regional aid for SMEs, the firms operating in the steel sector may also receive state aid for the following objectives:

- R&D (according to the conditions established in the Community Framework on state aid for R&D);<sup>53</sup>

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<sup>53</sup> European Commission (1996): *Community Framework for State Aid for Research and Development*, OJ C 45 of 17.2.1996.

- environmental protection (according to the conditions stipulated in the Commission guidelines applicable to this type of aid);<sup>54</sup>
- employment aid (according to Regulation 2204/2002);<sup>55</sup>
- training aid (according to Regulation 68/2001);<sup>56</sup>
- de minimis aid (or aid totalling less than 100 000 Euro over a period of 3 years - according to Regulation 69/2001).<sup>57</sup>

In what follows we summarize the conditions under which each of the above-mentioned types of aid may be awarded in the steel sector, as resulting from the mentioned regulations.

R&D aid: the European Commission traditionally had a favourable view of this type of aid, whose effects are in principle positive and less distorting than in other case of aid. At the same time, the Commission seeks to encourage the member States towards indirect forms of support for this type of investment (including, for example, fiscal facilities), as a modality to stimulate private investment in R&D and increase Europe's competitiveness in this sector.

In principle, the Commission considers that the distorting potential of R&D is directly proportional to its closeness to the market for its final products. From this perspective, R&D projects are classified into three main categories:

- fundamental research – defined as research oriented towards broadening the technical and scientific knowledge base, and which is not linked to industrial or commercial activities;
- industrial research – defined as the research oriented towards obtaining the know-how for the making of new products, or new production processes and services, or for improving them;
- pro-competitive development – defined as the process of transforming the results of an industrial research project into a new or modified production process, as well as the conceptual design of new products, to the extent that all such projects cannot be used directly for commercial purposes.<sup>58</sup>

Public financing of independent research carried out by non-profit organisations or universities (public or private), to the extent that its results are accessible on an equal basis to all potential beneficiaries, does not constitute state aid.

The Community Framework on R&D aid establishes maximum intensity ceilings for each of the categories of aid mentioned above:

Research categories	Maximum aid intensity ceilings (as % of the overall cost of the project)
Fundamental research	100%
Industrial Research	50%

<sup>54</sup> European Commission (2001): *Community Guidelines on State Aid for Environmental Protection*, OJ C 37 of 3.2.2001, pp. 315.

<sup>55</sup> *Commission Regulation (EC) No 2204/2002 of 12 December 2002 on the application of Articles 87 and 88 of the EC Treaty to State aid for employment*, OJ L 337 of 13.12.2002, p. 3-14.

<sup>56</sup> *Commission Regulation Nr. 68/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to training aid*, OJ L 10 of 13.1.2001, p. 20-29.

<sup>57</sup> *Commission Regulation (EC) No 69/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to de minimis aid*, OJ L 10 of 13.1.2001, p. 30-32.

<sup>58</sup> See Annex II to the Community Framework for R&D aid, *op. cit.*, and in particular footnote no. 32.

	(up to max. 75% if suppl. bonuses applicable)
Pro-competitive development	25% (up to max. 50% if suppl. bonuses applicable)
<b>Bonuses</b>	
SMES	10%
R&D project is carried out in an assisted region covered by Art. 87(3)(a) EC	10%
R&D project is carried out in an assisted region covered by Art. 87(3)(c) TEC	5%
Research is part of a Framework program financed by the EU	15%
Same as above, plus it involves cooperation among research institutions from at least two member States	25% (maxim)
Research involves cooperation among institutions from at least two Member States	10%

The above-mentioned ceilings must be respected no matter in what form the aid is awarded. Thus, when R&D aid is granted in indirect forms (such as for example fiscal facilities or state guarantees for loans from commercial banks), the public institutions implementing the aid measure are obliged to submit to the Commission all information necessary for the calculation of the overall amount of the aid awarded on their basis. Finally, aid awarded under schemes already approved by the Commission does not have to be notified for approval when disbursed to each individual beneficiary, except for cases where the overall cost of the aided project is over 25 million Euro, and the total amount of is proposed to be given is over 5 million Euro.

Environmental aid: Art. 6 EC establishes that environmental protection considerations must be taken into account in the shaping and implementation of all Community policies, including competition and state aid control.

Until the beginning of the 1990s, EC policy on environmental protection was mainly of a “corrective intervention” nature, being limited to the adoption of common standards for the protection of the environment and the financial support of measures destined to meet them. Starting with the last decade, however, the EU adopted a new, more dynamic approach, combining objectives of sustainable economic development with the objective of improving the quality of the environment. The new strategy recognises the important role played by incentives to improve environmental protection, but at the same time underlines the necessity that undertakings assume more responsibility in this respect. Thus, Art. 174 EC establishes that the “polluter pays principle”, according to which the costs of measures destined to reduce pollution should be borne by the undertakings responsible for it, must be taken into account in the implementation of all EC policies, including competition and state aid control. The ‘polluter pays’ principle is complemented by the ‘cost internalization’ principle, according to which the costs related to environmental protection must be reflected in the production costs of undertakings and in the price of their products.

In the 1994 version of the Guidelines on state aid for environmental protection, the Commission shows that, to the extent that environmental aid allows to the undertakings to artificially reduce their production costs, such aid is in contradictions with the polluter pays and

cost internalization principles established by Community law. However, the Commission takes a permissive view to such aid when granted in certain circumstances, such as:

- when the beneficiaries are unable to internalize all costs related to meeting the applicable standards of environmental protection, environmental aid may constitute an incentive to adapt to the new standards;
- when environmental aid is an incentive for the undertakings to apply higher environmental protection standards or reduce pollution further than required.

The 2001 amendment of the Guidelines<sup>59</sup> introduces a stricter approach to environmental aid. Underlying that the EU undertakings were allowed a period of 7 years (1994-2001) in order to adapt to the implications of the polluter pays and cost internalization principles, the Commission establishes that, for the future, the undertakings will have to respect them in full, and therefore aid destined to support investment for meeting environmental standards is no longer justified. By exception from this rule, the Guidelines allow:

a. investment aid related to meeting environmental protection standards, in particular:

- considering the difficulties met by SMEs in obtaining loans from the commercial banks, they will be allowed to receive environmental aid for a period of maximum 3 years after the introduction of new environmental protection standards;
- all undertakings may receive aid for meeting higher environmental standards than those established at the EU level, or in the absence of EC environmental protection standards;
- all undertakings may receive aid related to energy saving, the combined production of electricity and thermal energy, and for promoting the production of energy from alternative sources.

The maximum intensity ceilings applicable to the above circumstances are as follows:

<b>Beneficiaries</b>	<b>Maximum intensity ceiling (as % of the overall cost of the project)</b>	<b>Ceiling applicable to projects carried out in assisted regions covered by Art. 87(3)(a) EC</b>	<b>Ceiling applicable to projects carried out in assisted regions covered by Art. 87(3)(c) EC</b>
SMEs	15% (gross)	15+10% (gross) <i>or</i> the regional ceiling applicable to investment aid + 10%(gross)*	15+5% (gross) <i>or</i> the regional ceiling applicable to investment aid + 10% (gross)*
Projects for meeting higher environmental standards than those imposed at the EU level, or in the absence	30% (gross) + 10% bonus for SMEs	30+10% <i>or</i> the regional ceiling applicable to	30 + 5% (gross) <i>or</i> the regional ceiling applicable to

<sup>59</sup> European Commission (2001): *Community Guidelines on State Aid for Environmental Protection*, OJ C 37 of 3.2.2001, pp. 315.



of the latest		investment aid + 10%(gross)*	investment aid + 10%(gross)*
For investments linked to the decrease of energy consumption	40% + 10% bonus for SMEs		

\* to apply the higher ceiling.

In relation to all above, the costs that are eligible for aid should be understood to cover investment in the purchase of land necessary for environmental projects, buildings, equipment, installations meant to reduce pollution, production units that are less polluting, etc. The purchase of intangible goods, such as licenses for the use of products or methods, patents and know-how, may also be included in the definition of eligible costs, under the following conditions: i) the licenses and patents in question should be classified as depreciable; ii) the purchase price must be at the market level, from firms that have no corporate connection to the aid beneficiaries; iii) these purchases must be included on the firms' balance sheet and used for a minimum of 5 years.

Moreover, the above-mentioned ceilings apply to the part of the cost of investment that is strictly related to environmental objectives. For example, in the case of aid to meet stricter environmental standards than those established at the EU level, the aid intensity is calculated starting from the difference between the cost of the aided project and the cost of the project had it been undertaken to meet the EU standards only.

b. aid for the rehabilitation of polluted industrial sites, to the extent that the operation is carried out by a different undertaking than the one responsible for the pollution, while the latter cannot be identified or is in impossibility to cover these costs.

c. aid for the relocation of undertakings for environmental policy considerations (for example, the relocation of polluting production plants from the urban outskirts, etc.)

d. aid for covering the costs of consultancy on environmental protection themes, for SMEs.

e. operating aid (which is, as a general rule, prohibited throughout the EU, except when granted in certain circumstances in assisted regions covered by the provisions of Art. 87(3)(a) EC) linked to: i) the management of industrial waste; ii) the reduction of energy consumption. Such aid may be granted for a maximum period of 5 years, starting from an initial aid intensity of 100%, on condition that the intensity be progressively reduced every year, or may be awarded for longer than 5-year periods if not exceeding 50% of the costs of the aided project.

Finally, a few remarks about environmental aid in the form of reducing environmental taxes: such fiscal facilities are qualified in Community law as operating aid, and will be allowed only in exceptional circumstances: i) when the general taxation scheme in relation to which the facilities apply has as a purpose to meet higher environmental protection standards than those agreed at the EC level (and in which case the undertakings need a period of time to adjust to the stricter standards); ii) the general taxation measure to which the facilities relate does apply the common environmental protection standards agreed at the level of the EU, yet Community regulation allows temporary derogations for adjustment to the new standards.

## 2.2. State aid to the steel industry

### **2.2.1. Reasons for granting state aid to the steel industry**

European steel subsidies re-emerged in the 1970s and early 1980s, because of a deteriorating steel market, massive overcapacity, many uncompetitive European mills and the high labour-intensive characteristics of the European industry. Like US steelmakers at that time, the European industry was faced with restructuring to survive, but in Europe the national governments participated more directly in the process.<sup>60</sup>

In the 1970s, many European governments spent considerably for covering the state-owned firms' losses, rather than shutting down inefficient plants. Later, as the governments sought to put an end to the losses and privatize the steel plants, debt was forgiven and fresh aid was injected to help pay for plant closures that should have been made years earlier.

In the US, the restructuring process was relatively swift, but painful for the industry. Between 1974 and 1990, dozens of mills were closed, the raw-steelmaking capacity dropped by 35% (65 million annual net tons), and employment fell by 68%, as shown by Roger Ahlbrandt and Frank Giarratani in a 1992 study for the Sloan Foundation. The costs for restructuring were borne by workers, private investors, and the bank system, with little assistance from the state or federal taxpayers.

In Europe, taxpayers partly funded the restructuring, but this process has been slower and less effective than in the US. Politics dragged on the process and even spread the pain to more capable competitors. The number of jobs in the industry decreased by 57% during the period 1974-90, while the production capacity dropped by only 19% (38 million tons per year). Because of the slower restructuring in Europe, capacity utilization improved by only 71-75% over the period 1988-90, as compared with 85-89% in the US.

The European governments paid subsidies in the 1970s, even though the European Coal and Steel Community Treaty (ECSC) prohibited them.

As a result of the deep restructuring, the US steel industry started to expand again. In Europe, the overcapacity persisted, at a minimum 13-15 million tons in the middle of the 1990.

In the 1970s, the share of public ownership in the European steel industry was increasing. It was not always clear if state equity infusions and other financial assistance were based on political or economic considerations. "It became clear that a number of governments had gone over the mark" and were propping up loss-making mills for political reasons, says a source in the European industry. "That is when the Commission [of the EEC] stepped in and said, 'We have to put a structure in place to get it under control'. We had a Treaty that said subsidies can't happen, but they were happening".

The uncertainties related to the legality of state aids and their distorting impact on competition motivated the periodical interventions of the European Commission to discipline aid expenditure for this sector *via* the adoption and implementation of special rules, known as "State Aid Codes". In 1981 the Commission adopted the first Steel Aid Code, legalizing some of the subsidies and putting limits and conditions of their awarding. The ECSC Treaty prohibited subsidies to steel, but the Treaty of Rome permitted subsidies that did not distort intra-community trade in other sectors. The Steel Aid Code thus brought the rules for steel in line with the rules for competing industries, such as aluminium.

At the beginning of 1990s, after the second structural crisis of the European steel industry, the Commission proposed to the Member States a plan aiming at coordinated reduction

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<sup>60</sup> Source: New Steel, "The decline in European Subsidies", John Schriefer, June 1997.

of the excess production capacities, through Community co-financing the social assistance to dismissed steelworkers.

The plan was however rejected by the Member States, who solicited the approval of individual state aid to help restructuring their companies in difficulty. In December 1993, the Council approved by way of exception a series of individual aids for restructuring, directed to 6 companies from Eastern Germany, Italy, Spain and Portugal and, in 1995, for an Irish company. In return, the beneficiary steelmakers would reduce their annual production capacity.

After finding that the production capacity reduction plans negotiated with the Member States were not properly carried out, the European Commission decided to withdraw some of the measures to support the restructuring process (comprising Community aid to co-finance the compensations related to the restructuring process, protective commercial measures against steel imports from third countries, production against the third countries imports). As a result, the last “Steel Aid Code”, covering the 1997-2002 period (until the expiry of the ECSC Treaty), returned to a tighter state aid discipline.

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In the Summer of 2001, the world’s leading steel companies, through the International Iron & Steel Institute (IISI), issued a common call to governments for concluding a multilateral steel agreement.

The companies are in agreement that the present financial problems of the industry result from excess production capacity. They call for a rapid and positive response by the governments of the major steel producing nations to the proposal made on 5 June 2001 by the US for multi-lateral negotiations on the: elimination of inefficient excess steel capacity, rules that will govern steel trade in the future, the ways to strengthen multilateral discipline on government measures and industry practices that distort markets and ultimately contribute to global overcapacity.

All major OECD and non-OECD steel-producing countries are involved in these negotiations, which, starting with 2002, have made rapid progress, although there are still different views as for the regime to be applied to state aid. Despite a general consensus on the proposal that the agreement should include a prohibition on steel subsidies (the US called for the total elimination of steel subsidies), the EU countries insist for several narrowly defined exceptions on aid for R&D and environment.

### **2.3.2. Dynamics, amount, structure of state aids in EU countries**

Over the period 1980-1985, the European Commission (EC) approved 37 billion USD in steel subsidies by the Member states (see table below). More than half of this total was destined to cover the losses of failing companies.<sup>61</sup>

#### **European Commission – approved steel subsidies by country, 1980-1985**

- billion of dollars –

Country	Amount
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<sup>61</sup> The decline in European subsidies”, John Schriefer, Pittsburg Editor, New Steel, June 1997.

Belgium	4.21
Denmark	0.08
Germany	3.80
France	9.04
Ireland	0.26
Italy	13.33
Luxembourg	0.62
Netherlands	0.45
Great Britain	5.58
<b>EU Total</b>	<b>37.37</b>

Source: Thomas Howell et al, *Steel and the State „New Steel”*, June 1997.

Italy, France and Germany “captured” the greatest share of the public funds allocated to the steel industry as state aid during the 1980-1985 period. The structure of the state aid expenditure during the above-mentioned period was the following:

#### Structure of state aids, granted to the European steel industry in 1980-1985

- billion US dollars -

Type of aid	Amount	Objective
Grants	6.94	Investments
Loans	21.91	R & D
Debt conversions	1.72	Closures
Low interest loans	3.46	Continued operations
Loan guarantees	3.47	Emergency
Other	0.07	
<b>Total</b>	<b>37.37</b>	

Source: Roger Ahlbrandt and Frank Giarrantani, „*The EC, Responding to the Crises in the Global Steel Industry*”, 1987.

*Loans* (many of which later turned into forgiven debts), *loan guarantees*, and *the conversion of debt to capital* accounted for a great part of the 37 billion USD. Therefore the net level of subsidization is uncertain. Also, this tally does not include subsidies granted in breach of the Aid Code by regional governments. Subsidies authorized by the EU are not the only subsidies granted in practice. In a series of countervailing-duty cases filed against European carbon and speciality producers since 1992, US steelmakers alleged that the Europeans had received subsidized loans, tax exemptions, grants, and other forms of state aid not covered by the EU Steel Aid Code, which injured the US industry.

In the early 1980s, when demand and production were at their lowest, the Commission also implemented a temporary quota system and minimum pricing policy for the Community steel producers in the attempt to stabilize the market. The quota system ended in 1988.

**The benefits of these actions were questionable. By propping up the less productive steel companies or plants thereof and constraining the ability of the more efficient**

producers to expand, the policies of the European Commission may have inadvertently disadvantaged the most productive portion of the European steel industry, (Ahlbrandt and Giarrantani)<sup>62</sup>.

The State Aid Code was more politically acceptable than an outright termination of state assistance – which probably couldn't have been enforced.

During the 1980s the EC Member States were not prepared to permit a restructuring process dictated wholly by the market. Governments would not take the political risks of closing mills and firing workers. The Aid Code contained a kind of “permission” to grant subsidies: governments could give aid to restructure the industry at the condition to ensure that future aid would be unnecessary.

The Commission approved the last major aid-granting operations in 1994. In April 1994, the Commission authorized aid totalling about 8.3 billion USD to 6 (six) steelmakers, according to a Commission report on steel aid (see table 3 below). In return, the steelmakers would reduce annual capacity by 5.4 million tons and employment by about 36,000 people by the end of 1996.

#### State aid granted in the EC Member States in 1994

Company/Country	Amount Billion \$	Capacity reductions	Worker layoffs
CSI (Spain)	3.345	3.7 mtpy - steel 2.3 mt/year - iron 2.3 mtpy - hot band	1037
Sidenor ( Spain)	718	0.5 mtpy – steel 379,000 tpy-hot band	2593
Ilva (Italy)	2.905	2 mtpy – hot – rolled	115000
Siderurgia National (Portugal)	383	140,000 tpy – sections	1583
EKO Stahl (Germany)	746	360,000 t/y – sections/plate	8800
SEW Freital (Germany)	186	160,000 t/y – sections	1060

Source: EC, Monitoring of Art. 5 ECSC steel aid cases, Fifth Report, May 1996.

Rather than fresh cash injections, a large amount of the approved aid consisted of forgiving debt stemming from past loans and the transfer of state-owned assets to new corporate entities. Two of these recent aid cases – *Ilva* in Italy and *Eko Stahl* in East Germany – shed light on the subsidisation patterns and the role of aid in promoting restructuring.

The Italian government provided large equity infusions to the state-owned steel sector since the 1970s, including restructuring assistance during 1988-89. Despite having received aid previously, the Ilva Group – a steel conglomerate with more than 11 million metric tons of raw-steelmaking capacity in 1992 – was still struggling. In the early 1990s, the Italian government proposed a massive debt write-off and additional aid before privatizing the group's companies.

In 1994, the EU Commission approved debt forgiveness up to a maximum of 2.4 billion USD at current exchange rates, but then revised the figure downward to 1.87 billion USD in

<sup>62</sup> Source: Roger Ahlbrandt and Frank Giarrantani, „The EC, Responding to the Crises in the Global Steel Industry”, 1987

1996. The rest of the state aid expenditure was of 831 million USD in capital injections and 95 million USD in restructuring assistance for plant closures and workforce reductions at the new companies.

The restructuring of *Ilva*, along with *CSI* and *Sidenor* in Spain, was considered the final step of the transformation of Europe's public-owned steel sector, but the collapse of socialism in the Eastern Bloc gave rise to new problems, including the need to integrate and restructure the industry in former East Germany.

The restructuring and privatisation of *Eko Stahl* was part of the effort to reduce capacity and reinvest in the steel industry in East Germany.

Under an initial plan approved by the EU in 1994, the German Authority for Privatization (THA) was authorized to write off debts of 210 million USD through the end of 1994, to provide up to 128 million USD for additional operating losses in 1995-97, and up to 183 million USD for investments and repairs. The German privatization authority also could guarantee a 2.3 million USD.

At the end of 1994, the EU approved additional investment aid of up to 223 million USD and the operating income from the firms *Eko Stahl* and *Cockerill Sambre* (Belgium) would provide the rest of the 255 million USD required to get the plants in shape.

The EC reviewed other instances of state aid since 1994, including numerous cases of R&D and environmental aid, most of which were approved. In 1996, the Commission ruled that aid to four companies – *Walzwerk Ilsenberg* and *Neue Maxhutte Stahlwerke* of Germany, *Altiforni e Ferriere di Sevola* of Italy, and *Forges de Clabecq* of Belgium did not meet the requirements of the State Aid Code.

In the case of *Forges de Clabecq*, the region of Wallonia provided a capital injection of 42 million USD and bridging loans of 19.7 million USD.

The Commission concluded that these financial measures were not consistent with the actions of a private shareholder that has a reasonable expectation of earning a return on its investment. The Commission ruled that the company would have to return the aid, which eventually brought it to bankruptcy.

The closure of inefficient facilities and preparation of state-owned companies for privatization, as well as the strict state aid discipline imposed over the years by the Commission, had the effect that aid to the steel sector in the older Member States has been gradually brought down to a relatively low level. **In the 1990, the structure of the state aid expenditure for this sector improved too, the greatest part of it being directed towards R&D and environmental protection objectives.** According to the data presented by *Humbert Drabbe, Director at the Competition DG of the EC, whith the occasion of the II-nd European Steel Forum (November 10, 2000)*,<sup>63</sup> **since 1995, the average yearly amount of aid granted to the EU ECSC steel sector was 180 million Euro.** This sum represents only 0.5% of the amount granted to the manufacturing sector.

In terms of employment and turnover, the steel sector accounts for about 1 pct of the total (alloted to the manufacturing industry) and given this, the aid level to the steel sector must be considered low (statement relevant if we look at the aid previously granted to this sector).

According to the „*State Aid Scoreboard*” of 2003, drawn up and presented by the Commission on April 30, 2003, **the state aid for the EU steel sector declined from about 437 million euro in 1996 to 30 million euro in 2001**, although in accordance with the Commission Report from 2001 (COM/2001, 151 final) the amount would have been lesser.

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<sup>63</sup> Humbert Drabbe, Director at the Competition DG of the EC, „Steel restructuring and state aid’ the II-nd European Steel Forum, November 10, 2000.

Unlike the above – mentioned source, which is an annually brought up-to-date paper, aiming at making the catalogue of the state aids amount granted to EU main fields the *Commission annual and bi-annual Reports* ensure a more detailed and realistic view over the amount and structure of specific sector state aids.

The Art. 8 of the Commission Direction no.2496/96/ECSC from December 18, 1996, comprising the community's rules for steel state aid make specific requirements to the Commission "to draw up annual reports to the Council, regarding the application of the Decision and also to the Parliament and the Consultative Council to be informed".

The Commission Report covers all decisions adopted in 2000, of the Steel Aid Code<sup>64</sup>. Under the Code, the Commission took decisions concerning 17 cases, five(5) of which were approved without opening the investigating procedure, eight(8) were the object of final decisions and the other four (4) of a decision to initiate proceedings.

The following steel companies enjoyed by state aids in the year 2000:

- **Belgium** – *Sidmar, ALZ, Cockerill*;
- **Germany** – *Stahlwerke Bremen, Salzgitter, Georgsmarienhütte Saarstahl*;
- **Spain** – *Tubacex*;
- **France** – *Myriad*;
- **Italy** – *Acciaierie e Ferriere, Leali, Acciaierie e Ferriere, Vicenza, Acciaierie e Ferriere, Beltrane, S.Giorgio Nogaro Spa, Lucchini, Mura Spa, Siderpotenza*;
- **Austria** – *Voest Alpine Linz*.

**The cases that the Commission approved without raising any objections** concerned research and development activities carried out by undertakings in Belgium and in Germany and two cases consisted of environmental tax schemes, in Germany and Sweden.

**The cases that proved to be more problematic** were those of **investment aid for environmental protection**.

In three of those cases, the Commission took an initial decision to initiate proceedings and in one case involving five companies it took a final negative decision. It also took two partially negative decisions in two other such cases. (Tubacex - Spain and Salzgitter – Germany).

The Commission also took a new decision concerning the **Spanish company Tubacex** revoking its initial decision taken in 1997, which had been annulled by the European Court of Justice. It now decided that the debt rescheduling made in favour of the company public institutions was in line with the practice of a private creditor in similar circumstances and that no aid was involved.

**In the case of the French company Myriad**, The Commission decided to close proceedings taking note that, in the time since the opening of the procedure, the company had paid back the unduly received aid increased with the due interests. In two cases of tax credits for foreign investments made by steel companies, it took a negative decision concerning the Spanish law and initiated proceedings in the case of the French law.

The Commission also took a final negative decision concerning the regional aid that **Germany** had granted to *Salzgitter* and ordered its repayment. The aid was granted from the

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<sup>64</sup> The monitoring of the implementation of individual decisions taken under Article 95 of the ECSC Treaty are the object of separate reports according to the rules of such decisions, the two reports for 2000 having been approved by the Commission .

1980s to 1995 as tax incentives, under a 1971 German law, which provided for such incentives for companies located along the border with the German Democratic Republic and Czechoslovakia. The Commission had approved that law as an aid scheme compatible with the EC treaty. However, the ECSC Treaty does not provide for the possibility of such regional derogations and the aid was therefore incompatible.

**In the case of Cockerill (Belgium)**, it took a final negative decision, considering that the employment aid granted by Belgium was illegal and incompatible with the common market; the aid was granted illegally without prior notification to the Commission, in the form of social security reductions by the Federal Government.

**In the case of Italy**, on November 29, 2000, the Commission adopted a final negative decision on aid (€ 1.88 million) that the Italian had notified in September 1999 in favour of five undertakings towards investments they carried out between 1986 and 1994, for investments in energy conservation.

The five undertakings are: *Acciaierie e Ferriere Leali SpA; Acciaierie e Ferriere Beltrame, Vicenza SpA; Acciaierie e Ferriere Beltrame, S.Giorgio Nogaro SpA; Lucchini, Mura SpA; Lucchini, Lovere SpA*. The investments were considered by the Commission as not eligible for State aid because they were carried out at a time when such a type of investment was clearly excluded from environmental aid and the notified aid, more than ten years after the investments were made, would not have an incentive effect as required by the environmental guidelines and by the Code.

On December 21, 2000, the Commission took a final decision on aid notified by the Italian authorities in favour of *Lucchini and Siderpotenza*. It approved aid to Siderpotenza, amounting to € 0.574 million and took a negative decision on a further € 0.105 million to Siderpotenza and on € 698 million to Lucchini.

**In concluding the incompatibility of the aid, the Commission considered that the investments in question had been made for economic reasons and were not aimed at improving the environment.** Moreover, the detailed criteria to assess aid for environmental purposes were not met in the case in question.

**In the case of Austria**, the Commission decided to open proceedings concerning a proposal by the Austrian authorities to grant aid to *Voest Alpine, Linz*. The aid, amounting to € 2.17 million, is to help finance the cost of a new wastewater treatment and purification installation that the company is investing in and that will bring it into line with the new environmental standards.

The Commission has doubts about the reason for the investment in view of the age of its old installation.

### Decisions taken in 2000 under the Steel Aid Code

Country/Company	Amount (€ million)	Measure	Object	Commission decision
<b>BELGIUM</b>				
<b>Sidmar</b> (C57/99)	0,608 (p) 1,9 (n)	grant	Environment	partial (15/02)
<b>Sidmar and ALZ</b> (NN139/98)	Sidmar: 3,2 ALZ: 0,48	grant	R&D	no objections (12/7)
<b>ALZ</b> (n518/00)	0,745	grant	R&D	no objections (31/10)
<b>Cockerill</b> (c76/99)	13,8	social sec.reductions plus grant	Employment	Negative (21/12)



<b>GERMANY</b>				
<b>Ecological tax</b> (N 625/99)	n.a.	tax refund	Environment	no objections (15/02)
<b>Stahlwerke Bremen</b> C34/2000)	0,623	grant	Environment	open procedure (13/06)
<b>SALZGITTER</b> (C10/99)	n.a.	tax relief	Regional	negative (28/6)
<b>GMH</b> (43/00)	n.a.	service fee	Management contract	open procedure (19/07)
<b>Saarstahl</b> (N594/00)	0,153	grant	R&D	no objections (18/10)
<b>SPAIN</b>				
<b>Tubacex</b> (c9/95)	n.a.	debt. rescheduling	loan and social sec. Debt	No aid (31/00)
<b>Tax credits foreign investments</b> (C57/97)	n.a.	tax exemption	Foreign investment	negative (31/10)
<b>FRANCE</b>				
<b>Myriad</b> (C45/99)	1,6	grant	aid reimbursed with interest	close procedure (4/10)
<b>tax credits foreign investments</b> (C61/00)	n.a.	tax exemption	foreign invest.	open procedure (31/10)
<b>ITALY</b>				
<b>Five companies (1)</b> (c13/2000)	1,88	grants	environment	Negative (29/11)
<b>Lucchini and Siderpotenza</b> (C25/2000)	Lucch:6,98 Sid: 0,574(p) 0,105(n)	grants	environment	Lucchini: negative Siderpotenza: partial (21/12)
<b>AUSTRIA</b>				
<b>Voest Alpine Linz</b> (C24/2000)	2,17	grants	environment	open procedure (11/4)
<b>SWEDEN</b>				
<b>CO<sub>2</sub> taxation</b> (NN 71/2000)	n.a.	tax refund	environment	no objections (21/12)

Note: (p) refers to aid object of a positive decision; (n) refers to aid object of a negative decision.

(1) The five undertakings directly concerned by case C 13/2000 were: Acciaiere e Ferriere Beltrame, Vicenza SpA; Acciaierie e Ferriere Beltrame, S.Giorgio Nogaro SpA; Lucchinin, Mura SpA; Lucchini Lovere SpA;

*Source: REPORT FROM THE COMMISSION on the implementation in 2000 of Commission Decision n° 2496/96/ECSC of 18 December 1996, establishing Community Rules for State Aid to the steel industry(Steel Aid Code); Brussels, 21.3.2001; COM(2001) 151 final*

## **CHAPTER 3 COAL INDUSTRY**

### **3.1. Legislative framework for granting state aid in coal industry**

In European Community the coal industry entered a declining period starting with the 60's, the prices of hard coal produced by Member States being not competitive with the prices of imported coal from third countries. In the last four decades this sector has passed through a hard restructuring process and also a re-dimensioning of production accompanied by substantial subsidies granted at the level of Member States. Besides the subsidies directly linked to restructuring process and shutting down of production capacities, Member States have adopted measures meant to mitigate and counteract the regional social impact of crisis from coal industry, due to the fact that coal output was traditionally concentrated in some regions with a local economy centered on coal extraction. Such social programs stipulated a series of compensations and support measures for the miners losing their jobs, e.g. financial compensations for early retirement, compensations for wage cuttings, financial aids meant to stimulate the re-allocation of miners, retraining programs etc. European Community has supported such social programs by means of so-called "re-adaptation aids", financed from Community taxes applied to economic agents from steel and coal industry under the provisions of art.56 of ECSC Treaty.

Nowadays after almost four restructuring decades, only four member countries (out of 15) are still producing hard coal: Great Britain, Germany, France and Spain. Only production units from Great Britain are to a certain extent competitive comparing with prices on world markets (especially for open pits and less for underground mines), while in the three other Member States hard coal production continues to be subsidized<sup>65</sup>. In December 1993, European Commission adopted a Decision (valid until 23 July 2002 when ECSC Treaty was going to expire)<sup>66</sup> setting up specific rules for state aid in coal industry with the main aim to gradually and progressively cut the subsidies for this sector in the context of continuing the restructuring efforts and re-dimensioning the European coal production. Based on this decision European Commission and coal producing states had collaborated to fulfill the objectives of ECSC Treaty and state aid schemes for respective countries played an important role in the management of structural changes characteristic for the evolution of coal industry in the last 10 years. The provisions of ECSC Treaty and state aid schemes enabled the restructuring process and the adaptation of Community industry to the requirements of a more and more competitive and diversified energy market, simultaneously preserving the economic and social cohesion for mining regions and miners. Social dialogue was one of the main features for the industries under the auspices of ECSC Treaty and ECSC Consultative Committee had an important contribution for achieving this dialogue.

Decision No.3632/93/ECSC gives a large definition of state aid term and acknowledges the transparency of state aid granted to coal industry. The aid was going to be calculated by referring to international coal market and its amount was going to decrease gradually on medium and long term. Within the decision a clear distinction was made between the different types of state aid and it was mentioned the necessary restructuring of industry carried on in an adequate manner in order to minimize the social and regional effects.

In article 1 of the Decision one could find a certain explication of aid measures:

- a) direct or indirect support measures of public authorities related to

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<sup>65</sup> See *Report from the Commission on the application of Community rules for state aid to the coal industry*, COM (2002) 176 final.

<sup>66</sup> Commission decision No. 3632/93/ECSC of 23 December 1993 establishing Community rules for State aid to the coal industry.

production, marketing and foreign trade, which even they are not a burden for public budgets they offer an economic advantage to mining undertakings in the field of cutting the costs borne by them;

- b) allocation to the direct or indirect benefit of coal industry of expenses

deemed to be binding as a result of state intervention, without making a distinction between the aid granted by the government and that granted by public or private bodies charged by the state to administrate the aid;

- c) aid elements included in the financial measures taken by the Member

States for the mining undertakings, which are not considered as risk capital insured to an undertaking under standard practices of a market economy.

Based on the provisions of the articles 3-7 of the Decision, state aid was classified in several categories: a) operating aid; b) aid for activity reduction; c) aid for research and development; d) aid for environment protection. One may notice that state aid has been diversified, being granted not only for partial covering of production costs (based on economic performance criteria) but also for other complementary activities, like restructuring, research/development and environment protection.

When analyzing requests for authorizing state aid approved according to the provisions of the Article 9 of the Decision, European Commission checks if the involved states have delivered all the required information and based on it whether aid measures are in line with general criteria and objectives mentioned in article 2 of Decision or according to criteria mentioned in other articles. The aid granted according to Article 3 should not exceed the difference between production cost and international market price, but hard coal must not have a market price under that of similar product produced in third countries and the aid must not distort the competition between the coal users and is going to record annual corrections. The aid granted according to the Article 4 calls for the requirement to present and implement a closing plan, while the aid granted according to Article 5 should not exceed the costs to be covered and should be strictly limited to the cost mentioned in the Annex of Decision No.3623/93/ECSC. When evaluating the aid it must be taken into account the necessity to alleviate the negative social and regional consequences of mining restructuring activity, according to the provisions of Article 2(1) of the Decision, as well as its compatibility with the adequate functioning of the single internal market.

Article 8 of this Decision requested to hard coal producing member states to present for approval detailed plans for restructuring and cutting the production, at the same time proposing precise objectives for reducing the state aid for this sector.

Thus, in March 1997, Germany presented a plan to the Commission according to which until 2005 German hard coal production would be reduced to 25 million tons per year and the number of miners to 36000. Concomitantly, until the same date, the German federal government was going to cut the subsidies for coal production to 5.5 billion € per year (in 2001 the subsidies granted by the federal government for coal industry amounted to 9.2 billion € - but it is worth mentioning that the regional authorities from the 2 German lands where the coal production is concentrated, Saarland and North Rhine-Westphalia, also contribute to the subsidies given to this sector). In the case of Spain, European Commission approved a restructuring plan for the period 1998-2002 according to which until the end of this period Spanish coal production would be reduced to 14.5 million tons per year. France is going to stop the coal production until 2005 (it is worth mentioning that during 1986-2001 period 23000 French miners lost their jobs). At last, Great Britain submitted to European Commission a proposal for a scheme to modernize and restructure the coal industry within 2000-2002 period (until the ECSC Treaty was going to

expire), according to which the total subsidies granted in this period would not exceed 110 million £.

Once the ECSC Treaty expired, on 23 July 2002, the EU Council adopted a new Regulation concerning the state aids for coal industry<sup>67</sup>. Before analyzing the content of this regulation, it is worth mentioning some notices regarding its exact application aim. The official version in English of the Regulation refers to "coal industry" in general, but in Article 2 coal is defined as "high degree, average and inferior coal from A and B categories according to international classification system adopted by European Economic Commission of United Nations". Moreover, under the Article 3 the state aids settled within this regulation may be granted "only for coal extraction strictly linked to electric power and steel production from European Community". But in the official French version it is clearly pointed to "**hard coal extraction industry**", which means that lignite extraction for instance is not subject to this Regulation, while state aids for lignite extraction would subsequently be under the general rules regarding the state aid adopted for the application of Articles 87-88 TEC. The Spanish and Italian versions do not make such a distinction. In favor of this distinction we have the information made available by Directorate General for Energy within European Commission, which explicitly refers to "hard coal" in the section regarding coal state aid<sup>68</sup>.

The provisions of the new Regulation are so conceived to take into account on one hand the fact that hard coal industry continues to remain uncompetitive in general, while the restructuring and re-dimensioning process should continue after the ECSC Treaty expires, which justifies the granting of state aids meant to alleviate the economic and social implications of this process. On the other hand, due to the fact EU becomes more and more dependent on imports of primary energy resources from third countries it is necessary to maintain a minimum level of domestic coal production as an integral part of a comprehensive strategy for insuring the EU access to primary energy resources, which justifies the state aid granted to this purpose. In other words the new Regulation allows the granting of state aids for coal industry which come into line with one of the following two objectives:

- maintaining of a minimum "strategic" level of coal domestic production, and
- alleviation of social and economic consequences of closing the surplus extraction units.

The main categories of state aids covered by the Regulation are the following:

1. operating aids meant to cover the losses of extraction units which are going to be completely closed until the end of year 2007 (Art.4). The amount of these aids per coal extracted ton should not exceed the difference between production costs and benefits estimated to be obtained each current year (consequently the amount of aids will be recalculated and reajusted every year, even whether state aid scheme is multi-annual). Moreover the granted aid cannot have as effect the decrease of selling price of coal extracted in EU under the import prices for equivalent products from third countries. Such aids may be granted only for extraction units which had been noticed to European Commission by the Member States until the December, the 31<sup>st</sup> 2002 and have a plan for complete closing of production, including estimations related to the foreseen production up to the complete closing and the production costs etc.(Art.9 (4)).
2. aids for maintaining a minimum level of domestic production in EU

<sup>67</sup> Council Regulation No.1407/2002 of 23 July 2002 on state aid to the coal industry, OJ L 205 from 2.8.2002, pp.1-8.

<sup>68</sup> See [http://www.europa.eu.int/comm/energy/en/state-aid\\_1.html](http://www.europa.eu.int/comm/energy/en/state-aid_1.html).

(Art.5). These may be aids for investments or operating aids – *nota bene*, the two types of aids cannot be cumulated for the same beneficiary, in other words, this may receive an aid either first type or second type. Particularly aids for investments may be granted: i) only to extraction units which had not benefited in the past from such type of aid; ii) provided that they are able to demonstrate the economic viability of supported investment plan; iii) up to a maximum ceiling of 30% of the total supported investment plan; iv) payment of aid may be done only until December, 31<sup>st</sup> 2010; v) the amount of granted aid should not produce the effect of decreasing the price of extracted coal under the price level of equivalent imported products from third countries. Instead, the operating aids (or, in other words, aids meant to compensate the losses of ineffective extraction units) may be granted only for those extraction units included in a strategic plan for maintaining a minimum level of domestic coal production in EU (and their inclusion is justified from strategic and economic point of view), in such a way that the granted aid should not produce the effect of decreasing the price of extracted coal under the price level of equivalent imported products from third countries. Article 9(5) and (6) of Regulation compels the Member States to present until December, 1<sup>st</sup> 2002 detailed plans for the selection of extraction units which are going to be maintained in operation, their economic viability etc.

3. aids meant to cover contracted debts in the past as a result of implementing restructuring and rationalization production plans, e.g. expenses related to rehabilitation of the former extraction fields, as these do not cover current production expenses.
4. state aids for R&D projects, environment protection and training of labor force, which fulfill the requirements established by Community secondary legislation applied to these aid categories (these have been discussed in detail in the section referring to state aids for coal industry).

As concerns the supervision of implementing the above mentioned aid schemes which have been approved by European Commission, Article 9 of Regulation compels the Member States to report in maximum 6 months after the end of each production year how they have been applied.

### **3.3. State aids in coal industry**

#### **3.3.1. Motivations**

The major problem for Community hard coal industry has always been the high level of production costs, net superior to import prices. The production costs had recorded a rising trend in the main producing countries in 1975-1995 period, when they increased 3 times on average, excepting Great Britain where the costs considerably diminished after 1985. The very high level of costs had determined the ceasing of coal production in Belgium (where the costs reached about 200 ECU/t in 1990) and the drastically cut of coal production in France (where the costs reached 170 € in 2000). In spite of modernization, rationalization and restructuring measures undertaken by the Member States with the European Commission support, the production costs have been reduced to a less extent in Germany and Spain after 1995 and more evidently in Great Britain after 1990. As such the share of production in total apparent consumption (total deliveries = production + import) had reduced from 56% in 1992 to 30% in 2002 in favor of imports.

Despite the relatively high amount of state aid and considerable efforts made by the producers on technological and organizational field for improving labor productivity, the competitiveness of Community coal industry on international market laid on a decreasing curve because of two objective motives. The first reason is that the coal reserves with an easy access have been largely exhausted, which led to difficult geological conditions for very deep extraction, even under 1500 meters. Additionally, there have been added the more severe provisions of new regulations regarding the health and safety of workers and environmental protection, which also increased the production costs. This explains why the more performing machines and technologies could not lead to an important decrease of production costs.

The second reason is the extremely large difference between the production costs in EU and coal prices imported from third countries. Even when international prices are rising under the evident influence of increasing crude oil price trend more than the influence of demand/supply balance the difference is quite high. The extra- community producers headed by USA are working more accessible reserves, are applying more effective extraction methods and are using aggressive policies for export promotion (like China). Another explanation is linked to economic situation of some traditional exporters, such as Indonesia and South Africa, where the devaluation of national currencies together with the rising needs for free currencies, as well as with relatively low oil and natural gas prices, has contributed to strong downward pressures exerted on coal prices.

The gap between EU high production costs and international market prices is important because it constitutes the basis for the calculation of state aid. Production costs have significantly been reduced in Great Britain, where there have been maintained in operation the most profitable mines, and also in Portugal, where the extraction activity stopped at the end of 1994. Due to high cost level France decided to stop the production in 2005, while Germany and Spain have decided to continue their efforts for restructuring the coal production, but with an approach taking into account of social and regional requirements.

Another indicator which reveals the lack of competitiveness of Community hard coal production, as well as the lower level of labor productivity, is **the ratio between production volume and labor force level**, where the Community producing states have a weak point as compared to USA, Australia, Canada, South Africa. Other countries with a developed coal production, like Russia and Poland, which may compete with traditionally community production, are not standing too well at this indicator and neither at coal quality.

The Council Regulation No.1407/2002 revealed once more the unbalance between EU hard coal production and imported coal that found its expression in restructuring and decreasing measures of Community production, which emphasized the EU dependence on external primary energy resources. Commission Green Paper adopted on 29 November 2000 regarding European Energy Security Strategy lays the stress on diversification of energy resource both on geographical and structural level. The geopolitics and security risks from energy sector have called for a broader redefinition of the concept of energy supply security. Bound to this concept is the insurance of free access to coal reserves and potential availability of these reserves. In the European Parliament Resolution from 16 October 2001 on Green Paper on Energy Security Strategy has been underlined the coal importance as a domestic energy source and the necessity to grant a financial support to production, as well as the need for increasing the coal sector efficiency and for cutting the state aid. However, when comparing with other conventional energy resources, coal has a great disadvantage: a relatively low yield in electric power stations (30-40%) and an extremely high degree of pollution.

Consolidation of EU energy security justifies maintaining of some coal producing capacities and granting state aids. The restructuring of coal sector will have to continue since the most part of production remains uncompetitive against the imports. A minimum level of coal production may be acceptable under the circumstances that energy security implies a certain

percentage of total used resources to be insured from indigenous sources. The Member States are free to opt for any energy resources, but state aid will be granted according to the regulations applied to each category of resources.

### 3.3.2. Dynamics, amount, structure

In the next table it is presented the evolution of state aid authorized by EU in 1996-2001 period. Until the expiration of ECSC Treaty, in July 2002, state aid granted to coal industry had been evaluated under the rules established by European Commission Decision No.3632/93/ECSC.

<b>Authorized state aid (mil.€)</b>			
<b>Country/year</b>	<b>1996</b>	<b>2000</b>	<b>2001</b>
Germany			
-operating aid*	5361.8	2003.2	1789.5
-aid for reducing the activity**	0.0	1604.4	965.8
-other aids***	104.7	1086.0	1400.9
Great Britain			
-operating aid*	0.0	151.5	76.2
-aid for reducing the activity**	0.0	0.0	0.0
-other aids	512.8	0.0	0.0
Spain			
-operating aid*	310.3	292.7	274.3
-aid for reducing the activity**	462.8	405.6	350.2
-other aids***	255.1	422.8	444.6
France			
-operating aid*	0.0	0.0	0.0
-aid for reducing the activity**	87.6	389.6	349.1
-other aids***	592.3	620.6	642.3
Portugal			
-operating aid*	0.0	0.0	0.0
-aid for reducing the activity**	0.0	0.0	0.0
-other aids***	0.9	0.0	0.0

<b>TOTAL UE</b>	7688.3	6976.6	6276.9
-operating aid*	5672.1	2447.4	2140.0
-aid for reducing the activity**	550.4	2399.7	1665,1
-other aids***	1465.8	2129.5	2487.8
<b>Aid in €/t</b>			
-operating aid	51.33	34.42	33.2
-aid for reducing the activity	51.30	155.65	96.5

\* Aid granted under the Article 3 of Decision No.3632/93/ECSC

\*\* Aid granted under the Article 4 of Decision No.3632/93/ECSC

\*\*\* Debts (liabilities) that have remained under Decision No.2064/86/ECSC and aid granted under Articles 5-7 of Decision No.3632/93/ECSC

Source: Report from the Commission on the application of the Community rules for state aid to the coal industry in 2001, Commission of the European Communities, COM(2002) 176 final/2, Bruxelles, 2.07.2002

Subsidy policy or state aid granting has been under Commission control, but it has been carried on at the national level and with financial means of respective countries, not with Community funds. State aids granted for covering the production costs have considerably decreased in the 90's both in absolute volume and in the level per extracted ton as the coal production has significantly diminished. At the same time it has increased the level of aids for reducing the extraction activity and conservation of deposits, as well as other types of aids.

In **Germany**, state aid granted to hard coal industry under the provisions of Article 3 of Decision No.3632/93/ECSC has been restricted since 1996 to coking coal for steel industry, to coal for electricity generation and to maintain a certain number of underground miners. This aid, approved by the Commission, was meant to cover the difference between the production costs and the selling prices freely negotiated and formed under the influence of determinant factors on international market for the coal from extra-community countries. Production for domestic and industrial consumption had to be sold at the prices able to cover the production costs. The high unemployment zones, due to coal industry restructuring, are eligible for the aid directed to regional development, under the priorities set within the Objective No.2 of Structural Funds. This aid is a part of federal budget and fulfills the requirements of Article 2 (2) of Decision No.3632/93/ECSC.

For the year 2001 European Commission authorized a state aid for German hard coal industry of 4693.7 mil.€, out of which 1966.9 mil.€ for operating aid (under the Article 3 of Decision), 1604.4 mil.€ for reduction of the activity (under the Article 4 of Decision), 36.3 mil.€ for keeping the labor force in underground mines (under the Article 3), 1086 mil.€ for covering some exceptional costs (under the Article 5). Subsidies or operating aid are meant to cover the difference between the production costs and the international selling prices for extra-community coal, namely the losses recorded in those productive areas that fulfill the progress criteria to economic viability on medium term, as it is stipulated in the Articles 2(1) and 3 of the Decision No.3632/93/ECSC. State aid for activity reduction was allocated for closing some mines in 2000-2002 period. State aid for keeping labor force is meant to encourage qualified staff to preserve the underground jobs and to contribute to production rationalization, also to labor cost reduction. State aid for exceptional costs is meant to cover some restructuring costs, mainly social ones, but also costs related to the increase of working security in underground mines.



In **Great Britain**, European Commission authorized, for the year 2001, under UK Coal Operating Aid Scheme, an aid of 81,3 mil €, meant to cover the difference between production costs and selling prices on international market for similar quality coal. The aid was granted mainly to the mines Longannet (Mining Ltd) and Selby (UK Coal Plc), and secondary to the mines Hatfield (Hatfield Coal Co. Ltd), Betws (Betws Anthracite Co), Blenkinsopp (Blenkinsopp Colliers Ltd), Aberpergwm (Mining Ltd), Eckington (Moorside Mioning Co.Ltd), Hay Royds (Flack&Sonsa Ltd), Blaentillery No.2(Ffynonau Duon Mines Ltd). In the second part of the 90's British coal industry had not received any state aid, this being resumed in the year 2000 at a modest amount.

In **Spain** the state aid authorized by European Commission for the year 2001 amounted to 1121.1 mil. €, out of which 274.28 mil. € operating aid under the Article 3 of Decision No.3632/93/ECSC; 350.22 mil € aid for activity reduction under the Article 4 of Decision; 357.64 mil. € aid for financing compensatory payments for dismissed workers due to restructuring process under the Article 5 of Decision; 87 mil. € for covering technical exceptional costs linked to mine closing within the restructuring measures under the Article 5 of Decision. The Spanish Government requested additional aid of 6.7 mil. € for Gonzales y Diez SA (base on Article 3); 36.1 mil. € for Hunosa and 1.72 mil. € for Minas de la Camocha SA (based on Article 4); 87 mi. € for Hunosa and 2.37 mil. € for Gonzales y Diez SA (based on Article 5). This additional aid may be approved by European Commission if the respective country delivers additional requested information.

The operating aid of 274.28 mil. € was meant to cover the losses of 42 mining companies with a production of 10.7 mil. tons in 2001. The costs taken into account were calculated in constant prices with 1992 basis, and at the 2001 level the reduction of calculated costs was 18.5 % against 1994. The state aid for activity reduction of 350.22 mil. € was meant, excepting the costs of social payments backed by the state under the Article 56 of EEC Treaty, to workers from mining companies early retired or being out of work under a restructuring plan. The aid of 87 mil. € was meant to cover the depreciation of fixed assets value totally or partially closed or other exceptional costs resulted from progressive closing of mines within the restructuring policy.

In **France** the state aid authorized by European Commission for 2001 amounted to 991.4 mil. €, under the Articles 4 and 5 of Decision No.3632/93/ECSC, out of which 317.1 mil. € for activity reduction (covering of operational costs), 32 mil. € for activity reduction meant to cover some interests for loans engaged by Charbonnages de France in the years 1997-1999, 642.3 mil. € for covering some exceptional losses resulted from early retirements, unemployed caused by restructuring process, administrative, legal and fiscal provisions, additional activities resulted from restructuring process, previous prejudices caused by closed mines, covering of some costs related to social insurances.

## **CHAPTER 4. MOTOR VEHICLES**

### **4.1. General Aspects**

#### **Legal Basis**

Although EU Treaty does not contain specific provisions referring to a common policy concerning motor vehicle sector, the articles referring to competition and state aid – Art. 81-89 (85-94), as well as those regarding single market confer to European Commission the power to intervene on automobile market. Also, Commission may be authorized to negotiate with third countries (external policy). At the same time, Art. 157 (130) of Maastricht Treaty offers the legal basis for an industrial policy at Community level.

Starting with 2004, the automobile sector is integrated totally in “The new multisectoral framework on regional aid for large investment projects”<sup>69</sup>. The provisions of this framework contain stricter and stricter thresholds, inversely proportional to investment amount. This has followed after the application of some transitional rules, during the year 2003, which stipulated the eligibility for state aids up to a percentage of 30% maximum allowed for the region involved (comparing with 100% until then).

#### **Characteristics specific to motor vehicles sector**

This industry is by no doubt one of the most important industry of today global economy. It generates numerous jobs both directly and indirectly, has an important share in added value and in trade balance of many countries and represents one of the most significant expenditure in consumer budget. Many states, including European ones, looked at motor industry as one of the engines that are able to spill over the whole economy, from this point of view it was perceived as generating social welfare. As one of the main objectives mentioned in Rome Treaty had been the economic cohesion, numerous Member States of EU had tried, in the economic boom periods, to promote regional development by attracting motor producers in the assisted areas inside the national borders. On the other side, during recession periods, they offered support to domestic producers. It may say therefore that, at least in the first stages, the relationship between states and motor producers was greatly influenced and practically followed the economic cycle curve.

In the course of time European motor producers had and still have to pass some problems, as:

- Lower financial power as compared to American and Japanese competitors;
- An oligopolistic market, with some almost equal powerful producers, which means a more limited competition between these;
- Competition pressures on behalf of Japanese capacities from Europe;
- Increase in the number of new producers from Asia-Pacific region with a substantial export potential;
- Increase in imports of American and Japanese cars on European market.

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<sup>69</sup> OJ C70, 19.3.2002.

## **Objectives**

In the next few years one may anticipate that EU will remain the largest car producer in the world (42% in 2002, as compared to 35.4% in Asia and 22% in America), but also the largest distribution market. That is why the objectives of European policy in the field are:

- Creation of a common motor market, by removing the barriers affecting intra-community trade;
- Consolidation of competitiveness of European motor industry;
- Use of voluntary export restraints, with the aim to limit cheap imports and maintain competitiveness.

## **Dimensions of state aid**

Motor industry has been one of the most privileged sectors from the point of view of support given under state aid form. Thus one may estimate that, in 1977-1987 period, the aid received by this sector from Member States amounted to about ECU 26 billion, while between 1989 (when the first community framework on this industry came into force) and 1996, European Commission authorized state aids only of 5.4 billion ECU.

### **4.2. The legislative framework on state aid granting in motor vehicle industry**

In the last 25 years, car industry had passed through profitable and less profitable periods. While the first oil shock (1973-1975) had passed relatively fast for European producers, the second one (1979-1982) had demonstrated the need for some structural modifications in this branch. Later on, the year 1989 recorded the highest sales, but the year 1993 recorded the largest decrease of these after the second world war. After 1997 motor industry has recorded an increase rate higher than the other branches of processing industry.

Although the need for strengthening control over state aids granted to this branch became obvious ever since 1980-1986 crisis, specific rules could be adopted only in 1989 (peak year as concerns the sales). These were implemented rigorously in 1990-1993 period, but the new crisis period started in 1993 generated numerous critics on behalf of Member States. In this context, the adoption of a set of horizontal rules referring to state aid became a priority.

The dynamics recorded by this sector, as well as the variations of control policy of state aids may be pursued also by means of rules, points of view or action plans of European Commission from this period.

#### **1. *Commission Communication on European car industry (1981)***

This Communication is an economic policy document which underlines the necessity for:

- i) a closer cooperation within the sector;

- ii) introduction of an ex-post monitoring system of state aids, as a means of increasing the transparency and improving the coordination;
- iii) some large scale investment programs, which would also include financial community support, aiming at productivity increasing;
- iv) stimulation of research-development activity, by means of cooperation between companies, public entities and universities;
- v) geographical reorganization of car production, to the benefit of less favored zones and with the aim to improve the working conditions.

As one may notice, two main objectives seem to be pursued: supporting the increase of European producers competitiveness and supporting the less developed zones, respectively.

## **2. Action Plan (1983)**

The Commission Communication on economic policy referring to motor industry had been translated into an action plan which defined the following objectives:

- i) Strengthening of internal market, with the aim to diminish the price differences between Member States, by adopting a block exemption system of selective distribution systems and harmonization of national regulations, by introduction of an homologation at the European Commission level. Harmonization had to be achieved also in the field of taxes and duties and respectively in the field of energy saving. In all these respects Commission was going to make legislative proposals in order to harmonize the national policies.
- ii) Improvement of the branch structure and competitiveness, with support given by Regional Fund and European Investment Bank.
- iii) Improvement of the working conditions and employment.
- iv) Dialogue with trade partners.

In fact, until the end of 1987, European Commission had not issued any negative Decision on state aids granted to this branch, in spite of a stricter and stricter control of these aids. Aids granted under capital infusion form had been authorized for state owned companies or state participation companies – British Leyland and Volvo (in the absence of precise criteria on control and evaluation of these aid forms), but also aids for private companies –Fiat and Alfa Romeo- under the circumstances of engagements for cutting production capacities. It is obvious that political pressures on behalf of Member States, which looked upon motor industry as a strategic branch, played an important role in determining this situation.

Moreover, in 1983, European Commission had failed in the attempt to introduce a monitoring system based on the obligation of an ex-post notification of all aids the car producers had benefited from. This system - based on a specific notification printed form – had been contested by most producer states (Germany, Great Britain, France, Italy), either on technical reasons (sector defining, aid type defining) or on general reasons (endangering some industrial policy aspects).

Despite this, aids control had become more and more severe, the first negative Decisions (Renault, Peugeot) appeared but also more often the conditioning of restructuring aid on capacity closing.

### **3. Commission Memorandum (1988)**

This memorandum started from the assessment that, despite the restructuring and modernization efforts made in the 80's, European car industry was behind its main competitors from the point of view of productivity and quality. Therefore Commission offered through this memorandum additional means for speeding up the restructuring, proposing four action directions: (

i) Finalizing internal market through:

- technical harmonization;
- avoiding market fragmentation;
- approximation of duties system.

ii) Putting into practice of a common trade policy through:

- elimination of national restrictions for extra-community imports;
- stabilization of Japanese imports on community market;
- providing of a substantial local content in the case of transplants made by Japanese producers.

iii) Drawing up of a general strategy and a unitary policy in the field of state aids by continuing the sector restructuring.

iv) Stimulation of R&D activity, also including community support.

At the end of 80's the Decisions taken by European Commission in four state aid cases helped to create a consistent approach of restructuring aids, which has been used also in other sectors. It is a matter of Alfa Romeo, Renault, Rover and ENASA cases, four state companies which had suffered enormous losses in the course of the years. All these had excessive capacities, decreasing market shares and some even negative cash-flows. Willing to get them ready for privatization, the respective companies benefited from capital increases, loss compensations and debt exemptions. Although the involved member states expressed the opinion that the respective measures did not constitute state aid, European Commission opened the investigation procedures and concluded that they were salvation and restructuring aids. Conditions imposed in these cases present some interesting characteristics:

-The aids had been only partially approved and had been conditioned on the existence of a restructuring plan which involved capacity closing. The percentage of aid in total restructuring costs was approximately equal to the percentage of capacity to be eliminated.

- A certain percentage of aid was not authorized because either it did not belong to real debt of the company or it had not been used for innovation or it was excessive comparing with the total cost of restructuring.

- There had also been imposed some conditions which would be going to be fulfilled in the future, to the extent of restructuring plan implementation, which imposed an ex-post monitoring: carrying out of capacity reduction, banning other aids granting, performing a minimum of investments in assisted zones.

- In the case Alfa Romeo, where the company did not accept any capacity reduction and there was no restructuring plan and no positive effects on regional development, the aid was banned and it was decided its reimbursement.

In conclusion, at the end of 80's European motor industry had still numerous structural and competitiveness problems. One could assume that a new series of state aids could appear any moment. Therefore European Commission had drawn up, in 1988, a general framework draft on state aids in this sector, which had the following characteristics:

- a greater transparency of state aids;
- ex-ante notification obligation;
- a more severe control of regional and restructuring aids.

This "General Framework" had been adopted by European Commission in December 1988 and came into force one month later. In 1997 European Commission adopted a new general framework which enlarged its application sphere, by also including so-called "suppliers of first class components"<sup>70</sup>, and modified the notification threshold for projects with total costs over 50 million ECU (the previous threshold had been 17 million) or total gross aid over 5 million ECU. Preceding notification of all significant cases is compulsory, so it is an annual report of all granted aids. Standard notification and reporting printed forms are presented (annexes I and II).

As the differences between the two documents are important for underlining the pursued objectives by European Commission, they are further presented in parallel, in order to facilitate the comparisons.

#### **4. General Framework from 1989 (GF89) and General Framework from 1997 (GF97)**

Within both documents the main evaluation criteria of different types of state aid are detailed:

##### *a) Rescue and restructuring aid*

**GF (89).** This type of aid may be authorized only in the presence of exceptional circumstances, a restructuring plan and only when it is in the interest of Community that the respective company continues its activity and to become a viable one. Capacity reductions may be imposed.

**GF (97).** European Commission should insure that such an aid is, in principle, "one-off operation". Likewise European Commission will ban the aids that have as a purpose a net increase of production capacity. Moreover it will impose, as usually, reductions of installed capacity. These reductions must be proportional to aid intensity.

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<sup>70</sup> A supplier, either independent or not, which has a part of responsibility for designing and development and which produces, assembles and delivers subassemblies and modules to a motor producer, within the production and assembly stages. As normally they are partners, such suppliers are linked to motor producer through a contract, which as a rule, has a length of time almost equal to life duration of respective model. Such a supplier may also offer services, especially of logistic nature, as it would be the management of a supply centre.

b) Regional aid

**GF (89).** Regional aid for investments in new capacities or for extending the existing ones will be accepted by European Commission when its intensity is proportional to structural handicaps of assisted zone; the advantage brought to regional development must however be compared to the eventual negative sectoral effects, caused by a subsidized capacity increase<sup>71</sup>.

In order to evaluate such aids, European Commission introduced the cost/benefit analysis method (CBA), with the aim to quantify the structural disadvantages which an investor must face in the respective region, compared to another non-assisted zone, from inside EU. In this way European Commission used a specific company approach, when the companies evaluate by themselves the advantages and disadvantages of localization of a mobile project in a certain area as compared to other alternative areas. For making operational this approach, the first step is to identify an alternative location in a non-assisted area; in this respect the companies may themselves offer some help, in the case they had made studies or analyses referring to this aspect.

The next step consists in comparing the costs with *investment* from assisted area and from alternative non-assisted area. Usually there had been taken into account as handicaps those related to infrastructure or construction costs; the same is true nonetheless that the advantages of an investment in an assisted area – as it is the lower price land – are deducted from costs, thus getting a net handicap. The same approach is used also for determining the net operating structural disadvantages for the next five (projects started from zero) or three years (extending projects). Operating handicaps may include higher training expenses, additional transport or storing expenses, higher material expenses etc. Net handicaps should be declining in time, so that to justify the investor decision for investing in the respective area.

Evidently all this analysis is carried out with the assistance of some independent consultants and may lead to rejecting or diminishing some types of disadvantages supported by the companies. Finally, European Commission will accept a level of aid which compensates the beneficiaries of incremental costs these have to bear as a result of structural handicaps. In this way assisted area will be on an equal position with any other non-assisted areas as concerns attracting some mobile investments, the investor having not one kind of additional incentive for preferring the assisted area. In spite of this, such an incentive (called top-up regional) may be allowed up to a level of 3% from investment costs, provided that the respective project not to generate sectoral problems, for instance by creating overcapacities.

**GF (97).** European Commission acknowledges the valuable contribution which new investments made in this sector have brought to regional development. Preceding notification of these aids should allow to European Commission to compare the benefits brought to regional development with the possible negative effects on the whole sector. This means that the aid should be considered necessary, which signifies that the beneficiary must demonstrate clearly he has also at his disposal an economic viable alternative location. One could not be authorized any regional aid for a project which is not geographically mobile. At the same time the aid should be proportional to the regional problems intended to be solved with its participation. To this aim it must be performed a cost/benefit analysis which has to compare the costs the investor is going to bear in the respective region with those he might bear for the same project in another region.

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<sup>71</sup> See the decision for approving a state aid granted to FIAT Company for buliding a works in Mezzogiorno region, OJ C 37/15 (1993)

The cost/benefit analysis is not necessary in the case of aids with an intensity lower than 10% from regional admissible threshold.

*c) Aid for investments in innovation, modernization or rationalization*

**(GF 89).** The modernization aid should normally be borne by the companies. Aid for innovation and rationalization may be accepted when it leads to a restructuring which passes beyond what company would have financed from its own resources.

**(GF 97).** European Commission has in mind the need to increase the competitiveness of European motor industry. Thus in order to stimulate assuming the risks by producers, state aids up to 10% of eligible costs may be authorized. These have in view investments for innovation and must refer only to one factory. In return aids for modernization or rationalization may not be granted anymore.

*d) Aid for R&D*

**(GF 89).** This type will be accepted only when it refers to pre-competitive stage and does not lead to a simple modernization.

**(GF 97)** The aid is evaluated according to “Community framework on state aid for research and development”. In this context, one should do the distinction between applied industrial research and development in pre-competitive stage on one side and introduction of a new technology through productive investments or development in competition stage on the other side.

*e) Aid for environment protection and energy saving*

**(GF 89).** State aid should not be granted for making nonpolluting machines, because this is a normal preoccupation for developing any business. General measures, as those related to developing nonpolluting production methods may receive, under special circumstances, state aids, according to general framework on environment aids.

**(GF 97).** The aid meant to determine the observance of some standards already imposed by community legislation may not be accepted. Such aids may be authorized only under the conditions mentioned in “General Framework on environment protection”.

*f) Aid for vocational training related to investments making*

**(GF 87).** European Commission has a favorable attitude referring to this type of help, although it will take care for this not to exceed a reasonable intensity. Vocational training should lead to qualitative modifications in staff skill and have in view a significant percentage of this.



**(GF 97).** The favorable attitude maintains, but European Commission will make sure that the aids are not used only for cost reduction which the company will have to bear on normally. The new community framework on state aids for vocational training are applied in motor vehicles sector too.

*g) Operating aid*

**(GF 87).** This type of aid cannot be authorized, not even in unfavorable regions. This provision is identical in both documents. Member States which granted such aids in the context of exiting schemes had to eliminate them gradually.

**(GF 97).** General Framework had initially been conceived to be in force until 31 December 2000. Later on, by two Commission Decisions, its application period was prolonged one year by one, namely until 31 December 2002. In the course of 2003 some transition rules were applied, but starting with 2004 the new multisectoral framework has been applied to motor vehicle industry.

**5. New multisectoral framework on regional state aids for large investment projects**

On 13 February 2002 European Commission adopted a new system for controlling state aids destined to large and mobile investment projects (in the sense that they might be carried out in other locations too). This came into force on the 1 January 2004 and replaced the old multisectoral framework from September 1998, being valid until 31 December 2009. The characteristic of new framework is that it achieves a significant decrease of admissible aid levels and will apply also to synthetic fibres industry and motor vehicle industry, for which until then there were separate rules.

Thus the maximum admissible intensity of aid which a large investment project receives is calculated starting from the intensity ceiling fixed through regional map, which are automatically applied some reductions at, according to the following scale:

<b>Project dimension</b>	<b>Adjusting percentage of maximum ceiling</b>
Up to 50 million €	No reduction, 100% from maximum regional ceiling
For the share between 50-100 million €	50% of regional ceiling
For the share that exceeds 100 million €	34% of regional ceiling

Actually, formula for calculating the total amount of a regional aid for an investment project exceeding 100 million € is the following:

$$A=P \times (50+0.5 \times B+0,34 \times C)$$

where A is the total aid amount which will be approved, P is the maximum regional threshold applied in the respective assisted region, B is the share of investment cost between 50 and 100 million €, and C is the share of investment cost exceeding 100 million €.

Moreover according to the paragraph 24 of 2002 Framework it is forbidden to grant regional aids for investments made by companies that control over 25% from selling market of respective product (therefore, in other words, are in a dominant position, which might be strengthened through respective investment) as well as when investment project increases by over 5% the total production capacity already existing on respective market.

A cohesion bonus may be granted to projects financed from structural funds. For such projects, the admissible intensity calculated above might be multiplied by 1.15, taking thus into account the contribution to economic and social cohesion of EU. The new framework does not apply to restructuring aid, aid for R&D and aid for environment protection cases, where are still valid the rules established by specific regulations for every such type of aid.

It is not necessary the preceding notification of aids situated under certain ceilings, if these are granted within an aid scheme approved by European Commission. At the same time the notification remains compulsory in the case of new individual (ad-hoc) aids, with the exception of cases stipulated in Art.88(3) of EC Treaty and by the rules on notification exception adopted based on Regulation no.994/98.

The 2002 Framework forbids the granting of regional aids to the beneficiaries from steel industry, even to SME's (Article 4). As concerns the other so-called "sensitive sectors" (among which one may enumerate car industry, shipyards and synthetic fibres industry and which have been exempted from the application of 1997 Framework ) European Commission committed itself to make up, until 31 December 2003, a larger list with EU industrial sectors having structural problems (declining industries, where production capacities are excessive), identified, probably, as those having a negative growth rate of apparent consumption<sup>72</sup> in the last 5 years, which are going to be applied in the context of 2002 Framework a general interdiction to benefit from regional aids – with the exception of the case when the respective Member State may demonstrate that the respective product market has recorded a rapid growth (in the last 5 years the apparent consumption recorded a growth rate at least equal to the average of GDP at the level of European economic zone). The motor sector may be found (or not) on this list to the extent to which it is appreciated for suffering (or not) of serious structural problems.

However because of methodological difficulties, European Commission has decided to postpone the adoption of this list<sup>73</sup>. Consequently, the multisectoral regulation has been modified, the present text mentioning that sectors with serious structural problems may be mentioned on a list to be annexed to the framework. The technical feasibility and economic opportunity of such a step will be evaluated until the end of 2005, and the list- if it will exist – will be published until 31 March 2006 and will come into force on the 1 January 2007. Until the date of 31 December 2006 – and without affecting the provisions of Regulation no.70/2001 on state aid for SME's – in the case of state aids that exceed 5 million € (in gross subsidy equivalent) the maximum admissible intensity in motor vehicle sector will be limited to 30% from regional suitable ceiling.

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<sup>72</sup> Production+Import-Export

<sup>73</sup> Commission Communication on the modification of the Multisectoral Framework on regional aid for large investment projects (2002) with regard to the establishment of a list of sectors facing structural problems and a proposal of appropriate measures pursuant to Article 88 paragraph 1 of the EC Treaty, concerning the motor vehicle sector and the synthetic fibres sector, OJ c 263/03, 1.11.2003.

## **CHAPTER 5.**

### **SHIPBUILDING**

#### **5.1. General aspects**

Shipbuilding includes the building of self-propelled seagoing commercial vessels, repair or re-conditioning, and conversion of vessels of not less than 1000 gt.<sup>74</sup>

##### **5.1.1. Legal basis**

The measures taken by the Community in the shipbuilding sector have been based principally on Articles 87 (92) and 133 (113) of the EC Treaty, since they have involved the harmonization of rules relating to aid. Article 157 (130), added by the Maastricht Treaty, provides a legal basis for a Community industrial policy.

Currently, the rules enforced in this sector are contained in the “Framework on state aids to shipbuilding”<sup>75</sup>.

##### **5.1.2. Specific characteristics of the sector**

Certain features make shipbuilding unique and distinguish it from other industries such as short production series, the size, value and complexity of the units produced as well as the fact that prototypes are generally used commercially. As a result, shipbuilding is the only one that can receive aid for innovation.

##### **5.1.3. Objectives**

Starting with ‘70s, aids to shipbuilding have been regulated by several community regimes. As compared to other sectors, aids to shipbuilding have been sometimes more generous and sometimes stricter.

Currently, the policy in the European Union has two dimensions: (i) a quantitative and (ii) a qualitative adjustment. Thus, the European Union aims to rationalize the shipbuilding industry by means of a controlled cut-back in capacity (quantitative adjustment). While the workers made redundant should be retrained, the EU wants obviously maintain some reserve capacity for strategic, social, economic and industrial reasons. Assistance for existing shipyards is therefore aimed concentrate on modernizing and diversifying production machinery and on improving productivity and competitiveness (qualitative adjustment).

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<sup>74</sup> Conversion operations entail radical alterations to the cargo plan, the shell, the propulsion system or the passenger accommodation.

<sup>75</sup> “Framework on State Aid to Shipbuilding”, OJ C 317, 30.12.2003, p. 11.

#### **5.1.4. Size of state aids**

On average, since 1990, the annual amount of state aids to shipbuilding was between Euro 1.4 and 1.7 billion. Most of them have been operating and restructuring aids. Operating aids varied between Euro 198 million and 1.1 billion yearly.

#### **5.2. Legal framework for aids to shipbuilding**

Starting with '70s, state aids to shipbuilding have been included in a specific community framework. As a difference from other sectors, shipbuilding systematically benefited from operating aids. However, operating aid continued to be perceived as the aid that distorts the most the competitive environment. It aims to cover current operational costs and does not generate any incentive for investments or other measures to increase efficiency. In other words, such aids erode the competitive advantage of the most efficient shipyards.

Initially, the EU tried to limit state aids to a certain percentage of the contract price. However, the high ceilings for operating aids (over 30% of the contract) generated negative effects for the sector. At 1 January 1987, the 6<sup>th</sup> Directive entered into force<sup>76</sup> (for a period of four years), trying a stricter approach than the previous five ones. Its objective was to gradually eliminate operating aids, by reducing the maximum allowable intensity. As a result, this threshold has been decreased from 28% in 1987 to 9% in 1992.

In December 1990, the Council adopted the 7<sup>th</sup> Directive (90/684/EEC), for a period of 3 years.

In 1994, the European Union, Japan, South Korea, Norway and United States agreed to stop any aid to shipbuilding. The agreement – in the context of O.E.C.D.<sup>77</sup> – should have entered into force on 1 January 1996 but it didn't, because United States did not ratify it.

Efforts to decrease aids to the sector have not been continuous and coherent. After 1992, the maximum intensity remained unchanged. Starting with 1997, it was evident that most of the European shipyards were not as efficient as their competitors in Japan or Korea. Therefore, the Commission proposed a new approach which included the interdiction to operating aids and the use of other types of aid that could generate the envisaged changes.

As a result, on 29 June 1998, the Council adopted Regulation 1540/98<sup>78</sup> which introduced new rules on state aids to shipbuilding. It had the objective to apply to this sector rules similar to other industries, like the interdiction of operating aids. As a result, in December 2000, operating aids to shipyards have been stopped.

#### *The Regulation of 1998.*

Art. 3(1) provides for the elimination of operating aids up to the end of 2000. As a result of this provision, a large part of the objectives of the Commission were met. To compensate for this interdiction, the regulation allows for other types of aid aimed to increase competitiveness or to ease

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<sup>76</sup> Council Regulation 87/167/EEC of 26 January 1987 on state aids to shipbuilding, OJ L 69, 12.3.1987, p.55.

<sup>77</sup> OJ C 375, 30.12.1994, p. 1.

<sup>78</sup> Council Regulation (EC) No. 1540/98 of 29 June 1998 establishing new rules on aid to shipbuilding, OJ L 202 from 18.07.1998, p. 1-10.

restructuring, by diminishing the social effects it may have. As a result, member states are allowed to grant only the following aids:

- environmental protection aid, in compliance with the Community Guidelines;
- research and development aid, in compliance with the rules laid down in the relevant Community framework;
- investment aid for innovation (gross maximum intensity – 10%); this is a type of aid not possible in any other sector, with the exception of motor vehicle industry up to end of 2003;
- regional investment aid which is limited to supporting eligible expenditure as defined by the applicable regional aid scheme; the amount and the intensity should be lower than the applicable regional aid scheme (22.5% in regions under art. 87(3)(a) and the lowest between 12.5% and the regional intensity in case of regions under 87(3)(c);
- restructuring aid, in compliance with the general Community guidelines on state aid for rescuing and restructuring firms in difficulty, but in stricter conditions (referring to the permanent closures and monitoring);
- closure aid for facilities ceasing to be engaged in shipbuilding for at least 10 years without review.

The regulation expired on 31 December 2003.

#### *The Regulation of 2002<sup>79</sup>*

Following complaints in 2000 and 2001 from Community shipyards about unfair practices carried out in South Korea, the Commission carried out investigations into the behaviour of Korean shipyards and the financial support they have received from the public authorities. The investigations concluded that subsidies and export support had been granted, thus infringing the WTO rules, and that Community shipbuilding industry suffered serious prejudice, especially in relation to two types of ships (container ships and product/chemical tankers). For a third type (liquefied natural gas carriers), further examination was decided to be necessary.

On 27 June 2002, the Council approved a twin-track strategy to counter unfair Korean practices in this sector. Thus, the Council requested the Commission to continue negotiations with South Korea. Should no solution be found by the end of September 2002, the Commission will immediately launch its twin-track strategy, namely:

- the establishment of a WTO Panel and dispute settlement procedures against the South Korean authorities in relation to the subsidies granted; and
- the activation of a temporary defensive mechanism.

The defensive mechanism includes:

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<sup>79</sup> Council Regulation (EC) No. 1177/2002 of 27 June 2002 concerning a temporary defensive mechanism to shipbuilding, OJ L 172/2.7.2002, p. 1.

- operating aid up to a maximum of 6% of contract value may be authorised only for the two types of ships in which Community industry is suffering material injury as a result of unfair Korean practices;
- aid may only be authorised in relation to contracts for which there has been competition from a Korean shipyard offering a lower price than that offered by the Community yard;
- the mechanism will expire on 31 March 2004, to coincide with the approximate conclusion of the WTO proceedings.

The Procedural regulation<sup>80</sup> is applied to shipyards in the same way as to other industries. It is clear that the defensive mechanism is strictly limited in time and scope. It is designed to cover only those ship types most seriously injured by unfair Korean practices and to accompany the Commission's action in the WTO. It does not represent the re-introduction of general operating aid and does not undermine the recent progress made in reforming the state aid regime in this industry.

#### *The General Framework of 2003<sup>81</sup>*

The main objective of the regulation is to eliminate the differences in state aid regimes between shipbuilding and other sectors. Therefore, the general principle is that state aids may be granted in compliance with art. 87 and 88 of the Treaty and with the other legal acts adopted on this basis: Council Regulation 659/1999<sup>82</sup>, Commission regulation 68/2001 on training<sup>83</sup>, Commission Regulation 69/2001 on de minimis aid<sup>84</sup>, Commission Regulation 70/2001 on aid to SMEs<sup>85</sup>, Guidelines on rescue and restructuring aid<sup>86</sup>, Guidelines on aid to environmental protection<sup>87</sup> and Community Framework on aid to research and development.<sup>88</sup> However, the European Commission continues to take into consideration that there are still factors that affect the functioning of the shipyards:

- existence of over-capacities, low prices and other distortions on the world market;
- the nature of ships as very large capital goods, which raises the potential of State-supported credit facilities to distort competition;
- the existence of agreements within the Organisation for Economic Cooperation and Development ('OECD ') in the shipbuilding sector, namely the 1998 OECD Arrangement on Guidelines for Officially Supported Export Credits, which applies

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<sup>80</sup> Council regulation 659/1999 from 22 March 1999, OJ L 83, 27.3.1999, p. 1.

<sup>81</sup> *Framework on State Aid to Shipbuilding*, 2003/C317/06, OJ C from 30.12.2003, pag. 11.

<sup>82</sup> OJ L 83, 27.3.1999, p. 1.

<sup>83</sup> OJ L 10, 13.1.2001, p. 20.

<sup>84</sup> OJ L 10, 13.1.2001, p. 30.

<sup>85</sup> OJ L 10, 13.1.2001, p. 33.

<sup>86</sup> OJ C 288, 9.10.1999, p. 2.

<sup>87</sup> OJ C 37, 3.2.2001, p. 3.

<sup>88</sup> OJ C 45, 17.2.1996, p. 5.

in the Community pursuant to Council Decision 2001/76/EC of 22 December 2000.<sup>89</sup>

In this context, the objectives are to increase efficiency and competitiveness of European shipyards (mainly, by promoting innovation), facilitate reduction of unviable capacities and observe international commitments referring to export credits and development aid. In order to meet these objectives, **specific measures on innovation aid, closure aid, export credits and development and regional aid are included.**

Thus, innovation aid is compatible up to a maximum aid intensity of 20% gross, provided that:

- it relates to the industrial application of innovative products and processes, i.e. technologically new or substantially improved products and processes compared to the state of the art existing in this industry in the Community, which carry a risk of technological or industrial failure;
- the aid is limited to supporting expenditure on investments, design, engineering and testing activities directly and exclusively related to the innovative part of the project. Exceptionally, additional production costs that are strictly necessary to validate the technological innovation can be eligible to the extent they are limited to the minimum necessary amount.

The aid for partial or total closure of shipyards may be deemed compatible if the reduction in capacity is permanent and eligible costs refer to:

- payments to workers made redundant or retired before the legal retirement age;
- the costs of counselling services to workers made or to be made redundant or retired before legal retirement age, including payments made by shipyards to facilitate the creation of small enterprises which are independent of the shipyards in question and whose activities are not principally shipbuilding;
- payments to workers for vocational retraining;
- expenditures incurred for the redevelopment of the yard, its buildings, installations and infrastructure for use other than shipbuilding.

In addition, in the case of undertakings which totally cease shipbuilding, ship repair and ship conversion, the following measures may also be deemed compatible with the common market:

- aid of an amount not exceeding the higher of the following two values, as determined by an independent consultant's report: the residual book value of the installations, or the discounted operational profits obtainable over a projected three-year period, less any advantages the aided undertaking derives from the closure of the installations;

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<sup>89</sup> OJ L 32, 2.2.2001, p. 1, as amended by Decision 2002/634/EC (OJ L 206, 3.8.2002, p. 16).

- aid such as loans or loan guarantees for working capital needed to enable the undertaking to complete unfinished works provided that this is kept to the minimum necessary and a significant proportion of the work has already been done.

Undertakings receiving partial closure aid must not have benefited from rescue or restructuring aid in the past 10 years. Where less than 10 years have elapsed since the rescue or restructuring aid was granted, the Commission will allow partial closure aid only in exceptional and unforeseeable circumstances for which the company is not responsible.

The amount and intensity of aid must be justified by the extent of the closures involved, account being taken of the structural problems of the region concerned and, in the case of conversion to other industrial activities, of the Community legislation and rules applicable to those new activities.

In order to establish the irreversible nature of aided closures, the Member State concerned shall ensure that the closed shipbuilding facilities remain closed for a period of not less than 10 years.

Aid to shipbuilding in the form of *State-supported credit facilities* granted to national and non-national shipowners or third parties for the building or conversion of vessels and *aid granted as development assistance* to a developing country may be deemed compatible with the common market if it complies with the terms of the 1998 OECD Arrangement on Guidelines for Officially Supported Export Credits and with its Sector Understanding on Export Credits for Ships.

*Regional aid* may be deemed compatible if it meets the following conditions:

- the aid must be granted for investment in upgrading or modernising existing yards, not linked to a financial restructuring of the yard(s) concerned, with the objective of improving the productivity of existing installations;
- in regions referred to in Article 87(3)(a) of the Treaty and complying with the map approved by the Commission for each Member State for the grant of regional aid, the intensity of the aid must not exceed 22,5 %;
- in regions referred to in Article 87(3)(c) of the Treaty and complying with the map approved by the Commission for each Member State for the grant of regional aid, the intensity of the aid must not exceed 12,5 % or the applicable regional aid ceiling, whichever is the lower;
- the aid must be limited to support eligible expenditure as defined in the applicable Community guidelines on regional aid.

Aids for research & development and employment do not contain specific provisions for shipbuilding, the general rules having to be observed.



All plans to grant new aid to shipbuilding, ship repair or ship conversion, either in the form of a scheme or as individual aid not covered by a scheme, shall be notified to the Commission except if they fulfil the conditions set forth in one of the Regulations exempting certain categories of State aid from the requirement of prior notification.

The aid ceilings are applicable irrespective of whether the aid in question is financed wholly or in part from State resources or from Community resources. Aid authorized under this Framework may not be combined with other forms of State aid within the meaning of Article 87(1) of the Treaty or with other forms of Community financing, the cumulation of which produces an aid intensity higher than that laid down in the framework. Finally, in the case of aid serving different purposes and involving the same eligible costs, the most favourable aid ceiling will apply.

The Framework will be applicable from 1 January 2004 until 31 December 2006 at the latest. It may be reviewed by the Commission during this period, in particular in the light of the Community's international obligations.

### **5.3. Return to international competitiveness**

The EU maintains a world position in the high value added segment of shipbuilding. The problem of Japanese and South Korean competition remains crucial. The Community started negotiations with these two countries in 1988 with a view to bringing shipbuilding back into line with the internationally accepted rules and putting a stop to practices which distort competition and lead to unacceptably low prices. Negotiations within the OECD led to an agreement on 17 July 1994, meeting the main objectives of the Union. The agreement aims to eliminate all existing measures or practices which constitute obstacles to normal competitive conditions, namely direct and indirect support, anti-competitive regulations and unfair practices.

In response to the growing importance of the European maritime sector and the particularly vulnerable situation of the industry, the Commission has published, since 1988, a number of reports on the Community shipbuilding industry, including a 'Report on the State of the Shipbuilding Industry in the Community', which is revised annually. It also adopted, in 1991 and 1996, the communications on "New Challenges for Maritime Industries" (COM(91) 335) and "Shaping Europe's Maritime Future" (COM(96) 84), which seek to set out the Community's response to existing and future challenges. In October 1997, the Commission defined a new shipbuilding strategy (COM(97) 470), in which it proposed that the EU unilaterally apply the principles laid down in the OECD Agreement, introducing in 1999 stricter new rules for state aids.

Various forms of aid (mainly from the European Regional Development Fund and the European Social Fund) are granted for the development of the regions and the retraining of workers affected by the crisis in the shipbuilding industry.

## PART II

### COMPATIBILITY OF THE ROMANIAN LEGAL FRAMEWORK ON STATE AID RULES IN SENSITIVE SECTORS

The objective of this part is to check the compatibility with the *acquis communautaire* of the Romanian legal framework on state aid rules in sensitive sectors (steel, coal, motor vehicles, and shipyards). This part presents the main elements of Romanian legislation and the main problems identified in each of the above-mentioned sectors.

Law 143/1999, as modified by Law 603/2003, provides the general legal framework for the control and monitoring of state aids in Romania. The law defines the main legal concepts (state aid definition, types of state aids, existing aids, illegal and forbidden aids, state aid beneficiary, grantor of aid, etc.) and generally introduces the European system of *ex ante* control and *ex post* monitoring of state aids. The Competition Council has powers of decision, investigation and monitoring, similar to those of the European Commission (obviously, there are differences, because of the different levels at which the two systems operate, one national and the other supra-national).

Thus, Law 143 – Art. 2, 14, and 21 – introduces the EU system of control of state aids based on Art. 87 of the EC Treaty; the main elements are:

- state aids which distort the trade between Member States are forbidden (Art. 2(1));
- Art 2(2) lists the categories of aid which are exempt from the above prohibition: aids of a social character, granted to individual consumers and aids to make good damage caused by natural disasters or exceptional occurrences (**however, we have to mention that Law 603/2003 is not fully compatible at this point, because it mentions that these aids have not to be notified, a simple *avis* from the Competition Council being sufficient; as the European rules provide that such aid must always be notified to qualify for automatic exemption, the Romanian legislation should be modified accordingly**);

Art. 14(1) empowers the Competition Council to issue regulations, instructions or specific guidelines, in order to transpose the *acquis communautaire*. On January 2, 2003, the Council issued the following five regulations<sup>90</sup>:

- Regulation on regional aid and on aid for small and medium-sized enterprises;
- Regulation on rescue and restructuring aid;
- Regulation on training aid;

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<sup>90</sup> Official Journal of Romania no. 470, part I, July 2<sup>nd</sup>, 2002, pp. 1-32.

- Regulation on aid for R&D;
- Regulation on aid for environment protection.

Competition Council also adopted several other regulations and guidelines for the implementation of Law 143/1999:

- Guidelines on state aid and risk capital, published in the Official Journal no. 156&11.03.2003 (it transposes the Commission communication on state aid and risk capital – OJ C 235/21.08.2001) and entered into force at the date of publication;
- Multisectoral Regulation on regional aid for large investment projects, published in the Official Journal no. 165/17.03.2003, which transposes the Multisectoral Framework C107/07.04.98 in force in EU till 30.12.2003 for non-specified sectors;
- Multisectoral Regulation on transitional rules to be applied to state aid for large investment projects in non-specific sectors published in the Official Journal no. 165/17.03.2003, which transposes the the new Multisectoral Framework C70/19.03.2002 enforced starting July 24<sup>th</sup>, 2002 in steel sector and starting January 1<sup>st</sup>, 2003 in synthetic fibres and motor vehicles sectors;
- Guidelines on state aid in the form of guarantees published in the Official Journal no. 165/17.03.2003, which transposes the Commission Notice on the application of Art. 87 and 88 of EC Treaty to state aid in the form of guarantees (OJ C 071/11.03.2000);
- Guidelines on sales of land and/or buildings by public authorities which transposes the Commission Communication on state aid elements in sales of land and buildings by public authorities (OJ C 209/3/10.07.1997). The guidelines of the Competition Council have been published in the Official Journal no. 541/28.07.2003 and entered into force at the date of the publication.
- Regulation on state aid to employment (Official Journal no. 738/22.10.2003) which transposes the EC Regulation no. 2204/12.12.2002 (OJ L 337/13.12.2002).

#### *Procedures of recoupment/reimbursement of state aids*

In paragraph 1.4 we analyzed the issue of reimbursement of state aids in the European Union. In Romania, the main legal provisions on this issue are contained in:

- Law 143/27.07.1999 on state aids, as modified by Law 603/22.12.2003;
- Law 29/7.11.1990, as modified by general provisions of the Civil Procedure Code;

- Law 64/1995 on judicial re-organization and bankruptcy, as modified by Ordinance 38/30.01.2000 (Bankruptcy Law).

Illegal aids are defined in Art. 3(1) of the State Aid Law. It should be noted that this definition is less comprehensive than the European one, **because it does not cover non-notified changes made to aids already approved in the past.** Art. 5 and 6 of the Law provide that initiators and grantors of aids are obliged to notify to the Competition Council any intention to implement such measures, independently of their form and of the specific legal act (law, ordinance, government decision, etc.) by means of which they will be put into practice. Art. 7 provides that no aid can be implemented until the “Competition Council makes a decision of authorization or until the aid is considered to be authorized<sup>91</sup> (equivalent to *the stand-still clause* in the European legislation). If provisions in art. 5-7 are not observed, the Competition Council has to start procedures for recoupment, reimbursement or suspension of illegal aids, in accordance to provisions in art. 17-19, which are discussed below.

As we will see, the Law does not empower the Competition Council with direct attributions equivalent to those of the European Commission on recoupment of illegal aids. These differences can be explained by the fact that, in Romania, control on state aids is done at the national level. Therefore, situation in Romania is not similar to that in Member States: in the European Union, control on state aids is done by the European Commission on the basis of Community legal provisions and the Member States are obliged to comply with. In Romania, control is done by an administrative institution (Competition Council) on the basis of the State Aid Law which does not have precedence on any other Romanian law by means of which state aids are awarded. This creates legal, procedural and practical difficulties for the recoupment of illegal aids which will be mentioned below.

Art. 17(1) empowers the Competition Council to ask the relevant Court of Appeals (where the headquarters of the illegal aid grantor or beneficiary are situated) for the annulment of the administrative act and, consequently, for the recoupment, reimbursement or suspension of its payment. The legal distinction between recoupment and reimbursement is probably aimed to cover both those cases of illegal aid where a transfer of funds from public budget is involved and those where aid is indirect, by means of debt write-offs or rescheduling and other fiscal facilities. The suspension of the payments is a temporary measure up to the moment when the Court of Appeals makes a final decision; these provisions are similar to those in the EU Procedure Regulation. Art. 17(2) provides that the Court of Appeals may decide the suspension of the payments of illegal aid and that this decision may be contested to the Supreme Court.

It is to be noted that these procedures refer to “administrative acts by means of which the illegal aid has been granted” and do not apparently cover the normative acts (laws)

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<sup>91</sup> Such a formulation is not the most accurate, since it suggests that the Competition Council can make only positive decisions, i.e. decisions to authorize (either explicit or silent – when it does not make a decision in 60 days from the date when notification has become effective; however, art. 8 provides that the Competition Council may open an investigation and art. 12 that it may make decisions to authorize subject to conditions or decisions to forbid also.

which are involved in many cases. Actually, the Competition Council does not have the power to ask for the annulment of such aids in an administrative procedure, because the administrative courts do not have the power to challenge laws, government ordinances, or emergency ordinances. In order to be under the jurisdiction of an administrative court, the relevant act should be issued on the basis or when enforcing a normative act.<sup>92</sup> With regard to the control powers of the Council on the laws granting illegal aids, the State Aid Law provides for an unclear procedure, both from the point of view of its legal effects and of the possibilities to appeal in courts. Thus, in accordance to art. 17, paragraphs 3 and 4, when the Competition Council finds that an illegal aid has been granted by means of a law which infringed the provisions of Art. 5-6 (the obligation to notify and the stand-still clause), it sends a notice to the author of the law (presumably, the Parliament) and informs the grantor and the beneficiary. The parliament (or, the Government, in the case of ordinances or emergency ordinances) “is obliged to make a decision on the suspension of the law” in 10 days from the date when it received the notice (Art. 17(5)), and to notify to the Competition Council, together with the grantor, in 30 days. The Council will have to make a decision, asking for changes to be introduced in the law and on the recoupment or reimbursement of the aids already granted; the Parliament “should take into consideration” this decision (Art. 17(6)). Art. 18 provides for similar procedures when referring to forbidden aids. Finally, Art. 19(1)(b) provides that the Competition Council may ask, in the context of the annulment action introduced to the administrative court, for the recoupment or reimbursement of the interest associated to the illegal aid; the interest should be calculated from the date when the aid was at the disposal of the beneficiary and up to the date when the recoupment/reimbursement is finalized.

Several observations regarding these procedures are necessary. The Competition Council does not have the formal power to impose the annulment of the law by means of which an illegal aid has been granted and, consequently, its recoupment or reimbursement. The procedure in Art. 17 paragraphs 3-6 is rather a compromise, as long as the decision of the Council does not have legal binding effects for the author of the law. Moreover, the wording in para 6 shows that in such situations all the Competition Council can do is to ask for the modification of the law in order to become compatible with the State Aid Law; in other words, it can not ask for its annulment. On the other hand, it has to be recognized that such a compromise is the maximum that can be reached in the State Aid Law, which does not have any precedence over other laws in the Romanian legal system. If a legal procedure is to be put in place for the Competition Council, **the only solution that we can imagine is to introduce an article in the Constitution providing that the protection of a competitive environment is a constitutional value. Based on such a provision, the Competition Council may be able to ask for the annulment of the laws which infringe this principle.**

The procedure introduced by Art. 17 para 1-2 also contains unclear aspects which may block the attempt of the Council to annul administrative acts by means of which illegal aids had been granted and to obtain their recoupment or reimbursement:

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<sup>92</sup> See Court of Appeals Cluj, Commercial and Administrative Section, Decision no. 5/5.01.1999.

- It is not clear if the decision of the court to annul the administrative act and to ask for the recoupment/reimbursement of the aid has legal effects on the beneficiary also. If the beneficiary can not be brought in court by the Competition Council, then the decision of the court is binding only for the grantor; this raises serious doubts about the effectiveness of the enforcement of the decision.
- Also, it is not clear if the beneficiaries can intervene in the court. For instance, if the Competition Council has asked for the annulment of an act, the beneficiaries may be interested to go in court together with the grantor. Someone may argue that beneficiaries are a part in the trial due to the provisions of the Civil Procedure Code (art. 49-56). It remains to be seen however how interested beneficiaries are to intervene, as long as the ‘non-intervention’ could be more advantageous, because they may defend themselves in the context of the procedures enforcing the decision of the court, which is not binding for them as long as they are not a party in the process.
- The issues above are more pregnant if the aid is not an individual one, but an aid scheme – for instance, a law introducing fiscal facilities for certain beneficiaries. One of the first difficulties the Competition Council may face is to identify all the beneficiaries of the scheme (moreover, it is not difficult to imagine that in some cases the aid is illegal and in other cases is not). The other major difficulty will arise in the context of the enforcement of the decision to multiple beneficiaries.
- The last but not the least, it is unclear if the Competition Council can act in the context of Art. 17 para 1-2 when the grantor is not a component of public administration, but a bank (Savings Bank, for instance). In these cases, the grantor is not a party in the process, in conformity with the administrative proceedings.

Finally, there are several issues to be solved when the beneficiary is a firm in difficulty which is involved in procedures under the Bankruptcy Law. For instance:

- recoupment of interest is impossible when the beneficiary starts one of the procedures of reorganisation, liquidation, or bankruptcy (Art. 37 of the Bankruptcy Law);
- it is not clear if budgetary debts resulting from a decision of the administrative court to recoup or reimburse illegal aids benefit from the exemption from checking procedure provided in art. 58 in the Bankruptcy Law;
- Art. 30 of the bankruptcy Law excludes the possibility to ask the start of the reorganisation procedure in the case of firms which infringed the Competition Law. The case of infringements to State Aid Law are not taken into consideration and this may have significant effects: a firm may benefit the illegal aid up to the end of the reorganisation period (which may last up to 3 years); such a situation is in conflict with the basic principles, which ask for the restoration of the initial situation, before the illegal aid has been granted;

- Art. 108 provides that budgetary debts are the fourth to be payed, after the judicial expenses, bank debts and labour costs, which means that they may never be recovered.

As regards the **conformity** of the Romanian legal framework referring to state aids in sensitive sectors with the *acquis communautaire*, it must be said that regulations or specific other provisions – as requested by Art. 22(1) of Law 143/1999 – have not yet been transposed in the national legislation. As a result, general rules (as provided in the Law and other regulations) apply to these sectors also (with the exception of steel industry, where Art. 9(4) of Protocol 2 is relevant). We will underline below several shortcomings of the Romanian legislation in these specific sectors.

## CHAPTER 6

### STEEL INDUSTRY

As mentioned in chapter 2, section 2.1, in the European Union, after the expiry of the ECSC Treaty (July 23<sup>rd</sup>, 2002), state aids in this sector become subject to general (horizontal) rules issued for the enforcement of Art. 87-88 of the EC Treaty, with the following exceptions:

- aids for rescue and restructuring are forbidden (Commission Communication from March 2002<sup>93</sup>); only aids for closure of production capacities may be authorized;
- *regional aids for large investment projects* are also forbidden (Commission Communication from March 2002 and Multi-Sectoral Framework<sup>94</sup>), even in the case of SMEs; however, *regional aids for normal projects in the case of SMEs are allowed* if they observe the ceilings established by regulation no. 70/2001 on state aids to SMEs.<sup>95</sup>
- *aids for R&D, environment, employment and training* of employees are covered by the general rules which apply to all industries.

Such a restrictive policy aims to protect the results of a long restructuring process in the steel industry in the EU; the last restructuring aids have been authorized in 1993 and 1995 for 6 companies in East Germany, Italy, Spain, Portugal, and Ireland.

Which are the rules on state aids for rescue and restructuring in the steel industry enforced in Romania during the pre-accession period? Protocol 2 to the Association Treaty signed between Romania and the European Union<sup>96</sup> contains specific provisions for state aids in steel and coal industries. Thus, art. 9(1)(iii) provides that Romania will observe the rules in the ECSC Treaty. However, art. 9(4) provides the possibility for Romania, *as an exemption*, to continue to authorize aids for restructuring in the steel industry for a period of 5 years from the date of entry into force of the Association Treaty, if the following conditions were observed:

- the restructuring plan should lead to the restoration of the economic viability of the beneficiary under normal market conditions;

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<sup>93</sup> European Commission (2002): *Communication on rescue and Restructuring Aid and Closure Aid for the Steel Sector*, OJ C 70 from 19.3.2002.

<sup>94</sup> Communication from the Commission (2002): *Multisectoral Framework on regional aid for large investment projects*, OJ C 70 from 19.3.2002.

<sup>95</sup> Commission Regulation No 70/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to State aid to small and medium-size enterprises.

<sup>96</sup> Decision of the Council and the Commission of 19 December 1994 (94/907/ECSC, EC, Euratom), OJ L 357 din 31.12.1994, p. 1-.



- the amount and intensity of such aid are strictly limited to what is absolutely necessary in order to restore such viability and are progressively reduced.
- the restructuring programme includes measures of rationalization and reduction of excess capacities.

The Europe Agreements concluded with the other candidate countries included similar provisions, excepting Baltic states. The initial 5-year period expired on 31 December 1996 in the case of Czech Republic, Hungary and Poland and on 31 December 1997 in the case of Romania and Bulgaria. All these 5 countries requested a prolongation of this grace period. Hungary has withdrawn its earlier request in 2001 and confirmed that its steel industry would not receive any unlawful aid. As a result, no transitional measures have subsequently been agreed with Hungary.

During negotiations, in 2002, it became clear that, in the case of Slovakia, an agreement on the restructuring of its privatized steel industry could be reached, while in the case of the Czech Republic, Poland, Romania and Bulgaria specific transitional arrangements will be necessary.<sup>97</sup>

After the expiry of the ECSC Treaty on 23 July 2002, Protocol 2 has become redundant, as the provisions of the EC Treaty and relevant secondary legislation started to apply to steel industry also. In these context, to create the legal basis for such arrangements which, after the expiry of ECSC Treaty have to be based on Art. 87 and 88 EC Treaty, the ‘period of grace’ during which aid for restructuring the steel industry under the conditions in the initial Protocol 2 can be granted, has been prolonged for another 8 years or the date of accession, whichever comes earlier. In the case of Poland, this prolongation could be decided by the Association Council, while in the case of the Czech Republic, Bulgaria and Romania, due to the absence of a prolongation clause in the initial protocol 2, Additional Protocols to the Europe Agreements have been concluded. Conditions for the coming into force of the prolongation are the submission of a restructuring plan and business plans, fulfilling the criteria in art. 9(4) of Protocol 2 and the approval by the national monitoring authority (in Romania, the Competition Council). The plans will then have to be submitted to the Commission and after that to the Council for decision. The implementation of the plans will be monitored by the Commission and the national monitoring authority up to accession and by the Commission alone after the accession.

As a result, Romania can grant restructuring aids to steel industry only till 31 December 2005.

The European Commission identified the difficulties faced by the candidate countries in restructuring the steel industry in a *Communication* from 1998, which aimed to the elaboration of a global strategy of EU to support these countries in the restructuring of the industry:<sup>98</sup> the restructuring process faces difficulties due to the lack of funds

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<sup>97</sup> Peter Schutterle, *Enlargement: Pre-Accession State Aid after Accession*, in *European State Aid Law Quarterly*, vol. 2, no. 1, January 2003.

<sup>98</sup> Communication from the Commission to the Council the European Parliament and the ESCS Consultative Committee on A Global Approach to Promote Regional and Social Conversion and to

(despite assistance coming from various international financial institutions); the restructuring process generates regional and social problems (due to the concentration of this industry in specific regions); the lack of attractiveness for foreign investors is generated by environmental issues and inadequate regional infrastructure also.

We try below to answer to the following questions referring to state aid regime in the steel industry in the pre-accession period:

- a. Which is the preferential treatment for Romania in restructuring aids in the steel industry during the period of implementation of art. 9(4) of Protocol 2 and Additional Protocol?
  - b. Which will be the situation after the expiry of this temporary derogation?
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- a. Up to the end of 2005, Romania can grant aids for restructuring in the steel industry, while in the EU such aids are forbidden (excepting aids for permanent closure, as seen above).

Moreover, art. 9(4) of Protocol 2 is even *more relaxed than the general rules applied to rescue and restructuring aids in other industries* of the European Union. A brief presentation of these rules is necessary, in order to understand the above conclusion.

The European Commission issued the first *Guidelines* on rescue and restructuring aid in 1994<sup>99</sup> and modified them in 1999.<sup>100</sup> This last version will expire at 9 October 2004. In February 2004, the Commission published a draft of the new Guidelines; the main modifications are presented below.

The 1999 Guidelines (currently in force) contain the following main provisions:

- *Art. 2.1 clarifies the concept of “firm in difficulty”* which may benefit of rescue and restructuring aid. Thus, the Commission regards a firm as being in difficulty where it is unable, whether through its own resources or with the funds it is able to obtain from its owners/shareholders or creditors, to stem losses which, without outside intervention by the public authorities, will almost certainly condemn it to go out of business in the short or medium term.
- *Art. 2.2 defines “rescue aid” and “restructuring aid”.*

Thus, **rescue aid** is by nature temporary assistance that should make it possible to keep an

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Facilitate Industrial restructuring in the Central and Eastern European Countries: the Case of Steel, Bruxelles, COM(1998) 220 final din 7.04.1998.

<sup>99</sup> European Commission (1994): Guidelines on State aid for rescuing and restructuring firms in difficulty, OJ C 368 of 23.12.1994.

<sup>100</sup> OJ C 288 din 9.10.1999.

ailing firm afloat for the time needed to work out a restructuring or liquidation plan and/or for the length of time the Commission needs to be able to reach a decision on that plan. Such aids may be authorized for maximum 6 months (para. 24 of the Guidelines); this period can be extended, but only in exceptional circumstances. Rescue aids may only consist of liquidity support in the form of loan guarantees or loans (para 23 a). Finally, such aids should be restricted to the amount needed to keep the firm in business for the period during which the aid is authorised (for example, covering wage and salary costs or routine supplies).

Restructuring aid, on the other hand, should be based on a feasible, coherent and far-reaching plan to restore a firm's long-term viability. Aid for restructuring can take different forms, such as capital injections, debt write-offs, loans, relief from taxes or social security contributions, or loan guarantees. There are no provisions referring to the period for which the aid is authorised. This period is linked to the restoration of the viability of the firm (end of the restructuring plan).

- Art. 3.2.2 specifies *several conditions* that should be met for the aid to be authorised:
  - The restructuring plan, the duration of which must be as short as possible, must restore the long-term viability of the firm within a reasonable timescale and on the basis of realistic assumptions as to future operating conditions.
  - Measures must be taken to mitigate as far as possible any adverse effects of the aid on competitors (for instance, a limitation on the presence which the company can enjoy on its market or markets after the end of the restructuring period or diminishing of excess capacities).
  - The amount and intensity of the aid must be limited to the strict minimum needed to enable restructuring to be undertaken in the light of the existing financial resources of the company, its shareholders or the business group to which it belongs. Aid beneficiaries are expected to make a significant contribution to the restructuring plan from their own resources, including through the sale of assets that are not essential to the firm's survival, or from external financing at market conditions. To limit the distortive effect, the amount of the aid or the form in which the aid is granted must be such as to avoid providing the company with surplus cash which could be used for aggressive, market-distorting activities not linked to the restructuring process. The Commission will accordingly examine the level of the firm's liabilities after restructuring. The aid should not go to finance new investment that is not essential for restoring the firm's viability.
  - The beneficiary can not receive other type of state aid.
  - The firm may benefit of restructuring aid only once in 10 years (the so-called "one time, last time" condition). *An exception* to this rule is when the firm has been affected by external factors of which it is not responsible. *Another exception*

is for East-Germany companies which have received state aids up to 1 January 1996.

- *Provisions on monitoring of the aid and of the restructuring plan:* thus, where restructuring operations cover several years and involve substantial amounts of aid, the Commission may require payment of the restructuring aid to be split into instalments and may make payment of each instalment subject to confirmation, prior to each payment, of the satisfactory implementation of each stage in the restructuring plan, in accordance with the planned timetable. Moreover, in the case of aid to large firms, annual reports should be sent to the Commission on the implementation of the restructuring plan (the first report, in 6 months after the authorisation).
- Art. 3.2.4 contains provisions referring to the case when the restructuring plan is modified. If the aid is increasing, the compensatory measures are modified as well, becoming proportionally more restrictive.
- *In assisted areas* (as defined in art. 87(3)(a) or (c)), however, and unless otherwise stipulated in rules on State aid in a particular sector, the conditions for authorising aid may be less stringent as regards the implementation of compensatory measures. If regional development needs justify it, the required capacity reduction will be smaller in assisted areas than in non-assisted areas and a distinction will be drawn between areas eligible for regional aid under Article 87(3)(a) of the Treaty and those eligible under Article 87(3)(c) so as to take account of the greater severity of the regional problems in the former areas. The same applies to SMEs (art. 3.2.6 of the Guidelines).
- Finally, art. 3.2.7 clarifies the situations when measures aimed to support the redundant employees will be considered as state aids. Thus, measures like early retirement or unemployment benefits are not state aids if they can be enforced in any sector, in the same conditions. However, if such measures are selective, targeted on a specific sector or beneficiary, they will be considered as state aids, if the expenses incurred would have had to be supported by the beneficiary.

The Draft Communication from February 2004<sup>101</sup> introduces the following changes to the current regime of rescue and restructuring aids:

- A new concept of "urgency aid" is introduced (by replacing "rescue aid"), which would also allow the beneficiary to undertake urgent measures, even of a structural nature, like an immediate closure of a branch or another form of abandonment of loss making activities. The draft confirms the other conditions for the authorisation of rescue aids, including the 6 months period and the form they can take (loans or loans guarantees).

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<sup>101</sup> *Community Guidelines applying Articles 87 and 88 of the Treaty to the granting of urgency and/or restructuring aid to firms in difficulty*, [http://europa.eu.int/comm/competition/state\\_aid/others/](http://europa.eu.int/comm/competition/state_aid/others/).

- As regards restructuring aids, building on the 1994 guidelines, the 1999 guidelines continued to require a substantial contribution from the beneficiary to the restructuring, but without being more specific. The new draft communication provides that small enterprises should co-finance at least 25% of the costs of restructuring from their own resources (in exceptional circumstances, 20%), medium ones 40% (35%, in exceptional circumstances), and large companies at least 50%.
- The principle “one time, last time” is confirmed. No exceptions are being done anymore, like those for East-Germany companies in the 1999 Guidelines.

We said earlier that the rules provided in art. 9(4) of Protocol no. 2 for the steel industry in Romania are less binding than the general rules for rescue and restructuring aid in other industries in the European Union. Thus:

- Art. 9(4) *does not mention the “one time, last time principle”*; it is therefore possible that the European Commission will have a more relaxed approach for the aids in the steel industry in Romania, like for instance in the case of several successive strategies of restructuring which fail, but not due to bad administration of the resources allocated to this objective. There is also a precedent, in the flexible approach of the Commission vis-à-vis the aids for the restructuring of the East-Germany industry after their reunification. We will not go into details, because this regime is significantly different to that applied in the case of the candidate countries.<sup>102</sup> It should be noted however, that the European Commission and the German Government agreed on specific rules on the aids granted by Treuhandanstalt (THA – the German federal agency in charge with privatization), in the context of the privatization and restructuring of about 10000 companies in East Germany. This agreement has given to the Commission the possibility to control the various types of financial aids given by THA, including rescue aids, recapitalisation, debt write-offs, or aids in the context of privatisation. In this context, the Commission often “tolerated” infringements of “one time, last time” principle, in cases of failures of the restructuring plans. However, it has to be mentioned that this approach was valid mainly for other industries, and not for the “sensitive” ones. Therefore, these remarks should not be interpreted at all as an encouragement for granting rescue and restructuring aids which do not observe the European rules.
- Similarly, art. 9(4) *does not provide for the obligation of co-financing from the part of the aid beneficiary*. It is to be understood that this condition will be applied on a case by case basis, by taking into consideration the financial situation of the beneficiary and of the sector.

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<sup>102</sup> See Michael Schütte si Jan-Peter Hix 1995): “The application of the EC state aid rules to privatizations: the East German example”, *Common Market Law Review* 32, pp. 215-248; Stefaan Depypere (1998): “State aid policy enforcement in the new Länder of Germany – Status in 1997”, *EC Competition Policy Newsletter* No. 2, pp. 45-47.

- The condition to decrease the excess capacities is applied by the Commission in a more severe way in the sensitive sectors. On the other hand however, the community legislation – as showed above – is more permissive with beneficiaries operating in “assisted regions”, as defined in art. 87(3)(a) and (c) of the Treaty. Currently, the whole territory of Romania has the status of assisted region, as defined by art. 87(3)(a).
  - Finally, the limitation of rescue aids only to loan or loan guarantees will probably not be enforced so strictly in Romania, if taking into consideration the lack of budgetary resources and the difficulties of accessing other financing sources. In other words, it is possible to grant rescue and restructuring aids in the form of debt write-offs or other fiscal facilities. It is the case of a steel mill in Slovakia, which will benefit of fiscal facilities up to the end of 2009 or up to the moment when the total aid will reach a certain agreed amount.<sup>103</sup>
- b. What will be the regime of state aids in the steel industry in Romania after 31 December 2005?

As shown above, in the case of Romania, the validity of the provisions of Protocol 2 have been extended, by the Additional Protocol, up to end-December 2005. *There are opinions saying that this period may be extended again, in order to cover the whole period to the accession* (in the case that this date will be January 2007; it is difficult to speculate on the possibility of an extension if the accession date will be later). Arguments favouring this opinion are contained in the protocols concluded by Czech Republic and Poland which allowed for effective payments of aids up to the end of 2003, i.e. approximately the date of accession (May 2004). This may suggest that Romania will enjoy the same treatment. There are however arguments against. In the case of the countries which acceded in May 2004, the date of accession came first (before the end of the extension), a situation which will not occur in the case of Romania. Therefore, it should be mentioned that, if these provisions will not be extended up to the date of accession, then starting with 1 January 2006, Romania will have to observe the current rules in the European Union as they have been mentioned above: rescue and restructuring aids for the steel industry are forbidden (with the exception of those granted for permanent closures). **After the date of accession, Romania will not be allowed to grant rescue and restructuring aids in the steel industry in the absence of transitional periods as negotiated by Slovakia.**

A separate discussion should be done on rescue and restructuring aids to steel industry authorised under the provisions of Protocol 2 (i.e., up to December 2005) for restructuring plans which go over that date, or even over the date of accession. As a principle, state aids authorised during the pre-accession period will be considered as “existing aids” (so, “legal” aids) and therefore they will continue to operate, if they have been authorised by the national monitoring authority (Competition Council) and if the European Commission has not raised any objections. This principle is stipulated in Annex IV to the Accession Treaty signed by countries who became members of the

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<sup>103</sup> Janne Känkänen (2003): “Accession negotiations brought to successful end”, *EC Competition Policy Newsletter* Nr. 1, pp. 24-28.

Union in May 2004. On the other hand, the Protocols on state aid to steel industry in Poland and Czech Republic – annex to the Accession Treaty – contain specific provisions referring to rescue and restructuring aids in steel industry: **such aids can not be paid after the date of accession**; however, the end of the restructuring period is 31 December 2006, while for several of the beneficiaries (as mentioned in Annex 1 to the Protocol) payments should be done no later than end of 2003.

What are the conclusions that can be drawn for Romania? **For the aids authorised under the provisions in Protocol 2, effective payments should be finalised either before the date of accession (the optimistic approach) or before 1 January 2006 (the pessimistic approach; our opinion is however that this is less probable, taking into consideration that at the moment of writing we are in April – May 2004 and the restructuring strategy and the individual business plans have still to be analysed by the Commission and approved by the Council), even if the end of restructuring process will be after the accession date.** Analysing the case of Poland and the Czech Republic we may draw the conclusion that it exists a period of time considered as a “reasonable maximum” for the implementation of a restructuring plan and of the aid measures and that this period may expire anytime, from case to case, even before the accession date.

Before concluding, a short discussion on the aids granted in the context of the privatisation process is necessary. We can find two different situations: the first one, when rescue and/or restructuring aids are granted before privatisation, in order to restore the viability of the company and then to sell it, and the second, when privatisation itself is part of restructuring, thus trying to bring in private funds for covering the costs of the restructuring.

In both cases, the general criterion is the “market investor (creditor) principle”, as it has been presented in general lines in chapter 1, section 1.1.

In the first situation, the state is both owner and grantor of aid. The question to be answered is if the state is acting in the same way as a market investor will do in a similar situation. Most of the cases are involving capital injections, subsidised loans, debt write-offs or debt rescheduling.

In a Communication from 1984<sup>104</sup>, the European Commission explains the relationship between state aid and financial measures adopted by the state as an owner. According to this Communication, capital injections will not be considered as state aid if they are linked to new investments, the company is economically viable and does not operate in a sector in structural crisis (art. 3.2.(ii)). However, when the firm is in difficulty, capital injections may be regarded as state aids. More general, the community concept of state aids includes “any form of financial support granted by the state to a company partially or fully owned by the state and which does not correspond to the behaviour of a private investor acting on a free market.”

Regarding state aid in the context of the privatization of firms in difficulty, several principles have been developed in the community case law:<sup>105</sup>

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<sup>104</sup> “Application of Articles 92 and 93 of the EEC Treaty to public authorities’ holdings”, EC Bulletin 91984.

<sup>105</sup> Andrew Evans (1997) “Privatization and state aid control in E.C. law”, 4 *European Competition Law Review* pp. 259-264.

- Privatisation does not involve state aid when: shares are sold on the stock exchange; privatisation is done by means of tender to the best offer and the tender is open and non-discriminatory. Moreover, state aid will not be involved even when the price is lower than the bookvalue of the company, if this is the result of the future costs to be covered by the buyer in the context of restructuring.<sup>106</sup>
- Privatisation involves state aid when its costs are higher than those incurred by its liquidation.<sup>107</sup> It was the case when the British government sold Rover to British Aerospace.<sup>108</sup>
- When privatisation has as objective to obtain funds necessary for the restructuring, the European Commission may adopt a more relaxed approach towards the decrease in excess capacities.
- We have mentioned already in chapter 1 that the community case law recognises that the behaviour of the state should not be compared to that of a private investor that is looking for short-term profits, but to that of a private group that is enforcing a ‘structural’ economic strategy on medium or long term.<sup>109</sup>

**In Romania, the current legal framework of state aids in steel industry** derives from art. 9(4) of the former Protocol 2, Law 143/1999 (as modified by Law 603/2003) and the regulations adopted by the Competition Council. The legal framework during the period between the expiry of the Protocol (December 2005) and the date of accession remains unclear, two possibilities being taken into consideration: either the provisions of the Protocol are extended up to the date of accession or European rules have to be enforced, as mentioned above. From the date of accession, it is clear that the community rules will have to be observed. What is not clear after that date is if effective payments can still be done in the case of aids authorised before the accession (“existing aids”); looking at the countries which became members in 2004, it is probably that the answer to that question is no.

Referring to the current legal framework, several observations can be made:

- *aids for rescue and restructuring, aids for permanent closures*: in the absence of specific regulations issued by the Competition Council – which should transpose the conditions mentioned in art. 9(4) of former Protocol 2 – the legal framework remains somehow unclear, both for the grantors and for the beneficiaries. From a formal point of view, it may be possible that the Competition Council faces procedural difficulties to forbid or enforce negative decisions on the basis of Protocol 2. For instance, art. 4 of the *Regulation on rescue and restructuring aids* is mentioning that this regulation does not apply to the steel sector, without making it clear which are the rules to be

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<sup>106</sup> Decision of the European Commission 89/661 in the case *Alfa Romeo*, OJ L 394 [1989] p. 9.

<sup>107</sup> Decision of the European Commission 92/321 *Intelhorse*, OJ L 176 from 1992, p. 57.

<sup>108</sup> Decision of the European Commission 89/58 *Rover Group*, OJ L 25 [1989], p. 92.

<sup>109</sup> See cases *ENI Lanerossi* si *Alfa Romeo*, mentioned in Chapter 1, section 1.1.



applied in this sector (while the European Guidelines from 1999 contain such a provision).

- *regional aids*: the regulation issued by the Competition Council on regional aids explicitly mentions that it does not apply to the steel sector. Art. 1(2) provides that in the steel industry “legislation currently in force will apply up to the moment when specific rules will be adopted”. Consequently, the current Romanian legal framework does not provide for the interdiction of state aids for large investment projects in the steel industry, inclusively for SMEs. **At the same time, the rules for state aids for ‘normal’ investments done by SMEs are included in the same regulation; as a result, by excluding the steel sector from its scope, it means that such aids are also forbidden (which is not the case in the Community).**
- there are not other problems related to aids for R&D, environmental protection, employment and training.

## **CHAPTER 7 COAL INDUSTRY**

As shown in chapter 3, section 3.1, after the expiry of the ECSC Treaty (23 July 2002), state aids for hard coal are under the rules provided by Regulation 1407/2002.<sup>110</sup> If this regulation applies only to hard coal, then the other types of coal (like lignite, for instance) are under the general rules for state aids. In accordance to regulation 1407/2002, the following aids can be authorised:

- *operating aids*, to cover the losses of the units which will be permanently closed up to the end of 2007;
- *regional aids for investments*, up to 2010, if the investments are part of a coherent plan to maintain a minimum level of domestic production and if the beneficiaries did not receive such aids in the past; the same beneficiaries can obtain operating aids also;
- aids aimed to cover debts resulting from the implementation in the past of restructuring plans;
- aids for R&D, environment protection and training in accordance to general rules valid for all the sectors.

Romania has not yet transposed Regulation 1407/2002. At the same time – similar to the steel sector – the coal industry is not under the scope of the regulations on rescue and restructuring and regional aids. As a result, general rules apply to this sector. **In other words, currently in Romania, there is no legal framework on the basis of which regional aids or aids for rescue and restructuring in the coal industry can be authorised. An urgent transposition of Regulation 1407/2002 is therefore necessary.**

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<sup>110</sup> Council Regulation No. 1407/2002 of 23 July 2002 on state aid to the coal industry, OJ L 205 from 2.8.2002.

## **CHAPTER 8.**

### **MOTOR VEHICLES**

Starting 2004, state aids to motor vehicles industry in the European Union are subject to general rules as mentioned in art. 87-88 of the Treaty. **Specific rules for this sector exist only for regional aids for large investment projects:** the Multi-Sectoral Framework<sup>111</sup> provides that, up to 2006, the motor vehicle industry will be subject to lower intensity rates than those for other industries in assisted regions. Thus, regional aids for motor vehicle sector should not be above 30% of the maximum allowed intensity in the assisted region, in the case of investments larger than Euro 50 million or for aids larger than Euro 5 million.

In accordance with Decision 1811/2002 of the Association Committee, regional aids in Romania can meet the maximum aid intensity of 50%, respectively 65% for SMEs. Competition Council adopted the Multi-Sectoral Regulation on regional aids for large investment projects<sup>112</sup>, which transposes the community rules in this field (respectively, a ceiling of 30% of the maximum aid intensity, for large investment projects in the motor vehicle industry). From this point of view, Romanian legislation is in line with the community legislation. **One modification should still be made however to art. 24 and 28-29, which provide for a list of sectors with structural difficulties to be published at the beginning of 2004 (see paragraph 4.2, point 5 above). In this context, Romania has to transpose Commission Communication from 1.11.2003 on modifications to Multi-Sectoral Framework.**

The Regulation issued in 2002 on regional aids provides that in the motor vehicle industry (art. 1(2)) “legislation currently in force will apply up to the moment when specific rules will be adopted”. This wording is normal if taking into consideration that the Regulation has been adopted before the expiry of the specific Framework for motor vehicle industry in the EU, but can however create confusions.

On the one hand, someone could understand that the Regulation on regional aids does not apply to the motor vehicle industry and thus there is another lack of legislation, due to which such aids can not be authorized. On the other hand, someone else could understand that regulation on regional aid can be applied up to the moment when specific legislation will be enacted. **In order to eliminate such potential confusions, it may be sufficient to renounce to mention the motor vehicle industry in art. 1(2).**

There are no problems related to the other types of aid for this sector.

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<sup>111</sup> Communication from the Commission: *Multisectoral Framework on regional aid for large investment projects*, OJ C 70 from 19.3.2002. See also European Commission: *Communication on the modification of the Multisectoral Framework on regional aid to large investment projects (2002) with regard to the establishment of a list of sectors facing structural problems and on a proposal of appropriate measures pursuant to Article 88 paragraph 1 of the EC Treaty, concerning the motor vehicle sector and the synthetic fibres sector*, OJ C 263 from 1.11.2003, p. 3.

<sup>112</sup> Official Gazette of Romania no. 165/17 March 2003.

## CHAPTER 9 SHIPBUILDING

Currently, state aids for shipbuilding are regulated by a specific Framework.<sup>113</sup> The main principle is that state aids in this sector follow the general rules as mentioned in art. 87-88 of the Treaty. There are however specific rules for the following types of aids:

- *aids for innovation* may be authorized up to a maximum intensity of 20% if certain conditions are met (see chapter 5, section 5.2);
- aids to cover costs incurred by partial or total closures of capacities;
- aids to cover losses incurred by permanent closures;
- *export aids* and/or assistance to a developing country if they meet provisions in the 1998 OECD Arrangement;
- *regional aids*, but only for modernization and only in assisted areas (up to 22.5% in regions under art. 87(3)(a) and 12.5% in those under art. 87(3)(c)).

Romania has not transposed yet the specific Framework for this sector. The same comments as made above for the motor vehicle industry (referring to art. 1(2)) remain valid for shipbuilding also. On the other hand, Regulation on rescue and restructuring aids applies in shipbuilding (it is not exempted explicitly as the other sectors discussed above), but does not contain provisions referring to compensations for closures. **Therefore, Romania needs to transpose the specific community legislation. Until then, regional aids may be authorized up to a higher maximum intensity than that accepted by the community rules, while aids for innovation or export may not be authorized.**

There are other problems related to other types of aids (R&D, environment protection, employment, training).

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<sup>113</sup> European Commission (2003): *Community Framework on State Aid to Shipbuilding*, OJ C 83 from 23.3.2003.

### **PART III**

## **ASPECTS REGARDING PRE-ACCESSION PERIOD AND NEGOTIATIONS IN THE NEW MEMBER STATES**

Accession negotiations with candidate countries consisted, to a great extent, in insuring the transposition of community rules (“the *acquis*”) into the national legislation of new members. The targeted objective was obvious that the largest part of community legislation to be already in force at the accession moment.

After this moment, aids authorized according to the national legislation before accession date, may be granted only in two situations:

- either they are considered existing aids;
- or some transition periods have been accepted to allow a gradual alignment of incompatible aids against the *acquis*.

The existing aids are either “old” aids or “listed” aids<sup>114</sup>. The old existing aids are, in the case of the states which have become members at 1 May 2004, aids granted before 10 December 1994 (the date when came into force the Law on Special Economic Zones in Poland, by which 17 such zones had been set up and based on it numerous aids have been granted so far)<sup>115</sup>. The amount of these aids, which will produce effects after the accession date, is probably not significant.

On the other hand, after accession, existing aid in the sense of Article 87, paragraph 1, from CEE Treaty is that aid which had been approved by national authority, then notified to Commission and this one had no objection to it. These aids are included in the lists delivered by the candidate countries, which became members at 1 May 2004, to European Commission : i) in January 2003 (list 1) and ii) just before the accession (list 2).

In the case of list 1 the candidate countries should not deliver complete notifications of aids, but only a resume of individual cases and the arguments of national authorities<sup>116</sup>. It results then, that in these cases, European Commission will not do the same detailed analysis which is made in the case of state aids from Member States.

List 2 is “the intermediary period list” and consists of aids granted from the moment of signing the Accession Treaty until the real accession date. In the case when Commission has no objections to state aids on both lists, then they will be considered existing aids at the accession date.

The two lists are not, by their nature, the subject of accession negotiations. However list 1 needs the approval of European Council, because it will be annexed to Accession Treaty. No one of the Member States (the 15) had any objections to state aids on the list 1, maybe also due to the lack of detailed information. List 2 will be made without the implication of Member States, but only on Commission responsibility.

Lack of concrete cases makes it persist some ambiguities as concerns the conditions in which some aids might be excluded from respective lists. This fact reflects, in fact, the specificities

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116 Peter Schutterle, *Enlargement: pre-Accession State Aid after Accession*, In Europe State Aid Law Quarterly, vol.2, no.1, January 2003.

117 In the case of Romania and Bulgaria it will probably be fixed a date previous to this.

118 Actually, the necessary information refer to the measure title, period, authorization date, responsible authority, aid category, amount, as well as a short description.

of period, namely before the accession it is applied the legislation of respective country, while European rules and standards are not directly applicable.

Moreover European Commission accepts at least one of the main effects of existing aid notion, namely the paid amounts – before the accession – over the accepted thresholds or conflicting with other *acquis* provisions must not be recovered. This statement has to be corroborated also with the fact that – although it had asked to candidate countries to apply the *acquis* in the field of competition well before accession – however European Commission has never said that the incompatible aid granted based on national legislation in the pre-accession period would not be legal. Moreover, as concerns the state aids incompatible with single market requirements, European Commission has reserved its right to open formal investigations under the meaning of Art.88(3) of Treaty and Art.4 of Council Regulation no.659/1999 against one of the proposed measures by candidate countries on list 2. In conclusion aids which are not compatible will not be recovered, but they may not continue after the accession date without the approval of European Commission.

From the point of view of aspects related to legal safety, the beneficiary interests of state aids are protected until the accession date. However, it is possible in the case of aids which have, to a certain extent, the character of multi-annual programs – as some fiscal aids are - to occur also certain retroactive alignments, in conformity with national legislation. At the same time, the national legislation is still the relevant one also in the case in which some affected beneficiaries would ask for damages for canceling some aids they have got previously. In order to strengthen the legal safety they benefit from, the aid beneficiaries must address to national authority or aid supplier to check if the respective aid is on the list.

For example, list 1 contains, in the case of Czech Republic, over 250 state aid measures, of which over 150 are investment incentives granted based on a specific law. The reason for introducing them on the list lies in the fact that the respective law has been notified neither to national authority nor to European Commission as a state aid scheme.

In certain cases certain transitory periods are negotiated which have the aim either to offer to the new Member States an additional time for adaptation, or to avoid producing some excessive sectoral shocks in the old Member States. These transitory periods, which in fact represent some timing and temporary derogations from community law, are either granted or imposed to candidate countries. As a rule they are accompanied by clear conditions, which are meant to prevent the new Member States to get any competitive advantage from not applying the *acquis*, as for instance, the imposition of some production quotas for the countries that are allowed to grant restructuring aids for steel industry. These derogations, depending on the chapter, may be negotiated either collectively (e.g. in the case of free movement of persons) or individually, with every country separately, as it is the case of chapter 6 “Competition”. Moreover, through monitoring system put into practice – for instance, reports at every 6 months – European Commission exerts a rigorous monitoring until their removal.

The article 24 from part four of Accession Treaty (“Temporary Provisions”), title I (“Transitory Measures”) mentions that the measures enumerated in Annexes V-XIV will be applied in the conditions stipulated in these annexes. These measures represent, in fact, temporary derogations from the rules regarding the control of state aid in EU and have been obtained by some candidate countries in the course of accession negotiations. Practically five from the ten countries which have become members of EU at 1 May 2004 benefit from such derogations.

Accession Treaty includes also 8 more Protocols, of which 2 refer to steel industry from Czech Republic (Protocol 2 – three companies) and Poland (Protocol 8 – eight companies). These protocols contain also some transitory arrangements (which were previously approved by European Commission) and it is conceivable that Romania will benefit from the same treatment.

*Derogations obtained by some candidate countries*

A synthesis of derogations, **by types**, is presented in the next table:

<ul style="list-style-type: none"> <li>• <b>Postponings granted at the canceling of incompatible aids:</b> <ul style="list-style-type: none"> <li>○ Aids granted to SME's <i>Poland, but only for these situated in special economic zones (medium enterprises until 2010, small enterprises until 2011); Malta, Hungary – until 2011.</i></li> <li>○ Aids granted to local administrations <i>Hungary – until the end of 2007.</i></li> <li>○ Aids granted within off-shore regime <i>Hungary – until the end of 2005.</i></li> <li>○ Aids for environment protection <i>Poland – until the end of 2007.</i></li> <li>○ Aids for motor vehicle industry <i>Hungary, Slovakia – until the end of 2008.</i></li> <li>○ Aids for steel industry <i>Slovakia – until 2009.</i></li> <li>○ Restructuring aids <i>Malta - until 2008.</i></li> <li>○ Operating aids <i>Malta - until 2008.</i></li> </ul> </li> </ul>
<ul style="list-style-type: none"> <li>• Restructuring of steel industry <i>Poland, Czech R. – until 2006.</i></li> </ul>
<ul style="list-style-type: none"> <li>• Restructuring of shipyard sector <i>Malta – until 2008</i></li> </ul>
<ul style="list-style-type: none"> <li>• Reorganizing petroleum product market (elimination of state monopolies) <i>Malta – until 2005.</i></li> </ul>

Country analysis reveals that Poland benefits from a transitory arrangement on some fiscal facilities. This requires the modification of individual aids granted according to the Law of Special Economic Zones from 1994. Poland has got a derogation also for the steel industry (Steel Protocol) within the Accession Treaty, aiming at restructuring this branch until the end of 2006. In this context, Poland had the right to grant restructuring aid until the end of 2003 (the maximum approved amount includes aids granted in 1997-2003 period) to a predefined group of steel companies whose restructuring program ends in 2006. Poland has also the obligation to report, at every 6 months, on the implementation mode of restructuring plan. It is important to note that the aid may not exceed some pre-established amounts and may not be granted to other companies than those initially convened. **Recent evolutions are worth of mentioning. Starting with February, Polish Government has negotiated on privatization of steel works Huta Czestochova with LNM Group, steel works that was not included in the restructuring plan of steel industry, convened by Poland with EU. The sale has been postponed due to European Commission objections on state aid which was intended to be granted. This decision threatens the steel mill with bankruptcy. Available information at this moment show that negotiations will be**

**resumed after Poland comes to an agreement with EU on restructuring program of steel works and on state aids which will eventually be granted.**

Czech Republic benefits from a similar arrangement, related to restructuring program of steel industry. The mentioned conditional terms and deadlines are similar to those in the case of Poland, the only difference consisting of the number of involved companies (3 in Czech Republic, 8 in Poland) and evidently the maximum aid amounts which were going to be granted during 1997-2003 period. It is worth mentioning that after signing the Accession Treaty, Czech Republic tried once more to persuade European Commission to agree upon another state aid (under the form of an erasing of debts of 2 billion crowns) – for the company Trinecke Zelezarny (TZ) – for the reason that Czech Government had already given support to main competitor of TZ. European Commission rejected two times these requests, based on the argument that it would have been extremely dangerous to undertake something it would have seemed as a infringement of Accession Treaty. Any illegal aid would lead to a re-evaluation of all already approved aids.

**Slovakia** benefits from two transitory periods, within which it may continue to grant fiscal aids for two companies. These two belong to steel industry and motor industry, but the aids may be granted until the end of 2009, and respectively 2008, if certain conditions are fulfilled. At the same time European Commission has warned Slovakia on its concern regarding the observance of conditions for production reduction by the steel company and has asked for providing that all conditional terms stipulated by exceptional transitory arrangements are accomplished.

**Hungary** benefits from a transitory arrangement for removing certain individual fiscal aids for off-shore companies (until 31 December 2005) and SME's (until 31 December 2011), as well as aids granted by local authorities (until 31 December 2007). The other companies (others than SME's) will continue to benefit from these facilities, but with the observance of some conditions (e.g. regional aid granted to motor industry may not exceed an intensity of 30% in the case of companies which have started investment program before 2000 and respectively 20% for those that have started it in 2000-2002 period); the eligible costs that may be taken into account are those effected between 31 January 1997 and 31 December 2005, within a formal program conceived by the company not later than 31 December 2002 and notified to Hungarian Finance Ministry until 31 January 2003. It is interesting to notice that the admissible maximum intensity in the case of the companies which have started investments before 2000 is 75%, namely over the admissible maximum of community regulation in force.

**Malta** is the only candidate country which has got a transitory arrangement, which allows her to grant state aids (including operating aids) - limited to certain amounts - for two shipyard companies.



## PART IV THE SITUATION IN ROMANIA

This last part of the study is trying to analyze the state aids granting policies in some of Romania's sensitive sectors. To this purpose, the approach is rather a qualitative than a quantitative one, although the figures have their own importance and will not be overlooked.

But the sources referring to the amounts granted as state aids are poor and not always reliable. The following quantitative informations are available in the "*Strategy for restructuring the iron & steel industry of Romania*", drawn up by the Ministry of Economy and Trade in April 2004, which is going to be analyzed by the European Commission and submitted for approval to the European Council.

This strategy is based upon the report drawn up by the consultancy firm Roland Berger including an analysis of the Romanian strategy for restructuring the iron and steel industry and the individual viability plans of the existing firms. We resorted also to the Competition Office reports regarding the situation of state aids' granting in Romania<sup>119)</sup> and to the "*Scoreboard*" dedicated to the candidate countries<sup>120)</sup>. – drawn up in 2002, by the European Commission. **Consequently, the authors can't be kept responsible for the data presented, but it is for sure that the comments, opinions and analysis belong exclusively to them.**

The analysis concerning the **compatibility** of state aids awarded in Romania to the steel industry companies has to be carefully realized, in order to take into account the legislation in force at the respective moment. Thus, the *Law no.143/1999* concerning the state aid has been enforced at the beginning of the year 2000. During the period January 2000 – July 2002, the state aids notified to the Competition Council have been analyzed, exclusively, on the basis of the law provisions. But the law in its initial form has been somewhat incomplete, including only some general provisions from the EU legislation, without taking over the details concerning the conditions and criteria for granting state aids. Moreover, it contained some provisions contrasting with the European rules in this field, such as the former Article 12, which stipulated the following:

*"In case of a new state aid or an existing modified one, the Competition Council is assessing its positive effects over certain economic activities development while taking into account the risk of distorting the competition".*

Such an analysis which implies highly discretionary elements hasn't been accepted by the European Commission. For this reason the Law had to be modified at the end of the year 2003.

The first regulations adopted in strictly accordance with the EU legislation have been published in July, 2002 and have been enforced in January 2003. Since then, the adoption of EU secondary legislation has been in a steady progress.

To conclude, we can distinguish between several stages in the state aid granting process in Romania, which have to be distinctly analysed: 1) the period until the year 2000, when the community notion of *state aid* didn't exist in Romania; 2) the period January 2000 – January 2003, when although the Law has been in force the regulations weren't (with the consequence the

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<sup>119)</sup> – The Report concerning the state aids granted in Romania during the 1996-1999 period, published in the „Official Monitor” no.236 bis, from April 9, 2002;

-The Report concerning the state aids granted in Romania during the 1996-2000 period, published in the „Official Monitor” no.70 bis, from February 2, 2003.

Besides, the Competition Office has also drawn up the report concerning the state aids awarded in Romania during the 1999-2001 period, and respectively the Report for the 2000-2002 period.

<sup>120)</sup> State Aid Scoreboard autumn 2002, Special Edition on the Candidate Countries, COM (2002) 638 final, Brussels, 27.11.2002.

assessment of state aids was made on “non-harmonized” criteria, and yet legal); 3) the period after January 2003, when the legislation in Romania has been increasingly “harmonized” with the *acquis*.

## CHAPTER 10

### STEEL INDUSTRY

Compared with the above-mentioned periods, in case of the steel industry one must take also into account the date of December 31, 2005, when the prolongation of the transition period stipulated by the Protocol 2 (mentioned in the previous chapters) expires.

For a more simplified approach, the analysis will present the state aid situation phased into two periods: the state aid granted until 2002 and, respectively after this date when it is supposed they will become perfectly compatible with the Acquis, as it was transposed into the secondary legislation by the Competition Council.

Presently, the Romanian steel industry is almost entirely privatized (95% of the societies and social capital) as follows:

- **Sidex Galați** with **Ispat** (part of the LNM Holding Group Dutch Antilles), the second steel producer worldwide, in November 2001;
- **COS Târgoviște** with Mechel Trading A.G., a subsidiary of the **Conares Group** (Russia), in November 2002;
- **Industria Sârmei** – Câmpia Turzii, with Mechel Trading A.G too, subsidiary of Conares Group (Russia) in March 2003;
- **Donasid**, which represents a part of **Siderca Călărași**, with **Beltrame** (Italy), in August 2002;
- **Oțelul Roșu** with **Gavazzi** (Italy) and **C.S. Reșița** with Noble Ventures (USA) – have proved to be failures. Afterwards, Reșița has been taken over by the company TMK – Russia in February 2004. Oțelul Roșu is the only company with an uncertain ownership status;
- **Siderurgica Hunedoara** has been privatized in October 2003, with LNM Holdings Dutch Antilles;
- The **independent rolling mills** for long products and tubes have been almost entirely privatized before 2000.

During the accession negotiations, the European Commission accepted for Romania a steel producing capacity of about 9 million tons which, until the year 2010, must undergo a restructuring and modernization process, provided that the production will be fulfilled only under efficiency conditions, without hidden subsidies and with all tax liabilities paid. The 9 million tons will be allocated as follows: **Sidex-Ispat– Galați** – 6 million tons; **Siderurgica-Hunedoara** – 825000 tons; **Reșița** – 450000 tons; **Oțelul Roșu** – 300000 tons; **COS Târgoviște** – 629000 tons; **Industria Sârmei** – **Câmpia Turzii** – 385000 tons; **Donasid** – Călărași – 400000 tons.

**Sidex-Galați**, Eastern Europe's largest producer of steel flat products has been privatized at the end of 2001, with the Anglo-Indian Company LNM. It is the largest British investment in Romania, with LNM - now one of the world's largest steel makers - holding about 87 per cent of the new company's stock. The transaction value included the cash (gradual) payment of 60-70 million dollars and also involved an investment commitment worth of about 350 million \$ in the following 10 years.

In the pre-privatization period, Sidex accumulated debts of over 1 billion dollars mostly towards state institutions and utilities' suppliers, had a staff of 27000 employees and ensured (at the privatization moment) a share of 4% in GDP.

The Government has long hesitated before taking the decision to privatize Sidex, probably for fearing of social instability and the pression of some groups of interests.

According to a post-privatization analysis accomplished by the Anglo-Indian company **ISPAT**, the new owner of Sidex, unprofessional management was one of the most important causes of the huge debt - accumulated by Sidex - to the state and public institutions. Among other shortcomings one can mention: the perpetuation of the barter and compensation systems sales (in exchange for utilities) to the prejudice of cash transactions, which had as an effect a shortage of cash-flows; the proliferation of some intermediary „parasitical” commercial firms, which managed sales both on domestic market (also its limited size didn’t justify their „involvement”) as well as on the export markets.

The export offers were made for Sidex by three different trade companies, which apart from significant fees, benefitted (in their capacity of exporters) of the right to directly import raw materials exempted from taxes.

Nowadays, Sidex fulfils an annual crude steel output of 4.5 million tons, with 19000 employees.

**COS Târgoviște** and **Industria Sârmei – Câmpia Turzii** have been privatized with the company **Mechel Trading**, registered in Switzerland and belonging to the Russian group „**Conares**”. Beyond the allegations regarding the economic policy of „Conares”, it seems that both companies have favourable prospects for restoring the economic viability. Their cumulated production amounts to 700,000 tons of crude steel/year, being achieved with 11,000 employees. Both of them have good market outlets and updated technologies, being however disadvantaged by the deficient management. On the other side, if the privatization contract will not be changed so as to allow a decrease of the redundant jobs, the viability programs risk to fail.

A first privatization round of the **C.S.Reșița** and **Oțelul Roșu** companies took place during 1998-2000. The trade unions „pressures” coupled with the shiftless and the delays in the restructuring process created a lot of insurmountable problems. By the conditions included in the privatization contract, The Fund for State Ownership transferred to the investor a series of disfunctions, mainly financial (debts towards the state and the utilities’ suppliers) and organizational, with no guarantees from the new owner that he will implement the restructuring programmes necessary in order to restore the economic viability of the steel companies. Without implementing the necessary efficiency measures, these programmes and even the privatization of the two companies failed.

Later in 2004, **Reșița** has been taken over by the company **TMK (Russia)** at the symbolic price of 1 Euro. The whole value of the transaction has been of about 25 million euro, out of which 14.8 million euro in the form of technological and environmental investments and about 10 million euro, as commercial debts assumed by the new owner.

At the end of 2003, APAPS (The Authority for Privatization and Management of State Ownership) signed away the documents for the transfer of the property right on Petrotub Roman works, towards the steel group „LNM Holdings NV”. **LNM** acquired **Siderurgica – Hunedoara in a package with Petrotub Roman**. For Siderurgica it has been forecasted an output of about 300,000 tons of liquid steel, for 2004. In the precedent year, the loss registered monthly by Siderurgica only from the production process was about 3 million dollars.

Related to its financial potential, Siderurgica has about 4,000 employees in excess, while the key for this sector is now to produce at higher levels with fewer people, using modest equipment. The artificial capital infusions in order to keep the steel works functioning led to the above mentioned difficulties.

But Siderurgica Hunedoara has also some advantages such as: the highest market share among the long rolled products in Romania, a leader position both on domestic and export markets, location in a taxfree area, a restructuring program in progress, etc.

The economically viable share of **Siderca Călărași**, has been involved, in 2002, in setting up the joint-venture **Donasid** with the Italian firm Beltrame. The non-viable part of Siderca is still owned by APAPS, which is under way to wind it up.

### 10.1. Aids granted before 2003

From the European Commission's point of view, the state aids granted before 2003, do not raise too many problems, as long as they do not produce effects anymore. As for the state aids granted and authorized (or not) by the Competition Council, under criteria other than those similar to the Community rules, that are still producing effects (although they are classified as *existing aids*) it is required to make them *compatible* with the European legislation, namely, to make the necessary distinction between the state aids *authorisation* and their *effective granting* moments, which are usually not concomitant.

In the last 10-12 years, as a consequence of the credits contracted and not repaid in due time, the greatest majority of Romania's iron and steel undertakings, irrespective of their social capital structure *recorded very important debts* to the state and local budgets as well as to the utilities' suppliers (mainly electricity and natural gas) and the banks. These debts (and the corresponding penalties), coupled with the lack of investment funds, capital market shortcomings, different groups of interests, corruption and, above all, the difficult and obscure economic environment, had a negative influence on the economic and financial activity of these undertakings, since 1989. All these factors entailed great deferrals in the steel companies' attempts to enforce an effective restructuring programme of the steel sector by their own means.

To put it differently, the steel companies as well as the state in its capacity of owner had neither the means nor the courage or know-how to embark on a major restructuring program on their own.

However, at a given moment it has been realized that the *rescue* of these steel plants could arise only from the private sector.

Because of the relative „scarcity” of private investors, the privatization process was long and difficult, and in certain cases, even failed.

Eager for giving a new opportunity to the steel plants, the government used the state aids as a modality to keep them „alive” (functioning).

From this point of view, the state aids granted in the last decade, have been either **rescue aids** aimed at avoiding bankruptcy or **aids granted with the privatization occasion**, in order to conclude it successfully.

Because of the depressed financial standing of these steel plants, the state has always been in a defensive, unfavourable position during the privatization negotiations, being obliged to make various concessions.

Starting with 1993, Romania's steelworks benefited by state aids, amounting to 1362 million dollars, for the period 1993-2002, out of which more than three-quarters have been represented by state aids granted to **Sidex** before and particularly at the privatization moment.

### State aid for the steel industry granted during 1993-2002

- million dollars -

Company	Period (1993-2002)
Ispat-Sidex Galați	1,045.7
Siderurgica Hunedoara	33.9
COS Târgoviște	59.7
IS Câmpia Turzii	23.2
CS Reșița	148.4
Gavazzi Steel Oțelul Roșu	0
Siderurgica Călărași	26.5
Sidermet Călan	24.2
<b>TOTAL</b>	<b>1,362.4</b>

Source : "The Restructuring Strategy of Romania's iron and steel industry for 2004-2010 period"; Ministry of Economy and Commerce, April 2004

The following table presents the evolution (by years) of state aids awarded to the main steel companies in Romania :

**The state aid granted to the steel plants during the 1993-2002 period, staggered by years**

**- million dollars -**

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	Total
Ispat-Sidex Galați		34.8	11.5	27.1		19.7	26.2		911.6	14.8	1045.7
Siderurgica Hunedoara			8.7	6.0	5,8	13.4					33.9
COS Târgoviște		1.8	5.5	13.7		8.4		28.2	2.1		59.7
IS Câmpia Turzii			16.2	3.2	0.1	4.5					24.0
CS Reșița		33.5	2.4	1.3	6.3	2.3				102.6	148.4
Gavazzi Steel Oțelul Roșu											0.0
Siderurgica Călărași	5.2	6.6	6.0	5.2	1.3	1.0	1.2				26.5
Sidermet Călan			0.4			23,8					24.2
<b>TOTAL</b>	<b>5.2</b>	<b>76.7</b>	<b>50.7</b>	<b>56.5</b>	<b>13.5</b>	<b>73.1</b>	<b>27.4</b>	<b>28.2</b>	<b>913.7</b>	<b>117.4</b>	<b>1362.4</b>

Source: "The Restructuring Strategy of Romania's iron and steel industry for 2004-2010 period"; Ministry of Economy and Commerce, April 2004.

The following table presents the structure of the state aid granted to the iron and steel companies during 1993-2002, according to the aid categories:

## The State Aid structure by types

- million dollars -

The State Aid Type	ISPAT SIDEX Galați	SIDERURGICA Hunedoara	COS Târgoviște	IS Cămpia Turzii	CS Reșița	SIDERCA Călărași	GAVAZZI STEEL Oțelul Roșu	SIDERMET Călan	Total
Capital injections from the State Budget (SOF)		2.0			4.8	7.7			14.5
Capital injections from budgetary funds, in the form of long term loans without interest	32.5		11.9		5.2			5.7	55.3
Governmental loans/penalties payment	17.9					5.3			23.2
Penalties' write-off for non-payment of taxes	517.2		23.9		50.0	0.6		0.3	592.0
Tax reduction	10.3								10.3
Loans without interest		31,9	15.8	24.0	2.3	12.9		2.3	88.4
State guarantees for loans	68.6				33.5			15.9	118.0
Debt-equity swaps	394.4				52.6				447.0
Compensation payments to dismissed employees	2.6								2.6
Debt rescheduling to the state	2.2								2.2
Other aid types			8,1						8.1
<b>TOTAL</b>	<b>1045.7</b>	<b>33.9</b>	<b>59.7</b>	<b>24.0</b>	<b>148.4</b>	<b>26.5</b>	<b>0</b>	<b>24.2</b>	<b>1,362.4</b>

*Source: The Restructuring Strategy of Romania's iron and steel industry for 2004-2010 period, The Ministry of Economy and Commerce, April 2004.*

The greatest share in the amount of state aid granted during 1993-2002 has been hold by *penalties' write-offs* for non-payment of taxes and duties (44%) and by *debt equitz swaps* (33%).

The remainder represented by *cash injections, loans or loan guarantees* accounted for only 15-20% in the total amount of state aids granted to the steel industry.

### 10.2. The state aids granted for 2003-2010 period

The state aids foreseen for the steel industry during 2003-2010 amount to a total value of 1,069.7 million \$.

Almost half of this aid will take the form of debt write-offs, while tax exemptions awarded to *Ispat – Sidex* company will account for only 18% of total aid granted. The debts' write-offs to the utilities' suppliers account for 16% from the total amount

### Structure of State Aid foreseen in the Romanian steel industry during 2003-2010

- million dollars -

State Aid Supplier	State Aid Type	ISPA SIDEX Galați	SIDERURGICA Hunedoara	COS Târgoviște	IS Cămpia Turzii	CS Reșița	DONASID Călărași	Oțelul Roșu	Total
<b>The State Budget and the local budget</b>	Debts write - off	7.3	298.5	39.5	56.6	89.5		32.2	<b>523.6</b>
	Debts rescheduling	9.5		4.9	1.4				<b>15.8</b>
	Debt-equity swaps								<b>0</b>
	Tax reduction	189.7							<b>189.7</b>
<b>The National Health Insurance House</b>	Debts write – offs			1.2	1.9				<b>3.1</b>
	Debts rescheduling			1.1	1.9				<b>3.0</b>
<b>Utilities' Suppliers</b>	Debts write – offs		125.3	32.0	6.4			9,8	<b>173.5</b>
	Debts rescheduling			7.8					<b>7.8</b>
	Debt-equity swaps				20.0	1.2			<b>21.2</b>
<b>The Authority for Privatizing and Management of State Ownership</b>	Debts write – offs		37.6	7.5	3.5	3.0			<b>51.6</b>
	Debts rescheduling			3.0					<b>3.0</b>
<b>The Authority for Banking Assets' Valuation</b>	Debt-equity swaps		4.8						<b>4.8</b>
<b>Severance payments</b>		26.5	8.3						<b>34.8</b>
<b>Investments' loans and working capital</b>			10.3						<b>10.3</b>
<b>Capital injections</b>								20.0	<b>20.0</b>
<b>Others</b>			7.5						<b>7.5</b>
<b>TOTAL</b>		<b>233.0</b>	<b>492.3</b>	<b>97.0</b>	<b>91.7</b>	<b>93.7</b>	<b>0</b>	<b>62.0</b>	<b>1069.7</b>

Source: "The Restructuring Strategy of Romania's iron and steel industry for the 2004-2010 period"; Ministry of Economy and Commerce, April 2004.

One may notice that all aids awarded to the steel industry were almost entirely made up of *debt write-offs* and *rescheduling or debt-equity swaps*, only a small share - worth of 20 million dollars – going to be granted to **Oțelul Rosu** Company, in order to hasten and facilitate the privatization process, if this company will return to the state property by means of APAPS.



### 10.3. Analysis of state aid granting modalities

All these state aids are for *restructuring purposes*. As a consequence they are comprised in the individual viability plans of each steel plant and also in the „**Strategy for restructuring Romania’s steel industry during 2004-2010**”. These documents lie at the basis of the restructuring programme of this industry.

The *Strategy*, the individual plans and the Council’s decisions are going to be analyzed by the European Commission, which will submit them for approval to the European Council in case they are found **compatible**. In this respect a series of conditions have to be met.<sup>122)</sup>

Thus, the restructuring programme has to be drawn up in such a way as to eliminate any ambiguities and offer sufficient details to allow the foreign experts to check up on the credibility and viability of its scheduling, forecasts and conclusions. In this respect, the informations regarding the viability criteria, the aid proportionality and the capacity reductions are deemed to be of utmost importance.

As for the **viability**, the programme must prove that, at the end of the restructuring period and under normal market conditions the companies have restored their economic viability, which is that respective companies are able to make profit. This would correspond, in the case of the integrated mills, to a *gross operating margin* of at least 13.5% and a *minimum return on equity* of 1.5% of the sales at the end of the restructuring period. In the case of the non-integrated steel companies, the gross operating margin must be at least 10%.

In this respect, the European Commission resorts to a *viability test*, which makes the distinction between the **viability criteria** (which are benchmarks of the company’s financial performance) and the **special accounting conditions** (which, usually do not allow the companies to get short term profits through an under-investing strategy).

These **special accounting conditions** include *minimum* levels of financial charges (of about 3.5%) and *depreciation* (of 7% of turnover in the integrated mills and 5% for other steel companies) – as well as a decrease by a rate of 2.5%/year in the price-costs difference.

This last condition assumes that the forecasts must take into account a drop in prices and a costs’ increase (each by 1.25% per year), changes that are supposed to occur as a result of an expected competition improvement in the steel sector. The revenues and costs taken into consideration are exclusively those generated by the steel production process and not by other activities. Prices are current prices and not constant prices, because while prices are determined by market, costs are influenced by inflation.

In so far as the **proportionality** is concerned, the state aid must be strictly limited to what is absolutely necessary in order to restore the economic viability of these companies. Each firm will be required to offer twice a year detailed informations (until the end of the restructuring period) and to specify the exact amounts of aid awarded to this purpose.

The first value assessed is *the „minimum necessary” amount* of the aid for restoring the firm’s viability, taking into consideration the lowest value of the aid that could allow the steel company to pass the above – mentioned viability test.

After assessing this value, the next stage is the calculation of the *aid intensity* in order to be sure that the aid amount doesn’t exceed the value imposed by the objective (viability restoration) and the beneficiary brings its own contribution to the restructuring costs.

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<sup>122)</sup> Eva Szymanska, Max Leinemeyer, „Guidance for making a Steel restructuring programme”, European Commission, DG Competition, Brussels, February 2004.

The aid value has to be calculated according to the rules used by the European Commission. These rules stipulate that for subsidies awarded at the present moment the value taken into account is the *net subsidy equivalent* not the gross equivalent, if the subsidy generates tax obligations. The aid value has to be computed for all the aid types. For instance, in the case of loans guarantees, the state aid value is calculated as a difference between the interest rate effectively paid and the average interest rate on the market. This difference has to be increased by 4 p.p. or even more (in the case of failing companies, depending on the risk degree of the respective company), being quite possible to grow up to 100% if there will be no bank willing to award the loan without state guarantees.

Moreover, when the subsidies, loans, etc. have to be granted for a future period their amount must be assessed at their present value, being known that 1 million dollars awarded within 5 years has a much smaller value compared with 1 million granted today.

In this context, the aid intensity is calculated as a ratio between the present value of the net equivalent of the grant and the present value of the expenses deemed necessary to restore the firm's viability. If the result exceeds 100% it is obvious that the proportionality criterion is not observed.

The restructuring programme has to be linked to a global rationalization and reduction of capacity. To this purpose, the programme has to present the staggered evolution of the capacity closures over the whole restructuring period. The capacity will be **considered reduced when all capacities** (involved) will be permanently closed, namely when parts of them will be destroyed, so as a restarting would be impossible.

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The analysis of the restructuring strategy, of individual viability plans and of Competition Council's Decisions enable us to make the following comments and observations:

**a)** The restructuring strategy has been drawn up for 2004-2010 and will very probably cover a significant period of time when Romania will be already a EU member. Taking also into account the analysis from the Chapter 6<sup>123)</sup> one can conclude that, it is hard to believe that Romania would be allowed to award state aids any more after December 2005 – in the pessimistic scenario – or after the Accession moment – in the optimistic scenario.

If we refer to the temporary agreements concluded in this respect by EU with some of other candidate countries, it results that the restructuring measures will continue to be implemented even after the accession date, but will be limited to the necessary measures to meet the viability criteria, the capacity reductions and jobs decrease objectives.

Unfortunately, in the *Strategy* the state aids provided to be awarded during the next period are not structured by years, so that a more detailed analysis is not possible. This is one of the weak points of the restructuring programme, as against the detailation degree of informations required by the European Commission.

**b)** However, some of the Competition Council's Decisions are mentioning some more precise data when referring to the final term of a deferred payment. For instance, in **SC IS Câmpia Turzii** case, 2008 is mentioned as a final payment term. In other cases, the formulation has been more vague: „until the final term provided in the rescheduling timetable”.

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<sup>123)</sup> We have to remind the explanatory note from the Chapter 6, which provides that the former Protocol 2 doesn't require explicitly co-financing conditions by the aid beneficiaries, of the restructuring costs. This omission leads, logically, to the conclusion that the concrete financial situation of a specific beneficiary will be taken into account and the above mentioned condition will be applied flexibly, on a case by case basis.

Continuing state aids after the accession moment will entail some risks, being known that the aids' monitoring, after the accession moment, will be the responsibility of the European Commission only.

c) The restructuring *Strategy* doesn't offer an accurate picture about the calculation method of the restructuring costs, the minimum necessary state aid to ensure the company's viability and each beneficiary's own financing contribution. In these circumstances, the aid intensities mentioned in the Competition Council's decisions are only **allegations which can't be checked by independent experts in order to state if they are in accordance with the European Commission requirements.**

It is possible that information exists, but there are still problems related to the presentation modalities and the wrong emphasis on non-important aspects.

d) With regard again to the restructuring costs, where information exists, question marks appear also. In the Competition Council Decision, in **COS Târgoviște**' case, an amount of 97 million dollars is mentioned as restructuring financial cost; accidentally or not, the state aid value awarded for 2003-2010 is the same, resulting an aid intensity level of about 70%. If there is not simply a coincidence, the state aid appears equally at the numerator and at the denominator, being considered at the same time as a part of the restructuring costs. This arises a lot of concerns as for the correctness of the calculation.

e) There are also some misunderstandings regarding one of the special accounting conditions, which must be taken into consideration: that is the increase in costs and decrease in price<sup>117</sup>, each by 1.25 p.p. every year. This is corresponding to a gross operational margin reduction by 2.5 p.p. year; as a result, this viability criterion has to reach a level of 16% (13.5% + 2.5 p.p.) before applying the special accounting conditions.

This special condition (*the price-cost squeeze*) imposed to the calculation method of viability indicators is often considered by itself a viability criterion, which is not correct.

f) The Strategy refers permanently to integrated mills. However, it stipulates among the viability conditions, a *gross operational margin* for all steel plants (except for **Ispat -Sidex**) of minimum 10% and a depreciation rate greater than 5% of the turnover. But the above-mentioned levels are taken into consideration by the European Commission only for *other steel companies*, and not for integrated ones, where the corresponding figures are 13.5% and, respectively, 7%.

g) The calculation method of state aids is not in accordance with that recommended by the European Commission. The Competition Council should have calculated the gross or net subsidy equivalent of state aids which will be granted for the future period as well as the restructuring costs *at their present value*. Paradoxically, acting this way, the state aid value could have been smaller. Let's suppose, for instance that the state intends to enforce a write-off of a penalty worth of 1 million dollars. According to the current procedure, this write-off will be enforced at the end of the rescheduling period of the principal, actually within 5 years, provided that the beneficiary will have paid all current liabilities during this period.

In this case we are dealing with a debts' write-off of about 1 million dollars, 5 years later. But the *true state aid value* is the present-day value of this debt write-off namely **1 mil.  $\$/(1+a)^5$** , where „a” is a discount rate. Using, let's say a discount rate of 4%<sup>125)</sup>, the state aid value would be only 822000 dollars.

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<sup>117</sup> In english, price-cost squeeze

<sup>125)</sup> For instance, starting 1.01.2004, the European Commission use a reference rate of 4.43% for the Euro zone countries, of 5.68% for Great Britain, etc. It is obvious that the bigger is the discount rate the smaller the present value of the state aid.

h) Another element which could diminish the estimated value of state aids is related to the severance payments awarded in case of layoffs. This kind of payments can be considered state aids only if the respective firm would have been forced through its labour contract to support itself such payments in case of layoffs and the state is assuming now this role.

If the firm doesn't have this kind of liabilities, the amount awarded by the state cannot be considered state aid. In this situation the analysis must judge each steel company on a case by case basis.

i) There are some discrepancies between the amounts mentioned in the Competition Council's decisions and those in the **Strategy** for 1993-2002.

Thus, in the Council's decision for **COS-Targoviște** the following amounts are mentioned as state aids for the past period: 27.7 million dollars for 1993-1999; 22.8 million authorized by the Council for 2000-2002 as well as – in the same period – 1.8 million dollars awarded by local authorities; highlighting this last sum separately from those authorized by the Council suggests that the aid granted by local authorities has not been notified to and authorized by the Competition Council. However, the whole amount of state aid the Decision takes into account (52.3 million dollars) is significantly smaller than the level (59.7 million dollars) mentioned in the **Strategy**.

j) It doesn't result, clearly, if the state aids granted in the past are still producing effects, nowadays or in the future. In this respect we have remarked several differences in the wording of the decisions of the Council. For instance, in **Siderca Călărași** decision, it is specified that aids granted during 1993-1999 are *existing aids which are not producing effects anymore (a contradiction in terms)*. On the other hand, in **Siderugica – Hunedoara** case, there is not such a mention, which could lead to the conclusion that aids invoked for the past period are continuing to produce effects nowadays and in the future.

k) Keeping in mind the assertions from the Chapter 6, concerning the *permissivity* of the Protocol 2 provisions, there is no mention anywhere that it is for the last time these aids are granted. Moreover, the „Strategy” doesn't tackle with the *degressivity concept*, which means the gradual decrease of these aids over time. As in the *Strategy*, aids for the future period are not presented by years, the only comparison that can be made is between global data for the period until 2003 with data the period after that date. Or, in several cases, aids for the next period are substantially larger than those in the past period (COS Târgoviște, IS Câmpia Turzii).

l) **Sidex Galați** is a special case. The state aid granted at the moment of privatization has been authorized in 2002, by the Competition Council, before enforcing the regulations adopting the European criteria for state aid authorization. The European Commission criticized the Council's decision and asked to be made compatible with the EU rules. Its criticism aimed at the fact that the decision doesn't relate to the EU principles meant to ensure the viability and does not restrict the amount of state aid to what is absolutely necessary in order to restore the economic viability of the steel sector. Moreover the Competition Council decision is mentioning that the respective aid doesn't disturb competition and the international treaties to which Romania is a party, while the European Commission has a completely different opinion.

One can conclude in this case, that a **new analysis and “rewriting” of the whole aid motivation should have been necessary** – with eventual changes of the state aid levels - which should include at least the following ideas: (i) a restructuring plan analysis which can demonstrate the medium term viability of the company; (ii) the concept of degressivity; (iii) a demonstration to support the idea according to which the aid amount represents the minimum necessary level to achieve the viability objective; (iv) underlying the fact that this is the last aid the company will benefit from.

As referring to the environment protection aid, the Commission was not able to identify neither the eligible costs - that is the additional amounts necessary to cope with the environment

requirements - nor the aid amount for this purpose – on the basis on which one can check up if the aid intensity will not exceed a 15% level - as the Regulation for environment protection state aids stipulates.

The Competition Council has not performed such an analysis, the decision from 2002 being now included as such in the steel restructuring program. We doubt that the European Commission experts will accept this type of approach.

#### **10.4. Conclusions regarding the iron and steel industry state aids**

The above mentioned ideas, allow us to draw the following conclusions:

1. In Romania, the state aid for steel industry registered relatively low levels during the 1993-2000 period. Thus, according to the Competition Office Report (2000-2002), its share in the total aid granted to the manufacturing industry had the following dynamics: 0.1% in 1996-1997, 5.8% in 1999 and 10.6% in 2000.<sup>126)</sup>
2. The significant increase, starting with 2001, of state aids' share granted to sectoral objectives is due notably to the state aid for steel industry, which held about 98% of total state aid for sectoral objectives and, respectively, 75% of the state aid for manufacturing industry. This state aid increase can be explained by the state willing to keep functioning and successfully privatize several large companies.
3. The amount of state aid directed to the steel industry reached an all-time record in 2001, with the occasion of **Sidex** privatization and remained at high enough levels in the following 2 years too, in the context of the continued privatization process at the following companies: COS-Târgoviște, I.S.-Câmpia Turzii, Siderurgica Hunedoara, Petrotub Roman.
4. Romania benefits from a preferential treatment regarding the state aids granted for restructuring the steel industry, enforced by the Protocol 2, annex to the Association Treaty to EU and by the additional Protocol to the same treaty. The above mentioned documents allowed to Romania the possibility to grant state aids for steel industry restructuring, while in the EU area, after ECSC Treaty expiry, this type of aid has been forbidden. We have to remind that Romania is obliged under Chapter 6 (The Competition) provisions to already apply in the present the community rules concerning the state aids' granting.
5. Romania's approach – which has still to be validated by the European Commission – seems to be that the state aids granted in the past (1993-2002) don't have to be considered as restructuring aids because the allocation schemes have been instituted before the entry into force of the State Aid Law, although some of these schemes produced effects after this date. For this reason, the aids authorized by the Competition Council, at the beginning of the year 2004, for the period 2003-2010 seem to be considered by the Romanian authorities as the first (and last) restructuring aids.

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<sup>126)</sup> One can remark the non-concordance between the aid values for the year 2000 included in the Competition Office Reports for 1999-2001 and respectively 2000-2002 periods, on one hand and the data included in the European Commission **Scoreboard for 2002, the edition devoted to the candidate countries, where the steel aid share in the whole state aid is 4%, and that granted to the manufacturing industry, 7.4%. But even the weight of state aid in GDP is considerably different: while the Scoreboard is recording a share of 1.9%, the Competition Office Report for 2000-2002 mentions a share of 3.9%. Even after subtracting the aids for agriculture and fishery, the state-aid share in Romania's GDP is about 3.3%, considerably higher when compared to the average for the candidate countries (1.3%) and EU (0.8%). These discrepancies can be generated by the fact the figures are available from several different sources, suggesting some deficiencies in the state aid monitoring system in Romania.**

6. Keeping in mind the observation from the letter “f”, the viability plans drawn up for each of the seven integrated combined steelworks, show that all of them can become viable, from the economic point of view, until 2010.

7. According to the additional Protocol, granting of the restructuring state aid is conditioned by the pre-existence of a restructuring strategy for the steel industry and of individual viability plans for the industry enterprises. These documents, authorized by the Competition Council will be submitted to the Commission to be checked up and finally approved by the European Council.

## CHAPTER 11 COAL INDUSTRY

In Romania, the coal industry had recorded a slight increase in the first part of the 90's, followed by a striking decline of production in the second part of the last decade, mainly due to an important decrease of industrial production and implicitly of electricity production in thermo power stations, and secondary due to considerable losses recorded by this sector, especially in the underground mines.

Until 1998, Romanian authorities could not launch a restructuring strategy of coal industry due to bitter opposition of labor unions and due to the fact that the descending trend of crude oil and natural gas reserves and production did not allow a rapid substitution (on medium term) of coal in electricity generation, in spite of its low efficiency and very high environment pollution. Therefore the striking reduction of coal production in the second part of the 90's is less the result of implementing a rationalization and restructuring strategy, which would have had to be applied immediately after 1989, and more the effect of market forces, namely the evolution of supply/demand balance. Thus, in 1998 for instance, the electricity demand was by 40.6 % under 1989 level. In the next table it is presented the evolution of coal production in 1991-2001 period.

**Evolution of coal production in 1991-2002 period (th.tons)**

<b>Year/Production</b>	<b>Hard coal</b>	<b>Brown coal</b>	<b>Lignite</b>
1991	5411	645	29149
1995	6356	570	37062
1996	6965	605	37204
1997	5642	511	30093
1998	4331	369	23405
1999	3741	328	20465
2000	3241	26031.3	
2001	3526	29754.2	
2002	3360	27084.4	

*Source: Statistical Yearbook of Romania, 2002*

The first strategy of mining sector started in 1998, with the financial support of World Bank. Its objectives consist in adapting mining industry to market economy requirements, reduction of direct state implication as an owner, investor and subsidy supplier, increase of environment protection degree, mitigation of social problems caused by the closing of some capacities and recovery of the economy of mining zones. After 6 years of restructuring one may notice that the reduction of labor force and the closing of most uneffective mines, coupled with the increase of labor productivity and reduction of environment impact (by closing), represent clear results of this strategy, while the increase of efficiency by means of cost reduction, labor reconversion, development of investments and alternative activities constitute difficult to touch desiderata.

State was the only investor and owner of mines, very few mines being granted in the second part of 90's. In 1990-1999 period the state granted funds from the budget for investments of 1.15 billion \$, out of which 660 million \$ for coal. Investments from own company sources were almost negligible, also those coming from private investors or external credits. In order to

concentrate investments on profitable mines it was undertaken a cost/benefit analysis for 174 underground mines and open pits, based on 1997 data, which revealed that only 25 mines had a sub-unitary cost/benefit ratio. The analyses made in coal industry have pointed out that most hard coal and brown coal capacities are not profitable, the solution consisting in closing high loss mines and modernization of low loss capacities. Lignite open pits can be economic viable to a certain extent, while maintaining the underground mines is less economic justified.

Restructuring on organizational level meant transforming regimes autonome in national companies, as National Lignite Company (Oltenia), National Hard Coal Company (Petroșani) and National Coal Society (Ploiești). These companies had to cut the losses and debts to state budget, therefore the direct and indirect state subsidies had to be reduced to a great extent. At the end of the year 2001 budget debts of National Hard Coal Company amounted to 11500 billion lei, out of which 4300 billion lei taxes and 5600 billion lei social insurances. In case we cumulate the subsidies with fiscal arrears and investments made by state it results that mining industry generally, and coal industry especially, represent an enormous burden for the state budget and for Romanian taxpayer implicitly. For instance, in the year 2000, Ministry of Industry and Resources spent 250 billion lei for investments and 1900 billion lei for subsidies in the mining sector. In March 2004 it was announced that 11 mining companies are going to be exempted from the payments of fiscal debts to the limit of a ceiling of 4715 billion lei (about 112 million €), out of which National Lignite Company with 1981.9 billion lei (47 million €), National Hard Coal Company with 1379.9 billion lei (32.85 million €), National Coal Society Ploiești with 288.5 billion lei (6.9 million €).

The third organizational step of coal producing undertakings is to transform them into joint stock companies, which has to involve the removing of subsidies to a great extent, the cutting of production costs and the continuation of restructuring process. One may say that this has already started, by dissolving National Lignite Company and by setting up 3 energy complexes that include mines and thermo power stations. The labor unions strongly oppose to any restructuring programmes which have not been negotiated by the Ministry of Economy and Trade with them, particularly as these programmes imply new dismissals and mine closings.

Implementing of mining restructuring strategy involves a whole aspect range, which are difficult to approach and solve in a transition and accession to EU preparation period :

- closing of about 190 mines and open pits raise conservation and environment protection problems;
- compensatory payments (being even consistent ones) do not solve the unemployment problem in mono-industrial zones, as mining ones are; up to now the authorities have not found viable solutions in respect to vocational retraining and creation of new jobs, partially due to objective reasons (these cannot be achieved on short term, minor concern of domestic and foreign investors, poor physical infrastructure, low level of training and interest for reconversion);
- solving of ecological problems for operating mines is extremely difficult due to accumulation of negative externalities effects and due to financial constraints, as to limited level of training in the field of environmental management;
- parallel with considerable reduction of subsidies for operation, one should increase the allocations for mine closing, rehabilitation and conservation of environment, mitigation of unfavorable social effects;
- privatization and closing of non-profitable mines remain the main instruments for restructuring and making efficient the coal industry.

### **11.1. State aid in coal industry**



Romania gives support to coal industry by means of subsidies granting, which are meant to cover the difference between costs and incomes. The list of subsidized products is approved by the government every year, but the amount of subsidies is approved through state budget law. Direct subsidies are meant to cover the production costs and their level depends on the level of production and deliveries, being correlated with inflation rate, while indirect subsidies represent to relieve, cancel and wipe the budget debts or other debts.

Special rules for granting state aids exist only for hard coal, while general rules are applied to lignite extraction. At CNL Oltenia no subsidies have been granted starting with second quarter 1997. However the statement that lignite production is not at all subsidized must be nuanced, as long as CNLO has great debts to state budget. On the other side, CNLO continued to receive state aids for access to new deposits and for technological modernization of viable mines. One should underline the fact that “Strategy of coal industry for 2004-2010 period” mentions that it is necessary to reduce the direct implication of government, by means of “gradual diminishing of subsidies until their removal in the year 2007, in ores sector and lignite”. It is a matter of state aids which are still granted for lignite production at SNC Ploiești and those mentioned above at CNLO.

Besides direct and indirect subsidies the state provides some social transfers for mining staff and supports as owner important capital expenditures meant to modernize old capacities and allow investments in equipment and modern technologies.

In the first part of 90’s subsidies granted by state to mining industry remained at high enough levels. Starting with 1997 subsidies have drastically reduced, both for the whole mining industry and for the coal, once the restructuring process has started by closing dangerous mines or exhausting deposits mines, the labor force has strongly decreased and compensatory payments have been granted, the investments have been concentrated on modernizing potential profitable mines.

In the next table it is presented the evolution of state aids granted to mining industry and coal production in 1992-2002 period, mentioning that state aids in 1999-2002 period include also those for crude oil and natural gas extraction, therefore they are for the whole extractive industry.

**The evolution of state aids for mining sector in 1990-2002 period (mil.\$/€)**

Year/Sector	Mining Sector	Coal Sector
1990	528.4 mil.\$	337.8 mil.\$
1995	402.5 mil.\$	203.9 mil.\$
1996	384.9 mil.\$	138.7 mil.\$
1997	145.5 mil.\$	45.2 mil.\$
1998	118.9 mil.\$	40.2 mil.\$
1999	179.9 mil.€	60.8 mil.€
2000	192.0 mil.€	71.6 mil.€
2001	405.3 mil.€	91.5 mil.€
2002	184.0 mil.€	62.3 mil.€

Source: Competition Office, Report on state aid for 1999-2002 period.

In the year 2003 state aid granted in coal sector for hard coal was 10.3 mil.\$ for deposits access, 17.5 mil.\$ for social protection, 2.3 mil.\$ for environment works; at the same time it was

granted a production subsidy for hard coal amounting to 23.85 mil.\$, a decrease by about 5% as against 2000.

State aid granted to mining industry has recorded a constant decreasing trend in the last 7 years, except the year 2001 when it marked a sudden increase. A similar trend, maybe even more evident, has been recorded by the state aid granted to coal industry, which has diminished 5 times. The difference between the aids granted to coal industry and those granted to other mining and extractive sectors lies in the fact that the last ones address to horizontal objectives, like environment protection expenditures, salvation/restructuring etc.

In the next table it is presented the amount of state aid per employee and its share in the total state aid, as well as in the gross added value of the branch (including crude oil and natural gas extraction) in 1999-2000 period.

**The amount of state aid per employee and its share in the total and in the gross added value in 1999-2002 period (€ and %)**

	MU	1999	2000	2001	2002
The amount per employee in the extractive industry	€	1166.5	1605.4	2874.5	1352.9
The amount per employee in the coal industry	€	1332.8	1803.5	2033.3	1448.8
The share of extractive industry aid in the total national state aid	%	12.1	12.3	13.8	11.8
The share of coal aid in the total national state aid	%	4.1	4.6	3.1	4.0
The share of extractive industry aid in the gross added value of the branch	%	24.6	22.3	41.1	17.0
The share of coal aid in the gross added value of the branch	%	58.0	43.0	48.3	29.5

Source: Competition Office, Report on state aid for 1999-2002

From the above table data results a relatively reduced share of the aid granted to coal industry in the total state aid granted at national level or granted to extractive industry, but a high enough share of this aid, although at an evident decreasing share in the gross added value of the branch.

State aids for extractive industry had been granted for achieving some objectives:

- a) horizontal ones - environment protection, salvation/restructuring, other activities;
- b) sectorial ones – for operating;
- c) regional ones

In the next table it is presented the structure of state aid on objectives in 1999-2002 period.

**The structure of state aid on objectives in 1999-2002 period**

Aid/Year	1999	2000	2001	2002
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Total aid for extractive industry (mil. € current prices)	179.9	192.0	405.3	184.0
<b>Horizontal objectives</b> (mil. € current prices)	<b>120.8</b>	<b>120.4</b>	<b>313.8</b>	<b>121.7</b>
The share of horizontal objectives (%), out of which:	67.2	62.7	77.4	66.1
- environment protection (%)	1.6	5.8	0.5	0.6
- rescue/restructuring (%)	19.3	8.5	52.1	10.9
- other objectives (%)	46.3	48.4	24.8	54.6
<b>Sectoral objectives</b> , including operating aid (mil. € current prices)	<b>59.1</b>	<b>71.6</b>	<b>91.5</b>	<b>62.3</b>
The share of sectoral objectives (%), out of which:	32.8	37.3	22.6	33.9
- coal, aid for current production (%)	18.0	17.8	7.3	17.4
- coal, other aids (%)	14.9	19.5	15.3	16.5
<b>Regional objectives</b> (mil. € current prices)	<b>0.0</b>	<b>0.003</b>	<b>0.01</b>	<b>0.003</b>
The share of regional objectives (%), out of which:	0.003	0.002	0.003	0.002
- areas with national programmes for regional development	0.0	0.0	0.0	0.0
- unfavoured areas	0.003	0.002	0.003	0.002

Source: Competition Office, Report on state aid for 1999-2002 period

**State aids for horizontal objectives** aim at *environment protection*, that is pollution control and ecological operations after mine closing, *salvation/restructuring*, that is aid for companies with difficulties etc.

**State aids for sectoral objectives**, meant only for coal industry, aim at *current production*, that is operating, product subsidies, facilities regarding debt payment to state budget and social insurance budget, as well as *other objectives*, like investment support for technological modernization of viable mines, closing and conservation of non-profitable mines, stimulation of geological prospectings.

**State aids for regional objectives** had a tiny share in the total state aids for extractive industry and confined to modest sums granted in the context of policy concerning unfavoured zones.

In the next table it is presented the structure of state aid in coal industry according to financial used instruments (aid categories).

**The structure of state aid according to financial instruments during 1999-2002**

<b>Instrument/Year</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>
A. Budgetary expenditures				
Current prices (mil.€)	57.0	60.3	54.8	57.7
Share in total (%)	93.9	84.3	59.9	92.6
a) subsidies, allowances, bonuses (%)	72.8	71.4	50.9	73.0
b) participation to capital (%)	21.1	12.9	9.0	19.6
<b>B. Giving up to incomes</b>				

Current prices (mil.€)	3.7	11.2	36.7	4.6
Share in total (%)	6.1	15.7	40.1	7.4
a) exemptions and reductions at payment of fiscal duties (%)	1.2	0.2	0.4	0.0
b) interest exemptions at budget credits (%)	0.0	0.0	0.0	0.0
c) exemptions and reductions at payment of delay increases and penalties (%)	4.4	14.9	39.3	4.0
d) granting of state collaterals (%)	0.6	0.6	0.4	3.4

Source: Competition Office, Report on state aid for 1999-2002 period

From the above table data results that subsidies, allowances, bonuses hold the first place in the total state aid granted to coal industry, followed by state participation to capital and by exemptions, reductions, spreadings related to state budget debts.

## 11. 2. Conclusions with regard to state aid in coal industry

Available data allow the drawing of some conclusions:

1. In Romania state aid for coal industry placed on a decreasing trend, especially after 1997, when the restructuring process of industry started, it had been reduced over 5 times in 1991-2002 period.
2. State aid granted to coal industry had a share of 34% (in 2002) in the total aid granted to extractive industry and 4% in the total state aid.
3. Recently Romania stated that, starting with 2001, it has reoriented energy policy to domestic resources, especially coal. Although associated measures are linked to energy sector, however, they may constitute a indirect state aid for coal industry, by stimulating the use of this type of fuel. In this context, estimations of some Romanian officials pointed to a lignite production of 30 mil. tons in 2010 and 35-40 mil.tons in 2025, while hard coal production will not increase, it is going to be around 4.3 mil. tons per year, the focus being on production quality. We have serious doubts that things will happen like this, since the state aid will be granted only for the operating of mines which are going to be closed in the next future or for investments meant to maintain a certain minimum level of production.
4. Similar to steel industry, not always the compensatory payments granted to those dismissed represent a state aid, but only when mining companies would have been forced to support them.
5. As it has been showed in the chapter 7, now in Romania it does not exist the legal framework needed for granting regional state aids or salvation/restructuring aids in coal industry, being necessary the takeover of the Regulation no.1407/2002.

## CHAPTER 12

### SHIPBUILDING AND MOTOR VEHICLES

Information referring to state aids granted to shipyards from Romania are available only in “Note regarding the results of monitoring action on state aids granted to shipyards, in 2000-2001 period” drawn up by Competition Office at the end of year 2003.

To this end it has been ascertained that 9 shipyards had benefited from aids in the respective period, under the form of allowances at interest, exemptions from profit tax payment, spreadings and exemptions of delay penalties for budget duties payment, exemptions from custom duties payment and custom debt guarantee.

The next table presents some data referring to these state aids:

#### State aids in the shipyard sector

	2000	2001	Total
<b>State aids (th. €)</b>	8995.2	9431.9	18427.1
<b>Turnover</b>	243466.2	244599.0	488065.2
<b>Investments</b>	12192.7	23070.8	35263.5
<b>Employees</b>	20688	19588	-

Source: Competition Office

The forms these aids had been granted under are presented below:

#### Categories of aids

Type of aid	2000	2001
Interest subsidy	3658.4	3641.5
Rescheduling of social contributions at the privatization	27.4	9.3
Profit Tax exemption	2841.2	1714.1
Reduction of social contribution when hiring graduates	230.8	80.3
Custom duties exemption	2237.4	-
Social contribution penalties write-offs at privatization	-	3702.0
Penalties write-offs for taxes, fees and other budget incomes	-	284.7
<b>Total</b>	8995.2	9431.9

Source : Competition Office

Analysis of these aids allows the formulation of some remarks and conclusions:

- Shipyard sector has not been directly aimed at granting some state aids. The aids that sector had benefited from were the result of some state aid schemes which economic agents could benefit from, irrespective of the sector in which they deployed their activity (legislation

regarding foreign investments regime, arrears, stimulation of graduate employment, profit tax, social contributions, etc.).

- Fiscal facilities represent an important share in the total, but with a falling trend. Thus, facilities granted under the form of exemptions for profit tax, custom duties and VAT payment represented 56.5% in 2000 and 21.2% in 2001.
- Certain facilities which shipyards could benefit from had been eliminated by means of changing the legislation regarding profit tax and VAT. It is a matter of exemption for anticipated payment or for guarantee of custom duties, custom commission and VAT payment for completion imports afferent to complex exports.
- It is worth discussing if facilities granted to those that employed newly graduated persons (and that are included in the above tables) constitute state aid. Even if they are so, it is very likely to be compatible to Community legislation in force.
- Lack of specific legislation for granting state aids in the shipyard sector – discussed in chapter 9 – makes possible the granting of some regional aids with a higher intensity than that allowed in EU (maximum 50% against maximum 22.5%).
- The same legislative void does not allow the granting of some state aids in Romania which are permitted in EU, as it is innovation aid.

**In the car industry** two state aids are relevant in the context of current analysis. The first of them refers to SC Daewoo Automobile Romania SA. This company has received state aids for a limited period, respectively 1994-2001, aid scheme ceasing its validity and not producing effects nowadays.

On the other hand, Dacia SA has received in the context of privatization a series of facilities which it benefits from and will continue to benefit in the future. According to HG 445/1999 (therefore, before State Aid Law came into force) the company benefited from profit tax exemption for a five year period, starting with the first financial exercise in which it gets profit, provided that this is going to be achieved in maximum 3 years from the date of integral payment of shares price. Competition Council authorized the aid during the year 2003, when Dacia did not get any profit. The same situation was estimated for the year 2004, which would have meant that the company had not benefited at all from this facility. After that, the profit tax exemption has been prolonged until 2007, by means of a provision in the Fiscal Code. The Fiscal Code was authorized by Competition Council, which did not object against this provision.

The total amount of aid is about 60 mil.€, of which 32 mil. € already granted (under the form of fiscal facilities) and 28 mil. € (custom duties and VAT exemptions, write-offs of interests for delay of road duty payment), which are going to be granted until September 2004. State aid was authorized as regional and environment protection aid.

Some observations are necessary to be made:

1. The state aid amount of 28 mil. €, which the company is going to benefit from, does not take into account the profit tax exemption until 2007, introduced later on in Fiscal Code and which alters the intensity of state aid. Although the Fiscal Code as a whole was authorized, the Competition Council has to re-analyze the aid given to Dacia SA and at least to establish a maximum aid of which the company may benefit from. Evidently, even in this situation, state aid may prove to be compatible to *acquis communautaire*.

2. As it exceeds the presumed accession data, Dacia SA must be introduced on the existing aids list, aids which have been authorized by Competition Council and accepted by European Commission. Otherwise, at the accession moment, the aid will be considered as new aid and will enter into usual procedures of European Commission.
3. The maximum intensity of regional aid which a company in motor industry may benefit from is 30% out of maximum admissible intensity for respective region, therefore 15% in Romania case, and not 34% as the Competition Council Decision mentions.
4. Without more available details, the aid granted for environment protection does not seem to comply with the conditionalities in the relevant Regulation.

## CONCLUSIONS

This study aims to achieve several objectives regarding the control of state aid granted to the so-called ‘sensitive’ sectors – steel, coal, motor vehicles and shipbuilding. The first is an almost exhaustive analysis of the rules applicable to state aid for these sectors in the EU – that Romania must take over into its national legal system - and the way in which they are applied with respect to the current Member States. The second is to discuss the outcome of the negotiations carried out with the new Member States (which joined the EU in 2004) on the control of state aid for these sectors, in the context of Chapter 6 Competition (the negotiations chapter regarding the regime applicable to state aid in general, which does not contain however all the specific rules applicable to state aid for the sensitive sectors). The third is an overlook of the Romanian state aid policy for the sensitive sectors. The fourth is to discuss the compatibility of the policy objectives currently pursued in Romania with respect to state aid for the sensitive sectors with the relevant EU state aid regulation.

The analysis of the EU state aid regulation applicable in the sensitive sectors allowed us to draw the following main conclusions:

### *In the steel industry:*

- After the expiry of the ECSC Treaty (23 July 2002), state aid granted to the steel industry becomes, in general lines, subject to the general rules developed in the application of Arts. 87-89 EC.
- The European Commission published in March 2002 a *Communication on rescue and restructuring aid and closure aid for the steel sector*<sup>118</sup> prohibiting the granting of rescue and restructuring aid, in whatever form, to companies operating in this sector.
- The same Communication reminds that the granting of regional aid (or investment aid) in this sector is prohibited under the Multisectoral Framework on regional aid.
- The above-mentioned interdiction does not apply only to ‘large investment projects’ as defined in the Multisectoral Framework (i.e. state aid granted to support investment projects totalling more than 50 million Euro), but also to state aid to support large investment projects undertaken by SMEs.
- State aid to ‘normal’ investment projects undertaken by SMEs operating in the steel sector is allowed up to the maximum intensity ceilings established in Regulation 70/2001, namely, 15% of the total cost of the investment project for small enterprises, and 7,5% for the medium-sized enterprises.
- The Commission Communication mentioned above also allows the granting of state aid related to the closure of productions capacities.
- Besides aid for closure and regional aid to support investment projects undertaken by SMEs, firms operating in the steel sector may also receive the following types of state aid:
  - o state aid to support R&D (according to the conditions established in the Commission Communication on state aid for R&D);
  - o state aid for supporting environmental protection projects (according to the conditions established in the Commission Communication on state aid for environmental protection of February 2001);
  - o state aid for creating or maintaining jobs (according to the conditions laid down in the Commission Regulation No. 2204/2002);

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<sup>118</sup> European Commission (2002): *Communication on Rescue and Restructuring Aid and Closure Aid for the Steel Sector*, OJ C 70 of 19.3.2002.



- state aid for training (according to the conditions laid down in the Commission Regulation No. 68/2001);
- *de minimis* aid (aid totalling less than 100 000 Euro over a period of three years), irrespective of its form and objectives (according to Regulation 69/2001);

*For the coal sector:*

- After the expiry of the ECSC Treaty (23 July 2002), the Commission adopted a Regulation laying down specific rules concerning the granting of state aid to undertakings operating in this sector.
- As to the exact scope of application of this Regulation (or the definition of the coal sector for the purposes of state aid control), the French version of the text refers clearly to ‘huile’ (or hard coal), which would mean in practice that the Regulation does not apply to the extraction of lignite, for example. Thus, the extraction of lignite would be subject, from this perspective, to the general rules developed in the application of Arts. 87-89 EC. However, the Spanish and Italian translation of the regulation do not make such a distinction between hard coal and other types of coal. In favour of the distinction, nevertheless, pleads the information on state aid to the ‘hard coal’ extraction units as provided on the website of the Commission’s Energy Directorate.
- As a general rule, the Regulation allows the granting of state aid pursuing one of the following objectives:
  - maintain a ‘strategic’ minimum level of internal coal production in the Member States; or
  - to cushion the economic and social consequences arising from the closure of excess production capacities;
- The main types of state aid that may be awarded for this sector are as follows:
  - operating aid covering the losses of extraction units about to be definitively closed until 2007;
  - *investment aid* related to maintaining a minimum level of internal production (up to 30% of the total cost of the investment project, allowed only until the end of 2010, and to extraction units that have not previously benefited from such aid, and with the condition that the aid do not lower the prices of internal coal under those of equivalent imports) and *operating aid* to undertakings comprised in the strategic plan designed by the Member State concerned;
  - *state aid* destined to make good liabilities from the past that emerged in relation to restructuring and the rationalization of extraction;
  - *state aid* for R&D, environmental protection and training, under the conditions laid down in the respective EC regulations.

*For the motor vehicles sector:*

- as of 2004, the Multisectoral Framework on regional aid to large investment sectors is applicable to this sector;
- the European Commission was expected to publish by the 31<sup>st</sup> of December 2003 a list of the sectors with structural problems, e.g. excess production capacities - probably to be selected among those sectors that have registered a negative growth of consumption over the least five years – possibly including the motor vehicle sector; the sectors on this list would not be allowed to receive investment (regional) aid but in exceptional circumstances; the publication of this list of ‘sensitive’ sectors was however postponed until the 31<sup>st</sup> of March 2006;

- until the 31<sup>st</sup> of March 2006 – and without prejudice to the provisions of Regulation no. 70/2001 on state aid to SMEs – in the case of state aid granted to firms in the motor vehicles sector that is over 5 million Euro (gross) per beneficiary, the maximum aid intensity admissible will be limited to 30% of the regional aid ceiling applicable at the location of the beneficiary;
- state aid given in this sector for restructuring, R&D and environmental protection follows the specific rules applicable to these types of aid across the sectors.

*For shipbuilding:*

- the rules applicable to state aid for this sector are laid down in the ‘Framework on State aid to shipbuilding’ published in 2003; at present the Multisectoral Framework on regional aid to large investment project does not apply to the shipbuilding sector;
- the general principle resulting from the above-mentioned Framework is that state aid to firms operating in the shipbuilding sector should be granted in conformity with Arts. 87-88 EC and the legislation adopted in their application, such as: Council Regulation 1/1999 (the Procedural Regulation), Council Regulation 68/2001 on training aid, Council Regulation 69/2001 on *de minimis* aid, Council Regulation 70/2001 on aid to SMEs, Council Regulation 1177/2002 concerning a temporary defensive mechanism to shipbuilding, the Commission Guidelines on rescue and restructuring aid (1999 – a new draft was published in February 2004), the Commission Guidelines on environmental aid (2001), the Framework on State Aid for Research and Development (1996);
- there are, however, *specific rules* applicable in this sector to state aid measures destined to promote the competitiveness of EU shipbuilding (and in particular to promote innovation), to facilitate the reduction of excess production capacities, to meet international obligations concerning export credits, and regional aid;
- thus, *regional aid* may be granted if the following conditions are met:
  - o the aid is destined to support investment related to the modernization of existing shipbuilding capacities, or increase their productivity, and has no connection with the financial restructuring of the beneficiary firm;
  - o in assisted regions covered by Art. 87(3)(a) EC, the intensity of regional aid for this sector should not exceed a maximum ceiling of 22,5%;
  - o in assisted regions covered by Art. 87(3)(c) EC, the intensity of regional aid for this sector should not exceed a maximum ceiling of 12,5%, or the regional ceiling applicable, if the latter is lower than the former;
  - o the aid covers eligible expenditure according to the definitions laid down in the Guidelines on regional aid.

The answer to the question to what extent the legal framework applicable in Romania for the control of state aid given to the “sensitive sectors” is compatible with the corresponding *acquis communautaire* is different from sector to sector. Thus, at present (and until the expiry of Protocol 2 to the Association Agreement, in December 2005), the regime applicable to state aid for the **steel sector** in Romania is given by Art. 9(4) of Protocol 2, Law No. 143/1999 on state aid (as modified by Law No. 603/2003) and the Regulations adopted by the Competition Council in its application. The regulatory situation following the expiry of Protocol 2 (in December 2005) is still unclear, with the possibility to either prolong the applicability of Protocol 2 until accession, or start applying in full the *acquis* relevant to this sector - as it has been summarised above. Following accession, Romania will apply in full the *acquis* relevant to the steel sector, while it is still unclear whether after that date Romania will have the possibility to continue to implement state aid measures that have been approved before accession as “existing aid” – the precedent of the countries that joined the EU in May 2004 seems to exclude this possibility.

- The analysis of the current legislative framework leads to the following observations:
- state aid for rescue and restructuring, closure aid: **in the absence of a specific Regulation (to be adopted by the Competition Council) taking over the conditions for the approval of such aid to the steel sector as resulting from Art. 9(4) of Protocol 2 and the relevant *acquis*, these conditions remain unclear** for both the public authorities and/or bodies adopting such measures and for the aid beneficiaries. For example, the Competition Council's Regulation on rescue and restructuring aid specifically excludes the steel sector from its scope of application, though without making reference to the regime applicable to such types of aid for the steel sector (whereas the Commission Guidelines on rescue and restructuring aid of 1999 make such a reference).
  - investment aid: the Competition Council's Regulation on regional aid does not apply to the steel sector, while Art. 1(2) of the same regulation stipulates that, for the steel sector, regional aid follows the general regime until the adoption of specific rules. This implies that the Romanian legislative framework does not take over the interdiction resulting from EU regulation to award regional aid to large investment projects undertaken in the steel sector, including when undertaken by SMEs. **Furthermore, the rules applicable to regional aid for 'normal' investment projects undertaken by the SMEs are included in the Competition Council's Regulation on regional aid, and therefore the exclusion of the steel sector from the scope of application of the same regulation could generate confusion as to the possibility to award regional aid for 'normal' investment projects undertaken by the SMEs.**
  - we do not identify any incompatibility problems with respect to the rules applicable to R&D, environmental protection, employment and training aid.

For the **coal industry**, the report underlines that the Competition Council has not adopted yet a Regulation taking over the rules laid down in Council Regulation 1407/2002 (it is foreseen that such a Regulation will be adopted by September 2004). In addition, likewise to the case of the steel sector, coal is excluded from the scope of application of the Competition Council's Regulations on rescue and restructuring aid, closure aid, and regional aid. This means that, for the coal sector, these types of aid are subject to the rules laid down in the general law on state aid (Law No. 143/1999, as modified by Law No. 603/2003). **In other words, at the moment there is no legal basis for awarding these types of state aid for the coal sector in Romania. The report recommends that the Competition Council adopt as soon as possible a regulation transposing the rules resulting from Council Regulation 1407/2002.** Finally, the report does not identify incompatibility problems with respect to R&D, environmental protection, employment and training aid.

For the **motor vehicle** sector, the report does not identify major problems of incompatibility with the EU regulation. For regional aid to large investment projects undertaken in the motor vehicles sector (i.e. aid totalling over 5 million Euro, or supporting investment projects of over 50 million Euro), according to EU rules, the amount of aid awarded cannot exceed 30% of the regional intensity ceiling applicable in the assisted region where the project is undertaken. According to Decision 1811/2002 of the EU-Romania Association Council, the maximum intensity ceiling (net grant equivalent) applicable to regional aid on the whole Romanian territory until the 31<sup>st</sup> of December 2006 is of 50%, respectively 65% in the case of SMEs. The Competition Council adopted in 2003 a Regulation on regional aid to large investment projects that takes over the limitations resulting from EU regulation for the motor vehicles sector (maximum amount permissible 30% of the relevant regional intensity ceiling). From this perspective, the Romanian legislation is fully compatible with the *acquis*. **Nonetheless, the report suggests a modification of the Competition Council's Regulation on regional aid for large investment projects, namely of Articles 24 and 28-29, making reference to the publication by the end of 2004 of a list of**

**sectors with structural problems. In this sense, the Competition Council’s Regulation should take over the provisions of the Commission Communication of 1.11.2003.**

The Regulation issued in 2002 on regional aids provides that in the motor vehicle industry (art. 1(2)) “legislation currently in force will apply up to the moment when specific rules will be adopted”. This wording is normal if taking into consideration that the Regulation has been adopted before the expiry of the specific Framework for motor vehicle industry in the EU, but can however create confusions.

On the one hand, someone could understand that the Regulation on regional aids does not apply to the motor vehicle industry and thus there is another lack of legislation, due to which such aids can not be authorized. On the other hand, someone else could understand that regulation on regional aid can be applied up to the moment when specific legislation will be enacted. **In order to eliminate such potential confusions, it may be sufficient to renounce to mention the motor vehicle industry in art. 1(2).**

For the **shipbuilding industry**, the report underlines that the Competition Council has not yet adopted a Regulation taking over the specific Community rules applicable to state aid for this sector. Moreover, the observations made above in relation to the steel sector as to the content of Art. 1(2) in the Competition Council’s Regulation on regional aid are also valid with respect to the shipbuilding sector. The Competition Council’s Regulation on rescue and restructuring aid is applicable to the shipbuilding sector, but does not contain specific provisions regarding aid compensating for the losses incurred by renouncing to produce. **The report recommends that the Regulation in question be updated in this sense. As a transitory solution applicable until this omission is remedied, in a certain interpretation given to Art. 1(2), regional aid could be awarded to this sector up to the maximum intensity ceiling that was decided for the whole Romanian territory (which are higher than the community rules for this sector). On the other hand, state aid for innovation, export aid, etc. cannot be awarded.**

A specific importance present the aspects related to the pre-accession period, and the outcome of negotiations on state aid with the countries that became members of the EU in May 2004.

Some of the new Member States have negotiated so-called ‘transition periods’ on certain aspects of state aid control, whose purpose is to allow a more gradual adaptation to the *acquis* while diminishing the economic consequences of adapting to the new discipline on their sensitive sectors. The ‘transition periods’ involve in practice a temporary derogation from the application of specific EC rules on state aid, accompanied by conditions intended to prevent the new member States from deriving an unjustified competitive advantage from these derogations. Such conditions include, for example, the establishing of maximum production quotas for those countries that are allowed to award rescue and restructuring aid to the steel sector. These derogations were negotiated either collectively (for example, in the context of the Chapter on the Free Movement of Persons or individually, with each country, as within the Competition Chapter. Moreover, the application of the transition periods involves the set-up of a monitoring system – for example, reports to be presented to the Commission every 6 months.

Art. 24 in part IV of the Accession Treaty (“Temporary Provisions”), title I (“Transition Provisions”) stipulates that the measures foreseen in Annexes V – XIV will be applicable under the conditions stipulated in the same Annexes. These measures are in practice derogations from the EC rules on state aid. Five out of the 10 new Member States have obtained such derogations.

The Accession Treaty also includes 8 protocols, 2 of which refer to the steel sector in the Czech Republic (Protocol 2 – three companies) and Poland (Protocol 8 – eight companies). These protocols contain transitional arrangements (previously approved by the Council). It is to be expected that Romania will benefit from a similar treatment. The report discusses in some detail the content of the temporary derogations obtained by the new Member States.

Finally, interesting conclusions are drawn on the basis of an analysis of past state aid expenditures for the sensitive sectors in Romania, and in some cases, offers a discussions of estimated future state aid expenditures for the same sectors. From a methodological perspective, the report distinguishes between the period preceding to the year 2000 (when Romania did not have any legislation applicable to state aid), the period between 2002 and January 2003 (when Romania had a general law for the control of state aid, but no specific implementing regulations adopted by the Competition Council), and the period post-January 2003, when the Romanian legal framework for the control of state aid became closer harmonised to the *acquis*.

For the **steel sector**, the aid expenditure before 2003 does not raise difficult problems in terms of incompatibility with the obligations assumed by Romania in this field in so far such measures have ceased to produce effects. However, to the extent that such measures continue to produce effect, and depending on whether they have been screened and approved by the Competition Council or not, they qualify as existing aid and must be reported. In other words, it is necessary to distinguish between the moment when a state aid measure *has been approved* by the Competition Council and the moment from when it has started to *be put to effect* – in practice, these two moments seldom coincide.

State aid granted to the Romanian steel sector over the last decade was mainly destined to keep companies afloat and avoid their bankruptcy, in the hope of finding a buyer to also undertake their restructuring, or state aid granted related to the privatisation of the steel companies. The weak financial situation of the Romanian steel companies has always placed the Romanian state in a weak negotiation position during privatisation operations, thus being obliged to make concessions to the buyers.

The Romanian steel companies have been awarded over the period 1993-2002 1362 million USD, out of which more than  $\frac{3}{4}$  were given to one company (Sidex) prior and during privatisation. Out of this total expenditure, only 15-20% is represented by grants, loan subsidies and loan guarantees. The bulk of the expenditure is given by the cancelling of debts and tax arrears (44%) and the conversion of debts into stock (33%).

The total amount of state aid foreseen to be awarded to the steel industry over the period 2003-2010 is 1069.7 million USD. A large share of this amount (49%) will take the form of public debt write-offs, while fiscal facilities awarded to Ispat-Sidex represents 18%, and the write-off of debts to the public utility providers is 16%.

The report presents the conditions that must be met by the general governmental strategy for the restructuring of the Romanian steel sector, and respectively by the individual restructuring plans, to meet the approval of the Council. The report formulates observations and conclusions on the general sectoral strategy, individual restructuring plans, and more importantly, the decisions on state aid to this sector by the Competition Council, which are considered by the European Commission as an authentic test regarding Romania's compliance with the accession criteria in the domain of state aid control.

With respect to the **coal industry**, during the first half of the 1990s, state aid expenditure was quite high. Starting with 1997, the aid expenditure was drastically reduced at the overall level of the mining industry, coal extraction included, in relation to the launch of a restructuring process involving the closure of dangerous or almost-exhausted mining locations, the sharp reduction of the number of employees and the compensatory payments to those made redundant, the targeting of investment on modernising potentially-profitable extraction units. The report underlines, however, that Romania still does not have a coherent legal framework for the control of regional, rescue and restructuring aid for hard coal extraction units, whereas it is recommendable to transpose into the Romanian legal framework the conditions resulting from Regulation 1407/2002.

**Shipbuilding** in Romania has not made the object of specific state aid measures so far. This sector has benefited however from certain horizontal state aid schemes, such as those providing fiscal incentives to FDI, taxation benefits, incentives for the hiring of young graduates, etc.

In the absence of a specific legal framework laying down the conditions for the granting of state aid to this sector (as pointed out in chapter 9), the Romanian shipbuilding facilities can be granted regional level up to 50% of the cost of the investment projects, whereas in the EU the maximum aid intensity ceiling applicable to this sector is of 22.5%. To the contrary, this shortcoming of the Romanian legislation does not make possible the awarding of state aid types that are permitted in the EU, such as innovation aid.

Related to the motor vehicles industry, the report underlines that the bulk of the state aid expenditure corresponding to this sector in Romania was targeted towards two beneficiaries, Dacia and Daewoo. The report examines the state aid measure consisting of a waiver from tax on profit granted to Dacia Pitesti through the Fiscal Code, and underlines that, considering that this measure will continue to be applicable beyond the accession date, this measure must be included on the list of ‘existing aid measures’ (the measure was approved by the Competition Council and accepted by the European Commission). If not declared as existing aid, this measure could be qualified after accession as ‘new aid’, thus being open to a legality scrutiny by the European Commission.

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