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FIRST REPORT ON THE APPLICATION OF THE RULES FOR AIDS TO STEEL INDUSTRY

(presented by the Commission to the Council)

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to the steel industry

1. Part One: Policy on aids to the steel industry

- 1.1. By deciding on 1 February 1980 to apply a set of common rules to all aids granted to steel undertakings, the Commission equipped itself with one of the instruments which are essential both to its contribution to supporting and hastening a radical restructuring of the Community steel industry and to the maintenance of a single Community steel market.

- 1.2. In attenuating for the period during which these rules will be in force the principles concerning the prohibition of specific aids to the steel industry under Article 4 of the ECSC Treaty, but at the same time applying the same rules also to aids granted to the steel industry on the basis of regional and general aid schemes, the Commission recognized the need for State financial assistance to restore the competitiveness of the Community steel industry and also considered that priority should be given to the restructuring of the steel industry on account of the seriousness of its structural crisis.

The Commission realizes that it has thus directly assumed responsibilities. It will continue to fulfil them in the common interest, and in the conviction that subsidies must not be aimed purely at maintaining in operation manufacturing plant which, in view of its products, costs and prices, is no longer adapted to the new market conditions. It will continue to ensure that aids are granted only to the extent that they contribute in the long term to the modernization and adaptation of the Community steel industry, enabling it to face world-wide competition on the basis of modern plant, manufacturing at competitive prices products for which there is a demand, without any need for constant financial assistance from the State.

- 1.3. Although the new rules on aids to the steel industry have been in force only since early 1980 and a relatively small number of cases has since been notified to the Commission and examined by it, certain practical conclusions may be drawn from the experience gained; also some specific problems have arisen in connection with their operation.
- 1.4. The Commission has given its agreement to the aids notified to it only in so far as they satisfied the criteria laid down in the rules. The Commission has not authorized any aid not making an overall contribution to the restructuring of the steel industry.

However, it has emerged that although the adjustments carried out by undertakings with financial assistance from the public authorities during this time represent a step in the right direction, the scope of the restructuring process is still not sufficiently extensive. In the future, therefore, the Commission will even more than in the past scrutinize the aids' conformity with the rules in the light of the extent of restructuring, and in particular of the reduction in capacity indispensable to the restoration of an improved balance between supply and demand. The Commission considers that the radical restructuring of the Community steel industry must re-establish this balance in a relatively short space of time. When it is appraising aids to the steel industry envisaged by national authorities, it therefore has to consider, first and foremost, the effects of these aids at industrial level.

The maintenance of uncompetitive surplus capacity in the long term, by the granting of State assistance to an industry like steel, contributes neither to genuine regional development nor to the secure and lasting provision of essential jobs.

- 1.4.1. These considerations apply both to aid which could prove necessary at any given time to maintaining in operation firms which are basically sound and which have adjusted or could adjust to the new market conditions, but are in difficulty on account of the seriousness and length of the crisis, and to aid aimed at averting severe social problems.

The Commission takes the view that it is essential to ensure that rescue aid, for instance the granting of loans on special terms to enable an undertaking to keep minimum cash holdings, should only be granted when there are genuinely acute social problems and at the same time that these aids should remain true to their name, i.e. they should be granted for a strictly limited period, should not be repeated and should enable the undertaking to implement a genuine restructuring plan. The Commission feels that such rescue aid could well lose its character if repeatedly granted by the Member States ; its real justification having been abandoned, it could become permanent aid to continued operation. Such aid, however, does nothing to encourage undertakings to introduce the necessary changes in their production apparatus and performance. Moreover, in the crisis situation prevailing in the industry, it can sometimes lead to price levels whose competitiveness does not reflect the undertakings' competitive strength and not only distorts conditions of competition but hampers and delays the restructuring in the industry as a whole. The Commission can therefore only tolerate such aid to continued operation under strict conditions, linked to restructuring measures and reductions in capacity.

1.4.2. Similarly, in the case of investment aid, the Commission will rigorously ensure that investment complies with restructuring aims. Such aid directly affects the productive apparatus. If the Commission is to agree to the granting of State assistance for new investment and investment in modernization, which often automatically increases capacity, such assistance must comply in all respects with restructuring needs and the general objectives for steel. The Commission will also scrutinize the intensity of such aids mainly in the light of the extent to which investment contributes to the overall reduction in capacity whether at the level of the individual undertaking or within the wider framework of adjustments between different undertakings. The Commission firmly intends to make sure that the rules on investment aid are observed ; these rules will be all the more effective as the practical objectives of restructuring are defined on the basis of a joint decision of the Commission, the Member States and the undertakings themselves.

1.5. Looking beyond these questions of substance, however, the Commission must also point out that a number of procedural problems arose during the first year that the rules were applied. It attaches great importance to these questions, not on grounds of principle, but because observance of the rules themselves is conditional on observance of the relevant procedures. In practice, the Commission can only fulfil its responsibilities in administering the rules on aids if the Member States scrupulously respect, willingly and in good faith, the procedures they have undertaken to follow and that the Commission has decided to apply without exception.

1.5.1. In the course of the period during which the rules have been applied, aids have not always been notified in sufficient time and in some cases the Commission has had to remind certain Member States of their obligation to notify. This occurred in particular in cases involving assistance granted to steel undertakings under existing regional or general schemes. Under the new rules, in contrast to previous procedure, any aid to the steel industry must be notified, including regional and general aids ; some national administrative practices therefore had to be modified. However, the Commission has the impression that a number of Member States have not yet fully understood and accepted their obligation to notify all aids to the steel industry. The Commission insists on this obligation and stresses that aids granted to the steel industry in application of regional or general schemes must be notified to the Commission at the initiative of the Member States, and not only at its request. The Commission will take all steps available to it to ensure observance of this obligation to notify in advance, for it is well aware that in many cases the steel industry obtains State assistance under regional and general schemes. The Commission is therefore taking the opportunity in this first Report to remind all Member States of their obligations in this respect.

1.5.2. Another problem concerns the provision of funds by public authorities to their own undertakings, notably in the form of increased capital. In the present situation of grave crisis in the steel industry, there is a presumption that increases in capital made by States for their own public steel undertakings, particularly when such operations are repeated, involve some element of aid. One Member State has already informed the Commission that on this account it will notify all the funds it makes available to State-owned steel undertakings. The Commission assumes that all Member States in the same circumstances will also make the necessary advance notification.

1.6. In presenting this first Report on the application of the rules for aids to the steel industry, the Commission gives its assurance to the Council that it will ensure that the procedures and criteria laid down at the beginning of 1980 are strictly followed. It is convinced that it is only in this way that it can make a substantial and essential contribution to the long-term restoration of normal conditions of competition in the industry.

1.7. Part Two of this Report outlines the actual decisions taken by the Commission during the year on the basis of the new rules. There have in fact been few cases. This is due to the fact that a number of measures envisaged by the Member States have not yet been finalized and are not yet sufficiently precise and definite for notification and also because a fairly substantial number of aids had already been granted to the steel industry, notably under regional and general schemes, before the new rules came into force. The Commission therefore felt it worthwhile to outline cases of which it was informed, in an Annex to this Report.

1.8. As regards these latter aids, the Member States informed the Commission during 1978 and 1979 of a number of cases of specific aid granted to steel undertakings before the new rules were applicable ; the most

important of these were discussed at multilateral meetings with experts from the Member States. As the Commission previously pointed out in an answer to a Written Question, it considers that aids granted during these two years were in the main consistent with the objectives pursued by means of the current rules. Certain steel undertakings may have received regional and general assistance as well as these specific aids. However, the Commission has no information on the extent to which such assistance was granted, since this has only had to be notified to the Commission since the new rules came into force.

Part 2: Aid notifications from 1. 2. 1980 to 13. 2. 1981

2.1. During this period the Commission received nine notifications :

2.1.1. five cases of aids for individual investment programmes: two from the Federal Republic of Germany, two from the Netherlands and one from the United Kingdom;

2.1.1. aids for investment to restructure the Italian steel industry;

2.1.3. aids for continued operation in Denmark;

2.1.4. aids programmes for the Belgian and Luxembourg steel industries;

2.1.5. emergency aids for the Belgian steel industry.

2.2. In its examination of aids to the steel industry the Commission's principal concern is to ensure the achievement of the two objectives of the aids "discipline", i.e. that aid makes a genuine contribution to the restructuring of the industry and that it does not cause unwarranted distortions of competition. These principles have so far been applied in the following cases.

2.2.1. Investment aids (Article 2 of Decision n° 257/80ECSC)

2.2.1.1. Federal Republic of Germany

The Commission received notification of an aid for an investment programme to restructure and modernize a steelworks at Dortmund by replacing open-hearth furnaces by an oxygen plant and an associated continuous caster. The capacity of the new plant would be 2/3 of that of the open-hearth furnaces and the technology adopted would permit a substantially higher than normal scrap input as well as reduced energy consumption. There would be important reductions in employment at the works. The Commission gave a favourable opinion on this investment programme.

The aid for this project would be in the form of a loan at a reduced rate of interest from the Federal and Land Governments. The net grant equivalent of the aid was estimated by the Commission to be of the order of 12 %. The Federal and Land Government would receive a share of any revenue from the licensing of the technology.

Given the importance of the modernization and the extent of the capacity reduction for liquid steel as well as the existence of certain structural problems in the area concerned, the Commission considered that this aid conformed to the criteria of Article 2 of Decision n° 257/80/ECSC and accordingly decided not to raise any objections to its implementation.

2.2.1.2. Italy

The Italian Government informed the Commission of its intention to assist restructuring investment by the steel industry both at a steelworks near Naples and elsewhere by using general and regional aid regimes. Regional aid would be available in the Mezzogiorno in the form of grants at a rate of 20 % while general aid would be provided in the form of interest relief grants on loans of up to 15 years with a five year grace period for up to 50 % of investment costs. These interest relief grants would reduce the rate of interest to 30 % of the reference rate. The combined net grant equivalent of these aids is about 38 %.

The Commission examined this proposal in two parts.

First, as regards the restructuring of the steelworks near Naples, which involved the installations of continuous casting equipment, the modernisation of the works' heavy section mill and the construction of a hot wide strip mill, the Commission had given a favourable opinion under Article 54 of the ECSC Treaty. In view of the importance of the restructuring programme, of its compatibility with the Community's

restructuring policy and of the location of the works in an area of the Italian Mezzogiorno suffering from serious structural problems, the Commission considered that aids of this intensity were justifiable and accordingly decided not to raise any objection to their implementation.

Second, as regards the use of these aid systems to assist other steel investment programmes, the Commission was unable to examine the justifications and effects of these aids in the absence of information on the projects that the Italian Government intended to support. This problem was explained to the Italian authorities, who in consequence undertook to notify in advance the other individual cases of application to steel of the aid regimes in question. Accordingly the Commission considered that this second part of the original notification did not call for any further action at this stage.

2.2.2. Aid to continued operation (Article 4 of decision n° 25778U/ECSC)

As indicated in the annex, the Danish Government had in 1978 granted aid to assist in the financing a major steel restructuring programme involving a reduction in capacity. The aids proved to be insufficient to resolve the company's difficulties in financing the restructuring, a failure attributed to the fact that ferrous scrap prices had risen more rapidly in relation to steel prices than had been expected in 1978.

Accordingly the Danish Government decided to provide additional aid to the company in the form of a participatory loan of DKr 108 million. This is a long term unsecured loan which will be remunerated at a rate of interest equal to the rate of dividend on share capital up to 1985 and will thereafter bear a market rate of interest.

The Commission had some reservations about the restructuring plan in particular because it did not consider it sufficiently far-reaching to secure the company's long-term competitiveness. Following an undertaking by the Danish Government to ensure the closure of the company's medium-section mill by 30 June 1982 at the latest the Commission was in a position fully to approve the restructuring programme. In the light of this undertaking and of the further restructuring investment which the company had to carry out in the period up to 1985 the Commission considered that the aid could be considered an integral part of an approved restructuring programme. The aid was moreover of limited duration and of reasonable intensity and amount. In this latter connexion it should be noted that it formed part of a total financial package of DKr 450 million, the rest of which was to be provided by the shareholders and the banks.

Accordingly the Commission decided that the aid conformed to the criteria of Article 4 of Decision n° 257/80/ECSC and did not raise any objection to its implementation.

2.2.3. Belgian aid programme (Articles 2, 4 and 5 of Decision n° 257/80/ECSC)

The Belgian Government notified the Commission of the following aids :

- Aids for "strategic" investment programmes, involving estimated total expenditure of BF 22 bn, in the form of interest relief grants, state guarantees, accelerated depreciation and exemption for three years from the précompte immobilier (rates). These aids, which would be granted in application of the Economic Expansion Laws of 17. 7. 1959 and 30. 12. 1970, were estimated to amount to a net grant equivalent of 14 % to 17.5 %.
- Aids for "minor" investment programmes, involving total expenditure of BF 3.5 bn would be available on the same basis in the form of interest relief grants and state guarantees.

- A number of emergency aids had been granted in the form of state guarantees for 15 year loans with a five year grace period. These guarantees amounting in total to around BF 2 bn were required in order to avoid bankruptcy proceedings being started in respect of three companies.

The Commission examined these aids in the context of the restructuring plan for the Belgian steel industry. The aided investment programmes taken as a whole would result in an increase in production capacity even after taking account of the associated closures decided upon by the undertakings. Furthermore, there were serious doubts concerning the effectiveness of the restructuring plan in restoring the financial viability of the industry in the future. For these reasons the Commission considered that the investment aids did not meet the criteria of either Article 2 (for notified investment programmes) or Article 4 (for investment programmes not notified) (1).

For the emergency aids, the undertakings in question were all important sources of employment in areas suffering from regional problems. The Commission accordingly considered that they were required in order to cope with acute social difficulties pending the implementation of the restructuring plan. In view of their minimal intensity, it therefore raised no objection to these aids.

However, the Commission learned that the Belgian Government had decided to provide further guarantees for loans up to BF 1.5 bn for undertakings of the Triangle de Charleroi. In view of the effects that further emergency aids of this amount could have on the steel market the Commission considered that this case should be examined more thoroughly, in particular so as to ensure that the aids would contribute to the attainment of a better equilibrium between supply and demand.

For these reasons the Commission initiated the procedure of Article 93(2) of the EEC Treaty in respect of the investment aids and of the emergency aids for the undertakings of the "Triangle de Charleroi".

(1) Aids for investment programmes which do not require to be notified to the Commission under Decision n° 22/66 do not meet the first criterion of Article 2 and accordingly must be examined under Article 4 of Decision n° 257/80/ECSC.

2.3. The other aids that have been notified but which were still being examined by the Commission at the end of the period covered by this report were the following :

2.3.1. In the Federal Republic of Germany the Government has decided to aid the construction of a centralised coke and pig-iron production unit for the steel industry in the Saar. The closures associated with this restructuring plan will result in a reduction of pig-iron capacity of about 23 %. The aid notified would be in the form of grants amounting to DM 200 million, to be provided jointly by the Federal and Land Governments, and a further DM 80 million of regional grants.

2.3.2. The Netherlands Government has notified an aid in the form of an unsecured loan at a market rate of interest for the rebuilding and modernisation of coking capacity of a steelworks at IJmuiden. The total cost of the investment programme would be HFL. 440 million and the loan would be for an amount of HFL 200 million.

(An earlier notification of an aid for the modernisation of a hot wide strip mill was withdrawn by the Netherlands Government).

2.3.3. A third case still under examination concerned an aid for the restructuring of the production facilities of a special steel producer in the United Kingdom accorded on the basis of a regional aid system. The restructuring involves concentration of production at three works and the closure of a fourth works together with modernisation of some existing production facilities and will result in a significant capacity reduction (39 % for crude steel). Capital costs of the project would be UK£ 1.7 million and the aid, in the form of regional grants and exchange risk cover would have a net grant equivalent of 15 %.

- 2.3.4. The Belgian Government has notified the Commission of further emergency aids in the form of state guarantees for loans totally BF 6,456 million for five steel undertakings.
- 2.3.5. The Luxembourg Government notified an aid programme for the steel industry involving in particular investment aid for expenditure of FLUX 20 bn over the period 1980-1984 in the form of grants at a rate of 25 %. Additional measures in the form of certain tax facilities, loans at favourable rates of interest amounting to FLUX 29 million, state guarantees for ECSC loans and grants towards the cost of the Anti-Crisis-Division.

Aids and interventions prior to the entry into force of Decision n° 257/80/ECSC

- A.1. In Denmark the Government decided in 1978 to assist in the financing of a restructuring programme by providing aids in the form of a participatory loan of DKr 108 million and of guarantees for borrowing from Community sources (EIB and ECSC) up to a total of DKr 105 million.
- A.2. In the Federal Republic of Germany the Government decided to intervene to promote the restructuring of the Saar steel industry by providing investment grants payable in five annual instalments with a present value of DM 200 million and guarantees up to DM 900 million. The restructuring programme involved substantial modernization and rationalization of two of the three steel companies in the Saar following their takeover by another company and would result in a significant capacity reduction (ranging from 10 % to 25 % according to the stage of production). The cost of the programme was estimated at DM 1.3 bn for investment and DM 0.5 bn for social costs.
- A.3. In France, long-term loans totalling FF 1200 million were granted in 1977 and 1978 from the Economic and Social Development Fund (FDES) (1) under a recovery programme for the steel industry. In addition repayments of principal amounting to FF 90 million of earlier FDES loans were deferred, and the Government agreed to guarantee ECSC and EIB loans where necessary.
- Subsequently, the French Government decided on a financial reconstruction to reduce the industry's financial costs. Ownership of the steel industry was transferred to three new holding companies created by the industry's creditors. In addition the terms of existing FDES loans were modified in particular by a reduction in the rate of interest to a nominal level. Bonds would bear a similar rate of interest, to be made up to the coupon by a new fund created by the State. The amount of loans and bonds affected totalled FF 22,200 million. These were the main elements of the financial reconstruction which was expected to reduce the industry's financial charges to a level comparable to that in other Member States (from 13 % as a percentage of turnover in 1977 to around 5 %). At the same time the industry was to prepare and implement a restructuring plan.

(1) Fonds de Développement Economique et Social.

- A.4. For Luxembourg a notification was made of aid in the form of a grant of 12.5 % and of tax relief for an investment project involving the production of treated and coated sheet. The new plant would replace steel capacity closed in the area. The investment expenditure would be LFR 1.3 bn. It is understood that this aid has not yet been granted.
- A.5. The Netherlands notified aids in the form of grants totalling Hfl 53.6 million for an investment project involving the installation of a continuous caster at a cost of about Hfl 250 million.
- A.6. In the United Kingdom, the Government decided in March 1978 to finance the British Steel Corporation (BSC) exclusively by the subscription of capital, thus abandoning the previous arrangement by which the Corporation's financial requirements were met essentially by a mix of capital and loans. It was recognized that a capital reconstruction would be required in due course, but it was intended to undertake this only when the market situation and prospects became clearer. At the same time the BSC was to take steps to bring capacity more into balance with prospective demand.