

GUIDELINES ON STATE AID IN THE FORM OF GUARANTEES

Pursuant to Article 28 (1) of competition Law no. 21/1996 and Article 22 (1) of State Aid Law no.143/1999, the Competition Council adopts the present Guidelines.

Chapter I General provisions

These guidelines set up the State aid granted in the form of guarantees for implementing state aid Law no.143/1999, with its subsequent completions, further on named as „ Law ”. Guarantees are usually associated with a loan, credit, issuance of the bonds, etc to be contracted by a borrower with a lender.

These guidelines covers all forms of guarantees, irrespective of their legal basis and the transaction covered. Guarantees may be granted as individual guarantees or within guarantee schemes. If aid is involved, of this aid, in most cases benefits the borrower. However, in certain circumstances, there may also be an aid to the lender.

These guidelines do not apply to export credit guarantees.

Chapter II Scope

Section 1. Aid to the borrower

1.1. Usually, the aid beneficiary is the borrower. The State guarantee enables the borrower to obtain better financial terms for a loan than those normally available on the financial markets. Typically, with the benefit of the State guarantee, the borrower can obtain lower rates and/or offer less security. In some cases, the borrower would not, without a State guarantee, find a financial institution prepared to lend on any terms. State guarantees may thus facilitate the creation of new businesses and enable certain undertakings to raise money in order to pursue new activities or simply remain active instead of being eliminated or restructured, thereby creating distortions of competition. Thus, State guarantees fall within the scope of the Law.

1.2. The benefit of a state guarantee is that the risk associated with the guarantee is carried by the State. This carrying of a risk by the State should normally be remunerated by an appropriate premium. Where the State forgoes such a premium, there is both a benefit for the undertaking and a drain on the resources of the State. Thus, even if no payments are ever made by the State under a guarantee, there may nevertheless be a State aid under Article 2 of the Law. The amount of the State aid is assessed at the moment when the guarantee is given, not the moment at which the guarantee is invoked or the moment at which payments are made under the terms of the guarantee.

1.3. There is also a state aid in the form of a guarantee, the more favourable funding terms obtained by enterprises whose legal form rules out bankruptcy or other insolvency procedures or provides an explicit State guarantee or coverage of losses by the State.

1.4. The same applies to the acquisition by a public authority for holding in an enterprise if unlimited liability is accepted instead of the usual limited liability.

1.5. Guarantees given by the State directly, namely by central, regional or local authorities, as well as guarantees given by undertakings under the dominant influence of public authorities, may constitute State aid.

Section 2. Aid to the lender

2.1. Under certain circumstances the lender will benefit from the aid too.

2.2. In particular, for example, if a State guarantee is given ex post in respect of a loan or other financial obligation already entered into without the terms of this loan or financial obligation being adjusted, or if one guaranteed loan is used to pay back another, non-guaranteed loan to the same credit institution, then there may also be an aid to the lender, in so far as the security of the loans is increased. Such aid is capable of favouring the lender and distorting competition, and generally falls within the scope of the Law.

Chapter III Amount of the aid

3.1. In the case of an individual State guarantee, the aid element must be assessed by reference to the details of the guarantee and loan, or other financial obligation. The relevant factors include in particular the duration and amount of the guarantee and loan, the risk of default by the borrower, the price paid by the borrower for the guarantee, the nature of any security given, how and when the State could be called upon to pay a debt and the means, e.g. declaration of bankruptcy, to be used by the State to recover amounts owned by the borrower once the guarantee has been invoked.

3.2. The cash grant equivalent of a loan guarantee in a given year can be:

- calculated in the same way as the grant equivalent of a soft loan, the interest subsidy representing the difference between the market rate and the rate obtained thanks to the State guarantee after any premiums paid have been deducted, or
- taken to be the difference between (a) the outstanding sum guaranteed, multiplied by the risk factor (the probability of default) and (b) any premium paid, i.e. (guaranteed sum \times risk) - premium, or
- calculated by any other objectively justifiable and generally accepted method.

For individual guarantees, the first method should in principle be the standard form of calculation, for guarantee schemes the second one.

3.2.1. The risk factor should be based on the past experience of defaults on loans given in similar circumstances (sector, size of firm, level of general economic activity). The yearly grant

equivalents should be discounted to their present value using the reference rate, then added up to obtain the total grant equivalent.

3.2.2. Where, at the time the loan is granted, there is a strong probability that the borrower will default, e.g. because he is in financial difficulty, the value of the guarantee may be as high as the amount effectively covered by that guarantee.

3.3. If a financial obligation is wholly covered by a State guarantee, the lender has less incentive to assess properly, secure and minimise the risk arising from the lending operation, and in particular to assess properly the borrower's creditworthiness. Such risk assessment might also not always be taken over by the guarantor, for lack of means. This lack of incentive to minimise the risk of non-repayment of the loan might encourage lenders to contract loans with a greater than normal commercial risk and could thus increase the amount of higher-risk guarantees in the State's portfolio.

3.4. A percentage of at least 20 % not covered by a State guarantee is as an appropriate limit for inducing the lender to properly assess the creditworthiness of the borrower, this is under the assumption that the same level of security is provided by the company to the State and the credit institution, to properly secure its loans and to minimise the risk associated with the transaction. The Competition Council will therefore examine critically any guarantees covering the entirety, or nearly the entirety, of a financial transaction.

3.5. In the case of State guarantee schemes, the specific features of the individual cases may not be known at the time when the scheme is to be assessed. In these circumstances, the aid element is assessed by reference to the provisions of the scheme concerning amongst others the maximum amount and duration of loans, the category of enterprise and type of project eligible, the security required from the borrowers, the premium to be paid and the interest rates obtained by them.

Chapter IV

Conditions excluding the existence of aid

4.1. An individual guarantee or a guarantee scheme entered into by the State will be outside the scope of the Law when there is no aid which favours certain undertakings or the production of certain goods. In such cases, notification to the Competition Council is not necessary.

4.2. Also, a guarantee does not constitute State aid if all the following conditions are fulfilled:

- (a) the borrower is not in financial difficulty;
- (b) the borrower would in principle be able to obtain a loan on market conditions from the financial markets without any intervention by the State;
- (c) the guarantee is linked to a specific financial transaction, is for a fixed maximum amount, does not cover more than 80 % of the outstanding loan or other financial obligation, except for bonds and similar instruments, and is not open-ended;
- (d) the market price for the guarantee is paid. This price reflects, amongst others, the amount and duration of the guarantee, the security given by the borrower, the borrower's financial position, the sector of activity and the prospects, the rates of default, and other economic conditions.

4.3. The fulfilment of all the following conditions ensures that a State guarantee scheme does not constitute State aid under the Law:

(a) the scheme does not allow guarantees to be granted to borrowers who are in financial difficulty;

(b) the borrowers would in principle be able to obtain a loan on market conditions from the financial markets without any intervention by the State;

(c) the guarantees are linked to a specific financial transaction, are for a fixed maximum amount, do not cover more than 80 % of each outstanding loan or other financial obligation, except for bonds and similar instruments, and are not open-ended;

(d) the terms of the scheme are based on a realistic assessment of the risk so that the premiums paid by the beneficiary enterprises make it, in all probability, self-financing;

(e) the scheme provides for the terms on which future guarantees are granted and the overall financing of the scheme to be reviewed at least once a year;

(f) the premiums cover both the normal risks associated with granting the guarantee and the administrative costs of the scheme, including, where the State provides the initial capital for the start-up of the scheme, a normal return on that capital.

4.4. Failure to comply with any one of the above conditions set out in paragraphs 4.2. and 4.3. does not mean that such guarantee or guarantee scheme is automatically regarded as State aid. If there is any doubt as to whether a planned guarantee or scheme does constitute State aid, it should be notified.

4.5. There may be circumstances in which it is planned to use State guarantees to enable enterprises, and in particular small and medium-sized enterprises, to obtain loans that the market would not supply. The enterprises may be starting up, expanding fast or be small and hence unable to furnish the necessary security to secure a loan or obtain a guarantee. They may fall into the category of high-risk enterprises expected to move into profitability only in the long term and/or having a particularly high failure rate. This may be the case, for example, with projects concerning new, innovative products or processes. Such circumstances will generally not take State guarantees outside the scope of the Law. State guarantees given in such circumstances should therefore be notified to the Competition Council in the same way as State guarantees given in other circumstances.

Chapter V

Compatibility of state aid in the form of guarantees with competitive environment

5.1. State guarantees within the scope of the Law are examined by the Competition Council with a view to determining whether or not they are compatible with the competitive environment. Before such assessment of compatibility can be made, the beneficiary of the aid must be identified. This can be either the borrower, or the lender, or both.

5.2. In most cases the guarantee contains aid to the borrower. Whether or not this aid is compatible with the competitive environment will be examined by the Competition Council according to the same rules as are applied to aid measures taking other forms. The concrete criteria for the compatibility assessment are specified in the Competition Council's Regulations implementing the Law. The examination will take into account, in particular, the aid intensity, the characteristics of the beneficiaries and the objectives pursued.

5.3. The Competition Council will authorise guarantees only if their mobilisation is contractually linked to specific conditions which may go as far as the compulsory declaration of bankruptcy of the beneficiary undertaking, or any similar procedure. These conditions will have to be agreed at the examination by the Competition Council of the proposed guarantee within the notification at the stage when it is granted. In the event that a granting body wants to mobilise the guarantee under conditions other than those agreed at the granting stage, then the Competition Council will regard the mobilisation of the guarantee as creating a new aid which has to be notified under Article 6 of the Law.

5.4. Where the guarantee contains aid to the lender, such aid might, in principle, constitute operating aid, which in general is regarded as incompatible with the competitive environment.

Chapter VI

Consequences of the infringement of Articles 6 and 7 of the Law, respective non-observance of the notification obligations and standstill clause

6.1. Where a granting body does not observe the obligations of notification and suspension laid down in Article 6 and Article 7 of the Law, the aid element of the guarantee is to be qualified as unlawful, in accordance with Article 16 of the Law.

6.2. Where aid has been illegally granted, the beneficiaries of the aid contained in the guarantee will run a risk. If, after the examination, the Competition Council finds that the State aid is incompatible in the sense of the Law, it shall be recovered, repayed or suspended in accordance with Article 17 of the Law, even if this means the declaration of bankruptcy of the enterprise.

6.3. Guarantees differ from other State aid measures, such as grants or tax exemptions, in the sense that in the case of a guarantee the State also enters into a legal relation with the lender. Consideration has to be given to whether the fact that a State aid has been illegally granted also has consequences for third parties. In the case of State guarantees for loans, this concerns mainly the financial lending institutions. In the case of guarantees for bonds issued to obtain financing for undertakings, this concerns the financial institutions involved in the issuance of the bonds.

6.4. According to the provisions laid down in paragraph 6.3, lenders may have an interest in verifying, as a standard precaution, that the relevant rules on State aid have been observed, whenever guarantees are granted.

Chapter VII

Reports to be presented to the Competition Office by the granting bodies and recipients of aid

7.1. As there may be new developments on the financial markets and as the value of State guarantees is difficult to assess, the monitoring activity of the guarantee aids authorized by the Competition Council, pursuant to Article 26 of the Law, is of particular importance.

7.2. In addition to the usual data on expenditure, the reports to be presented annually to the Competition Office should give, for schemes and individual guarantees as well, data on the total amount of State guarantees outstanding, the total amount paid in the preceding year by the State to defaulting debtors, net of any funds recovered, and the premiums paid for State guarantees in the same year. This information will help in calculating the rate of default and will be used to reassess the value of future guarantees and, if necessary, the premium to be paid in the future.

7.3. The Competition Council may use such information to request appropriate measures to a grantor, according to Articles 13 and 19 of the Law, in order to alter an existing State guarantee aid if the competitive environment is distorted and the proper application of international agreements to which Romania is a party is affected.