

## **DECISION No. 340**

**Of 31.12.2004**

**Concerning the State aid granted to S.C. ISPAT-SIDEX S.A.**

**According to the conditions laid down in Protocol 2 on European Coal and Steel Community, Annex to the European Agreement establishing an association between the European Communities and their Member States, on one hand, and Romania, on the other**

### **THE COMPETITION COUNCIL,**

Having in regard the provisions of the Competition Law no.21/1996, published in the Official Gazette, Part I, no. 88 of April 30, 1996, amended and completed by GEO no. 121/2003 approved by Law no. 184/2004,

Having in regard the provisions of the Law on State Aid no. 143/1999, published in the Official Gazette, Part I, no. 370 of 03.08.1999, amended and completed by Law no. 603/2003,

Having in regard the provisions of the Europe Agreement establishing an association between Romania, on one hand, and the European Communities and their Member States, on the other hand, ratified by Law no. 20/1993, published in the in Official Gazette, Part I, no. 73 of 12.04.1993,

**Based on the following:**

### **I. PROCEDURE OF NOTIFICATION**

- (1) Under Note no. 17185/27.12.2004, registered at the Competition Council as no. RS-AS/110/29.12.2004, the Authority for State Assets Recovery (AVAS) notified, on the basis of article 6 of the Law no. 143/1999 on State aid with subsequent amendments and completions, the modification of the restructuring plan and of the existing aid, authorized by the Competition Council by Decision no. 99/2002, granted to SC Sidex SA Galati. The notification became effective at 29.12.2004.

### **II. The Legal basis for granting the aid**

- (2) In 2001, the Romanian Government has issued the Government Emergency Decree no. 119/2001 concerning some measures for the privatisation of S.C. Combinatul Siderurgic SIDEX S.A. Galati. The state aid has not been notified *ex ante* to the Competition Council, so until the notification date this has been illegal aid according to the provisions of the Law no. 143/1999 on State aid. Subsequently, by note no. 128/16.01.2002, registered by the Competition Council RS-AS no. 128/16.01.2002, the Authority for Privatisation and Management of State Ownership has submitted the notification formular for the state aid measures together with the Restructuring Plan of S.C. Sidex S.A. Galati. The Competition Council has issued the Decision no. 99 of 03.04.2002, by which the individual state for the Steel Company Sidex S.A. Galati was authorized as state aid for compensating losses derived fro the economic activity, state aid for rescue and restructuring and state aid for the protection of the environment in amount of ROL 37.858.289.812 thousand.
- (2) By G.E.O. no. 123/2004 for modifying and completing the Law no. 571/2003 on Fiscal Code, the facility of exemption from payment of profit tax was limited until 31<sup>st</sup> of December 2004.
- (3) By G.E.O no. 134/2004, the facilities approved initially by G.E.O no. 119/2001 regarding certain measures for privatizing SC Combinatul Siderurgic "Sidex" - S.A. Galați were limited also until 31<sup>st</sup> of December 2004.

### **III. Description of THE MEASURE**

#### **III.1. Description of SC Sidex SA Galati The description of the object activity, financial situation. Information about the relevant market**

- (4) The state company “Combinatul Siderurgic Galati” was founded in 1965. Under Law No. 15/1990, Government Emergency Decree (“GED”) 15/1990 and GED No. 29/1991, it became the joint stock company C.S. Sidex S.A. in 1991. The company is registered in the Galati Commercial Register under number J17/21/1991. In November 2001 it was sold to LNM Holdings N.V. (Netherlands) (“LNM”), which acquired approximately 91.6% of the share capital. The company is currently registered as S.C. ISPAT SIDEX S.A. Galati (“Ispat-Sidex”).
- (5) At 31 December 2001 the share capital of Ispat-Sidex was ROL 19,271,231,350,000, made up of 770,849,254 shares with a nominal value of ROL 25,000 per share.
- (6) Ispat-Sidex’s shareholder structure was as follows:

**Table 1**

<b>Shareholder</b>	<b>No. of shares</b>	<b>% shareholding</b>
LNM Holdings N.V.	705.965.328	91,5828%
SIF Moldova	52.974.418	6,8722%
Other shareholders	9.574.750	1,2421%
SIF Oltenia	2.334.758	0,3029%

*Source: Ispat-Sidex Business Plan*

- (7) LNM currently holds 789,552,813 shares (99.4%), while other legal persons hold 1,809,478 shares (0.2%) and other physical persons hold 3,033,411 shares (0.4%).
- (8) The shares of the company are traded on the RASDAQ market.
- (9) Ispat-Sidex holds various controlling and non-controlling stakes in the following companies:

**Table 2**

<b>Company Name</b>	<b>Activity</b>	<b>Shareholding (%)</b>
Sidex Trading	Import and export of Ispat-Sidex's products	100.00
Slc Min-Est SA Mahmudia	Gypsum char stone and chalk extraction	99.95
Sidex Monolitique	Manufacture of refractory ceramic products	80.00
TV Galati	Cable TV	18.00
Sidex International	Import and export of Ispat-Sidex's products	40.00

*Source: Ispat-Sidex's Business Plan*

- (10) Based on the Ispat-Sidex Business Plan, before privatisation the company employed approximately 27,000 people. In 2002 and 2003, as a result of a voluntary redundancy programme pursuant to GEO No. 119/2001, the workforce was reduced by around 9,000, to around 18,000. Ispat-Sidex foresees a workforce of 16,500 in 2008.
- (11) Ispat-Sidex manufactures hot and cold rolled steel products, heavy plates, sheets, including galvanised sheets, re-rolling billets and blooms, high diameter longitudinally welded pipes, spare parts for metallurgy, secondary products resulting from the technological flow, coke-chemical products, oxygen, nitrogen, argon etc. Steel products made by Ispat-Sidex are currently used in the automotive industry, shipbuilding, the construction industry, re-rolling and forged products, pipes and wire drawing.

- (12) As Ispat-Sidex operates an integrated plant, its technological flow includes all processes, from raw materials to finished products. It can be briefly described as follows:
- (13) *Coke and chemical plant:* includes six coke oven batteries operating at 75% of capacity. The batteries currently use imported coal as raw material and produce the coke which is sintered and used in the blast furnace for the production of pig iron and the resulting by-product, coke oven gas. After filtering, the coke oven gas is re-used as fuel and covers 25% of Ispat-Sidex's gas fuel needs.
- (14) *Sintering and blast furnace plant:* includes:
- i. A raw material station with capacity of 5.5 million tons;
  - ii. A sintering plant including 7 conveyer belts (3 of which are on stand-by), processing small pieces of ore to be used in the blast furnaces; and
  - iii. 6 blast furnaces (2 of which are on stand-by) supplying pig iron for the converters. The recovered blast furnace gas covers 34% of total gas fuel consumption.
- (15) *Refractory and steel plants:* include 3 steel sections (basic oxygen furnace or BOF) holding 3 combined blast converters each, 3 continuous castings, an electric steel shop and an auxiliary products shop. 4 of the 9 converters have been closed, leading to a capacity reduction of 3 million tons.
- (16) *Flat rolling section:* manufactures most of Ispat-Sidex's products. It includes a slabbing mill, two heavy plate rolling mills, a hot strip rolling mill, a cold strip rolling mill, a continuous hot immersion zinc coating stream for cold rolled strip and a semi-finished rolling mill.
- (17) *Auxiliary streams and capacity:* this includes spare parts and maintenance, power production and distribution in the steel industry and a transport exploitation plant.
- (18) The plant has all required licences issued by authorised institutions.

### **III.2. Privatisation of Sidex**

- (19) In June 1999 the Romanian Government signed two loan agreements with the International Bank for Reconstruction and Development (the "World Bank") to finance Romania's Programmes for the Adjustment of the Private Sector ("PSAL") and Institutional Development of the Private Sector ("PIBL"). Both these programmes included a component concerning the privatisation of 64 companies with majority-owned State capital, through consultancy services provided by investment banks and privatisation agents selected through international bidding.

- (20) It soon became clear that if Sidex was to be successfully privatised, the World Bank procedures would have to be accelerated, as Sidex was losing approximately USD 1 million per day. In March 2000, therefore, the Romanian Government agreed with the World Bank to remove Sidex from the PIBL programme and continue the process of privatising the company independently.
- (21) Because a number of actions towards selecting the privatisation consultant had already been taken, the privatisation process continued on the basis of the criteria published pursuant to the international bidding procedure developed by the World Bank and applied within the framework of the PSAL and PIBL.
- (22) The Romanian Government selected Fieldstone Private Capital Group, Deloitte & Touche, UEC and Linklaters & Alliance, which drew up the first feasibility study (including the privatisation strategy).
- (23) The privatisation strategy envisaged the negotiated sale of the majority stake in Sidex to strategic investors. The Romanian Government approved the strategy in Government Decision No. 1032/2000.
- (24) The privatisation process was carried out pursuant to GED No. 88/1997 (approved by Law No. 44/1998, amended and completed by Law No. 99/1999), the methodology approved by Government Decision No. 450/1999 (as amended), Government Decision No. 1032/2000 for the approval of the privatisation strategy and GED No. 34/2001 for the constitution of the privatisation commission, which was composed of state secretaries and general managers from different ministries.
- (25) The privatisation was advertised in the Romanian newspapers *Romania Libera*, *Evenimentul Zilei* and *Ziarul Financiar*, as well as the Financial Times (on 11 December 2000) and other publications. The deadline for submitting the final offers, initially set for 5 March 2001, was subsequently extended to 4 April 2001, and this extension was announced in the same publications.
- (26) LNM, Erdemir-Eregli Iron & Steel Works CO with Usinor–Sollac Mediteranee, GRIFCO and TNK KAZ Chrome bought the Presentation File.
- (27) LNM paid the participation guarantee with a view to obtaining access to the data room.
- (28) On 4 April 2001, i.e. the deadline for the submission of offers to purchase Sidex's shares, only LNM had submitted an offer, which was made public on 5 April 2001. The privatisation commission agreed with LNM on the general framework for the share purchase agreement.
- (29) Negotiations (34 meetings) which took place between 19 April and 16 July 2001 aimed to harmonise the requirements of the privatisation commission with those of the potential investor, on the basis of the technical and financial offer submitted.

- (30) The share purchase agreement between APAPS and LNM was signed on 25 July 2001. The Romanian Government approved the share purchase agreement in September 2001. The transaction was closed on 15 November 2001, when notification No. 8/2001 on the conclusion of the share purchase agreement was signed. The Romanian Government approved the memorandum on the conclusion of the privatisation contract on 25 November 2001.
- (31) The information submitted by APAPS (now the Authority for State Asset Recovery (“AVAS”)) leads to the conclusion that the privatisation was carried out in a transparent and open way.

### **4.3 The Privatisation Agreement**

- (32) The Share Sale–Purchase Contract between the Authority for Privatisation and Management of State Ownership (“APAPS”) and LNM Holdings N.V. (the “Privatisation Agreement” or the “Agreement”) was concluded on 25 July 2001. The Agreement has been subject to 11 amendments (addenda) which were concluded between October 2001 and April 2004. It provides for the acquisition of a controlling stake in Combinatul Siderurgic Ispat Sidex SA, including 74.32% of the shares held by APAPS and additional shares resulting from a debt for equity swap performed in accordance with the Agreement. The principal terms of the Agreement are as follows.
- (33) [...] <sup>1</sup>
- (34) *Representations and Warranties.* The Agreement provides for various representations and warranties regarding, *inter alia*, due authorisation and incorporation, no winding-up and bankruptcy, ownership rights, litigation, accounting records, financial statements, company liabilities and employment issues.
- (35) *Seller’s Covenants.* The Romanian State agreed to provide the Purchaser with a number of covenants regarding the business operations and restructuring of Ispat-Sidex, primarily concerning the conversion of certain of the company’s debts into equity, exemption from payments of taxes and fees, exemption from payments of custom duties, re-scheduling of social contributions and certain financial support for company employees taking early retirement.
- (36) *Purchaser’s Covenants.* The Purchaser agreed to a number of covenants regarding the business operations of Ispat-Sidex. The Purchaser also agreed to invest substantially in technology and environmental protection, and gave a number of commitments regarding employment and social policy.
- (37) Following the execution of the Privatisation Agreement on 25 July 2001, and as a result of Sidex’s worsening financial situation and delays compared with the original closing schedule, LNM became concerned that the economics of the

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<sup>1</sup> Confidential data

transaction had significantly deteriorated because of continuously mounting losses. Moreover, APAPS had not been able to fulfil all the conditions for closing: in particular, the CSFB and BCR loans had not been renegotiated as promised, which resulted in increased costs for Sidex; and the transfer of ownership of the thermal power plant located on Sidex's premises, had not been achieved. By the end of October 2001, LNM was entitled to delay the closing further or cancel the deal. Moreover, APAPS wished to limit its maximum indemnification obligations that would have resulted from the negative economic performance of Ispat-Sidex.

### ***III.4 LNM Group***

- (38) The LNM Group is the world's second largest steel producer, with a steel production capacity of 38 million tons, steel-making operations in 12 countries (the US, Canada, Mexico, Trinidad, France, Germany, Kazakhstan, Algeria, Romania, Czech Republic, South Africa and Indonesia) and approximately 120,000 employees worldwide. The Group's estimated annual revenue for 2003 was USD 12 billion (EUR 12.7 billion). Companies in the LNM Group produce a broad range of high quality, finished and semi-finished products for the flat and long product markets. The Group supplies steel to customers in over 60 countries, mainly the United States and Europe.
- (39) LNM Group production includes pig iron, slabs, blooms, billets, flat steel products (hot-rolled, cold-rolled, plate, hot dipped galvanised and electro-galvanised), long steel products (wired rod and bars), as well as pipes and wire products

### ***IV. Overview of the Measures Granted to Ispat-Sidex***

- (40) Ispat-Sidex benefited from the following measures in the context of its restructuring:

**Table 3 Summary of the measures (in nominal values)**

Measure	Aid Amount 1993-2000 (USD million)	Aid Amount 2001 (USD million)	Aid Amount 2002-2010 (USD million)
Guarantees granted by the State in 1994-1999	119,3		
July 2001 swap into shares of the Company's debts consisting of amounts paid by the Ministry of Public Finance as guarantor to the lender banks for loans granted to the Company and secured by the State		279,0	
November 2001 swap into shares of the Company's debts, consisting of amounts paid by the Ministry of Public Finance as guarantor to the lender banks for the loans granted to the Company and secured by the		41,2	

<b>Measure</b>	<b>Aid Amount 1993-2000 (USD million)</b>	<b>Aid Amount 2001 (USD million)</b>	<b>Aid Amount 2002-2010 (USD million)</b>
State			
Swap into shares of the Company of receivables payable to APAPS		14,4	
Swap into shares of the Company of receivables held by the Banking Debts Valuation Authority		29,4	
Swap into shares of the Company of debts to Electrica, Termoelectrica, Romgaz, Distrigaz and CFR Marfa, plus write-off of VAT collected relating to these debts		36,2	
Exemption from payment of all delayed increases and penalties relating to certain debts swapped into the Company's equity		511,4	
Exemption from customs duties and VAT on raw materials and imports for modernisation and investment			4,5
Exemption from payment of VAT on equipment supplies for the domestic market			0,5
Deferral of VAT collected and not paid			9,2
Exemption from VAT on domestic projects			0,2
Deferral of employer contribution to social security, health and unemployment fund			38,2
Exemption from payment of profit tax			40,4
Delayed payment interest on moratorium of Company's loan repaid by Romanian Government			8,0
Write-off of delayed increases and penalties for local taxes			7,3
<b>GRAND TOTAL</b>			<b>1131,7</b>

*Source: Ispat-Sidex Business Plan – Table 29.2*



## 7. Relevant Market Description

- (41) The measures granted to Ispat-Sidex may affect the following markets:
- (18) heavy plates market;
  - (19) hot rolled plates and strips market;
  - (20) cold rolled plates and strips market;
  - (21) galvanised plates and strips market;
  - (22) billets and blooms market; and
  - (23) welded pipes market.
- (42) The geographical markets for steel products are at least Community-wide, if not wider.
- (43) In 2000 the value and volume of the sales made by Sidex in Romania and its share of total sales were as follows:

**Table 4 The total sales and the share market of SC ISPAT SIDEX SA<sup>2</sup>**

Market share	Sales value (thousand ROL)	Sales volume (tons)	Share (%)
Heavy plate	[...]	[...]	[...]
Hot rolled plates and strips	[...]	[...]	[...]
Cold rolled plates and strips	[...]	[...]	[...]
Galvanised plates and strips	[...]	[...]	[...]
Billets and blooms	[...]	[...]	[...]
Longitudinally welded pipes	[...]	[...]	[...]

*Source: 2002 State aid notification to the Competition Council*

- (44) The 2001 market shares of Ispat-Sidex in the EU were:

**Table 5**

Market segment	Share (%)
Heavy plate	0.73
Hot rolled plates and strips	0.68
Cold rolled plates and strips	0.002
Galvanised plates and strips	0.003
Billets and blooms	0.7
Longitudinally welded pipes	0.0001

*Source: 2002 State aid notification to the Competition Council*

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<sup>2</sup> Confidential data

- (45) The 2001 worldwide market shares of Ispat-Sidex (excluding the EU) are as follows:

**Table 6**

Market segment	Market share (%)
Heavy plate	1
Hot rolled plates and strips	1.15
Cold rolled plates and strips	0.03
Galvanised plates and strips	0.005
Billets and blooms	0.85

*Source: 2002 State aid notification to the Competition Council*

- (46) In 2001 Ispat-Sidex's sales accounted for almost 4% of Romania's GDP. Moreover, 25% of GDP was directly or indirectly related to the company's activities.

## V.2 Product Sale Programme

**Table 7 Forecast situation of 2003–2008 sales volumes (in thousand tons)**

Products	Market	2003	2004	2005	2006	2007	2008
Heavy plate	Domestic	321	394	434	455	477	477
	External	1050	1036	998	980	962	962
	Secondary	205	170	168	165	162	162
Hot rolled plates and strips	Domestic	140	148	163	171	179	179
	External	1021	1261	1346	1307	1300	1300
	Secondary	105	191	190	172	171	171
Hot rolled plates and strips	Domestic	140	158	174	182	191	191
	External	308	453	598	731	724	724
	Secondary	79	114	153	187	185	185
Galvanised plates and strips	Domestic	39	53	58	61	64	64
	External	103	131	125	123	120	120
	Secondary	9	17	17	16	16	16
Welded pipes	Domestic	7	5	6	6	6	6
	External	9	28	27	27	27	27
Semi-finished	Domestic	244	250	250	250	250	250
	External	61	0	0	0	0	0
Plate	Domestic	0	0	0	0	0	0
	External	0	0	0	100	118	118
<b>Total</b>		<b>3857</b>	<b>4409</b>	<b>4707</b>	<b>4933</b>	<b>4952</b>	<b>4952</b>

- (47) [...]³

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- (48) The company will continue domestic sales to maximise its Romanian market potential. The forecasts are based on developments in the car industry, growth in the electrical appliances industry, a continuing increase in infrastructure investment and an increase in demand for steel products in the context of the privatisation process.
- (49) Regarding external markets, Romania supplies steel to neighbouring countries. Ispat-Sidex has the potential to become a stable supplier to the shipbuilding, natural gas and car industries in neighbouring countries.

## **VI. Assessment of the Measures**

- (50) As set out above, relations between Romania and the EU are governed by the Europe Agreement. Romania is not yet an EU Member State, and is doing its best to qualify under the Copenhagen Criteria for accession in 2007. Under the EA, Romania has undertaken to respect certain rules as regards the granting of State Aid to undertakings operating in Romania. The Competition Council must assess the aid granted in light of national law and Romania's obligations under the EA, which entitle Romania to grant State aid to the steel industry for restructuring purposes up to the date of accession, provided certain conditions are met. It is useful for the Competition Council to consider the *acquis communautaire* applicable to the State aid under consideration, bearing in mind the particular situation of the steel industry and the change in EC law applicable to the steel sector due to the expiry of the ECSC Treaty in 2002.

### ***VI.1 The character of State aid of the notified measures***

- (51) The term 'State aid' as described in Article 2 of the State aid Law consists of the following four constitutive elements: (i) a benefit (ii) granted through State resources (iii) to a certain undertaking or sector (selectivity), (iv) which potentially distorts competition and affects trade between (in this case) the EU and Romania.
- (52) In GEO no. 119/2001 the Romanian Government approved a number of obligations in the Privatisation Agreement with LNM which may be considered to contain elements of State aid. These obligations included the conversion of public claims into shares to be sold to LNM, facilities granted by the Ministry of Public Finances concerning external loans contracted by the company with the State as guarantor, exemption from the payment of certain customs and VAT duties and rescheduling of payments of social, health and unemployment fund contributions. The GEO no 119/2001 was modified by GEO no. 123/2004 and GEO no. 134/2004, which has limited the amount of these facilities. According to these normative acts, there will not be granted any facilities to SIDEX ISPAT after 31<sup>st</sup> of December 2004.
- (53) Finally, the parties agreed the company would enjoy relief from profit tax for three years starting from 1 January 2002. The amount of the benefit under the profit tax relief was not limited, but at the time of the Competition Council

approval it was estimated to amount to ROL 1,720,005,000 thousand (USD 52.3 million). The Business Plan provides the nominal value of this tax relief at around USD 40.4 million.

- (54) [...] <sup>4</sup>
- (55) The total value of the State's contributions under the Privatisation Agreement has amounted to ROL 30,597,716 million (USD 1,131.7 million)..
- (56) The package was financed by State resources, and undoubtedly meets the selectivity criterion as it was granted to a single company. It also has a potential impact on competition and trade, since the company's products are traded between Romania and the EU and it competes with other European companies.
- (57) The measures were agreed in a private share purchase agreement, and LNM paid a purchase price in consideration. In such circumstances, to establish whether the terms of the agreement benefited the purchaser, the State's behaviour must be compared with the hypothetical behaviour of a private investor in the same situation (the "private investor" or "market economy operator" test). In other words, would a private vendor have agreed to the terms laid down in the Privatisation Agreement? The Commission and the European Courts have consistently held that a private vendor would normally sell shares only for a positive purchase price, whereas in this case, owing to the various financial commitments by the State, the final purchase price (the balance between the State's financial obligations under the Privatisation Agreement and the price paid by LNM) was negative. A private vendor, would probably choose to wind up its company rather than accept a negative purchase price, and would accept such a price only in an exceptional situation where it was still more economic than winding up the business, i.e. if the liquidation costs exceeded the costs related to the sale of the business. When comparing these alternatives, only the costs which a private vendor would have to bear in a similar situation may be taken into consideration. The State's financial burden resulting from its typical public functions (such as the costs of unemployment benefit) must be excluded.
- (58) In this case, there are no indications that the State would have had to bear higher costs if Sidex had been liquidated than under the Privatisation Agreement. In light of these considerations, the whole package of the State's financial obligations approved by GEO. no. 134/2004 for modifying and completing GEO. no. 119/2001 and the profit tax relief until 2004, granted according to GEO no. 123/2004 for modifying and completing the Law no. 571/2003 on the Fiscal Code must be regarded as State aid within the meaning of Article 2 of Law No. 143/1999 on State aid with the subsequent modifications and completions (the "Law").

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<sup>4</sup> Confidential data

- (59) By Decision no. 395/25.10.2002, the Competition council authorized the specific allocation of aid as aid for environment protection. The Romanian government argues that the aid was approved on the specific legal basis of GEO 40/2002 and it considers that the general character of the provisions of GEO has to be taken into consideration. The Competition Council agrees that the nature of GEO 40/2002 has to be taken into consideration. This Ordinance lays down general rules linking certain benefits to payment of existing debts to the public sector (in this case, the Galati local authority). The law makes it possible for a company to obtain substantial reductions in amounts which it owes to the public authorities if it actually pays its debts according to an agreed schedule. Ispat-Sidex has taken advantage of this provision, and its debts have been reduced by USD 7.3 million as a result.
- (60) Secondly, a discount of this type corresponds to “market investor” behaviour (i.e., a creditor faced with a large number of unwilling debtors, which he knows may have difficulty paying, can resort to a similar motivational program to obtain as much actual payments as possible). Because it corresponds to the behaviour of a “market creditor” it is not considered as state aid.
- (61) Since this reduction is available to all companies in the same situation (and at least in practice is not discretionary, GEO 40/2002 measure is a general measure and thus does not constitute State aid. Therefore, for all the above reasons, there is no need to show necessity or that the amount paid is the minimum necessary.

## **VI.2 Compatibility Assessment**

- (62) When assessing the compatibility of the first State aid package, the Competition Council must evaluate whether the measures are compatible “with a normal competitive environment”, in accordance with the provisions of Article 2 paragraphs (2) and (3) of the Law, and the EA and the Implementing Rules. It must therefore assess whether the measures are covered by one of the exemptions to the general prohibition of State aid.
- (63) The general criteria applicable to State aid for the steel sector are laid down in Protocol 2 on ECSC products annexed to the EA.
- (64) The first State aid package aims to facilitate the restructuring of Sidex. According to Article 9 of Protocol 2, restructuring aid may be approved if it strictly fulfils the criteria, and if it is certain that the advantages that result from the survival of the undertaking will compensate for any distortion of competition, especially if the net effect of collective redundancies as a consequence of the company’s bankruptcy, combined with the bankruptcy’s potential effects on suppliers, would exacerbate unemployment problems nationwide.
- (65) The provisions of Article 9(4) of Protocol 2 on ECSC products, read with the relevant Commission guidelines on aid for the rescue and restructuring of firms in difficulty, allow Romania to grant restructuring aid to a steel company if:

- a. the firm is in economic difficulty;
- b. implementation of the restructuring plan leads to the viability of the company under normal market conditions at the end of the restructuring period;
- c. the value and intensity of the State aid are strictly limited to the minimum necessary to restore viability; and
- d. the aid is progressively reduced.
- e. the restructuring must be linked to a rational globalisation and reduction of production capacity in Romania.

### VI.2.1 Firm in Difficulty

- (66) According to the Commission's guidelines on restructuring aid, a firm is in difficulty when it is unable 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. The usual signs that a firm is in difficulty are increasing losses, diminishing turnover, growing stock inventories, excess capacity, declining cash flow, mounting debt, rising interest charges and falling or nil net asset value. In acute cases the company may already have become insolvent, or may be the subject of collective insolvency proceedings brought under its domestic law.
- (67) From 1998 until its privatisation, Sidex was in severe financial difficulties.
- (68) Following a cyclic decline at the beginning of year 1999, mostly due to the Asian crisis in 1997, the steel sector confronted by the end of 1999 and in 2000 a dramatic shift in demand and price that affected the company's financial situation.
- (69) An examination of the evolution of the main economic-financial indicators recorded during 1998-2001 shows the following:

a) *Diminishing of own assets:*

-USD -

	<b>1998 8,875.55</b>	<b>1999 15332.93</b>	<b>2000 21692.74</b>	<b>30.06.2001 29,060.86</b>
Own assets	365,928,872	389,060,147	52,571,966	-86,733,599
Losses	5,439,550	490,182,046	356,992,754	125,903,741

b) *Evolution of Turnover*

- USD -

<i>Year</i>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>30.06.2001</b>
Turnover	1,075,756,432	691,185,312	798,274,768	365,299,926

c) *Stock volume*

- USD-

<i>Year</i>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>30.06.2001</b>
Stocks	153,670,071	120,065,871	131,057,413	102,661,340

*d) Increase of the companies' debts*

- USD-

<i>Year</i>	<b>1998 8,875.55</b>	<b>1999 15332.93</b>	<b>2000 21692.74</b>	<b>30.06.2001 29,060.86</b>
<i>Total amount of debts, out of which</i>	914,984,258	1,241,235,812	1,444,938,365	1,220,588,999
<i>Debts to the State Budget</i>	289,650,026	730,161,799	979,726,237	875,156,136

*e) Rate of debts*

- USD -

	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>30.06.2001</b>
Total amount of debts (ROL thousands)	914,984,258	1,241,235,813	1,444,938,365	1,220,588,999
Total amount of liabilities (ROL thousands)	1,306,486,240	1,646,856,152	1,524,092,644	1,133,713,644
Total amount of debts /total amount of liabilities (%)	70	75.3	94.8	107.6

*f) Asset solvency calculated using the formula own assets/total liabilities*

USD

	<b>1998 8,875.55</b>	<b>1999 15332.93</b>	<b>2000 21692.74</b>	<b>30.06.2001 29,060.86</b>
Own assets	365,928,855	389,060,120	52,572,164	- 86,733,633
Total amount of liabilities	1,306,486,240	1,646,856,152	1,524,092,644	1,133,713,644
Assets solvency (%)	28	23.6	3.4	-7.6

- (70) The overall analysis shows that on 30 June 2001 the company was practically in a state of insolvency. The total loss of its own capital during the first half of 2001, heavily increasing losses, growing stock inventories, mounting total debts, mounting percentage of debts to the State budget within the total amount of debts and rising interest charges, prove the company's dramatic economic situation in June 2001.

## **VI.2.2 Restoration of viability through a coherent Restructuring Plan**

- (71) The granting of restructuring aid is conditional on the implementation of a restructuring plan which must restore the long-term viability of the company within a reasonable timescale, and on the basis of realistic assumptions as to future operating conditions. Restructuring aid must therefore be linked to a viable restructuring plan. The plan should provide for a turnaround that will enable the company, after completing its restructuring, to cover all its costs, including depreciation and financial charges. The expected return on capital should be

sufficient to enable the restructured firm to compete in the marketplace on its own merits.

### VI.2.3 Coherent Restructuring Plan

- (72) Following the negotiations with the Romanian state on the sale-purchase of the majority share-package, LNM undertook to draw up a Business Plan which included a plan for restructuring the company consisting of the realisation of technical and technological investments, as well as financial and social restructuring.
- (73) After the completion of the privatisation process, significant changes took place in the company's business practices through the injection of working capital, suppression of the barter system, optimisation of sales and marketing, enhancement of work force quality and improvements in economic efficiency through strict financial discipline. It should be noted that the measures in the restructuring programme have led to a 25% increase in production and a reduction in costs (especially a 33% reduction in energy costs), while steel-making capacity has been significantly reduced and capacity for finished products has remained constant.
- (74) In fact, the restructuring of the company has started in 1994, by closing the Sintering Plant and has continued in 1996 by closing the electrical steel plant (260 tons), of the coke plants (2050 tons), of the furnaces (3300 tons) and of the converters (3000 tons). Until the end of 2000 other converters were closed (1000 tons) and semi-finished rolling mills (4200 tons).

#### VI.2.3.1 Technical and Technological Restructuring

- (75) [...]<sup>5</sup>
- (76) The technical and technological restructuring comprises investment and modernisation measures, measures to eliminate break-offs and ensure technological utilities for production, and concentration on the technical parameters and operation practices of the plants.

**Table 8      Planned Investment in Technology in 2002–2008 Business Plan<sup>5</sup>**

USD million	2002	2003	2004	2005	2006	2007	2008	Total
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

<sup>5</sup> Confidential data



USD million	2002	2003	2004	2005	2006	2007	2008	Total
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
TOTAL	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Source: Ispat-Sidex Business Plan – Table 11

(77) [...]<sup>6</sup>

(78) The effects foreseen by Ispat-Sidex after completion of the technological investment include improvement of product quality, an increase in productivity, manufacture of products with high added value and a reduction in operating costs.

### VI.2.3.2 Environment Protection Programme

(79) To reduce the negative impact of its business activities on the environment, Sidex spent between 1990 and 1992 about USD 0.13/ton of steel produced, between 1993 and 1996 about USD 0.8/ton of steel produced and between 1997-2001 about USD 1.38/ton of steel produced.

(80) [...]<sup>6</sup>

**Table 9 Investment in environment protection included in the 2002-2008 Business Plan (in USD million)<sup>6</sup>**

Objectives	2002	2003	2004	2005	2006	2007	2008	Total
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Source: Ispat-Sidex Business Plan – Table 15

### VI.2.3.3 Employment Restructuring Programme

(81) Employment restructuring envisages a correlation between the number of employees and the level of technological progress and involves reducing the number of jobs in the production sector.

(82) Before privatisation the steel company had about 27,000 employees. In 2002 and 2003 approximately 8,000 employees were made redundant. According to Ispat-Sidex, in 2008 the workforce will number 16,500 employees.

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<sup>6</sup> Confidential data

- (83) The Business Plan includes the company's contribution of USD 22.2 million to employment restructuring in order to cover costs arising from the 2002 redundancy programme. The other costs corresponding to the restructuring of the workforce were borne by the State through the Social Insurance Budget. The compensatory payments were made directly to the employees and not through the company. The company paid the workers the entire statutory requirement under the redundancy law from its own resources.

#### **VI.2.3.4 Financial Restructuring**

- (84) The financial restructuring comprises a series of measures concerning the historical debts of Sidex, mainly the writing-off of penalties and other fees for failure to pay debts to the State budget on time. A large part of the accrued penalties corresponds to production capacities closed between 1990 and 2000. The debts corresponding to production capacities which were closed are reflected in the company's balance sheets between 1994 and 2000 and led to an increase in the company's debts. Failure to initiate an immediate financial restructuring led to a difficult economic-financial situation in 2001. Penalties and other fees for late payment continued to rise until ownership was transferred to LNM, when they were either written off or converted into shares.
- (85) The financial restructuring involved the following measures according to the provisions of GEO no. 134/2004 and GEO no. 123/2004:
- conversion into shares of claims owned by the Authority for Bank Assets Revaluation which were subsequently taken over by LNM under the Privatisation Agreement;
  - exemption from payment of penalties and other fees for late payment due on the date of issue of budgetary liabilities certificates by the creditor;
  - rescheduling of payments of social and health insurance contributions and contributions to the Unemployment Fund until 31<sup>st</sup> of December 2004;
  - deferral of VAT payment until 31<sup>st</sup> of December 2004; initially by GEO no 119/2001 the deferral was granted for three years from the date of finalizing the Share Purchase Agreement;
  - exemption from payment of customs duties and VAT for the direct importing of equipment, raw materials and any other products to realise the main object of the company's activity and investments in technology and environmental protection; according to the GEO no 134/2004 for the modification and completion of GEO no. 119/2001, the exemption is limited until 31 December 2004; initially by GEO no 119/2001 the exemption was provided for five years from the date of finalizing the Share Purchase Agreement.
  - exemption from payment of VAT on deliveries of equipment, raw materials and any other products on the domestic market to realise investments in technology and environmental protection; according to the GEO no 134/2004 for the modification and completion of GEO no. 119/2001, the exemption is

limited until 31 December 2004; initially by GEO no 119/2001 the exemption was provided for five years from the date of finalizing the Share Purchase Agreement

- writing off the company's debts to SC Electrica SA Termoelectrica SA, SC Romgaz SA, SC Distrigaz SA and SC Caile Ferate Romane Marfa SA at the closure date;
- conversion into shares of claims against the company by the Ministries of Public Finances and Labour and Social Solidarity, the health insurance authorities and other state institutions;
- conversion into shares of State claims regarding sums paid by the Ministry of Public Finances as guarantor of the lender banks on loans contracted by the company and guaranteed by the State, and related interest and commission, as well as the commission owed to the risk fund;
- write off of increases and penalties for late payment of local taxes calculated until 11 July 2002; and
- exemption from payment of the profit tax. According to the Government Emergency Ordinance no 123/2004 for modifying and completion of Law no. 571/2003 on the Fiscal Code, the exemption was limited until 31 December 2004; initially by GEO no 119/2001 the exemption was provided for five years from the date of finalizing the Share Purchase Agreement.

#### VI.2.4 Restructuring Costs, Financing Sources and the Forecast Financial Situation

(86) Restructuring costs include the costs of investment in technology and environmental protection, and employment and financial restructuring costs.

**Table 10 Financial Restructuring Costs (in USD million)<sup>7</sup>**

Financial Measures	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	Total	Financing Source
Debt for equity swap	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Debt write-off	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>TOTAL</b>	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Source: Ispat-Sidex Business Plan – Table 29.1

**Table 11 Technological Restructuring Costs ((in USD million) <sup>7</sup>**

Measure Modernisation/ Investments	1998-2001	2002	2003	2004	2005	2006	2007	2008	Total	Financing Source
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	

<sup>7</sup> Excluding the financial measures in 1993-1997, amounting to USD 73.4 million.

[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	Contribution from LNM
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	

Source: Ispat-Sidex Business Plan – Table 11

**Table 12 Environmental Restructuring Costs (in USD million)<sup>8</sup>**

Environmental protection measures	1998-2001	2002	2003	2004	2005	2006	2007	2008	Total	Financing Sources
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	Contribution from LNM
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	
[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	

Source: Ispat-Sidex Business Plan – Table 15

**Table 13 Employment Restructuring Costs (in USD million)<sup>8</sup>**

Social Measures	1998-2001	2002	2003	2004	2005 -2008	Total	Financing Sources
Staff Redundancies	[...]	[...]	[...]	[...]	[...]	[...]	Contribution from LNM Holdings

Source: Business Plan – Table 29.1

(87) [...]<sup>8</sup>

## VI.2.5 Restoration of viability

(88) [...]<sup>8</sup>

(89) However, considering that the steel industry represents a sensitive sector in the European economy, and taking into account the EU's experience in restructuring the sector, Annex B to the Commission's Guidance of February 2004 on drawing up a steel restructuring programme provides specific viability criteria to be fulfilled by restructured steel companies. The Competition Council has based the viability test on the Guidance.

<sup>8</sup> Confidential data

(90) The main viability indicators (criteria) are:

V<sub>1</sub> – gross operating margin;

V<sub>2</sub> – gross profit ratio.

(91) At the end of the restructuring period, the viability indicators for Ispat-Sidex must reach the following values:

V<sub>1</sub> must represent 13.5% times more of the revenue obtained from selling steel products;

V<sub>2</sub> must be 1,5% times more of the revenue obtained from selling steel products.

(92) To apply this test, Ispat-Sidex prepared a forecast of the evolution of the income statement, the balance sheet and the cash flow, based on current prices, i.e.

- Revenue forecast: based on sales prices and production volumes estimated in the context of potential development of the international steel market; and
- Operating costs estimated by applying different inflation rates for materials, energy and fixed costs.

(93) In the first set of financial forecasts, the application of the viability test is based on the company's revenues and costs. The costs and revenues taken into account are those relating to metallurgic production. The turnover is the result of cashed revenues from sales of steel products.

**Table 14 Income Statement based on current prices<sup>9</sup>**

USD thousand	2002	2003	2004	2005	2006	2007	2008
<b>Turnover, of which:</b> - Steel sales - Other sales - Variable Costs	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Contribution,</b> of which: Fixed costs	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Operating margin</b> Depreciation/ amortisation	[...]	[...]	[...]	[...]	[...]	[...]	[...]

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<sup>9</sup> Confidential data

<b>Profit/(Loss)</b> Provisions and Exceptional items -Financial Revenue -Financial charges	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Pre-tax profit</b> Tax <sup>10</sup>	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Net Profit</b> Dividend (67%)	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Retained earnings</b>	[...]	[...]	[...]	[...]	[...]	[...]	[...]

*Source: Business Plan, Table 19*

(94) Application of the Commission's viability test requires the income statement to satisfy the "minimum accounting conditions", i.e.

- depreciation/amortisation may not be lower than 7% of steel-related turnover; and
- financial charges may not be lower than 3.5% of steel-related turnover.

(95) Ispat-Sidex estimated the following figures for depreciation and financial charges:

**Table 15 Depreciation/amortisation<sup>11</sup>**

<b>USD thousand</b>	2003	2004	2005	2006	2007	2008
Turnover	[...]	[...]	[...]	[...]	[...]	[...]
Depreciation	[...]	[...]	[...]	[...]	[...]	[...]
% of turnover before adjustment	[...]	[...]	[...]	[...]	[...]	[...]
Minimum % of turnover necessary	[...]	[...]	[...]	[...]	[...]	[...]

*Source: Competition Council calculation based on the Business Plan – Table 19*

**Table 16 Financial charges<sup>11</sup>**

<b>USD thousand</b>	2003	2004	2005	2006	2007	2008
Turnover	[...]	[...]	[...]	[...]	[...]	[...]
Forecast financial charges	[...]	[...]	[...]	[...]	[...]	[...]
% of turnover before adjustment	[...]	[...]	[...]	[...]	[...]	[...]
Minimum % of turnover necessary	[...]	[...]	[...]	[...]	[...]	[...]

*Source: Competition Council calculation based on the Business Plan – Table 19*

<sup>10</sup> The company is liable to pay tax on profits from 2005 onwards, since the tax exemption is being effectively withdrawn from 2005. In 2003 the Company did not benefit of the tax relief as the Fiscal Code provides a general measure according to which the annual loss, established by the profit tax statement is deductible from the taxable profits from the following five years.

<sup>11</sup> Confidential data

- (96) Thus Ispat-Sidex does not fulfil the two criteria necessary for application of the viability test. According to the Commission's Guidance, the Competition Council therefore has to apply a "second set" of financial estimates of special accounting conditions to the "first set" of financial forecasts. These special accounting conditions include minimum levels of tax and depreciation, expressed as a percentage of steel sale revenues and obligations related to charges.

**Table 17 Depreciation/amortisation after adjustment according to the special accounting conditions<sup>12</sup>**

USD thousand	2003	2004	2005	2006	2007	2008
Turnover	[...]	[...]	[...]	[...]	[...]	[...]
Necessary surplus	[...]	[...]	[...]	[...]	[...]	[...]
Adjusted depreciation	[...]	[...]	[...]	[...]	[...]	[...]
% of turnover after adjustment	[...]	[...]	[...]	[...]	[...]	[...]

Source: Competition Council calculation based on the Business Plan

**Table 18 Financial charges after adjustment according to the special accounting conditions<sup>12</sup>**

USD thousand	2003	2004	2005	2006	2007	2008
Turnover	[...]	[...]	[...]	[...]	[...]	[...]
Necessary surplus	[...]	[...]	[...]	[...]	[...]	[...]
Adjusted financial charges	[...]	[...]	[...]	[...]	[...]	[...]
% of turnover after adjustment	[...]	[...]	[...]	[...]	[...]	[...]

Source: Competition Council calculation based on the Business Plan

**Table 19 Income statement after adjustment regarding depreciation and financial charges (in current prices)<sup>12</sup>**

USD thousand	2002	2003	2004	2005	2006	2007	2008
<b>Turnover, of which:</b>	[...]	[...]	[...]	[...]	[...]	[...]	[...]
- Steel sales revenues	[...]	[...]	[...]	[...]	[...]	[...]	[...]
- Other sales revenues							
Variable costs	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Contribution, of which:</b>	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Fixed costs							
<b>Operating margin</b>	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Depreciation/ amortisation							

<sup>12</sup> Confidential data

<b>Profit/Operating Loss</b> Provisions & exceptional items Financial Revenue Financial charges	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Pre-tax profit</b> Tax	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Net Profit</b> Dividend (67%)	[...]	[...]	[...]	[...]	[...]	[...]	[...]
<b>Retained earnings</b>	[...]	[...]	[...]	[...]	[...]	[...]	[...]

*Source: Competition Council calculation based on the Business Plan*

- (97) After application of the special accounting conditions, the amount of steel sales revenues must be reduced every year by 1.25%.
- (98) Fixed costs, variable costs and depreciation are increased every year by 1.25%.
- (99) The forecast viability analysis after the reduction in revenues and the increase in costs and depreciation results in the following figures:

**Table 20 Income statement after adjustments regarding depreciation and financial charges, as well as the price/cost squeeze (in current prices)<sup>13</sup>**

<b>USD thousand</b>	<b>%</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>
<b>Turnover (of which):</b> - Steel sales revenues - Other sales revenues	- 1,25	[...]	[...]	[...]	[...]	[...]	[...]
Variable Costs	+ 1,25						
<b>Contribution</b> Fixed costs	+ 1,25	[...]	[...]	[...]	[...]	[...]	[...]
<b>Operating margin</b> Depreciation/amortisation	+ 1,25	[...]	[...]	[...]	[...]	[...]	[...]
<b>Profit/Operating Loss</b> Provisions & exceptional items Financial revenue Financial charges	+ 1,25	[...]	[...]	[...]	[...]	[...]	[...]
<b>Pre-tax profit</b> Tax		[...]	[...]	[...]	[...]	[...]	[...]
<b>Net Profit</b> Dividend (67%)		[...]	[...]	[...]	[...]	[...]	[...]
<b>Retained earnings</b>		[...]	[...]	[...]	[...]	[...]	[...]

*Source: Business Plan, Table 26*

<sup>13</sup> Confidential data



- (100) After application of the special accounting special conditions and the calculation of the price/cost squeeze, the two viability indicators can be determined as follows:

$V_1$  (gross operating margin) = (marginal costs)/ (steel sale revenue)

$V_2$  ( gross profit ratio) = (pre-tax profit + financial charges)/ (steel sale revenue)

**Table 21 EC Viability criteria**

%	2004	2005	2006	2007	2008	Target
$V_1$ (gross operating margin)	16.4	17.6	16.4	14.5	13.9	13.5
$V_2$ (gross profit ratio)	9.2	10.5	9.3	7.4	6.7	1.5

*Source: Business Plan, Table 25*

- (101) On the basis of these calculations, and without a detailed verification of the input data, the Competition Council concludes that throughout the period assessed (2004-2008) the undertaking forecasts to comply with the viability criteria laid down by the Commission.

## **VI.2.6 Value and Intensity of the Aid Limited to the Minimum Necessary**

### **VI.2.6.1 Minimum value of the aid**

- (102) According to Article 9 of Protocol 2, restructuring aid must be limited to the minimum necessary to enable restructuring to be undertaken in light of the company's existing financial resources.
- (103) As the balance sheets for the years 1998-2001 show, before it was privatised in March 2001 Sidex was practically insolvent and fulfilled the criteria for being declared bankrupt. On 30 June 2001 it had negative own assets (ROL -2,520,553 million or USD -86.7 million), mounting debts (ROL 35,471,366 million or USD 1,221 million) and no liquidity.
- (104) Given the company's disastrous financial situation, the only way to keep it on the market was to privatise it. However, it was clear that no private investor would acquire the company without the State's participation in its financial restructuring. In order to achieve the best possible purchase price, i.e. to privatise the company with as low a State contribution as possible, the Romanian Government carried out a transparent and open tender procedure. The privatisation project was announced in regional, national and international newspapers. Four different companies showed interest in participating by buying the tender documentation file. The initial deadline for the submission of final offers was extended once. However, finally only one potential investor (LNM) paid the participation guarantee to obtain access to the due diligence data room. AVAS confirms that LNM did not know it was the only interested party. Only LNM made an offer, which was published on 4 April 2001. Negotiations then took place between the

State and LNM and ended with the signature of the Privatisation Agreement on 27 July 2001 (for more details see Section 6 above). The sales procedure was similar to sales procedures previously approved by the Commission. All bidders had enough time and information to conduct due diligence in order to prepare their bids. A sale only on the basis of the offers in the tender would not have been possible, as the value of a company, unlike that of buildings, is not static. Negotiations therefore had to take place. As the best and only offer was accepted, the price paid by LNM should normally be considered as the market price, and thus the offer requiring the minimum of State aid necessary for the restructuring.

- (105) Competition Council has analyzed the unconditional nature of the tender procedure. According to Section 11.4.1(a) and (b) of the Privatisation Agreement, LNM is obliged to maintain the number of employees for a period of five years after privatisation (except for reductions in consequence of (early) retirements and others). Negotiations with LNM on this obligation were difficult. The requirement on an investor to maintain a certain number of employees has a direct impact on the minimum aid which potential bidders request in their offers. LNM's obligation to maintain a certain level of employment thus increased the amount of State Aid required beyond what was necessary to restore the company's viability.
- (106) Furthermore, even in cases where only the ECSC Treaty was applicable, and not Protocol 2, i.e. in cases where restructuring aid to steel companies was in principle excluded, the Commission has acknowledged that under specific circumstances exemptions from these strict rules must be made. The ECJ's case law has accepted this approach, holding that the Aid Codes represented a binding legal framework only for aid compatible with the ECSC Treaty and enumerated in it and, that the Commission has power to rely on Article 95 ECSC Treaty in order to adopt individual decisions. The Commission has taken decisions under this Article particularly to avoid a social crisis caused by massive unemployment:
- (107) Furthermore, all Aid Codes provided for exemptions from the ban on regional aid in favour of certain countries or regions (e.g. the Fifth Aid Code for Greece and East Germany).
- (108) In this context, the Competition Council observes that Sidex is located in a region eligible for derogation under Article 88(3)(a) EC concerning the economic development of areas where the standard of living is abnormally low or where there is serious underemployment. The Competition Council therefore concludes that under exceptional circumstances such as in this case, when the social stability of a whole region is in danger if restructuring is carried out without transition, an employment clause is a necessary and acceptable tool of restructuring aid, especially when the clause provides only for the temporary maintenance of a certain workforce - already considerably lower than before the restructuring - in order to facilitate a socially acceptable transition from a heavily overstaffed public company to a profitable market player.

- (109) Ispat-Sidex's steel mills are located in Galati, one of Romania's largest regions, with a population of 641,600 and an official unemployment rate (12.2%) which is much higher than the national average (8.2%). A total of 123,185 people in Galati have jobs, while 29,470 people are unemployed (although not all of them seem to be reflected in the official unemployment rate, which if all 29,470 people are taken into consideration is nearly 20%). The region depends heavily on Ispat-Sidex, which is by far its largest employer. Every reduction in Ispat-Sidex's workforce is likely to lead immediately and inevitably to a serious social crisis.
- (110) The fact that the Privatisation Agreement contained the employment clause does not mean that the aid was not limited to the minimum necessary to restructure the company in a socially acceptable way. As the employment clause, the only condition to which the Privatisation Agreement was finally subject, is entirely justified, the openness and transparency of the Tender Procedure leads to the presumption that the State aid granted in the Privatisation Agreement was limited to the minimum. In fact, no other international steel company was willing to take the risk of participation in Sidex's restructuring.
- (111) As in 2004, Sidex Ispat fulfil the EC viability criteria, the State aid was limited, as a consequence no aid will be paid or granted starting with 1<sup>st</sup> of January 2005.

#### **VI.2.6.2 Intensity of the aid**

- (112) The criterion of the intensity of the aid requires an examination of whether the minimum necessary aid is still too high, i.e. the State's participation is too large to be considered proportional and therefore cannot be justified, even if this means that the company concerned may not be restructured at all. In the EU a significant investor contribution is necessary, but this has not in the past been systematically required in the accession countries. Furthermore, even in the EU steel industry the company's contribution in the rare restructuring cases was generally minimal.
- (113) The intensity of the restructuring aid is 57.5% (USD 1,131.7 million/ USD 1,967.8 million). The Competition Council takes the view that in the special circumstances of this restructuring case, this is an appropriate level of State aid intensity.

#### **VI.2.7 No Undue Distortion of Competition – Compensatory Measures**

- (114) The compulsory limitation or reduction of the company's presence on the relevant market represents a compensatory measure in favour of its competitors. Compensatory measures should be in proportion to the distorting effects of the aid and, in particular, to the relative importance of the firm on its market or markets.
- (115) The Competition Council has assessed the closures and reductions of capacity undertaken by Sidex between 1993 and 2000, and concludes that their scale is such as to compensate for any negative effects arising from the granting of the aid. The closures between 1993 and 2000 should be taken into account, since

restructuring of Sidex was already taking place in this period. The company's weak financial situation in 2001 and the resulting need to find a strategic investor were mainly due to the long restructuring process which started in the early 90's. The capacity reductions as shown in Table 22 below demonstrate that the rationalisation and reduction in capacity of Sidex was considerable and appropriate, and therefore compensates for any distortion of competition.

## **VI.2.8 Progressive Reduction of the Aid**

(116) Table 21 demonstrates that the Restructuring State aid will be progressively reduced with a peak in 2004. The level of State aid in 2004 is due to the fact that the Profit Tax Relief will be paid for the first time in 2004.

**Table no. 21 The evolution of State aid**

<b>Restructuring aid 1993 – 2000</b>									
<b>Year</b>	<b>1993</b>	<b>1994</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>TOTAL</b>
State aid amount (million USD)	0	34.84	11.50	27.12	0	19.71	26.10	0	<b>119.3</b>
<b>Restructuring aid 2001 (million USD)</b>									<b>911.6</b>
<b>Restructuring aid 2002 – 2008</b>									
<b>Year</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	
State aid amount (million USD)	12.8	19.1	68.9	0	0	0	0	0	<b>100.8</b>

## **VI.2.9. Link to a rational national globalisation and capacity reduction programme**

(117) The restructuring must be part of a national restructuring programme for the whole steel sector which leads to rational globalisation and capacity reduction. In fact, the Ispat-Sidex restructuring is part of the overall restructuring of the Romanian steel sector which began in 1993 and will end in 2008. The European Commission has been provided with the “Strategy for Restructuring the Romanian Steel Industry for the period 2004-2008” (the “National Restructuring Programme” or “NRP”) of November 2004, a study completed by experts of the Romanian Ministry of Economy and Trade. On the basis of the restructuring measures already undertaken in the nineties, the Ministry has developed Romania's steel strategy for the next four years. The NRP was confirmed by the consultancy firm Roland Berger which assessed it on behalf of the Commission.

- (118) From 1990 Romania's steel production started to decline, due to the low domestic demand for metal. In 1993 the steel industry had a capacity of 17.4 million tons of steel per year. In 2003 capacity was about 9.4 million tons of steel per year.
- (119) At the end of the restructuring period, steel operational capacity in Romania will represent about 9.0 million tons per year, including 5.7 million tonnes at Ispat-Sidex. After the restructuring programme is completed, Romania's steel industry is expected to reach the technical-economical level of European performance.
- (120) The level of steel producing capacity at Sidex and/or Ispat-Sidex is as follows:

**Table 22 Evolution of Ispat-Sidex steel production capacity**

	Name of capacity/installation	Capacity closed (thousand tonnes/year)	Year/period	
			Closing	Break-up/Dismantling
1	Coke plant	- 2,050	1990-2000	1995-2005
2	Sintering installations		1994 -2000	1995 -2005
3	Furnace	- 3,300	1994- 2000	1995 -2005
4	Steelmaking electric converting	- 260 -3,000	1998 1993-2000	2005 2005 - 2006
5	Rolling mill - slabbing - long semi-finished	- 3,600 - 600	1993 2000	1995 -2005 2005
	<b>Totals</b>			
	• <b>coke plant</b>	<b>- 2,050</b>		
	• <b>furnace</b>	<b>- 3,300</b>		
	• <b>steelmaking</b>	<b>- 3,260</b>		
	• <b>rolling (incl. semi- finished)</b>	<b>- 4,200</b>		

*Source: Annex to the Strategy for Restructuring the Romanian Steel Industry for the period 2004 – 2008*

- (121) The Competition Council takes the view that the closures and reductions of capacity undertaken by Sidex between 1993 and 2000 represent a substantial and important part of overall capacity reductions in the framework of the restructuring of the Romanian steel industry.

### **VI.3. Annual monitoring and reporting**

- (122) According to article 17 of the Regulation on State aid for rescuing and restructuring firms in difficulty, the Competition Council continuously monitors the implementation manner of the Restructuring Plan, so that it would not divagate from the accomplishment of the Restructuring Plan's objectives. Any modification of the Restructuring Plan or of the State aid's quantum must be notified, for re-assessing the granting conditions for the State aid.
- (123) The implementation modalities of the Restructuring Plan will be closely monitored by the Competition Council in order to ensure that there will be no increases of

the production capacities, major deviations from the restructuring measures and the State aid would not lead to the creation of supplementary liquidities that could be used for other activities than those provided by the Restructuring Programme.

## **VIII. Conclusions**

(124) Taking into account the above presented, the Competition Council concludes the following:

1) The financial measures taken by the Romanian authorities by GEO no. 123/2004 for modifying and completing the Law no 571/2004 on the Fiscal Code and by GEO no. 134/2004 for modifying and completing GEO no. 119/2001, in order to restructure Sidex Ispat, constitute aid in accordance with the Law no. 143/1999 on State aid, with the subsequent amendments and completions.

2) The financial measures taken by GEO no. 40/2002 for the recovery of budgetary arrears does not constitute aid.

2) The State aid granted for Sidex Ispat, as modified by GEO no. 134/2004 and GEO no. 123/2004 meet the authorization criteria established in the Protocol 2 regarding the CECO products, Annex to the European Agreement establishing an association between Romania, on one hand, and the European Communities and their Member States, on the other hand, so they are compatible with the normal competitive environment.

## **DECIDES**

**Art. 1.** According to paragraph (1) and (2) of Article 12 of Law No. 143/1999 on the State Aid, with the subsequent modifications and completions, authorizes the modification of the State aid authorized by the Competition Council by Decision no. 99/2002, granted to SC Ispat Sidex SA Galati. Also, by this decision it is authorized the State aid granted to SC Ispat Sidex SA Galati during the period 1993-1999, in amount of ROL 740,022 million (USD 119.2 million).

**Art. 2.** The total amount of State aid authorized by this decision in benefit of SC Ispat Sidex SA Galati during the period 1993-2008 is of ROL 30,597,716 million (USD 1,131.7 million).

**Art. 3.** According to paragraph (2) (a) of Article 12 of Law No. 143/1999 on the State Aid, with the subsequent modifications and completions, concludes that the financial measures taken by GEO no. 40/2002 for the recovery of budgetary arrears does not represent state aid.

**Art. 4.** This Decision shall be applicable as of the date it is communicated.

**Art. 5.** According to the provisions of Article 29 of Law No. 143/1999 on the State aid, as amended, this Decision may be challenged by the interested parties at the Court of Appeal Bucharest, Administrative Litigation Section, within thirty days of the date of its communication.

**Art. 6.** This Decision shall be notified by the Secretariat General of the Competition Council to:

- Authority for State Assets Recovery, str. Cpt. Av. Alexandru Serbanescu, nr. 50 sector 1;
- S SC ISPAT SIDEX SA, Str Smardan, nr. 1, Galati.

**Art. 7.** The General Secretariate and the Direction for State aid Authorization will follow the enforcement of this decision.

**PRESIDENT**

**MIHAI BERINDE**