COMMISSION OF THE EUROPEAN COMMUNITIES

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RESTRUCTURING OF THE ITALIAN PUBLIC STEEL INDUSTRY

COMMUNICATION OF THE COMMISSION TO THE COUNCIL

Commission communication to the Council

Re: Italy - Implementation of plan to restructure the public steel industry
Italian request for an extension of the restructuring completion date

Ref.: Commission Decisions Nos 89/218/ECSC of 23 December 1988 and 90/89/ECSC of 13 December 1989

I. Introduction

1. Having consulted the Consultative Committee and with the unanimous assent of the Council, the Commission adopted Decision No 89/218/ECSC on 23 December 1988 (OJ No L 86/76, 31.3.1989) authorizing the Italian Government to grant the public steel industry aid totalling LIT 5 170 billion. Articles 2 to 7 of the Decision specified the conditions governing the authorization and the terms on which aid could be granted.

   In response to a request made on 23 March 1989 by the Italian Government, the Commission adopted Decision No 90/89/ECSC of 13 December 1989 (OJ No L 61, 10.3.1990) which amended the preceding decision, in particular as regards the postponing of certain deadlines for closures and transfers of assets.

2. The main purpose of the aid in question was to achieve the financial restructuring of the public steel industry by covering part of the debts incurred by Finsider, which was in voluntary liquidation,

as part of the restructuring plan set up by the Italian Government in 1988.

With the assistance of independent experts, the Commission had examined the plan from the point of view of its ability to ensure the future viability of Ilva.

It concluded that, if the plan were rigorously adhered to, Ilva would have a reasonable chance of attaining viability by the end of 1990 under normal market conditions.

The plan was to be carried out between 1988 and the end of 1990, following the timetable provided for in the above-mentioned Decisions.

3. To enable the Commission to check that the restructering measures provided for in the plan were carried out in accordance with the timetable, Article 5(2) of Decision No 89/218/ECSC required the Italian Government to supply six-monthly reports containing details of the progress that the aid recipient had made towards viability under the restructuring plan.

On the basis of Article 8(3), the Commission also required a monitoring system to be set up through an independent consultant in order to supervise the strict implementation of the restructuring plan.

The reports received to date relate to the periods 1.1.1989-30.6.1989, the first three quarters of 1989, first quarter 1990, first half 1990 and the third quarter of 1990. Only the report for the fourth quarter of 1990 is missing.

The Italian Government also informed the Commission in a series of letters of various measures taken to comply with other conditions laid down in the above-mentioned Decisions.

4. In view of the fact that the deadline for completion of the restructuring plan and for payment of the relevant aids expired on 31 December 1990, it is now necessary to take stock and, in particular, to verify that the conditions set out in the above-mentioned Decisions have been complied with.

II. Situation at 31 December 1990 with regard to restructuring of the Italian public steel industry

1. Creation of Ilva

1.1. On 31 December 1988, Ilva received most of the viable assets totalling LIT 6 766 billion and some of the debts amounting to LIT 3 123.5 billion from Finsider, Italsider, Nuova Italsider and Terni Acciai Speciali, all of which were in voluntary liquidation.

The following plants were part of this first transfer:

- ordinary steel flat products: the Taranto, Cornigliano, Novi Ligure and Marghera plants;
- long products: the Piombino and Condove plants;
- stainless steel flat products: the Terni and Turin plants.

On 31 March 1990, Ilva received a second transfer of assets totalling LIT 240 billion, which included the Bagnoli and Turin plants owned by Italsider in liquidation.

In view of the fact that Article 4 required Finsider's assets and liabilities to be transferred to Ilva by 31 March 1989 at the latest, the Italian Government has essentially complied with this requirement, since all the assets to be closed down or sold to private companies were not included in the transfer to Ilva.

When, however, in response to a request from the Italian Government the Commission decided to postpone the closure dates for Sesto San Giovanni to 30 September 1990, and for Bagnoli and Turin to 31 December 1990, it was considered advisable to transfer those assets immediately to Ilva, particularly as the amount involved, LIT 240 billion, was relatively small compared with the initial transfer.

1.2. The amount of the liabilities to be transferred from Finsider to Ilva was to be such that the total net financial charges borne by the latter during the restructuring period, ending on 31 December 1990, would be brought to 5.5% of the company's turnover.

In 1989, the net financial charges borne by Ilva amounted to 5.9% of turnover, despite an exceptional turnover of LIT 10 556 billion.

In 1990, net financial charges remained at 5.9% of turnover.

Thus the amount of the debts transferred from Finsider in liquidation to Ilva was sufficient to bring the financial charges borne by the latter during the restructuring period to a level in excess of the requisite minimum of 5.5%.

2. Plant closures

Under Article 2 of Decision No 89/218/ECSC, the following plants were to be definitively closed:

(in thousand tonnes)

	Pig iron	Steel	Finished products hot-rolled	Finished products cold-rolled
Bagnoli	2 350	2 700		
Campi (heavy plate)		350	400	
Turin (merchant bar, wire rod)		375	250	
Terni (concrete reinforcing bar)			300	
Sesto S. Giovanni (merchant bar, wire rod)			230	
Turin				708
Total	2 350	3 425	1 180	708

With the exception of the closure of the cold-rolling mill at Turin, the other plants referred to above were closed on the appropriate dates. More specifically, the Campi, Turin (merchant bar, wire rod), and Terni plants were closed by 31 March 1989, the closure of Sesto S. Giovanni being completed by 30 September 1989.

As regards the liquid phase at Bagnoli, the closure took place three months before the deadline of 31 December 1990.

It can therefore be concluded that the Italian authorities complied with their obligation to close definitively all the plants referred to in the two Decisions within the periods stipulated, with the exception of the Turin cold-rolling mill.

3. Sales to the private sector

Pursuant to Article 3 of Decision No 89/218/ECSC, the folliwng plants were to be sold to the private sector:

(in thousand tonnes)

	Pig iron	Steel	Finished products: hot-rolled	Finished products: cold-rolled
Marghera (heavy and light sections)			130	
S. Giovanni Valdarno (light sections)			150	
Sisma (heavy and light sections, wire rod)		240	230	
Trieste	590			
Lovere		145		
Total	590	385	510	

All the above plants were to be sold by 31 March 1989, with the exception of the Lovere plant which was to be sold by 31 December 1989.

Having opted to sell the plants by public invitation to tender and having selected the most financially advantageous offer, the Italian authorities transferred the plants described above to the following enterprises:

Plant	Purchaser
Marghera	Sidermarghera SpA
San Giovanni Valdarno	Ferriera del Valdarno Srl
Sisma	Leali Luigi SpA
Trieste	Altoforni e Ferriere di Servola SpA
Lovere	Fin. Lo SpA

The steel plant in Aosta referred to in Article 3(3) of Decision No 89/218/ECSC was finally integrated on 31 July 1989 into Ilva following the introduction of a specific restructuring plan regarded as likely to restore its viability.

As part of that integration, Nuova Deltasider SpA in liquidation transferred the assets of Deltacogne SpA and liabilities including debts of LIT 316 billion to Ilva.

The price paid by Ilva, based on an independent appraisal, was LIT 4 billion.

The Italian authorities have thus essentially complied with the conditions of Article 3 of Decision No 89/218/ECSC, as amended by Decision No 90/89/ECSC.

4. <u>The financial results of the restructuring</u>

4.1. In assessing the viability of the plan to restructure the Italian public steel industry, the Commission used the same criteria as those it imposed during the earlier restructuring of the Community steel industry.

According to those criteria, an enterprise may be deemed viable when its gross operating profits are equal to at least 12.5% of turnover. This is regarded as the minimum needed to allow an enterprise to make adequate provision for depreciation, financial charges and a minimum return on own capital.

In the present case, the restructuring plan was intended to restore viability in the Italian public steel industry by achieving a gross operating profit at the end of the plan of 12.9%, starting from a gross operating profit of 2.4% in 1987, on the basis of an estimated fall in production costs and sales prices of 2.5% per annum (price-cost squeeze).

This result would be achieved as follows:

- 22% through closures and the cessation of certain activities;
- 10% through the combined modification of volume and product mix;
- 68% by improving internal management; in practice, over half the improvement was achieved by reducing the workforce.

4.2. In practice, the following results were obtained:

	Billion LIT	
	1989 (a)	1990 (b)
Gross operating profits according to the plan	727.6	886.8
Actual results in relation to plan:		
- cost-price squeeze	715.2	24.0
- volume/product mix	7.9	(211.0)
- employment costs	36.0	153.7
- production process	(28.2)	51.0
- general expenditure	20.5	19.0
Real gross operating profits	1 479.1	1 010.5
Real gross operating profits in relation to turnover	15.9%	11.8%

NB: (a) not including results of Deltacogne
(b) provisional results.

The clearly positive result of the cost-price squeeze compared with forecasts is explained by the exceptional market conditions enjoyed by the Community steel industry in 1988 and 1989. These conditions, however, gradually deteriorated in 1990, with a fall in prices in the last quarter of 1990. It should be noted that because of the overall results for 1990, Ilva fell just short of the gross operating profits forecast.

In addition, the estimated 9% cut in employment was exceeded, enabling the company greatly to improve its productivity, particularly in 1990.

On the other hand, investment delays prevented the company from achieving the results anticipated, although much of the lost ground has been made up since the start of 1990.

In short, it would seem that the application of the restructuring plan has allowed the Italian public steel industry to produce sufficiently good results to restore financial equilibrium, although it has not achieved a gross operating profit of 12.9% of turnover.

That is why the company should continue to improve performance in order to close the considerable gap between its production costs, especially at Taranto, and those of its most efficient Community competitors.

5. <u>Aid granted to the Italian public steel industry</u>

Under Article 1 of Decision No 89/218/ECSC, the maximum amounts of aid to be granted to the public steel industry were broken down as follows:

(a) Aid for financial restructuring and other operating aid:
   - redemption of up to a maximum of LIT 4 432 billion of Finsider's debts;
   - coverage of losses up to a maximum of LIT 245 billion deriving from the continued provisional operating of the ECSC installations of Finsider to be closed down or sold off;

- a contingency appropriation of maximum LIT 288 billion to cover the risk that proceeds from the realization of Finsider's assets did not reach the LIT 1 500 billion forecast;

(b) Closure aid:

- coverage of expenditure incurred by the closure of steel plants up to a maximum of LIT 205 billion.

By Decision of 10 April 1990, the Commission authorized the Italian Government to grant a first instalment of aid totalling LIT 2 989 billion (or two-thirds of the maximum amount approved) for the partial redemption of Finsider's debts.

As the Italian Government did not request the release of any further aid instalments before the deadline of 31 December 1990, the amount of aid paid was limited to that first instalment.

It should also be noted that, pursuant to Article 6(2) of Decision No 89/218/ECSC, the Commission released the aid after being satisfied of the fulfilment of the conditions provided for in Decisions Nos 89/218/ECSC and 90/89/ECSC.

In the case in point, however, the cold-rolling plant at Turin was not closed down. Thus even if the Italian authorities had applied for the release of a second instalment of aid in good time, the Commission would have been obliged to reject it.

6. Conclusions:

It emerges from the foregoing that:

- the restructuring plan was for the most part carried out within the time limits set;

- the financial results achieved by the Ilva Group indicate a return to viability by the Italian steel industry which should, however, continue its efforts to reduce production costs in relation to other Community competitors;

- it must be concluded that the Italian Government has not fulfilled all the requirements of Decisions Nos 89/218/ECSC and 90/89/ECSC as the Turin cold-rolling mill was not closed by the date stipulated;

- aid granted within the time allowed totalled two-thirds of the maximum amount.

III. New request made by the Italian authorities on 12 March 1991 for a six-month extension to the deadline for implementation of Decisions Nos 89/218/ECSC and 90/89/ECSC

1. By letter dated 28 December 1990 from the Ministry for State Holdings, forwarded by the Italian Permanent Representative's Office on 7 January 1991, the Italian authorities informed the Commission that they planned shortly to apply for authorization to replace the closure of the Turin cold-rolling mill with equivalent reductions in capacity, and for the release of a second aid instalment pursuant to Decision No 89/218/ECSC.

Then by letter dated 12 March 1991 from the Italian Permanent Representative, received on 15 March 1991, the Italian authorities asked the Commission on the one hand to release a second and last instalment of aid amounting to LIT 2 188 billion and on the other to authorize the replacement of the closure of the Turin cold-rolling plant (MPP 708 Kt/year) by the closure of the Cornigliano No 1 cold-rolling mill (MPP 600 Kt/year) and a capacity reduction of 108 Kt/year at Racconigi, both of which would be effected by 30 June 1991.

In support of their request, the Italian authorities pointed out that:

- despite the inevitable delays due to the authorization procedure, the objectives of the restructuring plan had been fully complied with in accordance with the ECSC decision;

- the new compnay Ilva had achieved in 1989-90 the financial and management results predicted, as confirmed by the consultant responsible for the quarterly analyses;

- on the basis of a balance sheet not yet approved by the company's bodies, gross financial charges in relation to turnover amount to 6.6%; consequently, the minimum percentage of 5.5% imposed by the Community decision has been fully reached, as have the objectives relating to adjustments in employment levels;

- the replacement of the proposed closures will produce a significant improvement in management efficiency, which is fully in line with the Community decisions on the plan to restructure the public steel industry.

2. Aid concerned by the release request

2.1. The Italian authorities estimate that LIT 4 493 billion in aid is required to redeem Finsider's debts equivalent to the loss in value of the transfer to Ilva.

The losses in value in question may be broken down as follows:

	(in billion LIT)
Value-loss linked to first transfer	2 649
Value-loss in mining holdings	113
Value-loss in Cogea holdings	286
Value-loss linked to the second transfer	930
Finsider's net financial charges in 1988-89	1 177
Operating results 1988-89 (excluding plant to be closed or sold)	(650)
TOTAL	4 493

2.2. As regards the aid needed to cover losses resulting from the provisional operation of Finsider's ECSC activities to be closed or sold, the Italian authorities estimate the amount at LIT 222 billion.

The breakdown of losses by year, in billion Lire, is as follows:

	1988	1989
plants to be closed	-157.3	-88.8
plants to be sold	+8.1	+16.0
	-149.2	-72.8

The 1990 results of the few remaining plants not yet closed down, namely the liquid phase at Bagnoli and the Turin cold-rolling mill, were included in Ilva's results and therefore did not form part of the results of Finsider in liquidation.

2.3. As regards the aid intended to offset the losses incurred through the realization of Finsider's assets, the Italian authorities have fixed the amount required at LIT 264 billion.

According to the Italian authorities, the losses in question may be broken down as follows:

	(in billion LIT)
- Losses resulting from the transfers of the Marghera, S. Giovanni Valdarno and Trieste plants	83
- Value-loss in respect of amounts owed by ATB in liquidation	11
- Loss of value resulting from the transfers of Deltacogne	170
	264

2.4. As regards closure aid, the Italian authorities estimate that LIT 198 billion will be required, broken down as follows:

Plant	(in billion LIT)
Turin (merchant bars, wire rod)	38.3
Campi	131.0
Terni (concrete reinforcing bars)	3.1
Sesto S. Giovanni	25.6
	198.0

3. As regards the plant closures in question, the Italian authorities have requested that the reduction in MPP of cold-rolled products provided for in the plan (-708 000 tonnes a year by closing the Turin plants) be achieved by dismantling mill No 1 at Cornigliano (MPP of 600 Kt/year) and technically reducing production by 108 Kt a year at ITA's cold-roling mill in Racconigi, or through a 108 Kt/year reduction in the MPP of the Taranto annealing furnaces.

In support of this request, the Italian authorities point out that:

- maintaining production at the Turin plant increases the economic viability of the plan to restructure public steel undertakings. On the one hand, improved efficiency in the Turin installations in recent years produced a LIT 51/kg reduction in processing costs, due both to an increase in productivity (-342 workers) and to a reduction in energy consumption, improved yields, etc. On the other hand, the impact of a production of 708 Kt/year of cold-rolled steel on Ilva's gross operating profits would, if

Turin were closed, be LIT 79.8 billion a year or LIT 109.4 billion if Cornigliano were closed down and Racconigi's production reduced. Thus the proposed substitution would allow Ilva to increase its gross operating profits by LIT 29.6 billion.

- Conditions in the Italian steel market are very different now from what they were in 1987 when the steel restructuring plan was introduced.

  The fact that other facilities have been sited near the Turin plant in order to supply the motor vehicles branch (electrogalvanizing line) is evidence that the new market situation has encouraged Ilva, in particular at the request of Fiat, to develop Turin as a centre for the production of rolled products for vehicles, which has as a result acquired considerable importance as a supply source for the industry downstream.

  Fiat for its part has expressed satisfaction with the service provided until now by Ilva and concern about the closure of the plant, a concern it has already expressed in the past.

  Under the CIPE/CIPE plan, production was to have been transferred to Novi Ligure once the new continuous annealing furnace had entered into service; this, however, will not be possible until mid-1992.

The closure of the Turin mill on 31 December 1990 would have entailed distributing its production among the other available Ilva plants, i.e. Novi Ligure, Taranto and the cold-rolling mill at Cornigliano, DR1/1. This would make supplies to Fiat difficult, especially the "just-in-time" supplies it requires, and would damage its efficiency.

From Ilva's standpoint, the closure would have seriously jeopardized the confidence placed in it by its major customer in Italy, with the inevitable financial consequences. The closure of the Turin cold-rolling mill does indeed seem to be critical, both as regards Ilva which could experience severe difficulties with supplies to its traditional customers and as regards the Italian car industry and its related sectors.

It should also be noted that the continuation of cold-rolling activities is encountering serious environmental difficulties.

4. Assessment

4.1. Essentially, the Italian request is for a six-month extension to 30 June 1991 of the deadline for implementation of Decisions Nos 89/218/ECSC and 90/89/ECSC. It is also proposed to replace the closure referred to in Article 2 of Decision No 89/218/ECSC of the Turin cold-rolling mill by the closure of mill No 1 at Cornigliano and a capacity reduction at Racconigi, both of which produce the same types of cold-rolled product as Turin.

Secondly, the request for the release of the second instalment of aid concerns aid authorized in Decision No 89/218/ECSC and not the granting of fresh aid; it is in fact simply a question of extending the 31 December 1990 deadline provided for in the above-mentioned Decisions.

Because, however, the deadlines in both Decisions for the closure of the Turin installations and for requests for a second instalment of aid expired on 31 December 1990, the Italian request dated 12 March 1991 is not admissible under the said Decisions.

As a result, the Italian request must be dealt with by the procedure provided for in Article 95 of the ECSC Treaty, bearing in mind that the request essentially concerns an extension of the deadline for implementation of the Decisions.

4.2. The Italian authorities have requested that sufficient aid be released to redeem its debts of LIT 4 493 billion.

Article 1(a) of Decision No 89/218/ECSC provides, however, for the redemption of a maximum of LIT 4 432 billion of debts.

Consequently, the aid released should be limited to LIT 4 432 billion.

As the Commission has already released a first instalment of LIT 2 989 billion, the balance to be released for debt redemption amounts to LIT 1 443 billion.

4.3. As regards the aid to cover losses stemming from the temporary operation of plants to be closed down or sold, it would seem that the Italian request for the release of aid totalling LIT 222 billion satisfies the tests of the above-mentioned Decisions as it relates to losses stemming from the provisional operation of Finsider's ECSC activities due to be sold or closed down.

It should be noted that as a result of extending the deadline for the closure of the Bagnoli and Turin plants from 30 June 1989 and 31 March respectively, to 31 December 1990, losses were reduced as the plants concerned achieved gross operating profits in 1988 and 1989.

4.4. With regard to the aid to cover losses arising from the transfer of Finsider's assets, it seems that the LIT 83 billion to cover losses due to the sale of the Marghera, S. Giovanni Valdarno and Trieste plants satisfies the tests of Decision No 89/218/ECSC and may therefore be released.

On the other hand, the LIT 11 billion to cover the loss in value of amounts owed by the non-ECSC enterprise ATB cannot be regarded as aid to cover losses stemming from the realization of Finsider's assets because there is no loss of value in assets and ATB was not sold.

The same is true of the LIT 170 billion relating to the Aosta plant since, instead of selling it, Finsider in liquidation made use of the possibility afforded by Article 3(3) of Decision No 89/218/ECSC to integrate it into Ilva.

Apart from the non-ECSC nature of ATB, it would seem that the two value-losses concerning ATB and Aosta could have been eligible for aid to redeem Finsider's debts pursuant to the first indent of Article 1(a) of Decision No 89/218/ECSC.

But the LIT 432 billion ceiling has already been exceeded (see point 4.2 above) in the Italian request, so that even on that basis, aid for ATB and Deltacogne could not be released.

4.5. The closure aid of LIT 198 billion could be released since it is below the ceiling and corresponds to expenditure relating to plant closures provided for in Decision No 89/218/ECSC, with the exception of the Turin cold-rolling mill.

4.5. In short, the release of the second and last instalment could relate to:

	Requested by Italy	Ceiling	Commission proposal
Aid to redeem debts	4 493	4 432	4 432
Aid to cover losses	222	245	222
Aid to cover losses resulting from the realization of assets	264	288	83
Closure aid	198	205	198
	5 177	5 170	4 934
Aid already released	2 989		2 989
Second instalment	2 188		1 945

The amount to be released as a second and last instalment would thus be LIT 1 945 billion.

The aid should not be paid, however, until the closure of the Cornigliano No 1 mill has been verified. As the closure deadline is 30 June 1991, it would be desirable to fix 31 August 1991 as the deadline for payment of the second and last instalment to give the Commission time to check that the conditions have been fulfilled.

5. With regard to the Italian request that closure of the Turin cold-rolling mill be replaced by closure of mill No 1 at Cornigliano and capacity reductions at Racconigi, it should be borne in mind that:

- the Turin cold-rolling mill was not one of the key closures in the restructuring plan. When the Commission called for closures to offset aid, it concentrated more on reductions in hot-rolling capacity or, as in the said plan, on the closure of the liquid phase at Bagnoli, than on reductions in cold-rolling capacity.

  It should also be noted that all the other closures took place within the period stipulated and even, in the case of Bagnoli, three months in advance:

- as the capacity reduction proposed by the Italian authorities concerns the same type of products and involves the same quantities, it would contribute as much to the structural reorganization of the Community steel industry as the closure of Turin;

- despite the forecasts of the restructuring plan, the Turin plant will in future be viable. In addition, the closure of Turin would lead to a fall in Ilva's gross operating results compared to the results obtained by maintaining Turin in operation and making reductions elsewhere.

To ensure that an equivalent industrial result is obtained, however, the capacity reduction at Racconigi should be both verifiable by the Commission and irreversible, so that the reduction can be considered equivalent to a closure.

At the beginning of April, the Commission checked on the spot that the necessary modifications to reduce cold-rolling production capacity by some 100 Kt/year at Racconigi had been completed. It was noted that an open cooling system for the motors of the cold-rolling mill had replaced the closed system used before.

A closed circuit, however, can be reinstalled for approximately ECU 100 000. There would thus be no major economic barrier to increasing production capacity in the mill in question.

The Italian authorities should therefore be asked to give the Commission an undertaking that the capacity reduction in the cold-rolling plant will be permanent. They should also be asked to notify the Commission in advance of any modifications to the mill to enable the Commission to check that capacities have not been increased.

IV. Proposal

In view of the foregoing, and on the basis of Article 95 of the ECSC Treaty, the Commission requests the Council, after consulting the ECSC Consultative Committee, to give its unanimous assent to the Commission's proposal to adopt a decision amending its Decisions of 23 December 1988 (89/218/ECSC) and 13 December 1989 (90/89/ECSC) concerning aid which the Italian Government plans to grant to the public steel industry and authorizing:

- the replacement of the definitive closure referred to in the table in Article 2(1) of the Turin production of 708 000 tonnes of cold-rolled product by the closure of mill No 1 at Cornigliano producing 600 Kt/year of cold-rolled product and a definitive reduction of 108 Kt/year in the capacity of the Racconigi cold-rolling mill;

- the extension of the deadline provided for in Article 2(3) for the closure of mill No 1 in Cornigliano and the capacity reduction at the Racconigi mill to 30 June 1991;

- an eight-month extension to 31 August 1991 of the original deadline of 31 December 1990 for the granting of aid provided for in Article 6(5).