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## COMMISSION POLICY ON SECTORAL AID SCHEMES

( Communication from the Commission to the Council )

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### SUMMARY

The Danish Presidency has requested a statement on Commission policy on sectoral aid schemes as a basis for an exchange of views on this subject between Council and Commission.

The attached memorandum underlines the Commission's institutional responsibility in this field. It outlines the Treaty policy on competition, its development and relevance to current economic problems, particularly in view of social pressures, capacity problems and the danger of protectionism. It explains the Commission policy and methods, emphasizing the flexibility of approach, but stressing the Community aspects, the need to obtain positive results, particularly viable economic structures, and to overcome the danger of preserving the status quo or transferring difficulties from one Member State to another. It discusses the relevance of Community frameworks on aid for whole industries and the principles involved in handling individual cases. The memorandum concludes by stressing the continuing consultation that takes place on state aid policy between the Commission, the Parliament and Member States.

Subject: Commission policy on Sectoral Aid Schemes

### Introduction

1. The Commission has been requested by the current President of the Council to prepare a statement on its policy on sectoral aid schemes to facilitate an exchange of views on this subject between the Council and the Commission. In submitting this statement the Commission would underline that in the field of decisions on the compatibility of State aids with the Common Market the Treaty places responsibility on the Commission.
2. This exchange of views is particularly welcome in the light of current circumstances. The economic crisis, with the resultant high levels of unemployment and slow growth, could lead to the danger of a drift towards protectionism, both internally within the Common Market through the growth in number and intensity of State aids, as well as externally. While State aids have a role to play in securing an orderly adjustment to new economic structures viable on a world-wide basis in the longer-term, their use to preserve the status quo will serve only to hinder the adjustments to Community industries that are necessary to secure the economic and social future of the Community.

### General Principles

3. The Treaty lays down the basic principle of the incompatibility of State aids with the Common Market (Article 92(1) EEC), implementing Article 3(f) of the EEC Treaty, which provides for the institution of a system ensuring that competition in the Common Market is not distorted. It also provides for derogations in favour of certain categories of aid (Article 92(2) and (3) EEC) and places responsibility for the management of the application of these derogations on the Commission.

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3.1. There are three undeniable reasons for adhering to this system:

- the customs union would be quite useless and would collapse if Member States could invalidate it by granting aids;
- the Common Market makes little sense unless businesses tackle the market on the strength of their own resources without any aid to distort competition between them, except where such aid is clearly justified in the general interest of the Community;
- lastly, and as a corollary, a system which leaves the field open for competition and does not allow aids to interfere with the optimum distribution of production factors is essential to economic and social progress.

3.2. This does not, however, mean that a restrictive attitude must be adopted towards aids designed to remedy situations in which market conditions:

- obstruct progress towards certain economic and social objectives;
- or permit these objectives to be achieved only within unacceptable time limits or with unacceptable social repercussions;
- or intensify competition to such an extent that it risks destroying itself.

The Commission considers that aid should be authorized when it is needed to correct serious regional imbalances, to encourage or speed up necessary changes or developments in certain industries, to enable for social reasons a smooth adjustment of certain activities or to neutralize, at least temporarily, the distortion of competition due to action outside the Community.

The objectives, forms, and conditions of such aids, whose justification is that they facilitate the orderly development of Community structures, do not conflict with the general objectives quoted in 3.1. above. It therefore follows that such aid must not be given if the need for it

is not clearly established, or merely to preserve the status quo, nor has an excessively destructive effect on competition, or transfers difficulties unduly from one Member State to another.

The new context

4. The granting of State aids has assumed increasing importance as a result of the industrial difficulties and particularly the growing unemployment that have resulted from the recession. Structural problems were developing in all Member States prior to the current economic crisis. However, the results of the increase in petroleum prices, the persistence of inflation, the instability of exchange rates, and the growth of export-orientated industries in developing countries have accentuated the need for structural adaptation of economies. All the Member States find themselves in a position of transition, characterized by the need to adapt their industries to the consequences of these changes.

The European Council, conscious of this situation, at its meeting in Copenhagen on 7/8 April 1978 underlined the need to re-establish the competitiveness of industries in difficulties and stated that this remained the chief object for the policy of Member States in this field. In this context the European Council emphasized the need to overcome the grave problems posed by structural overcapacity in many industries and the need to promote an industrial structure which could face up to world-wide competition.

5. The application of the State aid rules of the Treaty has presented particular problems to the Commission during the past few years. These problems arose as a result of the general economic pressures indicated above.
  - 5.1. During the period 1975-76 it was not clear whether the problems were essentially of a short-term conjunctural nature, which would be resolved by a natural recovery in the economy, or whether the problems were of a more deep-seated structural nature. Bearing in mind also the strong social pressures which were prevalent in most Member States to preserve existing structures as a way of fighting rising unemployment, there was a tendency to introduce measures of aid as a short-term palliative in the hope that the basic situation would correct itself fairly rapidly.

- 5.2. It has been increasingly recognized that the economic problems of Member States are of a basic structural nature and that this structural problem is the one that requires to be tackled if economic recovery is to take place and a new phase of social and economic progress is to be initiated. This objective cannot be obtained by indirect protectionism brought about through the use of State aids which have the effect of impeding the exploitation of the economic opportunities that exist in the changing world economy and which could undermine the cohesion of the Community's economy which is a pre-condition for further progress.
- 5.3. In this context it should be noted also that control of State aids within the Community is the result of certain international obligations (Article XVI of GATT). Moreover, in the current multilateral trade negotiations (MTN) certain of our partners are pressing for a strengthening of such control as a quid pro quo for alignment of its legislation on countervailing duties with the GATT rules.
- 5.4. As far as aids in EFTA countries are concerned, the Commission is well aware of the problems of competition involved in some cases, especially as regards Scandinavian countries. This general problem is currently under discussion with the Member States. As long as these discussions are under way, the Commission does not consider it appropriate to take a decision of principle. However, if there were specific complaints the Commission would examine these on a case-by-case basis according to the relevant dispositions of the existing free-trade agreements concluded with these EFTA countries.

#### General applications

6. The Treaty rules are not a static instrument but give the Commission a flexibility to accept the realities of the situation at both Community and Member State level. Given conditions of the past few years, a certain multiplication of sectoral aids, particularly in the Member States with economic structures less well adapted to the new situation in the world economy is seen as an inevitable reaction to the pressure to which their economies are subject, bearing in mind particularly the social pressures created by limited growth and rising unemployment.
7. In determining its position on individual aid proposals the Commission has developed a number of basic criteria:
  - 7.1. In the context of changing economic and social situations to ensure that the Community dimension is taken into account within the actions of Member States; in particular that action is taken only where there is real need, that that action will lead to a restoration of long-term viability and that

all these actions will give added efficacy to the economic, social and regional policies of the Community. State aids should seek to solve long-term problems and not to preserve the status quo or put off decisions and changes which are inevitable. In balancing the Community and national interests, the Commission endeavours to ensure that industrial problems and unemployment are not transferred from one Member State to another.

- 7.2. The Commission accepts that the need to adapt structures should be qualified by taking into account the short-term social costs involved. Time is necessary for adjustment. While State aids should not be used simply to preserve existing structures limited use of resources to ameliorate the social and economic costs of change, for example in the form of rescue operations or even controlled operating aids for a strictly limited period (crisis measures), can be accepted.
- 7.3. The intensity of aid given should be proportionate to the problem it is sought to resolve. In this respect problems, whether regional or industrial, should be overcome with a minimum disturbance to competition and respect for the difficulties which have to be solved in each Member State.
- 7.4. Moreover, the Commission is also concerned to ensure that proposed aid measures should be degressive (e.g. in the rate and/or amount of aid); limited in time; and clearly linked to objectives for restructuring of the sector concerned.
8. The principles of competition laid down in the Treaty limit the initiatives that the Commission can take in the field of State aids and determine the role of the Commission in handling cases of State aid, which is principally to react to the initiatives envisaged by Member States.

Therefore, the principal method of operation of the Commission is a case-by-case examination of proposals from Member States to grant aid. Such proposals, if their economic impact can be judged in advance, are considered in the light of the provisions of the Treaty and in particular the derogations of Article 92(3) EEC Treaty. If, as is the case in most general aid schemes, it is not possible initially to judge the effect of an aid proposal, the Commission will review the individual cases of application of the aid in question in the light of the general principles outlined above. This examination will include the application of the principles defined in any framework for aid to specific sectors.

9. The Commission does not systematically define a priori such general principles to be followed by Member States because of the danger of generalizing the use of the aids within Member States even where they are not strictly necessary and the inflexibility which would result, as such frameworks cannot take into account the specific characteristics of the industry concerned in each Member State. However, in cases where it has become evident that an industry faces a situation of particular difficulty throughout the Community, or shall face such difficulties, it is possible to develop certain guidelines which indicate the policy the Commission will pursue in matters of subsidies for this industry. Such guidelines have been developed in particular in cases where industries are in crisis, for example textiles, shipbuilding and steel, under the rules of CECA, or because particular industries are growth points which should be stimulated in the common interest. In other areas where Member States face problems of a similar nature or intensity, for example regional aid and aid for the environment, the Commission has also developed this kind of framework.
10. The Commission has to take into account also the sectoral effects of certain other types of aid given, for example, aids for regional development or social purposes, such as employment aids. The Commission has applied restrictions when necessary (see point 13. below).

#### Policy in specific sectors

11. Acting within the above policy the Commission has approached equally the problems created by industries in crisis as well as those where the problem is growth. The former group has concerned shipbuilding (four successive Council Directives on aid), textiles (general principles on aid first elaborated in 1971 and refined and extended in 1976), man-made fibres (proposal of appropriate measures under Article 93(1)) and steel (general principles were proposed to Member States in April 1977 and a proposal for a Decision under Article 95 ECSC sent to the Council and the Consultative Committee in May 1978).



11.1. The Commission's approach in the case of industries in crisis cited above has been based on certain common principles. The Commission has recognized that the crisis in these industries has threatened either a disorderly rundown of their activities with serious adverse consequences for employment in general, or a series of interventions by Member States designed to protect their industries, possibly by transferring difficulties to other Member States, with aid levels being fruitlessly bid-up at substantial cost to all Member States. The general purpose of the Commission's initiatives has been to avoid both of these undesirable eventualities and at the same time to encourage the establishment of industries able to compete freely on the world market. To these ends it has accepted the justification for aids where these have facilitated adaptation to the new market conditions in an orderly manner. Such adaptations require (a) either an actual reduction in capacity or the avoidance of undesirable increases in capacity; and (b) the restoration of the competitiveness of Community industry.

11.2. In more concrete terms this has led to the specification of the following principles in these initiatives:

- aids should not be given where their sole effect would be to maintain the status quo. Production aids as such are therefore in principle inadmissible, unless firstly they are conditional on action by the recipient which will facilitate adjustment (e.g. restructuring programmes); and secondly they are limited in time;

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- similarly, rescue measures have been recognized as necessary to provide a breathing space while longer term solutions to an enterprise's difficulties are worked out, so as not to frustrate any required capacity reductions, such rescue measures should be limited to cases where they are required to cope with acute social problems;
- aids for investment should not result in capacity increases, since it is a common feature of the industries concerned that capacity is excessive. (The Commission has sought in certain instances to apply this criterion in the case of regional aids - a point discussed in paragraph 13. below).

12. As far as concerns industrial growth sectors, the Commission, while it is in principle positively disposed to their stimulation, emphasizes in its decisions the benefits to be obtained from Community-wide cooperation in such actions. The principal competitive problems facing the Community come from States outside the Community, in particular those highly industrialized and/or technically advanced. The Commission has encouraged Member States to promote an active policy of development in the fields of computer technology, electronics, aeronautics, particularly by general promotion of research and development. It has raised no objections therefore to the use of State aids to attain these objectives.

In this context mention should be made also of the favourable position the Commission has adopted to proposals to promote the availability of finances for the creation of new undertakings and the development of small and medium-sized enterprises.

13. In considering its policy on sectoral aid schemes the Commission has also taken into account the sectoral effects of other types of aids. In particular:

- Aids to employment. The Commission has distinguished between aids designed to promote new work places and those designed to maintain existing jobs. In regard to the latter it has considered that if such

aids are concentrated on sectors which face acute difficulties in all Member States, and are not associated with substantial plans for reorganization, their granting will lead not to the solution of the social and industrial difficulties, but to their transfer to other Member States. For these reasons it has recently imposed important restrictions on such an employment aid.

- As concerns regional aid, bearing in mind the general objectives of the Treaty and in particular the derogation of Article 92(3)(a) and (c) EEC Treaty covering the grant of regional aid, the accumulation of sectoral with regional aids is not excluded in principle. However, where a point of extreme overcapacity has been reached in a particular sector, the Commission has demanded from Member States that even regional aid which would encourage investment that would lead to an increase in capacity should not <sup>in principle</sup> be granted, for example in the case of the synthetic fibre industry, and shipbuilding.

#### Conclusion

14. The Commission welcomes this opportunity for a fruitful exchange of views on State aids with the Council, which it is ready to renew, without prejudice to its competences. It would note that Member States are already associated with its decisions on matters of State aid through a constant stream of consultation at both bilateral and multilateral level. This practice of the Commission was explained in letters of the President of the Commission of 5 January 1977 and 11 April 1978. Furthermore, the Commission would recall that in its Annual Report of Competition Policy addressed to the Parliament its policies and actions are described in detail. On the basis of this report the Commission is prepared to hold periodic discussions on its policy with the relevant experts from the Member States.