II

(Acts whose publication is not obligatory)

COMMISSION

COMMISSION DECISION

of 17 November 1987

on aid for shipbuilding and ship repair in Italy — Article 10 of Law No 111 of 22 March 1985

(Only the Italian text is authentic)

(88/281/EEC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community, and in particular the first subparagraph of Article 93 (2) thereof,

Having given the parties concerned notice to submit their comments as provided for in the said Article 93, and having regard to those comments,

Whereas

I

On 20 August 1984, the Italian Government notified a scheme of aid for shipbuilding and ship repair covering the period from 1 July 1984 to 31 December 1985.

The Commission decided on 10 October 1984 to open the procedure laid down in Article 93 (2) of the EEC Treaty.

On 22 March 1985, the President of the Italian Republic promulgated Law No 111 introducing the notified aid.

Article 12 of the Law provided that the President of the Italian Council of Ministers could amend by decree any elements not approved by the Commission so as to make them compatible with the common market.

The promulgated law did, in fact, contain new elements, notably in its Article 10, which provided for additional aid for building up stocks. This aid forms the subject-matter of the present Decision.

By telex from the Ministry for Shipping dated 7 May 1985, the Italian Government officially informed the Commission of these new elements in Law No 111.

On 8 July 1985 the Commission decided to close the Article 93 (2) procedure. The decision authorized *inter alia* production aid for shipbuilding at the same level as that which prevailed when the previous scheme was first implemented (period from 1 January 1982 to 31 December 1983, extended until 30 June 1984) and production aid for ship repair, the minimum value of eligible contracts being fixed, however at Lit 200 million instead of Lit 100 million and the maximum rate being reduced by two points, i. e. 8 % instead of the 10 % (13 % instead of 15 % in the Mezzogornio) provided for in the Law.

The total budget for all aid to the shipbuilding and ship repair sector, including investment aid, aid for research and development and demolition aid, was set at Lit 900 000 million for the duration of the scheme.

As for the aid for building up stocks, on the other hand, to which a further Lit 60 000 million was devoted on top of the overall budget of Lit 900 000 million, the Commission considered Article 10 of Law No 111 to be too imprecise, especially as the Italian Government had yet to decide how it would be implemented. The Commission therefore decided to defer assessment of this provision.

By letter dated 28 January 1986 , the Italian Government notified the Commission of a draft decree layng down rules for the award of the aid provided for in Article 10 of Law No 111.

The Commission requested additional information by letter dated 20 March 1986, to which the Italian authorities replied by telex dated 7 May 1986.

The draft notified by the Italian Government provides for a grant of 12,5 % per year of the value of raw materials, semi-finished products and finished products stored in the shipbuilding or ship repair yard but not yet allocated to a specific order. Only large yards qualify.

Yards applying for aid must provide on 31 March of each year a detailed inventory for each category of raw material, semi-finished product and finished product stored in warehouses or on slipways. The list is examined by the 'Registro italiano navale', the only body empowered by law to carry out checks in connection with aid to Italian shipyards. These checks are based on the yards' bookkeeping records. As soon as the inventoried goods are assigned to a firm order, the aid is discontinued.

The Italian authorities acknowledge that the stock requirements of Italian yards do not differ markedly from those of yards in the other Member States, but claim that the measures in question are justified by the fact that the cost of money has made the tying-up of capital in warehouses and stores more expensive in Italy and that the expense has steadily increased as the crisis has deepened.

They point out, moreover, that the aid must be considered exceptional and temporary, covering only the three years from 1984 to 1986.

After a preliminary scrutiny, the Commission came to the conclusion that, in view of the conditions under which the aid was awarded, its intensity in relation to the cost of building a ship could not be calculated once and for all as the stocks covered by the aid were not intended for a single ship and the period of storage could vary.

In the course of bilateral talks, however, the Italian authorities admitted that, since the type of product concerned ranged from raw materials to finished products, the stocks in question could account for up to 40 % of the cost of a single vessel.

In that case, the grant amounting to 12,5 % of the stocks' value would represent an intensity of five points which would have to be added to the basic rate of direct production aid, namely 25 % (30 % for the Mezzogiorno).

In the case of stocks held by ship repair yards, where their turnover should as a rule be faster, it was felt that the maximum intensity could be reduced by half, giving 2,5 points to be added to the basic rate of 8 % (15 % for Mezzogiorno).

The Commission considered that, by its very nature, such aid, which should go first and foremost to those yeards which have no orders so as to enable them to anticipate new work, was tantamount to an aid for continued operation pending new orders and would have the effect of delaying the capacity cuts and implemetation of the restructuring measures on which the Commission has based its approval of aid under the existing scheme.

The Commission therefore concluded that the aid did not fulfil the conditions for exemption under Article 92 (3) of the EEC Treaty.

By letter dated 8 July 1986, it requested the Italian Government to submit its comments. The other Member States were informed on 10 December 1986 and interested third parties on 24 December 1986.

II

The Italian Government, submitting its comments under the procedure by letter dated 4 September 1986, stated that the measure in question was exceptional and of limited duration. It challenged the Commission's interpretation both as to the purpose and as to the intensity of the aid provided for in Article 10 of Law 111.

In the Italian Government's opinion, the purpose of the aid was to limit the cost of servicing the sums large shipyards had to borrow in order to build up their stocks, this cost being particularly high in Italy owing to the level of interest rates.

As regards the aid's intensity, the Italian Government argued that, according to the estimates made by the competent department, the amount eligible for assistance in the first year of the scheme's operation, namely 1984, would only be some Lit 100 000 million, the grants paid would amount to approximately Lit 13 000 million and, in view of the time limits for payment, the grant equivalent would represent only 1,3 % of the value of

annual production. In view of the fact that the budget devoted to these grants for the period 1984 to 1986 came to only Lit 60 000 million, the average intensity over the three years should therefore not be any higher.

Four Member States submitted their comments in accordance with the procedure.

III

Article 6 (1) of Council Directive 81/363/EEC of 28 April 1981 on aid to shipbuilding (1), as last amended by Directive 85/2/EEC (2), sets out the conditions under which aid to this sector may be considered compatible with the common market; it must be progressively reduced and it may be granted only if linked to the attainment of industrial restructuring objectives. Article 6 (2) states that, when assessing the compatability of such measures with the common market, the Commission must take account of all the aid which the Member State concerned provides for the construction, sale and acquisition of ships insofar as this aid affects the shipbuilding sector and of the budgetary funds allocated to this aid as a whole and in particular crisis aid.

In agreeing to most of the measures provided for in Law 111/85 in favour of shipbuilding, the Commission authorized production aid at a level of 25 % of the contract price for large shipyards (30 % for shipyards in the Mezzogiorno). The budget devoted to this aid amounted to Lit 620 000 million for the period from 1 July 1984 to 31 December 1986. In taking its decision the Commission took account of market conditions and the gravity of the crisis in the shipbuilding sector in Italy and agreed to there being no progressive reduction of the aid and to retention of the original rate for the period 1981 to 1983.

The aid provided for in Article 10 of Law 111 would have the effect of reducing the cost of producing ships and must therefore be added to the contract-related aid already agreed to by the Commission.

Whatever the method used to calculate the aid's intensity, whether it be based on a single ship as is the Commission's practice or on the value of annual production as it the Italian authorities' practice, the maximum rate of aid per contract already authorized by the Commission is systematically increased by at least 1,5 points. Calculated in purely budgetary terms, if one takes account of the production aid budget of Lit 620 000 million, or 25 % of a turnover of Lit 2,48 billion, the budget of 60 000 million assigned to aid for building up stocks represents in relation to this turnover figure an additional subsidy of 2,5 points. Article 6 (3) of Directive 81/363/EEC provides that the maximum level authorized by the Commission may be exceeded, but authorization to exceed this level may be given only as an exceptional measure for specific contracts, each case being examined on its merits, and Article 6 of Law 111 already covers the possibility of resorting to these provisions.

When they submitted the shipbuilding aid scheme to the Commission, the Italian authorities undertook to implement a restructuring plan aiming at a reduction in production capacity which, measured in terms of employment, would amount to a cut of 20 % spread over the period 1984 to 1986. An aid mechanism for financing stocks is, where it is not limited to raw materials but extends to semi-finished and finished products, first and foremost a system of operating aid enabling yards to begin building ships without having received an order for them. Shipyards are thus kept in existence artificially and are under no immediate pressure to carry out a structural adjustment of shipbuilding capacity as other Member States of the Community have already done. It is clear that this state of affairs contravenes the spirit of Article 6 of Directive 81/363/EEC, paragraph 2 of which states that the Commission must pay attention to 'the need for adaptation of the shipbuilding industry to the conditions and constraints prevailing on the market' and that it must 'verify that the programme of adaptation of the industry is comparable with those carried out in the other Member States'.

This paragraph states further that the Commission must take account of all the aid which the Member State concerned provides for the construction, sale and acquisition of ships, insofar as it affects the shipbuilding sector, and that it must also examine all the budgetary funds allocated thereto. Apart from the budget of Lit 620 000 million assigned to production aid for large shipyards, those same shipyards qualify for grants of up to 30 % of the amount of investments aimed at rationalization and restructuring, and the funds earmarked for this purpose amount to Lit 50 000 million for the same period. A further Lit 60 000 million is set aside for research, some of it going to the same shipyards.

Moreover, the Italian shipbuilding industry, which is heavily dependent on domestic shipowners, indirectly benefits from the substantial assistance granted to the latter under Law 361/82, as amended by Law 848/84, in respect of the new ships they cause to be built. It is indisputable that the aid granted on stocks would have the effect of reducing the cost of building ships and hence of enabling yards to quote a lower price, whereas other yards in the Community do not enjoy such advantages. The spectrum of aid measures available to large shipyards is therefore sufficiently broad and hence (quite apart from the untoward effects it would have) the addition of aid for building up stocks is unjustified.

(1) OJ No L 137, 23. 5. 1981, p. 39.
(2) OJ No L 2, 3. 1. 1985, p. 13.

IV

The aid for ship repair granted in the form of production aid is aid within the meaning of Article 92 (1) of the EEC Treaty. In agreeing by way of exception to the provisions of Article 4 of Law 111 providing for contract-related grants, the Commission took account of the state of the Italian ship repair industry. It nevertheless inserted restrictions in its decision, increasing the minimum value of contracts qualifying for assistance from Lit 100 million as provided for in the Law to Lit 200 million, and reducing the rate of award from 10 % to 8 %. In the case of yards in the Mezzogiorno, this rate remained fixed at 15 %. The Italian authorities undertook to send the Commission a restructuring plan for both the public sector and the private sector in order to reduce the industry's size in the light of the substantial overcapacity existing in the Community. In 1985 this overcapacity could be put at 332 dry docks, of which 48 were in Italy. In the case of ship repair, aid for building up stocks is difficult to quantify precisely in terms of intensity in view of the many different types of repair and the faster turnover of stocks. However low this intensity may be, it would still have the effect of eliminating all or some of the restrictive element which the Commission has introduced into the system of direct production aid.

It is, at all events, operating aid which enables yards to reduce their production costs and hence quote more competitive prices than yards in other Member States, against a background, moreover, of cutthroat competition due to overcapacity and the level of prices charged by certain third countries. It is therefore likely to distort competition between Community yards and is hence incompatible with the common market.

When it authorized aid for ship repair under certain conditions, the Commission expressed the view that such aid, which was to remain exceptional, would enable the Italian Government to bring the size of the sector more into line with the market's requirements. In view of the situation of the ship repair sector in Italy, the aid could assist the restructuring of the sector without such restructuring having too great an impact on employment in the regions concerned. The higher rate of award applicable in the south of the country answered the need to take account of the special situation obtaining in that region. While additional aid in the form of grants for building up stocks would run counter to the objectives set for the aids already authorized, the aids as a whole would run counter to the EEC Treaty in that they would enable Italian ship repair yards to charge abnormally low prices compared with other Community yards without contributing to the attainment of the objectives laid down in Article 92 (3) of the EEC Treaty.

V

The Italian Government has not been able to give, nor has the Commision found, any grounds to establish that the aid for building up stocks in the shipbuilding industry meets the conditions required to make it compatible with the rules laid down in Directive 81/363/EEC ; in the case of the similar aid to ship repair, no grounds have been found to establish that it is compatible with the common market under Article 92 (3) of the EEC Treaty.

The compatibility of the aid with the common market must be assessed from a Community point of view rather than from that of a single Member State.

As regards more particularly the argument advanced by the Italian Government of the need to compensate for the disadvantage suffered by Italian shipbuilding and ship repair yards as a result of the high rates of interest they have to pay on amounts borrowed to build up their stocks, the Commission considers that this is a phenomenon inherent in the economy of a Member State and that, in parallel with these special circumstances, the relative weakness of the Italian lira compared with other foreign currencies is a phenomenon which makes Italian yards more attractive, especially as this sector in Italy does not depend on foreign countries for its supplies. Consequently, the additional aid, the minimum intensity of which would be 1,5 %, would be both an incentive to anticipate orders and a saving on production costs not made by other Community yards despite the fact that they, too, have to bear the cost of carrying stocks inherent in the proper functioning of a shipbuilding or ship repair yard.

The aid would therefore have the effect of delaying the restructuring of the large Italian shipyards, which must do as yards in the other Member States have done and bring their production capacity more into line with demand, and of distorting competition between Community yards.

In conclusion, the aid provided for in Article 10 of Law 111 for building up stocks in the shipbuilding industry does not fulfil the conditions necessary to benefit from the provisions of Directive 81/363/EEC and the aid for building up stocks in the ship repair industry does not fulfil the conditions necessary to qualify for exemption under Article 92 (3) of the EEC Treaty. The aid is therefore incompatible with the common market,

HAS ADOPTED THIS DECISION:

Article 1

The aid for shipbuilding and ship repair in the form of a grant equal to 12,5 % per year of the value of stocks of raw materials, semi-finished products and finished products provided for in Article 10 of Italian Law 111 of 22 March 1985 is incompatible with the common market.

Article 2

The Italian Government may not implement the provisions of Article 10 of Law 111 of 22 March 1985 and it shall inform the Commission within two months of the date of notification of this Decision of the measures it has taken to comply therewith.

Article 3

This Decision is addressed to the Italian Republic.

Done at Brussels, 17 November 1987.

For the Commission

Peter SUTHERLAND

Member of the Commission