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EUROPEAN STATE AIDS IN THE CURRENT FINANCIAL CRISIS

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Abstract: *The paper presents the aid measures and the types of state aid proposed by the European Commission for the current financial crisis, which assumes extraordinary policy responses, "but for a limited period". The new framework is a temporary one and it will be applicable only until 31 December 2010. These European Union initiatives, taken at the end of 2008, were adjusted at the beginning of year 2009, by regards aid in the form of guarantees. The changes of temporary framework contain additional State aid measures to facilitate the companies' access to finance. The unblocking of the credit flow should allow Europe to come out of the recession, even stronger and prove confidence in the Commission.*

Key words: *Financial crisis, Guarantees, Subsidized loans, Green products, State aid rules.*

1. Introduction

The international financial crisis determined the European Union Member States to ask aids. The level of subsidies must be achieved in a coordinated manner, observing the principles of European Community and the rules of competition.

The European Commission reacted early in October 2008, when the "Communication on the application of State aid rules to measures taken in relation to financial institutions in the context of current global financial crisis" was adopted, together with some decisions for corresponding rescue aids to financial institutions.

In November 2008, "A European Economic Recovery Plan" was also established, having two acting directions: to boost the purchasing power for increasing consumption and people's confidence and actions to ensure the economic sustainability by investing in technologies for a greener economy on the long term.

In December 2008, a document of the European Commission, "Communication on the recapitalisation of financial institutions in the current financial crisis", was adopted for maintaining the adequate levels of loans to companies in real economy.

Although these EU initiatives were taken at the end of year 2008, the financial and economic crisis began a deep economic downturn.

2. State Aids in European Union

Appropriate state aids to promote economic activities and sectors or to develop certain regions, in a sustainable way – represents an intervention which

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affects the principles and the rules of competition.

In 2007, 80% of the state aid was given for horizontal objectives such as employment or training and this tendency continued in 2008, as compared with a proportion of about 50% in the 1990's, with a view to increasing the expenditure in the research and development field and for a healthier environment. [1]

The different types of state aids which are controlled by the European Commission are:

(a) *Transfer of State resources,* which are not necessarily granted by the state itself, but by the public or private entities established by the state. The financial forms of state resources transfer can be: grants, interest rate rebates, loan guarantees, capital injections, allowances.

(b) *Aids for economic advantage,* in situations of abnormal undertaking of a business, like: a private privilege for freely using the public infrastructure, favourable conditions for risk capital, public properties bought or rented by companies under the market price, the state buys land at a value higher than the market level.

(c) *Selectivity* in giving state aid affects the competition between firms in some activity sectors. This principle makes the difference in the regional or sector schemes, as compared to other kind of measures with a general character, such as the nation-wide fiscal measures, which are applied for all firms from all member countries of the European Union.

(d) *Competition and trade effect* suppose that the beneficiary unfolds an economic activity and activates in trade activities on the market with other EU member-states. The minimum aid is considered to be inefficient as to the effects for competition and trade between EU states.

If the aid is meant to be used for services of general interest, then it may not be considered as a state aid. There are also some kinds of aid which are not considered to be State aid, like: aid given to recipients who are not enterprises, structural EU funds, the aid of multinational entities, as EIB and EBRD or European Space Agency or aid for Defence and Public Works.

The forms in which the aid is provided can be: grants and tax exemptions, equity participation, soft loans, tax deferrals and guarantees.

The grants and tax exemptions can be given through the budget or through the tax or social security system, as: subsidies, tax credits, allowances, exemptions, rate relieves, lower social security contributions.

The equity participations appear as financial transfers made to the recipient entities by the public authorities, which operate as a private investor in normal market conditions.

The soft loans and tax deferrals represent a main aid category, referring to transfers to the recipient entities, which have an interest in using and saving the capital during the period they have at their disposal.

The guarantees are aid elements which correspond to the benefit for some nominal amounts received by entities, free of charge or at rates lower than the market level, if a premium is paid to cover the risk.

In 2008, the aid with and without crisis measures was about 95% in industry and services. The structure of aid instruments given in 2008, in industry and services, is presented in Figure 1.

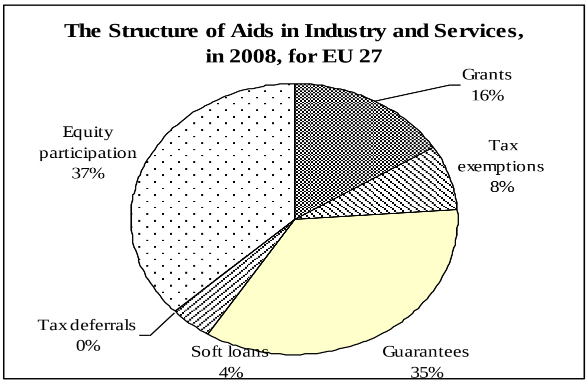

Fig. 1. *The shares of aid instruments in total aid for industry and services, in EU 27, in 2008*

Since the financial crisis, the State aid has risen because the EU Member States tried to support their economies, especially the financial sector. The estimates of the aid element based on the guarantee volume through the measures implemented during 2008 by the Member States were for guarantee schemes - 10% of the guaranteed amount; for rescue and restructuring banks at 20% of the guaranteed amount.

3. Statistical Coordinates of the Economic Crisis

The economy of the European Union began to decrease in 2008, continued the descending trend to a wider extent in 2009, and it is supposed to increase in 2010 and 2011.

The economic activity contraction from the second half of 2008 meant the decline and the end of GDP growth. The EU-wide unemployment was approximately 7% in 2008 and it continues to rise in the coming years up to 10%.

Figure 2 shows the evolution of the main macroeconomic aggregates in the European Union area, during 2005-2008 and Autumn-2009 based forecast until 2011. The public consumption does not decrease in 2009, as the other annual macroeconomic dynamics for: GDP, private consumption, employment, government balance as % in GDP.

The GDP decline was about 4% for the entire year 2009 as compared to the previous year and it could be stabilized in 2010 with a small growth expected to be 0.75% and 1.5% in 2011.

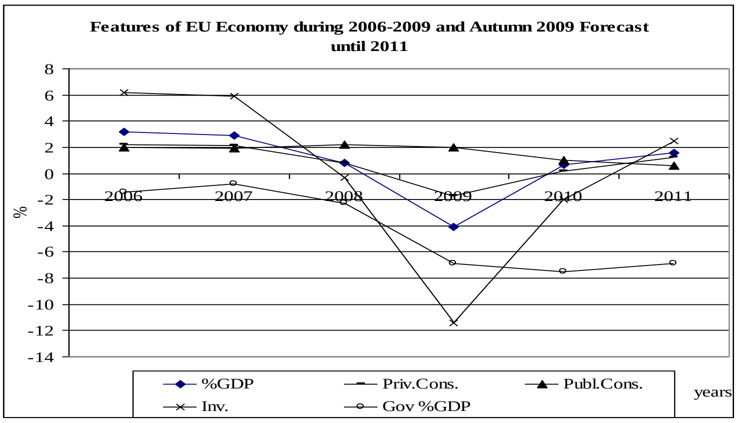

Fig. 2. *Macroeconomic Development of EU Economy during 2006-2011 (y-o-y)*

As compared to 2005, investments increased in 2007 and 2008, with the same intensity; in 2009 there was a decrease of more than 12%, which has continued to go down in 2010. In 2011, it will attain the level from 2009, as it is shown in Figure 3.

The GDP dynamics is mostly the same as the private consumption, recording a decreasing tendency until 2009 and then a slow increase in 2010 and 2011 considering the 2009 based forecasting. The public consumption continues to increase during the entire period analyzed. The government balance as percentage in GDP decreased in 2009 and the trend is expected to continue in the next two years.

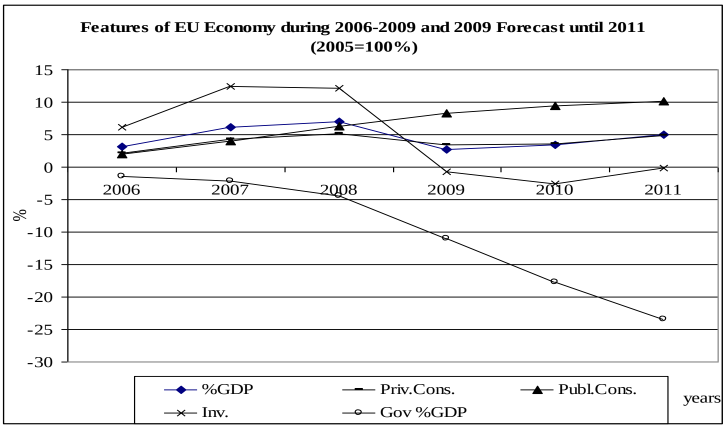

Fig. 3. *Macroeconomic Tendencies of EU Economy during 2006-2011 (base 2005)*

The level of State aid, as a percentage of GDP, decreased on average by around 2% per year between 2002 and 2007, reaching less than 0.5% in 2007.

The banking sector received great amounts of aid, contributing significantly to the State aid expenditure in 2008. The Temporary Framework measures were taken to sustain the real economy.

4. Application of the Temporary Framework for State Aid

The temporary framework for state aid measures taken during the financial and economic crisis are considered to be crisis measures. The need for new temporary aid to guarantee financing and investment have materialized in some measures which enable the Member States to grant some specific aid until the end of 2010, under current conditions until 31st December 2010.

The temporary framework is aimed at companies which have financial difficulties in the current economic period, receiving aid up to €500,000 for the next two years, state guarantees for loans having a reduced premium, subsidized loans, especially for actions referring to environmental protection and green products and "risk capital aid up to € 2.5 million per SME per year (instead of the current €1.5m) in cases where at least 30% (instead of the current 50%) of the investment cost comes from private investors". [2]

Only the companies which can prove that they were not in difficulty before 1 July 2008, can benefit from this temporary framework of State aid; the need for supporting their economic situation can be considered only as an alteration induced by the financial and economic crisis.

The temporary nature of this framework of state aid underlines the seriousness of the financial and economic crisis. The State aid rules and some instruments are meant to support the sustainability of overall European economy development, as follows:

a) "De Minimis" aid

The current "De Minimis" Regulation is an aid up to €200,000 to be given based on an aid scheme for only one undertaking over a three year period. The temporary aid measures can not be cumulated with the "De Minimis" measure.

b) Guarantees aid

For the specified period, the temporary framework awards subsidized loans as State aid if: "a reduction of up to 25% for SMEs (15% for large companies) of the annual premium to be paid for new guarantees granted in accordance with safe harbour provisions as set out …, or to guarantees calculated through methodologies already accepted by EC", reduction given for maximum two years, "the maximum loan must not exceed the total annual wage bill of the beneficiary", and "guarantees may not exceed 90% of the loan and may relate to both investment and working capital" [2].

c) Subsidized interest rates

A methodology of establishing the reference rate for a company considers the credit level. The differences in companies' rates were a consequence of their specific conditions. The interest rate equals the rate of the European Central Bank plus a premium which is the difference between this one and the one year average of inter-banking rate, considered for the period January 1, 2007 and June 30, 2008 – plus the risk premium in accordance with its profile field.

The discounts and reduced rates will be available for interest payments before 31st December 2013.

d) Aid for green production

The aid for green products consists in reducing the interest rate for their production. They are related to investment loans for improving the environmental protection and financing projects for new green products. The conditions of this kind of aid impose the starting of investments in 2010; the appearance of new products on the market must take place at least two years before the standard is stated. The aid will take the form of loans for two years, given with 50% reduction in the interest rate for SMEs and with 25% for large enterprises, until 31st December 2010. The loans cover the investments in tangible and intangible assets.

There are also other measures adopted by the European Commission, such as: changes in the admitted level for risk capital investments in SMEs and more relaxed rules for short term export credit insurance. The deadline for announcing the aid schemes was 31st July 2009.

5. Subsidized Loans

To reduce the large regional disparities between the development degree of EU member states, the aid for horizontal objectives was approved depending on their primary objectives.

During the last years, a proportion of 26% from the total aid for regional development aid was for industry and services. Its distribution was quite different for the EU members: for France and Spain, the proportion was 40%, in Greece - 75% as compared to the EU-12 average which was 44%. A quarter of the aid for industry and services was used for the environment. The average proportion of the EU-12 countries was 6%, while developed countries had great proportions allocated for environmental care: Sweden with 86%, Netherlands with 65%, Austria - 42%, the United Kingdom - 41% and Germany - 40%. The most developed countries allocated great shares for this kind of horizontal objectives, proving their care for high standards of life quality.

6. State Aid for Regional Development in Romania during 2007-2013

In January 2007, Romania was considered eligible for regional development aid for the whole period 2007-2013. All the Romanian administrative regions have the maximum intensity of 50%, except Bucharest region, with 40% of the total sum, depending on the GDP per capita level for each region. [3]

The aid for RDI activities had a share of 16% of the EU horizontal objectives aid. The following countries benefited of this kind of aid with the mentioned shares: Belgium - 46%, Luxembourg -36%, Finland - 29%, Romania - 26% and France - 25% [4].

The spring 2010 updated version of the "Report on recent developments on crisis aid to the financial sector" does not contain any mention about Romania [5].

The Commission has approved 61 schemes under the Temporary Framework. [4]

For Romania, 16 guarantee measures have been authorized, having the primary objective to "remedy for a serious disturbance in the economy". The measures of Temporary Framework 2008-2010 are available for Romania from 01.06.2009 to 31.12.2010.

The guarantee schemes are meant to boost real economy, providing help for the companies encountering financing difficulties. The aid is subsidized guarantees for *investment and working capital loans* until 31st December 2010. Respecting the rules of EC Treaty for this kind of aid, the guarantee schemes are given only for those companies which were not in difficulty on 1st July 2008.

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