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## PANEL 3. SOCIAL ASPECTS AND FINANCING OF INDUSTRIAL RESTRUCTURING

Topic 6. Financing the industrial restructuring

**INDUSTRIAL RESTRUCTURING PROGRAMMES IN POLAND  
SEEN FROM THE POINT OF VIEW OF THE STATE BUDGET\***by Mr. **Artur Kawaler**, Director, Department of National Economy Finance, Ministry of Finance  
Poland**1. Introduction**

Started in 1989, the process of political transformation initiated fundamental changes in national economy. With the advent of market economy, brought about by economic changes, the principles by which enterprises had operated so far had to be changed. However, in certain branches of economy the process of change was not easy. The problems associated with conversion processes were too huge for some sectors of national economy to deal with on their own. The most telling examples are hard coal mining and iron and steelworks sectors. The troubles they were struggling with soon affected transport sector, leading to a near bankruptcy of the state railways, which compelled the government to intervene in yet another sector of the national economy.

In my speech I would like to focus on these three sectors not only because they are covered by the government programmes currently underway. I have selected them also because of their size, their significance for national economy, social consequences they entail and the amount of public investment (chiefly budgetary funds) they need. When the restructuring of industry is discussed in the exclusive context of its consequences for the state budget, the selection of these three sectors is not accidental. Taking hard coal mining as an example, it can be easily seen that the involvement of the state budget in financing the current government

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programme for this sector is unprecedented in its scale. The three sectors are also a show-case for three different ways of financing.

## 2. Scope of tasks covered by restructuring processes

### 2.1. Hard coal mining sector

Hard coal mining sector has required the government's intervention ever since the beginning of transformation. This support has taken a form of budgetary funds allocated on a yearly basis (see Table 1). As the sector used to be orientated in the past towards achieving the maximum coal output regardless of coal quality, natural conditions of deposits and mining costs, it needed a profound restructuring, including downsizing of its production capacity. Given its significance for Poland's economy and a necessity to ensure energy safety (about 50 percent of electric energy is obtained from hard coal), the sector enjoyed a special treatment by the successive governments in 1990s.

Ever since the beginning of political transformation in Poland there have been attempts to restructure hard coal mining industry. However, restructuring projects had to be aborted one by one because of the sector's difficult financial situation, decline in the world prices of coal, limited budgetary allocations for recovery operations and the changing conceptions for the sector's reform. Although failed, these projects had some positive effects such as a significantly downsized employment (from 415,700 employees in 1989 to 207,900 in December 1998), adoption of the rules for coal trading, initiating the action for concentration of mining operations and the rational use of fixed assets and initiating the process of closing down unprofitable coal-mines with mined-out deposits.

Table 1 – the sector's assorted economic parameters and amount of budgetary support in the years 1989 – 1998

YEARS	EMPLOYMENT	SALES in million tons	NET FINANCIAL RESULT (in PLN m)	TOTAL DEBT (in PLN m)	BUDGETARY SUBSIDIES (in PLN m)
1989	415.740	174,0	34,7	109,6	331,6
1990	387.898	144,9	- 41,6	648,3	921,6
1991	352.887	137,5	- 353,5	1.457,0	614,1
1992	336.434	126,2	- 1.258,2	2.990,1	177,7
1993	319.562	131,2	- 1.500,7	5.454,0	145,3
1994	291.862	129,0	- 191,8	6.749,9	330,5
1995	274.851	131,4	- 782,1	8.134,0	779,1
1996	259.062	133,3	- 1.789,3	9.889,1	462,0
1997	243.304	132,6	- 3.383,5	13.346,4	707,2
1998	207.935	114,3	- 4.276,2	16.524,9	1.007,5

Source: Programme "Hard coal mining. A policy of the state and the sector for the years 1996 – 2000" adopted by the Council of Ministers on 30 April 1996

For the reasons given above, the successive restructuring programmes adopted in 1990s failed to yield the anticipated results.

The combination of high costs of coal mining and transport to the ports, related to Poland's unfavourable geological and mining conditions, and a decline in the prices of power coal exported to Western Europe caused the Polish coal to lose its competitiveness on international markets. This was coupled with a significant decline in the domestic demand for coal caused by, among others, a growing popularity of alternative energy sources and more rational use of coal in the economy.

The sector's financial situation was growing steadily worse. Its debt was so high as to pose a threat to public finances. On 31 December 1997, the debt of mining enterprises exceeded PLN 13.3 billion, of which about PLN 1 billion to the state budget and over PLN 2.5 billion to the state social-security fund (ZUS).

To address that situation, a programme was devised for "Reform of coal mining sector in Poland in the years 1998 – 2002". While examining the state of coal mining sector in 1997, it was found that the main reasons for the Polish coal sector to have been generating losses and unsuccessfully deal with the situation were:

- 1) overcapacity of 10-12 million tons in relation to the market demand,
- 2) overemployment of 50,000 – 60,000 persons translating into high costs of coal mining.

The programme was adopted by the Council of Ministers on 30 June 1998. The main goal of the programme is to make mining enterprises profitable. To achieve that goal and alleviate social effects of employment downsizing, the programme intends to:

- limit production capacity by closing mainly the least effective coal-mines,
- downsize employment,
- remove mining damage and intensify actions for limiting the harmfulness of mining to the environment,
- create new jobs,
- initiate economic activity of the communes on whose territory mining enterprises are being closed down.

The above tasks are fully financed by the state budget.

In view of the sector's debt, it is also necessary to carry out financial restructuring of mining enterprises as a condition for improvement of their economic standing.

## **2.2. Iron and steelwork sector**

The Polish iron and steelwork sector entered the period of political transformation with unfavourable assortment of products, a capacity exceeding the market demand, huge overemployment, low quality of production, a high consumption of energy and charge materials and a high index of environmental deterioration. In the output structure of Polish iron and steelworks, semi-products largely dominated over high value-added products.

In 1990s, steelworks took out bank credits and made a huge effort to upgrade their production processes. At the same time, the Polish market was increasingly opening to foreign competition, as required by, among others, the Association Agreement between Poland and the European Communities. At that time, the Polish government wanted to obtain investors for Polish steelworks, which was not an easy task in view of the Polish market's openness and a high overcapacity of European steelworks.

The current situation of Polish steelwork industry, to which contributed the Asian and Russian crises and the withdrawal of strategic investors in the years 1998 – 2000, has compelled the government to take steps to prevent the bankruptcy of the sector's enterprises. This goal is to be implemented through the Programme for Restructuring Iron and Steelwork Sector, adopted by the Council of Ministers on 5 June 2001. The basic assumptions of the Programme are to reduce employment, consolidate the steelworks' production and restructure their debt. The most important element of the restructuring process is the cancellation of the sector's debt.

### **2.3. Railway transport**

In view of unprofitability of passenger transport, the main source of income for the Polish state railways operator (PKP) is the carriage of goods. By the end of 1997, profits from the goods transport were sufficient to set off losses generated by passenger transport as well as high (in comparison to other state railways) costs of labour. A decline in coal volumes, which accounted for about half of revenues from goods transport, a decrease in steelworks' output and new opportunities for transport of liquid fuels by pipelines brought losses to the railways. The carrier relied on a transport of mass-scale goods for its existence, so once this business began to shrink the losses were immense, causing a sudden increase in debt and the loss of investment capacity. In its turn, the lack of investment in rolling stock put railways at a disadvantage to road transport, which resulted in even higher losses, debt and eventually the loss of credit capacity.

Aware of the significance of an efficient transport system for national economy, in view of the imminent bankruptcy of the state railways, the government made another effort to restructure the sector.

A programme for restructuring the state railways envisages action in the following four areas:

- 1) restructuring of finances in relation to public creditors,
- 2) restructuring of assets with the aim of rationalising them and solving issues related to property rights,
- 3) downsizing of employment – 43,400 lay-offs accompanied by social protection packages,
- 4) legal and organisational restructuring with the aim of creating a holding structure and the conditions favourable for privatisation. The railways will be divided into an infrastructure business, transport businesses and other businesses.

These tasks will be implemented with the minimum assistance from the state budget.

## **3. Sources of financing for the restructuring programmes**

### **3.1. Hard coal mining sector**

The programme for restructuring mining sector, initiated as the first of restructuring programmes in 1998, is financed in full by the state budget. It is estimated that the state budget will have expended about PLN 9 billion by the end of the programme in 2002. This amount covers expenses that will need to be incurred by 2006 in the follow-up to the programme.

### **3.2. Iron and steelwork sector**

The state budget provides subsidies for social protection packages distributed as a part of employment restructuring process. Social protection packages are co-financed on a pro rata basis by own funds of the steelworks, subsidies from the state budget and EU aid funds obtained from Phare programme. In the years 1999-2002 the state budget will provide PLN 200 million.

### **3.3. Railways**

To finance tasks resulting from the government programme, the state railways will issue bonds at a nominal value of PLN 3,900,000,000. The funds raised that way will allow PKP to repay some of its obligations to trading partners to ensure business continuity. The Council of Ministers may provide a surety for or guarantee of repayment of obligations arising from the bonds. To redeem bonds, PKP will obtain funds from privatisation of spun-off businesses. This means that apart from public legal obligations, involvement of the state budget in restructuring the railways will be minimal. The conception of carrying out so huge and complex a restructuring process without involvement of the state budget, but at a cost of future proceeds from privatisation, has been adopted for the railways in view of Poland's geographical location. Regardless of

PKP's current value, the high value of Polish railway market, which is closed to foreign operators, should be taken into consideration.

### 3.4. Social aspect of restructuring processes

Apart from their financial aspects, the social impact of the three restructuring programmes must be taken into consideration. Restructuring of these sectors will cause – in the years 1998-2003 - the downsizing of employment by 165,000 persons. With Poland's unemployment ratio of 17 percent, this element of restructuring process will be the most sensitive, and costly, one. This is one of the reasons for classifying these three programmes as the government's biggest of current undertakings. A number of social-security and occupational mobility packages have been devised for downsized employees. Older employees are offered three or five-year pre-retirement leaves (by the time they become eligible for retirement benefits they will be receiving about 75 percent of their last wages). Younger employees are offered severance pays that provide them with funds to start a business activity on their own account, the opportunities for vocational retraining and taking up job in another sector and counselling. The entitlements to social protection packages are laid down in the laws concerning the restructuring of particular sectors. It is estimated that expenditures from the state budget on employment downsizing in mining industry will total PLN 7,300.4 million in the years 1998-2006 and in steelwork industry PLN 200.0 million in the years 1999-2003. The restructuring of employment in the state railways will be financed by proceeds from the issue of PKP bonds. The costs of issue, however, are estimated at PLN 1,100.0 million.

## 4. Involvement of the state budget

High losses, the lack of financial liquidity and increasing debt create a difficult situation for enterprises. Their bankruptcy would have a serious impact on national economy. On 31.12.2000 total debt of mining industry, steelworks and the state railways was PLN 37,844.5 million including PLN 11,071.2 million towards the public sector, which accounts for 34,4 percent of the state budget's total obligations. Basic economic parameters are shown in the table 2.

Table 2

In PLN million

Specification	mining industry	steelworks	railways
Total debt	22.075,5	8.642	7.127,0
Including			
To the state budget			
To Social-Security Fund, Labour Fund, Guaranteed Employee Benefits Fund	3.021,8	320	201,5
	8.160,0	579,3	2.331,9
Financial result	-1.614,8	-778,0	-2.142,6
Revenues	15.012,0	14.851	7.916,1
Employment (thousands)	155	38,7	169,4

The sectors under discussion must undergo a profound restructuring process in which the state budget will be involved. A necessity to simultaneously implement three restructuring programmes is a huge burden for the state budget and the whole public finance sector. The scope of changes that need to be financed and the amount of assistance necessary for the sectors to get out of debt necessitated the adoption of special solutions, as reflected by the restructuring programmes.

The government programmes provide a detailed description of structural changes in particular sectors and include a financial projection for each of the goals to be implemented under the programmes. The mandate for implementation of each programme is provided by the laws concerning the sectors' restructuring. Among others, the laws provide a basis for execution of special provisions on restructuring of finances and employment, at the same time defining a scope of tasks to be carried out under multiannual programmes financed by the state budget.

To globally evaluate all consequences for the state budget of the implementation of the discussed programmes, three aspects need to be considered:

- 1) the amount of budgetary expenditures,
- 2) indirect involvement of the state budget through sureties or guarantees,
- 3) tax exemptions and allowances and the amount of cancelled debt of a public legal nature, indirectly affecting the state budget.

#### 4.1. Expenditures of the state budget

4.1.1. As a part of the Reform of mining industry, the following tasks were selected for financing:

- 1) reduction of mining capacity by financing the physical closure of coal-mines (total and partial),
- 2) mining damage removal and land reclamation,
- 3) downsizing of employment by financing social protection packages,
- 4) financing of coal allowances (or cash equivalents) for retired or disabled workers of coal-mines which have been closed down or placed in the state of total liquidation – in which case the State Treasury acts as a legal successor,
- 5) releasing, for the time of the reform, the working coal-mines from the obligation to provide coal allowances (or cash equivalents) to retired or disabled workers,
- 6) incurring costs related to compensatory pensions and employee claims towards ex-employers,
- 7) creating new jobs – interest rate support for preferential credits for the mining communes to be utilised for investments in infrastructure, or for employers from sectors other than mining who will create new jobs for ex-miners,
- 8) incurring costs of establishing and running the Mining Labour Office,
- 9) incurring costs of monitoring the reform of mining sector.

Table 3 – budgetary expenditures on hard coal mining industry in the years 1998 - 2002

In PLN thousand

Years	Reform financing	Other expenditures
1998	757.875	13.430
1999	1.451.003	32.053
2000	1.575.030	6.100
2001	1.431.946	10.950

2002	960.155	600
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Source: Ministry of Finance

From the beginning of the Reform till 30 June 2001, mining capacity has been downsized by 27.7 million tons, employment by 92,510 persons of which 63,900 benefited from social protection packages. The expenditures to date from the state budget on social protection packages have amounted to PLN 4,668.2 million. The distribution of budgetary subsidies for particular tasks carried out as a part of the Reform is illustrated by the table below.

Table 4 – distribution of budgetary subsidies for the tasks implemented as a part of the Reform

Task	In PLN thousand				
	1998	1999	2000	2001	2002
Closure of coal-mines	217.902	337.999	454.477	246.886	146.000
Downsizing of employment, coal allowances for retired and disabled workers, compensatory pensions	501.974	1.070.704	1.077.991	1.111.860	788.615
Mining damage removal	28.000	30.000	30.000	30.000	6.000
Creation of new jobs	-	-	262	30.900	7.240
Running of job counselling centres	-	2.500	2.500	2.500	2.500
Reform monitoring	9.999	9.800	9.800	9.800	9.800
<b>TOTAL</b>	<b>757.875</b>	<b>1.451.003</b>	<b>1.575.030</b>	<b>1.431.946</b>	<b>960.155</b>

Source: Ministry of Finance

In the years 1998 – 2002, expenditures on mining industry will have amounted to PLN 6,239.1 million, of which PLN 6.176,0 on the Reform. It should be noted that the expenditures of the state budget on the mining communes are not included in Table 4. These amounts are not, *sensu stricte*, allocated to mining industry, yet they are closely related to the Reform and, as a result, should not be overlooked. Moreover, they are envisaged in the law on the restructuring of mining industry, in which the right to compensatory subsidy is laid down for the mining communes which in the years 2001 – 2002 have lost revenue due to the failure of mining enterprises to pay operational fees, provided that the loss of revenue equals not less than 10 percent of a commune's own revenues obtained in the same year. Mining communes are also entitled to a bigger share in revenues from the personal income tax.

In 2001, PLN 29 million was allocated for compensatory subsidies and the communes' increased share in tax receipts amounted to PLN 223 million (this is the amount that would have been otherwise received by the state budget). It is estimated that in 2002 these amounts will be, respectively, PLN 30.3 million and PLN 224.6 million.

It should be noted that apart from the expenditures on restructuring, the state budget provides financial support to investments related to environmental protection or enhancing the safety of miners' work (e.g. equipment for mining rescue services). In the years 1998 – 2002 such expenditures amounted to PLN 63

million.

Regardless of the costs already incurred, the reform of mining industry will continue to be a financial burden for the state budget for years to come. In the years 2003 – 2006, the state budget will incur costs of:

- 1) downsizing of employment – the multiannual forms of Miner Social Security Package,
- 2) closing and securing coal-mines against the risk of flooding after closure,
- 3) in the years 2003-2004 – costs of refunding contributions to Social Security Fund, Labour Fund, Guaranteed Employee Benefits Fund to the employers from a sector other than mining who have hired ex-employees of mining enterprises,
- 4) from 2003 onwards – cash equivalents of coal allowance for retired and disabled employees of the closed coal-mines.

It is estimated that in the years 2003 - 2006 approximately PLN 3 billion will have to be allocated in the budget for mining industry.

Table 5 – financial projection of budgetary expenditures in the years 2003 – 2006

Specification	In PLN million			
	2003	2004	2005	2006
1	2	3	4	5
Closure of coal-mines	75,9	74,8	73,8	
Employment downsizing	698,5	524,7	387,8	290,8
Refund of contributions to Social Security Fund, Labour Fund, Guaranteed Employee Benefits Fund to non-industry employers	5,1	2,6		
Cash equivalent of coal allowance	230,5	224,7	219,1	213,6
<b>Total</b>	<b>1.010,0</b>	<b>826,8</b>	<b>680,7</b>	<b>504,4</b>

Source: Ministry of Economy

**4.1.2.** In spite of the fact that the programme for restructuring steelwork industry was adopted in June 2001 and the law concerning employment took effect at the beginning of this year, the restructuring of employment has been subsidised by the state budget since as early as 1999. In the years 1998 – 2001 employment was downsized from 78,200 persons to 35,700 persons. The target level of employment in 2003 is 30,600 persons. Since 1999, PLN 40 million has been allocated each year for this purpose.

**4.1.3.** A tender will be soon announced for servicing of the issue of 7-year bonds of the Polish Railways valued at PLN 1.5 billion. The issue will be covered by the sureties and guarantees of the government. As mentioned before, total funds obtained for the restructuring of the Polish Railways from credits and bonds guaranteed by the government may not exceed PLN 3.9 billion. The sureties and guarantees granted to the Polish Railways to date concern credits in the amount of PLN 1,767,552,000. The work on creating a new holding-like organisational structure of the state railways has been progressing. The first spun off businesses are being prepared for privatisation. The proceeds from the first series of bonds will be spent on paying off civil legal obligations in the amount of PLN 1,394 million. Assets are being reviewed and put in order, and it is estimated that the sale of redundant assets will bring a revenue of PLN 480 million. The funds will be used, among others, to create modern logistical bases in attractive locations. By 31.12.2001 employment has been downsized to 122.694 persons.



Apart from the restructuring programme, the state budget supports investments in railway infrastructure with the amounts equalling each year several hundred million zlotys. For instance, in 2001 and 2002 these subsidies amounted to, respectively, PLN 365 million and PLN 155 million.

## **5. Liabilities**

Stating that the three Restructuring Programs are the most expensive from the point of view of public finances, and specifically for the State Budget, one must take into account not only the budget expenditure necessary to incur. Talking about budgetary expenditures one must also take into consideration the income side of the budget, i.e. failure by these sectors to meet their public and fiscal obligations.

While remembering the high cost of these problem sectors for public finances it is necessary also to point to one more aspect, namely, failure by enterprises to comply with the good payer practice (to meet obligations as due). This has its justification. While introducing tax relieves, even if significant, certainly affects budget income that income may still be realistically assessed. However, if a taxpayer ceases suddenly to meet its obligations the financial policy of the state is disturbed or even becomes impossible to pursue.

Wishing to focus on the problem of liabilities and the process of restructuring debts to the state budget it is necessary to consider simultaneously the debt of sectors in question to the Social Insurance Institution (ZUS), the Labor Fund and the Guaranteed Employee Benefits Fund. These funds are often called "parabudgets" since their responsibility is to finance a selected portion of state tasks, and they receive grants from the state budget. Since the deficit of these funds is financed with budget grants (failure to meet obligations by the mining sector to these funds affect indirectly the situation of the state budget. For these reasons, when analyzing the mining sector indebtedness to the state budget it is fully justified to treat jointly liabilities to the budget and to those earmarked funds ("parabudgets").

If there is a deficit preventing ZUS from meeting its statutory tasks it receives grants from the state budget. In 2001 the grant was equal to PLN 28,776 million. The 2002 budget bill anticipates a grant for ZUS in the amount of PLN 34,069.8 million. According to the 2002 financial plan of the Social Insurance Institution, enclosed as an appendix to the budget law, ZUS' receivables in 2001 were equal to PLN 4,377 million and are estimated at PLN 10 billion for the current year. The Labor Fund deficit in 2001 reached PLN 1.12 billion, while unpaid receivables of the Fund were equal to PLN 408 million. In 2001, the state budget grant was provided at PLN 2.65 billion and in 2002 it will be PLN 3,634.6 million. The Guaranteed Employee Benefits Fund forfeited its financial liquidity in the last quarter of the previous year. It may still be regained in the second half of this year provided that, among other things, enterprises from the three sectors improve their payments discipline.

The above data show that the financial situation of the funds in question determines the amounts of necessary state budget expenditure. On the other hand, the debt of these sectors to the above funds strongly affects their financial situation. It is worth noting that in 2002 grants from the state budget to ZUS and the Labor Fund will amount in total to PLN 37,704.4 million.

It should be reminded for the sake of comparison that the planned budget deficit this year is to be equal to PLN 40 billion and the level of state budget revenue and expenditure is to be at PLN 143.97 billion and PLN 183.97 billion, respectively.

### **5.1. Debt Restructuring Mechanisms**

These mechanisms are strictly defined in particular restructuring laws. Subject to financial restructuring are monetary liabilities of enterprises to the public sector. These are amounts payable to: the state budget (with some exceptions), the Social Insurance Institution (ZUS), the Labor Fund (FP) and the Guaranteed

Employee Benefits Fund (GFSP), the Environmental Protection Fund (under environmental charges and penalties) and municipalities

Financial restructuring of the enterprises being restructured may take the following forms:

- 1/ cancellation of all or part of debts
- 2/ deferment of debts by a certain period of time
- 3/ spreading of debt into installments
- 4/ conversion of debts into stock or shares
- 5/ exemption from current charges and penalties

Financial restructuring will proceed on the basis of individual agreements between mining enterprises and creditors, provided that the enterprise first meets a number of statutory conditions (e.g. submits a recovery program, prepares a debt repayment schedule, makes current payments as due, observes the remuneration growth limit). Each law defines precisely which debt may be restructured, up to what amount and on what principles.

Later this chapter deals only with those debt restructuring solutions which apply directly or indirectly to debts to the state budget, i.e. also to the Social Insurance Institution (ZUS), the Labor Fund (FP) and the Guaranteed Employee Benefits Fund (FGSP).

### 5.1.1. Pit Coal Mining Sector

In the mining sector the most far-reaching debt restructuring instruments have been applied. Subject to debt restructuring are liabilities together with interest by way of cancellation with respect to part of them, with the rest being spread into installments. The exception is VAT the repayment of which is only deferred and spread into installments. Interest on VAT liabilities is forgiven once the principal is paid. In the case of completely liquidated mines listed by name in the law, all liabilities, including also civil law liabilities, are taken over by the state treasury.

Before the commencement of the government program, the sector debt totaled PLN 13,346.4 million and its level became a threat for public finances. The structure of indebtedness is illustrated by table 6.

Table 6 – breakdown of liabilities at the end of 1997 by major creditors

PLN million		
Item	Amount	Percentage
1	2	3
State budget	929,9	7,0
ZUS, FP, FGSP (social funds)	2.534,8	19,0
Municipal budgets	172,7	1,3
Environment funds	4.129,2	30,9
Fund for Disabled	140,5	1,1
Other (civil law)	5.439,5	40,7
<b>Total</b>	<b>13.346,4</b>	<b>100,0</b>

Source: Ministry of Economy

As shown, the debt of the mining sector to ZUS, FP and FGSP represents approx. ¼ of the total debt and accounts for PLN 5,634.2 million.

### Current Status of the Debt Restructuring Process

As of June 30, 2001, mining enterprises had the total of 96 debt restructuring arrangements with creditors. Among these, seven arrangements with ZUS and one arrangement with the Tax Office had the nature of individual decisions issued on the basis of applications seeking to open debt restructuring proceedings under the Act on Restructuring the Mining Sector (...).

Table 7 – status of debt restructuring arrangements

In PLN thousand

No.	Creditor	Number of arrangements signed	Debt subject to restructuring	Method of restructuring	
				deferment	cancellation
1	2	3	4	5	6
1	State budget	12	820,3	803,4	16,9
2	Social Insurance Institution	7	82,1	17,8	64,3
3	Fund for disabled	40	169,3	55,2	114,1
4	Minister of the Environment	32	319,4	200,7	118,7
5	Municipalities	4	5,6	5,5	0,1
6	Voivode	1	6,3		6,3
7	<b>TOTAL</b>	<b>96</b>	<b>1.403,0</b>	<b>1.082,6</b>	<b>320,4</b>

Source: Państwowa Agencja Restrukturyzacji Górnictwa Wegła Kamiennego S.A.

The total amount of debt subject to all arrangements in force on June 30, 2001 reached PLN 1,403 million. Out of the debt covered by the restructuring arrangements, PLN 320.4 million was anticipated to be cancelled and PLN 1,082.6 million was stipulated to be deferred.

Table 8 – breakdown of debts proposed for restructuring

PLN thousand

Item	Debts proposed for restructuring			cancellation						deferment		
	Total	Main liabilities	Accumulated interest	Total	Main Liabilities	Accumulated interest	Total	Main liabilities	Accumulated interest	Total	Main liabilities	Accumulated interest
1	2	3	4	5	6	7	8	9	10			
<b>Total</b>	<b>15.143.710,8</b>	<b>9.003.375,8</b>	<b>6.140.335,0</b>	<b>9.797.551,5</b>	<b>4.812.779,3</b>	<b>4.984.772,2</b>	<b>5.346.159,3</b>	<b>4.190.596,5</b>	<b>1.155.562,8</b>			
State budget	2.470.159,3	1.887.308,0	582.851,3	773.099,0	378.865,8	394.233,2	1.697.060,3	1.508.442,2	188.618,1			
ZUS, FP, FGSP	6.604.730,6	4.135.416,4	2.469.314,2	3.771.617,6	2.151.501,0	1.620.116,6	2.833.113,0	1.983.915,4	849.197,6			
PFRON	367.012,1	212.273,6	154.738,5	348.725,4	197.413,8	151.311,6	18.286,7	14.859,8	3.426,9			
Minister of Environment	969.432,5	582.141,9	387.290,6	561.922,7	256.132,5	305.790,2	407.509,8	326.009,4	81.500,4			
Voivode	2.998.967,3	1.233.649,2	1.765.318,1	2.959.762,9	1.207.555,5	1.752.207,4	39.204,4	26.093,7	13.110,7			
Marshall of Voivodeship (self-government)	1.036.304,1	550.921,8	485.382,3	688.583,9	222.068,1	466.515,8	347.720,2	328.853,7	18.866,5			
Voivodeship Environmental Inspector	678.361,6	394.507,5	283.854,1	675.285,7	392.242,7	283.043,0	3.075,9	2.264,8	811,1			
Municipalities	18.743,3	7.157,4	11.585,9	18.554,3	6.999,9	11.554,4	189,0	157,5	31,5			

Source: Państwowa Agencja Restrukturyzacji Górnictwa Wegła Kamiennego S.A.

The total amount of debt proposed by the mining sector for inclusion in the restructuring process is

equal to PLN 15,143.7 million, out of which PLN 9,979.5 million is anticipated to be cancelled (64.7%) and PLN 5,346.2 million to be deferred (35.3%).

Out of the debts proposed to be cancelled the majority (over PLN 7,200 million) are liabilities incurred prior to March 31, 1998, hence in major part (50.9%) they consist of interest. In the debt proposed to be deferred the percentage of interest is much smaller and equal to 21.6%.

The largest creditor of mining enterprises is the Social Insurance Institution. In the statement of debts covered by the restructuring process liabilities to ZUS account for 43.6% of the total debt of mining enterprises. Debts to ZUS, FP, FGSP and the state budget represent the amount of PLN 9,074,889,900, i.e. 59.9% of all debts being restructured.

Table 9 – breakdown of debts proposed for restructuring under the applications seeking to open debt restructuring proceedings

In PLN thousand

Item	Debts proposed for restructuring	Percentage
1	2	3
<b>Total</b>	<b>15.143.710,8</b>	<b>100,0</b>
State budget	2.470.159,3	16,3
ZUS, FP, FGSP	6.604.730,6	43,6
PFRON	367.012,1	2,4
Minister of Environment	969.432,5	6,4
Voivode	2.998.967,3	19,8
Marshall of Voivodeship (self-government)	1.036.304,1	6,9
Voivodeship Environmental Insoector	678.361,6	4,5
Municipalities	18.743,3	0,1

Source: Panstwowa Agencja Restrukturyzacji Górnictwa Wegla Kamiennego S.A.

The debt shown in the table 9, planned for restructuring, amounts to PLN 15,143.7 million, provided that PLN 9,797.5 million is to be cancelled and PLN 5,346.1 million deferred. As may be noticed based on these plans nearly half of all debt of the mining sector (with the global indebtedness being equal to PLN 20,142.9 million) is to be cancelled. It should be underlined that the amounts planned to be cancelled and deferred shown in table 8 above are merely debtor's proposals and assume the maximum use of the restructuring mechanisms available under the Act on Restructuring the Mining Sector.

It should be noted that debt restructuring proceeds by way of an arrangement between the debtor and the creditor, and it is difficult to assume the latter's outright concurrence with whatever the mining sector proposes. To illustrate this statement it is enough to compare the amount of debt proposed to be restructured (PLN 15,143.7 million) with the amount being currently restructured (PLN 1,403 million) under concluded arrangements. As of now, i.e. one year before expiration of the Act on Restructuring, it accounts for only 1/10 of the amount planned to be restructured.

Upon commencement of the reforms, the sector was indebted for PLN 13.3 billion and by the end of 2000 the debt reached PLN 22 billion. As of September 30, 2001, the debt was equal to PLN 20.1 billion. It should be noted that for the past year the level of debt has been stable and even slightly declined.

The largest problem faced by the Reform is the lack of use of the restructuring mechanisms provided for in the Act on Aligning (...). Conclusion of debt restructuring arrangements according to the status as of June 30, 2001 for the total of PLN 1,403 million is not a satisfactory outcome. Without fully setting in motion the restructuring processes the economic situation of particular entities will not improve. The main problem of

coal companies is currently their lack of liquidity. In this situation the positive financial result reported at the end of 2001 will not be a permanent development.

## **5.2. Steel Sector**

Due to the fact that liabilities to the state budget and ZUS represent a relatively small percentage of steelworks' total debt and their risk of bankruptcy is related to their huge indebtedness to suppliers and cooperants, mainly under bank borrowing, the following solutions have been applied using the debt restructuring model.

Liabilities, together with interest, to the state budget and the Labor Fund will be deferred till December 31, 2005 and subsequently their repayment will be spread into installments until 2010.

Trade liabilities, debts under bank borrowing and liabilities to ZUS may be repaid with bonds. Due to the steelworks' low creditworthiness (business credibility) in the financial market handling of the bond issue was entrusted to a special government agency which restructures enterprises. Agencja Rozwoju Przemyslu S.A. is a shareholder in approx. 700 enterprises, many of which it manages directly, and additionally has at its disposal funds for their restructuring. Proceeds from the bond issue or facilities taken by the Agency may be used to repay civil law liabilities and debts to ZUS. In return the Agency will take up shares in steel companies. The government may provide guarantees and sureties for up to PLN 600 million for the obligations resulting from the bonds issue or for the credit repayment. The debt restructuring process in the steel sector has not commenced.

## **5.3. Railways**

With respect to PKP's liabilities the following solutions have been adopted. Repayment of the principal will be deferred and spread into installments. The debt should be repaid by 2005. At that time interest on the debt will be cancelled.

Restructuring of debts to the public sector has not commenced. As a priority, railways repay their trade liabilities.

## **6. Summary**

Despite the use of various methods and sources of financing the restructuring process, the involvement of the state budget is significant. However, restructuring efforts have been necessary. The high indebtedness of these sectors is dangerous not only for public finances, also civil law liabilities to suppliers are destructive for the business environment of a given sector.

The need to take up these reforms has put the Polish government in a very difficult situation. As the financial condition of the mining, steel and railways sectors affects directly the status of public finances until the restructuring processes are completed and the sectors turned around the state budget situation will not be easy.

The slower economic growth in 2001 and the accumulation of problems in the public finance sphere have caused that this year's budget is extremely difficult. The need to save and to reduce expenditure refers to each discipline financed by the state budget. Savings had to be sought also in financing the restructuring process. Under the most costly program for the state budget, restructuring of the mining sector, it was decided at the beginning of the Program that mining companies should be relieved for the duration of the Reform of the obligation to finance the cost of coal allowances (or cash equivalents) for retired miners. For the reasons named above it became necessary to shorten that period by one year. In consequence, in 2002 mining companies will incur expenditure to that end of approx. PLN 161 million. It should be noted that the most

costly mining program has a great chance to be successful, which is an incentive for continued efforts to improve the structure of the Polish economy. One year before the conclusion of the restructuring program the mining sector has shown a net profit for the first time over a decade. This example is positive, especially since no other country in the world has ever reformed its mining sector at such a pace and on such a grand scale. The other two restructuring programs are still at the initial stage of implementation and it is difficult to attempt to sum them up.

