STATE AID CONTROL IN THE FINANCIAL CRISIS

From rescue to restructuring and to resolution

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Jacques Derenne, member of the Brussels and Paris bars
Partner, Head of EU Competition & Regulatory
Professor, University of Liège & Brussels School of Competition
Outline

• Basics of EU State aid control
  - Notion of "State aid"
  - Compatibility assessment & procedure
    > Commission & national courts

• Before the crisis

• Pending the crisis – Evolution
  - rescue, restructuring, sovereign debt, towards resolution tools

• New set of legislative rules since 2013
  - Single Resolution Mechanism
Notion of State aid (Article 107 (1) TFEU)

- **Advantage** ("in any form whatsoever" - "favouring")
- **Selective** ("certain")
- Transfer of State resources and imputability to the State ("granted by a Member State or through State resources")

- Risk of distortion of competition
- (likely to) Affect trade between Member States

Competition between Member States: need for a supranational, independent arbitrator (European Commission)
Compatibility assessment (Article 107 (3) TFEU) 
Procedure (Article 108 TFEU)

- **Unlawful aid ("illegal")**
  - aid not notified
  - aid notified but implemented before Commission decision
  - misuse of existing aid

- **Incompatible aid**
  - lawful or unlawful aid
  - aid not exempted
    - various types of exemptions

- **National courts**
  - obligation to protect subjective rights of third parties
  - ensure that Commission can carry out its compatibility assessment
  - no stay of proceedings
  - enforce Commission negative decisions

- **Exclusive powers of Commission**
  - Compatibility assessment
  - prohibition to implement incompatible aid
  - obligation to order recovery if unlawful
Before the crisis: traditional approach
Financial crisis - outbreak

- Liquidity or solvency problems
- Affecting fundamentally sound banks
- Systemic effect
  - Stability of the entire financial system in jeopardy
  - Potential impact on the whole economy
- Member States intervened on an unprecedented scale by granting State aid in order to
  - Prevent collapsing of further banks
  - Restore the provision of credit
Traditional approach outside the crisis

- Banking sector subject to State aid control
- Rescue & Restructuring 2004 Guidelines (107(3) c) TFEU)
  - rescue aid
    > temporary (six months)
    > non structural measure (reversible)
  - restructuring aid
    > restructuring plan
    > long term viability
  - own contribution
    > aid limited to the minimum necessary
- compensatory measures
  > avoid undue distortions of competition
Pending the crisis: evolution of the Commission's approach
October 2008 – March/April 2009

• October 2008: on the edge...
  - "State aid rules are part of the solution not of the problem"
• Urgency
  - need for guidelines and legal certainty
  - flexibility
• Avoid the systemic crisis
  - "sound" and "unsound" / distressed banks
  - beyond 6 months
  - structural rescue measures
  - but consistency with the principles
    > limited in scale and time
    > prevent undue distortions of competition
    > own contribution (remuneration)
• A co-ordinated approach
  - aid regimes

• Κρίσις, κρίσεως
• Κρίνω
• Κρασίς
New legal basis: Article 107(3) b) TFEU

- "aid to remedy a serious disturbance in the economy of a Member State"

- Three precedents
  - 1975 (V Report, § 133); 1987 (OJ L 76/18); 1991 (XXI Report, § 251)

- Rejections
  - CL (OJ 1995 L 308/92); GAN (OJ 1997 L 78/1); NR (NN 70/07); WestLB (NN 25/08); Sachsen LB (C9/08)

- CJEU: "regional disturbance is insufficient"
  - T-132/92 & T-143/96, Freistaat Sachsen
  - C-301/96, Germany v Commission

- Since 2008: over 300 aid schemes and individual decisions
  - €4.5 tn (around 25% of EU GDP)
Financial crisis – main principles

• Proportionate aid measures
  - aid limited to the minimum
  - contribution by the beneficiary

• Return to long term viability
  - well targeted aid
  - stress tests
  - restructuring plan if needed

• Avoiding undue distortions of competition
  - structural and behavioural remedies
Financial Crisis – [2008-2010]
Source: Commission Staff Working Paper, October 2011

Figure 5.1: Evolution of EURIBOR-OIS spread and of State aid support to the financial sector pledged by Euro Area Member States

EURIBOR-OIS spread* measures the confidence of banking institutions in their counterparts - a high spread indicates a low level of confidence. It is an indirect indicator of the health of the banking system.

EURIBOR-OIS spread* (rhs)

Aid pledged (asset and liability side) by Euro Area Member States (lhs)

Source: Ecowin; Commission services
* Spread between EURIBOR (interbank market rate) and OIS (overnight rate swap index)
Compatibility assessment of aid to banks since October 2008
Summary of developments

- **13 October 2008 – 31 July 2013**
  - Communications (Banking, Recapitalisation, Impaired Assets, Restructuring, Prolongation)
  - Focus on rescue aid, then restructuring

- **1 August 2013 – 31 December 2014**
  - New Banking Communication
    > More effective restructuring process
    > Strengthened burden-sharing requirements (shareholders, subordinated debtholders)
    > Assets quality reviews, stress tests

- **1 January 2015 – 31 December 2015**
  - Bank Resolution and Recovery Directive (BRRD)
    > default option is insolvency if not "resolved" in the public interest
    > exception: "precautionary recapitalisation"

- **1 January 2016**
  - Bail-in requirement
    > at least 8% of liabilities, senior debt, uncovered deposits
New legislation beyond State aid rules (1)

Crisis prevention

• Stronger prudential requirements
  
  - Capital Requirements Directive IV
    
    > Directive 2013/36/EU
    
    > Sufficient level of capital
      
      • Quantity
      
      • Quality
    
  
  - Single Supervisory Mechanism (SSM)
    
    > Regulation No 1024/2013
    
    > ECB empowered for the supervision over banks in the euro area
New legislation beyond State aid rules (2)
Tools to deal with unsound or failing banks


- Each institution to prepare a full recovery plan setting measures
  - dismissing management and appointing temporary administrator
  - convening a meeting of shareholders to adopt urgent reforms
  - prohibiting the distribution of dividends or bonuses, etc.

- Resolution authority in each Member State
  - resolution plan for each individual firm, “failing or likely to fail”
  - most appropriate resolution tools in each scenario
  - effect private sector acquisitions
  - transfer business to temporary structure
  - asset separation (“good bank/ bad bank”)
  - investors and creditors to be bailed-in before public funds can be used.
New legislation beyond State aid rules (3)
Tools to deal with unsound or failing banks

2. Regulation No 806/2014 (SRM) (1.1.2016)

- Single Resolution Mechanism (SRM)
  - to ensure that the complicated resolutions (e.g. in case of cross border resolutions) can be managed more efficiently with binding effect for all Member States.

- SRM built around
  - Single Resolution Board (SRB)
  - Single Resolution Fund (SRF).


- Strengthens the protection of tax payers' deposits in case of bank failures (deposits to be guaranteed up to €100 000 per depositor).
Current rules applying to the Commission’s assessment

• Two-fold assessment in case of resolution:
  - compatibility under the 2013 Banking Communication
  - compliance with BRRD provisions.

• Recent examples
  - Italy
    > Banca Romagna, 2/07/2015, case SA.41924
    > 4 banks, 22/11/2015, cases SA.39543, SA.41134, SA.41925, SA.43547
  - Hungary
    > Magyar Kereskedelmi Bank (MKB), 16/12/2015, case SA.40441
  - Portugal
    > Banco Internacional do Funchal, 21/12/2015, case SA.43977
  - Croatia
    > Resolution scheme for small banks, 5/10/2016, case SA.46066
Unpacking Complexity
Unfolding Opportunity
Thank you for your attention!

Jacques Derenne
Partner, Head of EU Competition & Regulatory
Tel: 32 2 290 7905
jderenne@sheppardmullin.com