Bundesverband der Deutschen Volksbanken und Raiffeisenbanken e. V.
Bundesverband deutscher Banken e. V.
Bundesverband Öffentlicher Banken Deutschlands e. V.
Deutscher Sparkassen- und Giroverband e. V.
Verband deutscher Pfandbriefbanken e. V.

Die Deutsche Kreditwirtschaft

Comments

by the German Banking Industry Committee[1] on the COMMUNICATION FROM THE COMMISSION on the Draft Commission Notice on the notion of State aid pursuant to Article 107(1) TFEU

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Berlin, 10 March 2014

The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent more than 2,000 banks.

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[1] EU Register of Interest Representatives Number: 52646912360-95.

I. Preliminary comments

As part of its initiative to modernise the EU State aid rules, the EU Commission proposed specifying the notion of State aid. Based on the foregoing, the EU Commission conducts a Consultation on its Draft Communication on the notion of State aid. After its adoption, the Communication should serve as practical guidance for the determination of State aid pursuant to Article 107(1) of the Treaty on the Functioning of the European Union (TFEU).

The Commission announced its Communication on the notion of State aid as early as May 2012, i.e. already in its "EU State Aid Modernisation (SAM)" Communication. [Yet,] The publication of a draft was postponed several times. On 17 January 2014, the EU Commission published a draft which, initially, was available in English only and which allows an eight-week deadline for consultation purposes (instead of a window of time of three months, minimum, which used to be available for other State aid consultation documents). Given the scope of the Communication, we hold the view that a profound legal analysis of the interpretation of the Communication's legal provisions would require a significantly longer consultation period than two months.

Hence, the present comments by the apex associations cooperating under the auspices of the German Banking Industry Committee (Bundesverband der Deutschen Volksbanken und Raiffeisenbanken, Bundesverband deutscher Banken, Bundesverband Öffentlicher Banken Deutschlands, Deutscher Sparkassen- und Giroverband und Verband deutscher Pfandbriefbanken) are merely focusing on a limited number of issues.

II. Serious concerns over the *de facto* expansion of the EU Commission's mandate

The notion of State aid is defined by the treaty on the Functioning of the European Union (TFEU). In this regard, there is no scope for discretionary assessments on the part of the EU Commission. Based on the foregoing, also the Communication on the State aid notion shall be entirely without prejudice to the European Courts. After all, the TFEU's interpretation and application shall be exclusively incumbent upon the latter.

However, contrary to this, we believe that due to its binding effect upon the EU Commission, the Communication itself will become *de facto* applicable and legally binding also upon Member States; its impact will go far beyond a mere specification of State aid rules aimed at facilitating an easier, more transparent and more consistent application of the State aid notion. In our view, the EU Commission thus expands the scope of its regulatory mandate. In the final analysis, by virtue of its selective choice (of certain rulings) the Commission prejudges the interpretation of the case-law established by European Courts. This results in a *de facto* interpretation *sui generis* of the State aid notion which is subsequently supposed to be legally binding upon all Member States and the EU Commission. Yet, this is not covered by the scope of the EU Commission's mandate.

Notwithstanding this general criticism, we appreciate the present opportunity to share our comments on a number of individual, non-exhaustive issues contained in the current Communication.

III. Comments on individual rules concerning the principle of the market economy operator (MEO)

- **Point 4.2.3.3. Counterfactual analysis in the case of prior exposure to the undertaking concerned**

Point 109 sets out: *"The fact that the public entity concerned has prior economic exposure to an undertaking (for instance, if it is an equity holder or if it has provided loans or guarantees) should be taken into consideration when examining whether a transaction is in line with market conditions. However, such prior exposure should not in itself be the result of previous State aid or of an intervention that was not carried out on market terms."*

In our view it is inappropriate for the Commission to interpret the wording in combination with the court ruling on Bank Burgenland to the effect that in the event where there is a prior exposure that was subject to State aid terms, there shall no longer be eligibility for meeting the criterion of an MEO. Such an interpretation by the EU Commission is at odds with the Court of Justice of the European Union ruling in the Case T-11/95 BP Chemicals v Commission quoted in footnote 132. Under point 170, the Court points out that "the mere fact that a public undertaking has already made capital injections into a subsidiary which are classed as 'state aid' does not automatically mean that a further capital injection cannot be classed as an investment which satisfies the private market economy investor test".

Hence, the Court concludes that any individual State transaction shall, on principle, have to be reviewed separately concerning satisfaction of the market economy operator test if several subsequent exposures are not deemed to feature any direct time-related, structural and economic link.

Similarly, in the pending case "Kingdom of the Netherlands and ING Groep NV v European Commission", the opinion of the Attorney General expresses the view "that, if that amendment is assessed as a separate measure, it becomes quite possible to compare the State's behaviour with that of a private investor". From the point of view of the Attorney General, the crucial question is: "Would it have been rational for a private investor who, for whatever reason, held securities on the same terms, and who was attentive to market conditions, to have agreed to the same amendment to those terms?" (Point 40f.)

Furthermore, such an interpretation would be equally backed by point 84 of the present Draft Communication. Under the Draft Communication, the Commission explicitly points out that "when the later intervention was a result of unforeseen events at the time of the earlier intervention, the two measures should normally be assessed separately".

In our view, for subsequent exposures, satisfaction of the market economic operator test can also, in principle, be achieved where there is a prior exposure of State entities that is in line with State aid. For instance, if and when a loan is extended to a competitive company at a point in time where it is not yet evident that this company will subsequently become financially distressed (i.e. if thus the respective State driven follow-up aid measures were not foreseeable at the point in time of the first-time loan approval) this lack of a time-related and economic link between the first and the subsequent loan means that any potential, subsequent loans should be examined separately on the basis of the economic market operator (MEO) test. This is also in line with current market practices and the rationale applied by banks in such cases.

Under this approach, where the subsequent loan exclusively serves the purpose of stabilising prior exposures or, moreover, avoiding / minimising sovereign losses, it has to be permissible also for the State (following aid compliant first-time loans subject to the EU State aid rules as part of a subsequent exposure) to show that he meets the market economy operator test. Thus, the State would behave like any other private creditor who extends subsequent loans in cases where this can prevent a loss of the prior exposure.

However, barring state creditors (contrary to private creditors) from "rescuing" their prior exposure where such rescue operation is in line with current market practices is incompatible not only with the economic market operator (MEO) criterion but would also distort the level playing field for public as opposed to private creditors. After all, the underlying rationale behind the MEO criterion consists precisely in allowing governments to behave like any private creditor. In the final analysis, such an unequal treatment would lead to a breach of the non-discrimination principle enshrined in the EU's *acquis communautaire;* what is more, it would also be a violation of the entrepreneurial freedom protected as a basic right under Art. 16 of the Charter of Fundamental Rights.

Furthermore, under the provisions of the Draft Communication, the MEO criterion should be deemed to have been met at least in cases where - under similar economic conditions and along with the public creditor - also private creditors carry out parallel support interventions with regard to their exposure. In this case, based on a comparison with the behaviour of a given private creditor, the State would even render the specific benchmark test. Also from the EU Commission's point of view, this is ideal proof for the presence of public entities' behaviour that is in line with market conditions.

The EU Commission has not carried out any comprehensive analysis of the existing court rulings with regard to the MEO criterion. In this context, we refer to the following case-law: Hamsa, EDF and ING Groep NV (Hamsa v. Commission [2002] ECR II 3049; EDF [2012] C-124/10; ING Groep NV v. Commission T-29/10 and T-33/10). In our view, this case-law unequivocally clarifies that the application of the MEO criterion as part of a case-by-case assessment shall and must be based on the benchmark of a hypothetical private creditor. In our view, the conclusion that a change in the repayment terms - for instance due to a capital injection (in the form of State aid) - constitutes *ipso facto* State aid is inadmissible according to the ING decision. Based on the foregoing and in line with the existing case-law, we consider that the application of the EMO criterion shall also be appropriate for scenarios where the intervention that needs to be assessed was preceded by a State intervention which did not take place under market conditions but under conditions that were in line with state aid.

- **Point 4.2.3.4. Specific considerations to establish whether the terms for loans and guarantees are in line with market prices**

Point 116 reads as follows: "*It should be recalled that this reference rate [EU reference rate] is only a proxy. ….. If comparable transactions have typically taken place at a lower price than that indicated as a proxy by the reference rate, the Member state can consider that this lower price is the market price."*

In our understanding, this wording is based on the assumption of a general rule subject to exceptions with regard to the application of the EU reference rate structure is based on rules / exceptions.

Based on decision-making practise established by the EU Commission, the question of the absence of State aid or, moreover, the calculation of the State aid element in loans shall be based on the EU Commission's EU reference rate. Hence, based on a risk adjusted assessment approach, the EU reference rate should be either the no-aid benchmark or the benchmark for identification of the aid amount under a promotional loan.

This approach makes sense both in terms of the underlying economics and also on the grounds of practicality. Particularly in the event of broad based schemes with low aid amounts, the identification of suitable specific market benchmarks would incur a high level of legal uncertainty along with huge administrative costs in the absence of any tangible competitive benefit for companies. The EU Commission has also drawn the economically correct conclusions from this by consistently requesting in its precedent decision-making practise that reference rate be used as a benchmark for the identification of the aid amounts / no-aid verification of loans extended under promotional schemes. Hence, on the grounds of legal certainty and consistency, the EU Commission should not depart from its decision-making practise.

We understand that the EU Commission perceives a need to carry out a case-by-case analysis on the basis of specific market benchmarks for comparable funding instruments when it comes to large projects with a considerable funding scope. In this context, such an approach is helpful indeed. After all – as opposed to broad-based schemes - large investment projects may have a considerable impact on competition between different Member States. Based on the foregoing, it should be permissible to interpret the aforementioned paragraph within this meaning, too.