



EUROPEAN COMMISSION

Brussels, 30.9.2011
C(2011) 7056 final

**Subject: State aid n° SA.33103 (2011/N) – Spain
Recapitalisation of Catalunya Banc**

Madam,

1 PROCEDURE

- (1) On 26 March 2010, Spain informed the Commission that the *Fondo de Reestructuración Ordenada Bancaria* ("the FROB")¹ had resolved to participate in the integration project of three saving banks, namely Caixa Catalunya, Caixa Tarragona and Caixa Manresa, creating the CatalunyaCaixa Group (hereafter "CatalunyaCaixa") with assets totalling EUR 81 billion². The FROB agreed to subscribe for EUR 1 250 million of convertible preference shares in CatalunyaCaixa.
- (2) On 31 March 2010, the Commission services considered that the requirements for CatalunyaCaixa to benefit from the FROB were met (concluding that, based on the Bank of Spain's assessment, the merging entity was fundamentally sound and its integration plan was viable, so that there was no need for a restructuring plan) and informed the Spanish authorities accordingly.

¹ The FROB has been established, in the context of the financial crisis, to provide public support for the consolidation of the Spanish banking sector by, inter alia, strengthening the capital buffers of credit institutions. The FROB has an initial funding capacity of EUR 9 billion, of which EUR 6.75 billion is contributed by the State Budget and the rest (EUR 2.25 billion) is contributed by the Deposit Guarantee Funds. The Commission adopted on 28 January 2010 a decision not to raise objections (case N 28/2010, OJ C57 of 9.3.2010, p. 2) on the FROB as a recapitalisation scheme for fundamentally sound institutions.

² As of 31 December 2009.

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- (3) On 28 July 2010, the FROB subscribed for convertible preference shares issued by CatalunyaCaixa for a total amount of EUR 1 250 million, representing 2.37% of its risk weighted assets³.
- (4) On 18 February 2011, Spain adopted a reinforced solvency framework⁴ for its entire banking sector, which, inter alia, obliged all credit institutions to meet higher solvency levels by 30 September 2011⁵. As a result of the new legislation, the Bank of Spain informed CatalunyaCaixa on 10 March 2011 that under the new regime it required EUR 1 718 million of additional capital in order to meet the 10% solvency ratio⁶ (known as "capital principal") over its risk weighted assets,.
- (5) On 28 March 2011, CatalunyaCaixa formally requested from the FROB the amount of EUR 1 718 million, while analysing other alternatives measures to reduce that amount.
- (6) On 26 April 2011, the Spanish authorities submitted to the Commission a draft recapitalisation plan for CatalunyaCaixa in accordance with the new solvency framework approved by the Spanish authorities in February 2011.
- (7) On 28 July 2011, CatalunyaCaixa transferred its financial business to a newly established banking entity, Catalunya Banc S.A (hereafter "Catalunya Banc"). The transfer did not extend to the charitable function (Obra Benéfico Social – "OBS"), which remained in the saving bank, CatalunyaCaixa.
- (8) On 23 September 2011, the Spanish authorities notified to the Commission their intention to inject additional capital of EUR 1 718 million into Catalunya Banc since Catalunya Banc was not able to raise funds in financial markets or through another private solution. The FROB is in the process of completing the valuation of Catalunya Banc carried out by three independent valuers on its behalf. On the basis of that valuation the FROB will inject EUR 1 718 million in the form of new ordinary shares issued by Catalunya Banc.
- (9) Spain exceptionally accepts that the decision be adopted in the English language.

2 DESCRIPTION OF THE MEASURE

2.1 The beneficiaries

- (10) The CatalunyaCaixa Group includes CatalunyaCaixa, a Spanish saving bank⁷, as parent entity and other subsidiaries providing a range of financial services. It is the result of the

³ As of 31 December 2009.

⁴ See Royal Decree-Law 2/2011 of 18 February 2011: "Real Decreto-ley 2/2011, de 18 febrero para el reforzamiento del sistema financiero".

⁵ This deadline may be extended under certain limited circumstances.

⁶ According to article 1 of Royal Decree-Law 2/2011 of 18 February 2011 on the strengthening of the Spanish financial system, the so called "core capital ratio" is to be required on a consolidated and solo basis.

⁷ "*Cajas de ahorros*" are credit institutions that have no shareholders, but instead are governed by their members. Their legal form is a private charity that holds a banking license and is entitled to provide banking services as commercial or cooperative banks do. Profits are partially used to strengthen their capital and the remainder is used to fund the social activities that each *caja de ahorros* carries out through its OBS.

merger carried out on 1 July 2010 of three savings banks, Caixa d'Estalvis de Catalunya, Caixa Tarragona and Caixa Manresa. That merger was implemented within the framework of the FROB.

- (11) Within the framework of the Spanish Royal Decree of 18 February 2011, CatalunyaCaixa transferred on 28 July 2011 its banking business to a newly established banking entity, Catalunya Banc S.A CatalunyaCaixa now exercises its financial activities indirectly through Catalunya Banc. The charitable function (OBS) has remained in the saving bank, CatalunyaCaixa.
- (12) Catalunya Banc operates mainly in the region of Catalonia reaching a market share of [12-13%*] in deposits and [11-12%] in loans to customers. At a national level its market share is around [2-3%] in deposits and [3-4%] in loans to customers⁸. It ranks fourth among Spanish saving banks by assets.
- (13) Catalunya Banc's main figures are:

	30.06.2011	
Total assets	[75-76 000]	million €
Loans to customers	[50-52 000]	million €
Retail deposits	[26-29 000]	million €
Total wholesale funds	[31-33 000]	million €
Employees	7 338	
Number of branches	1 219	

* Business secret: contains confidential information, where possible, figures have been replaced by ranges in [brackets].

⁸ At 31 December 2010.

2.2 The aid measures already received by the beneficiary

- (14) In the context of the Spanish recapitalisation scheme approved by the Commission on 28 January 2010⁹, CatalunyaCaixa benefited from a recapitalisation measure of EUR 1 250 million via convertible preference shares¹⁰ ("FROB I measure") on 28 July 2010.
- (15) CatalunyaCaixa has benefited from the Spanish Guarantee Scheme¹¹ since its creation. Outstanding guaranteed senior debt currently amounts to EUR [...].

2.3 The events triggering the measure

- (16) Following the outbreak of the financial crisis in 2008, the Spanish authorities laid down via the Royal Decree-law 9/2009 the legal foundations for the restructuring of the savings bank sector. The sector had several structural limitations, such as the legal restrictions on the raising of capital and a complex and weak corporate governance system. CatalunyaCaixa benefited from a first capital injection from the FROB to support the merger of the three savings banks and its restructuring¹².
- (17) In July 2010, CatalunyaCaixa failed the stress test of the Committee of European Banking Supervisors (CEBS) with a capital shortfall of EUR 1 032 million, even though the stress test exercise incorporated the FROB I measure.
- (18) Catalunya Banc still faces important challenges: high exposure to real estate sector¹³ which drives up its non-performing loans¹⁴, structural funding and liquidity issues with constrained access to wholesale market and a loan-to-deposit ratio of [...], as well as exerted pressure on its net interest because of the heightened competition for deposits currently evident in the Spanish banking sector¹⁵. Its rating is Ba2, with a negative outlook.
- (19) In March 2011, following the new solvency requirement to reach 10% of capital principal over its risk weighted assets by 30 September 2011, the Bank of Spain communicated to CatalunyaCaixa the need to recapitalise the entity up to EUR 1 718 million.

9 Commission Decision in Case N28/2010, Recapitalisation measures in favour of the banking sector in Spain, OJ C57 of , 9.3.2010, p.2.

10 The FROB I securities constitute perpetual convertible preference shares and are part of the non-core Tier 1 capital of the beneficiary. The annual coupon is a minimum of 7.75% with an additional fifteen basis points as a step up clause every year until the fifth year.

11 The Commission adopted on 1 June 2011 a decision not to raise objections (SA 32990/N) on the fifth prolongation of the Spanish Guarantee Scheme for credit institutions.

12 The merger involved an integration plan, approved by Bank of Spain, setting out the commercial strategy of the group, rationalising the branches network and the workforce.

13 The overall exposure of Catalunya Banc to the real estate sector represents [...] of its balance sheet.

14 The non-performing loan ratio stood at 5.7% on 31 March 2011.

15 CatalunyaCaixa has been offering high interest rates on savings accounts (up to 5%).

- (20) In July 2011, CatalunyaCaixa failed the European Banking Authority (EBA) stress test exercise with a core tier 1 ratio of 4.8%¹⁶.

2.4 The additional aid measure: measure to strengthen Catalunya Banc's capital position

- (21) In December 2010, as the result of the capital shortfall detected in the 2010 CEBS stress test exercise, CatalunyaCaixa applied to the FROB again for an additional recapitalisation of EUR [...] in the form of preference shares. However, following the increase of the solvency requirements in February 2011, CatalunyaCaixa suspended that recapitalisation application to the FROB. Instead it requested a further recapitalisation measure from the FROB in favour of Catalunya Banc in the form of ordinary shares.
- (22) Catalunya Banc's failure to meet the new regulatory capital requirements has triggered the need for an additional recapitalisation, in order to achieve the 10% risk weighted assets solvency ratio required by Spanish legislation.
- (23) The recapitalisation will be achieved through issuance of EUR 1 718 million of ordinary shares by Catalunya Banc. The capital injection represents 3.5% of the bank's risk weighted assets as of 30 December 2010. The subscription will be done on the basis of a valuation of Catalunya Banc which will be carried out by three independent valuers.

3 POSITION OF THE SPANISH AUTHORITIES

- (24) The Spanish authorities accept that the measure constitutes State aid and request the Commission to verify if the proposed measure is compatible with the internal market on the basis of Article 107(3)(b) of the Treaty on the Functioning of the European Union ("the TFEU"), as it is necessary in order to remedy a serious disturbance in the Spanish economy.
- (25) In particular, the Spanish authorities submit that the measure is (i) appropriate and well-targeted; (ii) necessary and limited to the minimum amount necessary; and (iii) proportionate as designed to minimize negative spill-over effects on competitors.
- (26) *Appropriate and well-targeted.* The Spanish authorities submit that Catalunya Banc is important within the Spanish financial system, especially in its geographical operating area¹⁷.
- (27) *Necessary and limited to the minimum amount.* The Spanish authorities submit that the measure proposed is required to bring Catalunya Banc's solvency position in line with the new solvency requirements in Spain. In addition, the measure is limited in size to what is necessary to ensure that Catalunya Banc and CatalunyaCaixa meet a solvency ratio of 10% of its risk weighted assets required by the Spanish banking rules¹⁸.

¹⁶ Under the EBA definition of core tier 1, the generic provisions and the convertibles bonds are not taken into account. Had they been taken into consideration, CatalunyaCaixa's core tier 1 ratio would have reached 6.3%.

¹⁷ Catalunya Banc's market share in deposits in the region where it operates is [12-13%].

¹⁸ See footnote **Error! Bookmark not defined.**.

- (28) Finally, the Spanish authorities observe that the measure is limited in time since it will form part of a restructuring plan that will be developed by Catalunya Banc. The restructuring plan is to be approved by the Bank of Spain and will be notified to the Commission thereafter.
- (29) *Proportionate*. The Spanish authorities submit that the terms and conditions of the measure proposed together with the terms and conditions imposed on Catalunya Banc contain an extensive range of safeguards against possible abuses and distortions of competition.
- (30) The Spanish authorities have also provided the following specific commitments:
- (i) To notify to the Commission for approval any increase in the principal amount of the measure proposed;
 - (ii) To suspend any payments by CatalunyaCaixa to the OBS for new projects;
 - (iii) To refrain from distributing any dividend and from making any payments on hybrid instruments, unless those payments stem from a legal obligation, and not to exercise a call option on the same instruments without prior approval of the Commission; in addition before undertaking any other capital management deals (e.g. buy-back) on hybrid instruments and/or any other equity-like instruments, Catalunya Banc must consult with the Commission in advance;
 - (iv) To seek prior approval of the Commission before amending any commitments or constraints mentioned in this decision;
 - (v) To notify a restructuring plan within six months as of the date of the adoption of the decision in line with the principles laid down in Commission's Communication on the return to viability and the assessment of the restructuring measures in the financial sector ("the Restructuring Communication")¹⁹ and the Commission Communication on "The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis" ("the Banking Communication")²⁰.

4 ASSESSMENT

4.1 Existence of State Aid

- (31) The Commission first has to assess whether the measure constitutes State aid within the meaning of Article 107(1) TFEU. According to that provision, State aid is any aid granted by a Member State or through State resources in any form whatsoever which distorts, or threatens to distort, competition by favouring certain undertakings, in so far as it affects trade between Member States. The Commission in that context observes that the Spanish authorities do not dispute that the measure constitutes State aid.
- (32) The Commission observes that the intervening authority, the FROB, is directly financed through State resources.

¹⁹ OJ C195, 19.8.2009, p. 9.

²⁰ OJ C 270, 25.10.2008, p. 8.

- (33) In addition, the measure confers a selective advantage on the beneficiary of the aid, Catalunya Banc, and thereby on CatalunyaCaixa. In particular, the measure provides capital and allows Catalunya Banc to restore its regulatory solvency ratio and to avoid technical insolvency. As regards CatalunyaCaixa, the measure allows it to restore its regulatory solvency ratio and to honour its obligations to the OBS with both the assets and liabilities not contributed by it to Catalunya Banc as well as with the dividend flow obtained from its equity stake in Catalunya Banc.
- (34) As regards the advantages conferred by the measure being provided by the State, the Commission notes that it would not have been provided by a market economy investor expecting a reasonable return on his investment particularly in light of its size.
- (35) The Commission finds that the measure distorts competition as it allows Catalunya Banc (and Catalunya Caixa which runs the banking activity through Catalunya Banc) to obtain the capital necessary to avoid technical insolvency and its exit from the market.
- (36) The Commission finds that the measure is also likely to affect trade between Member States because Catalunya Banc competes on the Spanish retail market, the mortgage lending markets and the commercial lending markets. In all those markets, some of Catalunya Banc's competitors are subsidiaries and branches of foreign banks.

Conclusion

- (37) On the basis of the forgoing, the Commission considers that the measure fulfils all the conditions laid down in Article 107(1) TFEU and that this measure qualifies as State aid to Catalunya Banc and to CatalunyaCaixa.

4.2 Compatibility of the aid

- (38) As regards compatibility with the internal market of the aid provided to Catalunya Banc and CatalunyaCaixa, the Commission must first determine whether the aid can be assessed under Article 107(3)(b) TFEU, i.e. whether the aid remedies a serious disturbance in the economy of Spain. Subsequently, the Commission, using that legal basis, has to assess whether the measure proposed is compatible with the internal market principle.

4.2.1 Legal basis for the compatibility assessment

- (39) Article 107(3)(b) TFEU provides that aid falling within the scope of Article 107(1) TFEU may be regarded as compatible with the internal market where it "*remedies a serious disturbance in the economy of a Member State*".
- (40) Given the present circumstances in the financial markets, the Commission considers that the measure may be examined under Article 107(3)(b) TFEU. The Commission has acknowledged in its approval of the Spanish scheme²¹ that there is a threat of serious

²¹ See Commission Decision N 28/2010, OJ C 57, 9.3.2010 p.2 and Commission Decision N 317/2010, OJ C 242, 9.9.2010, p. 2.

disturbance in the Spanish economy and that State support of banks is suitable to remedy that disturbance. Despite a slow economic recovery that has taken hold since the beginning of 2010, the Commission still considers that requirements for State aid to be approved pursuant to Article 107(3)(b) TFEU are fulfilled in view of the reappearance of stress in financial markets. The Commission confirmed that view by adopting in December 2010 a Communication that prolongs until 31 December 2011 the application of State aid rules to support measures in favour of banks in the context of the financial crisis²².

- (41) The Commission observes that market conditions remain difficult globally since the last quarter of 2008. The Commission notes that Spain in particular has been severely hit by the financial, economic and sovereign crisis. The economic downturn combined with the fall in property prices and the exposure of some Spanish credit institutions to land and property development loans have led to significant impairment of their asset portfolios.
- (42) The Spanish authorities have acknowledged that, given Catalunya Banc was unable to close its capital shortage before the established deadline either by capital-generating organic measures or by attracting fresh private capital, no alternative other than the capital injection by the FROB was available.
- (43) Without the proposed capital injection Catalunya Banc and CatalunyaCaixa, which has the control of the banking entity, would be non compliant with the new solvency framework with severe adverse impacts on other banks and the wider financial system in Spain. The assessment of the Spanish authorities is that the bank's weakness has the potential to inflict severe losses on other financial institutions, destabilising the Spanish financial markets and triggering a generalised confidence crisis at the present delicate juncture.
- (44) For those reasons the Commission accepts that in the current circumstances the recapitalisation in favour of Catalunya Banc, and accordingly of CatalunyaCaixa, is necessary to avoid a serious disturbance in the economy of Spain.

4.2.2 *Compatibility assessment*

- (45) In line with point 15 of the Banking Communication, in order for an aid to be compatible under Article 107(3)(b) TFEU it must comply with general criteria for compatibility under Article 107(3) TFEU, which imply compliance with the following conditions²³:
 - a. *Appropriateness*: The aid has to be well targeted in order to be able to effectively achieve the objective of remedying a serious disturbance in the economy. It would not be the case if the measure were not appropriate to remedy the disturbance.
 - b. *Necessity*: The aid measure must, in its amount and form, be necessary to achieve the objective. Thus it must be of the minimum amount necessary to reach the objective, and take the most appropriate form to remedy the disturbance.

²² Communication from the Commission from 1 January 2011, of State aid rules to support measures in favour of bank's in the context of the financial crisis, OJ C 329, 7.12.2010, p. 7.

²³ See paragraph 41 of Commission decision in Case NN 51/2008, *Guarantee scheme for banks in Denmark*, OJ C 273, 28.10.2008, p.2.

c. *Proportionality*: The positive effects of the measure must be properly balanced against the distortions of competition, in order for the distortions to be limited to the minimum necessary to reach the measure's objectives.

(46) The Recapitalisation Communication elaborates further on the three principles of the Banking Communication and states that recapitalisations can contribute to the restoration of financial stability. In particular the Recapitalisation Communication states that recapitalisations may be an appropriate response to the problems of financial institutions facing insolvency²⁴.

4.2.2.1 *Compatibility with the Banking and Recapitalisation Communications*

a. Appropriateness of the Measure

(47) The recapitalisation measure aims at reaching the minimum capital requirement of 10% for Catalunya Banc, and accordingly for CatalunyaCaixa, taking into account possible further losses stemming from its loan portfolio in the near future. The recapitalisation will be in the form of new ordinary shares in Catalunya Banc.

(48) The Commission considers that the measure is appropriate because it effectively meets its objective to ensure that Catalunya Banc and CatalunyaCaixa are in compliance with the regulatory capital requirements, and thus remedies a serious disturbance in the economy.

b. Necessity – limitation of the aid to the minimum

(49) According to the Banking Communication, the aid measure must, in its amount and form, be necessary to achieve its objective. That requirement implies that the capital injection must be of the minimum amount necessary to reach the objective. In that context, the Commission observes that the amount of the measure will ensure that Catalunya Banc, and CatalunyaCaixa, will again fulfil the regulatory capital requirements.

(50) As regards the remuneration Catalunya Banc has to pay, the FROB will receive no fixed remuneration on its capital injection given that the rescue aid is granted through ordinary shares. The FROB will only be remunerated if Catalunya Banc is in a position to pay out a dividend or if the equity stake taken by the FROB through the proposed measure is sold to a third party or bought back by Catalunya Banc at a profit.

(51) Based on the information available, the Commission is not in the position to ascertain whether there is a prospect for an adequate remuneration of the proposed recapitalisation. Paragraphs 15 and 44 of the Recapitalisation Communication explain that lower remuneration in duly justified cases can be accepted in the short-term for distressed banks on the condition that the lower remuneration will be reflected in the restructuring plan. The Commission considers that it is justified that no remuneration is paid for the recapitalisation measure provided that the absence of remuneration will be compensated by in-depth restructuring in the restructuring plan.

²⁴ Recapitalisation Communication, point 6.

c. Proportionality – measures limiting negative spill-over effects

- (52) Spain has committed that CatalunyaCaixa will suspend payments to the OBS for new projects. It has also committed that Catalunya Banc will suspend dividend and coupon payments on outstanding hybrid instruments unless those payments stem from a legal obligation, will not exercise a call option on the same instruments and will not carry out any other capital management deals (e.g. buy-back) on hybrid instruments and/or any other equity-like instruments without consulting with the Commission in advance.
- (53) Therefore, taking into consideration the difficulties that the Catalunya Banc is facing combined with the need to maintain financial stability in Spain, the Commission considers the measure to be sufficient to minimise the distortions of competition caused by the aid during the rescue period. That evaluation is, however, without prejudice to additional measures to address distortion of competition that may be needed to ensure that the restructuring plan of Catalunya Banc can be approved.

Conclusion

- (54) The Commission, thus, concludes that: (i) the recapitalisation measure is appropriate and necessary to restore the solvency position of Catalunya Banc and accordingly of CatalunyaCaixa, as it is limited to the minimum; (ii) Catalunya Banc must submit a restructuring plan within six months from the date of this decision, which will take account of the competitive impact of the support given by making commensurate provision for compensatory measures; and (iii) there are sufficient measures in place limiting the negative spill-over effects for other competitors to enable the Commission to temporarily approve the measure as emergency aid. The Commission can, therefore, temporarily approve the measure for six months.

4.2.2.2 Restructuring plan

- (55) As regards the need for an assessment of the institution's balance sheet and activities, the use of recapitalisation for a distressed bank can only be accepted on the condition of the bank's winding up or a far-reaching restructuring²⁵. The Commission furthermore observes that the Spanish authorities have committed to submit a restructuring plan for Catalunya Banc within six months.
- (56) The Commission, therefore, takes note of the commitment of the Spanish authorities to submit a restructuring plan for Catalunya Banc taking into account all aid measures CatalunyaCaixa and Catalunya Banc have received to date²⁶. The restructuring plan shall fulfil the requirements of the Restructuring Communication as regards return to viability, burden-sharing and measures limiting the distortion of competition. The restructuring plan should be submitted to the Commission within six months from the date of this decision.

²⁵ See point 44 of the Recapitalisation Communication.

²⁶ The total aid received by the FROB will amount to 5.87% of the entity's risk weighted assets.

CONCLUSION

- The Commission concludes that the measure notified (EUR 1 718 million of capital injection) in favour of Catalunya Banc and CatalunyaCaixa constitutes State aid pursuant to Article 107(1) TFEU.
- The Commission finds that the rescue aid in favour of Catalunya Banc and CatalunyaCaixa is temporarily compatible with the internal market for reasons of financial stability on the basis of Article 107(3)(b) TFEU. The measure is accordingly approved for six months or, if Spain submits a restructuring plan within six months from the date of this decision, until the Commission has adopted a final decision on the restructuring plan.
- The Commission recalls that the Spanish authorities have committed to submit an in-depth restructuring plan.
- The Commission notes that Spain exceptionally accepts that the adoption of the Decision be in the English language.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

http://ec.europa.eu/eu_law/state_aids/state_aids_texts_es.htm;

Your request should be sent by registered letter or fax to:

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Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President