



EUROPEAN COMMISSION

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C(2011) 7031 final

**Subject: State aid n° SA.33096 (2011/N) – Spain  
Recapitalisation of NCG Banco**

Madam,

## 1 PROCEDURE

- (1) On 29 June 2010, Spain informed the Commission that the *Fondo de Reestructuración Ordenada Bancaria* ("the **FROB**")<sup>1</sup> had resolved to participate in the integration project between *Caixa de Aforros de Vigo, Ourense e Pontevedra* and *Caja de Ahorros de Galicia* creating Novacaixagalicia, with total assets of EUR 76.2 billion<sup>2</sup>. The FROB agreed to subscribe for EUR 1 162 million of convertible preference shares in Novacaixagalicia.
- (2) On 29 June 2010, the Commission services considered that the requirements for Novacaixagalicia 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.
- (3) On 18 February 2011, Spain adopted a reinforced framework<sup>3</sup> for its entire banking sector, which inter alia, obliged all credit institutions to meet higher solvency levels by 30 September 2011. As a result of the new legislation, the Bank of Spain informed Novacaixagalicia on 10 March 2011 that it required EUR 2 622 million of additional capital in order to meet the 10% solvency ratio.

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<sup>1</sup> The FROB was established in 2009, 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. To date, the FROB has invested EUR 9.6bn in the recapitalisation of seven banking groups. The FROB's total budget amounts to EUR 99bn

<sup>2</sup> As of 31 December 2009.

<sup>3</sup> Royal Decree Law of 2/2011 of 18 February 2011.

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- (4) On 27 May 2011, the Spanish authorities submitted to the Commission a first draft recapitalisation plan for Novacaixagalicia drafted in accordance with the new legal solvency framework approved by the Spanish authorities in February 2011. The plan presented various alternatives for the intended recapitalisation of Novacaixagalicia.
- (5) On 24 June 2011, the Commission services provided their feedback on the first draft recapitalisation plan presented by the Spanish authorities.
- (6) On 14 September 2011, Novacaixagalicia approved the contribution of all of its banking assets and liabilities, with the exception of those attached to its *Obra Benéfico-Social* ("OBS")<sup>4</sup>, to NCG Banco S.A. ("NCG Banco") in exchange for all of the ordinary shares in NCG Banco.
- (7) NCG Banco failed to raise capital from private sources before the deadline established by the Spanish authorities.
- (8) On 23 September 2011, the Spanish authorities notified to the Commission their intention to provide NCG Banco with a capital injection of EUR 2 465 million through the FROB. The legal basis for the measure proposed is Article 9 of Royal Decree-Law 9/2009 of 26 June 2009, *on bank restructuring and credit institutions equity reinforcement*.
- (9) The FROB is in the process of completing the valuation of NCG Banco carried out by three independent valuers on its behalf. On the basis of that valuation the FROB will inject EUR 2 465 million in the form of new ordinary shares issued by NCG Banco.
- (10) Spain exceptionally accepts that the decision be adopted in the English language.

## **2 DESCRIPTION OF THE MEASURE**

### **2.1 The beneficiaries**

- (11) Novacaixagalicia is a Spanish saving bank ("*Caja de Ahorros*"), registered with the Bank of Spain as a result of the integration of two local savings banks ((*Caixa de Aforros de Vigo, Ourense e Pontevedra* and *Caja de Ahorros de Galicia*). Cajas de Ahorro 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.
- (12) NCG Banco is a commercial bank registered with the Bank of Spain. NCG Banco was incorporated on 14 September 2011 by Novacaixagalicia. Novacaixagalicia contributed all of its banking assets and liabilities to NCG Banco, with the exception of those attached to its OBS, in exchange for all the shares of NCG Banco. Those shares were valued at EUR [...\*] million. NCG Banco operates mainly in the region of Galicia in Spain where it has a 41,4% market share, while its market share at a national level is of around [2-3]%

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<sup>4</sup> OBS are charity institutions funded by the "Cajas de Ahorro". Each Caja de Ahorros has an OBS, and each receives part of the Caja de Ahorros' profits that are not used to build up reserves.

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

(13) NCG Banco's main figures are:

	<b>30.06.2011</b>	
Total assets	[75-76 000]	million €
Loans to customers	[53-54 000]	million €
Retail deposits	[35-37 000]	million €
Total wholesale funds	[34-36 000]	million €
Employees	7.167	
Number of branches	1.147	

## 2.2 The aid measures already received

- (14) On 29 June 2010, the FROB decided to support Novacaixagalicia by subscribing EUR 1 162 million in newly issued convertible preference shares. The aid represented nearly 2% of Novacaixagalicia's risk weighted assets ("**RWA**") and was earmarked for assisting the merger of two local savings banks, *Caixa de Aforros de Vigo, Ourense e Pontevedra* and *Caja de Ahorros de Galicia* under the Spanish recapitalisation Scheme approved by the Commission<sup>5</sup>.
- (15) Novacaixagalicia issued EUR [...] of senior unsecured debt under the Spanish Guarantee Scheme<sup>6</sup>. Outstanding guaranteed debt of EUR [...] was transferred to NCG Banco as Novacaixagalicia's contribution of its banking assets and liabilities.

## 2.3 The events triggering the measure

- (16) On 19 February 2011, the Spanish authorities approved a new solvency framework for credit institution operating in Spain<sup>7</sup>. The new legal framework established that by 30 September 2011 any credit institution without private investors holding at least 20% of its equity or with wholesale funding exceeding 20% of its financing needs had to meet a solvency level (defined as "*capital principal*"), set at 10% of its RWA. The new rule applies at consolidated and solo level<sup>8</sup>.
- (17) On 10 March 2011, the Bank of Spain informed Novacaixagalicia that it needed to reach a 10% capital principal representing, at the time, a capital deficit of EUR 2 622 million.
- (18) On 14 April 2011, the Bank of Spain approved the recapitalisation plan submitted by Novacaixagalicia, which included various strategies and measures to reach the new solvency levels by 30 September 2011. The plan incorporated some capital-generating organic measures that would reduce Novacaixagalicia's capital deficit from EUR 2 622 million to EUR 2 465 million.

<sup>5</sup> The Commission adopted on 28 January 2010 a decision not to raise objections (case N 28/2010, OJ C 57, 9.3.2010, p. 2) on FROB as a recapitalisation scheme for fundamentally sound institutions.

<sup>6</sup> Commission Decision case SA 32990, Fifth prolongation of the Spanish Guarantee Scheme for credit institutions, OJ C 206, 12.7.2011, p.8

<sup>7</sup> See footnote 3 above.

<sup>8</sup> 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.

- (19) In July 2011, Novacaixagalicia passed the European Banking Authority (EBA) stress test exercise with a core tier 1 ratio of 5.3%<sup>9</sup>.
- (20) The recapitalisation plan for NCG Banco envisaged a combination of private and public capital injections. However, since the envisaged private strategic investors have not been able to complete their intended investments before the 30 September 2011 deadline, the FROB decided to close NCG Banco's capital deficit by subscribing EUR 2 465 million of new ordinary shares. The capital injection represents 4,67% of the bank's RWA as of 31 December 2010 and brings its capital principal level to 10%. As a result of the capital injection, the FROB will have a majority stake in NCG Banco and will sit on its Board of Directors.

### 3 POSITION OF THE SPANISH AUTHORITIES

- (21) 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.
- (22) 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.
- (23) *Appropriate and well-targeted.* The Spanish authorities submit that NCG Banco is important within the Spanish financial system and, especially, in its geographical area<sup>10</sup>.
- (24) *Necessary and limited to the minimum amount.* The Spanish authorities submit that the measure proposed is required to bring NCG Banco's solvency position at consolidated level in line with the new solvency levels established in Spain. In addition, the measure is limited in size to what is necessary to ensure that NCG Banco meets a solvency ratio of 10% capital principal of its RWA required by the Spanish banking rules.
- (25) 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 NCG Banco. The restructuring plan is to be approved by the Bank of Spain and will be notified to the Commission thereafter.
- (26) *Proportionate.* The Spanish authorities submit that the terms and conditions of the measure proposed together with the terms and conditions imposed on NCG Banco, contain a range of safeguards against possible abuses and distortions of competition.
- (27) The Spanish authorities have also provided the following specific commitments:
- (i) To notify to the Commission any increase in the amount of the measure proposed;

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<sup>9</sup> 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, Novacaixagalicia's core tier 1 ratio would have reached 6.5%.

<sup>10</sup> NCG Banco's market shares in Galicia and Spain are 41.4% and [2-3%] respectively.

- (ii) 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, NCG Banco must consult with the Commission in advance;
- (iii) To suspend any payments by Novacaixagalicia to the OBS for new projects;
- (iv) To seek prior approval of the Commission before amending any commitments or constraints mentioned in this decision;
- (v) To notify a restructuring plan for NCG Banco within six months 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**")<sup>11</sup> 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**")<sup>12</sup>.

## 4 ASSESSMENT

### 4.1 Existence of State Aid

- (28) The Commission first has to assess whether the measure constitute 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 favoring 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.
- (29) The Commission observes that the intervening authority, the FROB, is directly financed through State resources.
- (30) The measure confers a selective advantage on the beneficiaries of the aid, NCG Banco and Novacaixagalicia. In particular, the measure providing capital allows NCG Banco to restore its regulatory solvency ratio and avoid its technical insolvency. As regards Novacaixagalicia, the measure also allows it to restore its regulatory solvency ratio and to honour its obligations towards the OBS with both the assets and liabilities not contributed to NCG Banco and with the dividend flow obtained from its equity stake in NCG Banco.
- (31) The Commission notes that the recapitalisation would not have been provided by a market economy investor expecting a reasonable return on his investment, especially given its size..
- (32) The Commission finds that the measure distorts competition as it allows NCG Banco and Novacaixagalicia – which runs its banking activity through NCG Banco - to obtain the capital necessary to avoid technical insolvency and its exit from the market.

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<sup>11</sup> OJ C195, 19.8.2009, p. 9.

<sup>12</sup> OJ C 270, 25.10.2008, p. 8.

- (33) The Commission finds that the measure is likely to affect trade between Member States as NCG Banco and Novacaixagalicia compete on the Spanish retail savings markets, the Spanish mortgage lending markets and the Spanish commercial lending markets. In all those markets, some of NCG Banco and Novacaixagalicia's competitors are subsidiaries and branches of foreign banks.

### *Conclusion*

- (34) 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 the measure qualifies as State aid to NCG Banco and Novacaixagalicia.

## **4.2 Compatibility of the aid**

- (35) As regards compatibility with the internal market of the aid provided to NCG Banco and Novacaixagalicia 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.

### *4.2.1 Legal basis for the compatibility assessment*

- (36) 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*".
- (37) 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 scheme<sup>13</sup> that there is a threat of serious 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 crisis<sup>14</sup>.
- (38) The Commission observes that market conditions have remained difficult globally since the end of 2008. The Commission notes that Spain, in particular, is being 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.

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<sup>13</sup> See Commission Decision N 28/2010, OJ C 57, 09.03.2010 p.2 and Commission Decision N 317/2010, OJ C 242, 09.09.2010, p. 2.

<sup>14</sup> 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.

- (39) The Spanish authorities have shown that NCG Banco and Novacaixagalicia - which has control of NCG Banco - have been unable to close a capital deficit before the 30 September 2011 deadline through capital-generating organic measures or to attract private capital to meet the new solvency requirements in Spain.
- (40) The Spanish authorities have acknowledged that given that NCG Banco was unable to close its capital deficit before the established 30 September 2011 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.
- (41) Without the proposed capital injection, NCG Banco and Novacaixagalicia would be non compliant with the existing 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 capital weakness has the potential to destabilize the Spanish financial markets and triggering a generalized confidence crisis at the present delicate juncture.
- (42) For those reasons, the Commission accepts that in the current circumstances the recapitalisation in favour of NCG Banco (and accordingly Novacaixagalicia), is necessary to avoid a serious disturbance in the economy of Spain.

#### 4.2.2 *Compatibility assessment*

- (43) 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 conditions<sup>15</sup>:
- 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.
  - 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.
- (44) The Recapitalisation Communication<sup>16</sup> elaborates further on the three principles of the Banking Communication and states that recapitalisation 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 insolvency.<sup>17</sup>

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<sup>15</sup> See paragraph 41 of Commission decision, Case NN 51/2008, *Guarantee scheme for banks in Denmark*, OJ C 273, 28.10.2008, p. 2

<sup>16</sup> See also Commission Communication on the application from 1 January 2011, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 329, 7.12.2010, p. 7.

<sup>17</sup> Recapitalisation Communication, point (6)

#### *4.2.2.1 Compatibility with the Banking and Recapitalisation Communications*

##### *a. Appropriateness of the Measure*

- (45) The measure aims at bringing NCG Banco's and Novacaixagalicia solvency position in line with the minimum capital principal requirement of 10% of RWA. The recapitalisation will be in the form of new ordinary shares in NCG Banco.
- (46) The Commission considers that the measure is appropriate because it effectively meets its objective to ensure that NCG Banco and Novacaixagalicia are in compliance with the current regulatory capital requirements and thus remedies a serious disturbance in the economy.

##### *b. Necessity – limitation of the aid to the minimum*

- (47) 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 the NCG Banco and Novacaixagalicia fulfils their regulatory capital requirements.
- (48) As regards the remuneration that NCG Banco 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 NCG Banco is in a position to pay out dividends or if the equity stake taken by the FROB through the proposed measure is sold to a third party or bought back by NCG Banco at a profit.
- (49) 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. Points 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.

##### *c. Proportionality – measures limiting negative spill-over effects*

- (50) Spain has committed that NCG Banco 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 or any other equity-like instruments without consulting with the Commission in advance.
- (51) Therefore, taking into consideration the solvency of NCG Banco and Novacaixagalicia 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 for NCG Banco can be approved.



## *Conclusion*

(52) The Commission, thus, concludes that: (i) the recapitalisation is appropriate and necessary to bring the solvency levels of NCG Banco and Novacaixagalicia) up to the new legally required level established in Spain, as it is limited to the minimum; (ii) NCG Banco must submit a restructuring plan within six months from the date of this decision, which should reflect the level of distress and the size of the State recapitalisation; 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 rescue aid. The Commission can, therefore, temporarily approve the measure for six months.

### *4.2.2.2 Restructuring plan*

(53) 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 restructuring<sup>18</sup>. The Commission furthermore observes that the Spanish authorities have committed to submit a restructuring plan within six months.

(54) The Commission, therefore, takes note of the commitment of the Spanish authorities to submit a restructuring plan for NCG Banco and Novacaixagalicia taking into account all aid measures Novacaixagalicia and NCG Banco have received to date<sup>19</sup>. 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.

## **CONCLUSION**

- The Commission concludes that the measure notified (EUR 2 465 million capital injection) in favour of NCG Banco and Novacaixagalicia constitutes State aid pursuant to Article 107(1) TFEU.
- The Commission finds that the emergency measure in favor of NCG Banco and Novacaixagalicia 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.

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<sup>18</sup> See point 44 of the Restructuring Communication.

<sup>19</sup> See the section on *The aid measures already received* above.

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Yours faithfully,  
For the Commission

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