



EUROPEAN COMMISSION

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Subject: State aid N725/2009 - Ireland

**Establishment of a National Asset Management Agency (NAMA):
Asset relief scheme for banks in Ireland**

Sir,

I. PROCEDURE

- (1) On 7 April 2009, the Irish Minister for Finance announced his intention to introduce an asset relief scheme for banks in Ireland.
- (2) On 29 September 2009, the Irish authorities pre-notified the asset relief measure.
- (3) From September to December 2009, the Irish authorities and the Commission services held several meetings and telephone conferences, and the Irish authorities provided additional information.
- (4) On 23 December 2009, the asset relief measure was notified to the Commission. Further information submissions and exchanges of information took place between 5 January and 17 February 2010.
- (5) Following discussions with the Commission services, the Irish authorities provided several commitments on 18 February 2010.

Mr Micheál MARTIN,
Minister for Foreign Affairs,
Department of Foreign Affairs
80, St. Stephen's Green,
Dublin 2,
Ireland

II. DESCRIPTION

1. Introduction

- (6) In order to restore stability to the Irish banking system in the context of the financial crisis, the Irish authorities notified their intention to establish the National Asset Management Agency (NAMA). NAMA will be established under the aegis of the National Treasury Management Agency (NTMA)¹ and will acquire and manage assets from a number of participating financial institutions.
- (7) The establishment of NAMA intends to address the issue of asset quality in the Irish banking system by allowing participating financial institutions to sell to NAMA assets whose declining and uncertain value prevents the longer-term shoring-up of bank capital and the return to a normally functioning financial market.
- (8) The draft legislation to enable the creation of this body, the National Asset Management Agency Bill 2009 ("the Bill"), was published on 10 September 2009 for consultation purposes. The Bill was presented to the Dáil (one of the Houses of the Irish Parliament) on 16 September 2009. The National Asset Management Agency Act 2009 ("the Act") was passed into law on 22 November 2009 and came into operation on 21 December 2009.
- (9) At this stage, the Irish authorities anticipate that NAMA will arrange and supervise the purchase of approximately EUR [...] billion worth of land, development property and associated commercial loans from certain financial institutions in Ireland² for an estimated purchase price of around EUR 54 billion. The purchase price will be paid through the issuance by NAMA of State-guaranteed senior debt securities for 95% of the purchase price and the issuance of (non State-guaranteed) subordinated debt securities for 5%. The issued securities will be held by the participating credit institutions pro rata their share in the assets transferred to NAMA. It is anticipated that the State-guaranteed debt securities will then be used by the participating credit institutions as collateral to receive financing from the European Central Bank, helping improve the liquidity position of these banks.
- (10) It is anticipated that assets will be transferred by "impaired borrower" exposures across all participating institutions as opposed to transferring portfolio of loans per institution³. That transfer process is expected to take place in seven tranches starting from the end of February 2010. The Irish authorities aim to complete the transfer process over six to twelve months following the adoption of the decision.

¹ The NTMA is the asset and liability management arm of the Irish Government. Its fundamental role is to borrow for the Government and manage the National Debt.

* Confidential information

² These numbers are based on preliminary work performed on the portfolios of the 5 applicant institutions (see paragraph (12)). These numbers have not been verified or validated by the Commission as the valuation exercise is still being carried out for these institutions and as these institutions have not yet formally been recognised as participating institutions.

³ See paragraph (18) for a description of impaired borrower relationship.

2. Objectives of the measure

(11) The set up, rules and powers of NAMA have been designed to allow the agency serve the purposes set out in the Act, namely:

- the serious threat to the Irish economy, the stability of credit institutions in Ireland and the need for the maintenance and stabilisation of the financial system in Ireland, and
- the compelling need to (i) restore confidence in the Irish banking sector and to underpin the effect of Irish government support measures in relation to that sector, (ii) remove uncertainty about the valuation and location of certain assets of credit institutions of systemic importance to the Irish economy by addressing the issue in an expeditious and efficient manner, (iii) facilitate the availability of credit and achieve a recovery in the Irish economy, (iv) protect Ireland's interest in respect of the guarantees issued pursuant to the guarantee schemes⁴, (v) protect the interests of Irish taxpayers, and (vi) facilitate restructuring of credit institutions of systemic importance to the Irish economy.

3. Eligible institutions

(12) Any credit institution, including Irish subsidiaries of foreign credit institutions, may apply to join the asset relief scheme, within 60 days after the establishment day of the scheme. This 60 day application window opened on 21 December 2009 and closed on 19 February 2010. Five institutions have formally applied Allied Irish Bank (AIB), Educational Building Society (EBS), Bank of Ireland (BoI) and Anglo Irish Bank) and Irish National Building Society (INBS). The table below shows the total assets of financial institutions based in Ireland:

Bank	Total assets 2008 EUR bn	% of total
Bank of Ireland	194.1	26.5%
Allied Irish Bank	179.5	24.5%
Anglo Irish Bank	88.5	12.1%
Permanent TSB	74.3	10.1%
Bank of Scotland (Ireland) (Lloyds)	54.1	7.4%
Ulster bank (RBS)	48.7	6.6%
National Irish Bank (Danske)	28.2	3.8%
EBS	21.4	2.9%
KBC Ireland (KBC)	21.1	2.9%
INBS	14.4	2.0%
ACCBank (Rabobank)	8.4	1.2%

⁴ CIFS Scheme, Commission Decision of 13.10.2008 Guarantee scheme for banks in Ireland, in case NN 48/2008, OJ C 312, 6.12.2008, p. 2; and ELG Scheme, Commission Decision of 20.11.2009 Credit Institutions Eligible Liabilities Guarantee Scheme, in case N349/2009

(13) The Minister, after consultation with the Governor of the Central Bank and the Regulatory Authority, will designate participating institutions within three months of application, based on the three following factors :

- the applicant credit institution must be systemically important;
- the Minister must be satisfied that the acquisition of bank assets from the applicant credit institution is necessary to achieve the purposes of the Act, having regard to the support available or received by the applicant institution, the financial position of the applicant institution and the resources available to the Minister;
- the applicant credit institution must have complied with all relevant obligations under the Act.

(14) These three factors are further detailed in Annex I to this decision and include very specific criteria to assess the applicant credit institutions.

4. Eligible assets

(15) The Irish authorities intend to concentrate on assets from the riskiest parts of the portfolios of the participating institutions, namely land and development loans and associated loans. The assets targeted by the measure are (i) all loans issued for the purchase, exploitation or development of land⁵ as well as loans either secured or guaranteed by land, and (ii) some of their associated commercial loans.

(16) The associated commercial loans are loans made to a small number of large developers who constitute the largest borrowers in respect of land and development loans. It is anticipated that, given their interconnected nature with land and development loans, these associated commercial loans are likely to become impaired, if not impaired already.⁶

(17) These interconnections and inter-linkages between land and development loans and associated commercial loans can take many forms, including the following⁷:

- lending whereby the collateral of an associated loan is cross-collateralised or cross-defaulted with land and development loans;
- lending whereby the borrower has land and development loan exposure to one credit institution and an associated loan exposure to another credit institution;
- lending whereby the security for land and development loan exposure is also security for an associated loan; and

⁵ However, for AIB, Anglo Irish Bank and BoI, a minimum threshold of EUR 5 million will be applied, in order to (significantly) reduce the number of borrowers (and the corresponding due diligence efforts), while including the majority of the loans in volume.

⁶ The majority of loans include loan-to-value covenants which if breached and not waived will trigger a "technical event of default" on the loan. [...] The existence of cross default clauses between land and development loans and commercial loans to the same borrower then means that the commercial loan is also in technical default.

⁷ The actual definition of associated commercial assets in the Act is quite broad to allow NAMA to capture the entire borrower relationship and root out most of all potential impairments to come from a relationship.

- lending whereby the total indebtedness of borrowers and associated obligors (e.g. connected companies, joint venture partners, guarantors) is of an amount that would adversely affect the stability of any of the participating credit institutions or of the financial system in Ireland.
- (18) According to the Irish authorities, eligible assets are expected to be concentrated on a small number of very large real estate developers, involved across the whole cycle of property development. Loans to such developers are closely interconnected and inter-linked (through cross default and cross guarantee clauses for example as described in footnote 6) which is viewed as significantly contributing to the impairment problems currently threatening credit institutions in Ireland. Therefore, the approach to determining asset eligibility under the scheme is based on the concept of impairment at the borrower relationship level as opposed to impairment at the asset level only (impaired borrower relationship).
- (19) Assets to be included in the scheme must have entered participating institutions' balance sheets before 31 December 2008.

5. Indicative portfolio description

- (20) Based on the work undertaken so far by the Irish authorities in relation with the five prospective participating credit institutions, loans with an aggregate nominal value of approximately EUR 82.5 billion have been identified as of February 2010 as likely to be eligible assets for transfer to NAMA⁸.
- (21) The estimated EUR 82.5 billion⁹ in loans is held by five institutions, namely: (i) Anglo Irish Bank (*[...]*), (ii) AIB (*[...]*), (iii) BoI (*[...]*), (iv) INBS (*[...]*) and (v) EBS (*[...]*)
- (22) The estimated EUR 82.5 billion in loans is made up of approximately EUR 30 billion of loans backed by land (*36.4% of total*), EUR 22.5 billion of loans backed by development property (*27.3% of total*), and EUR 30 billion of associated commercial loans (*36.4% of total*).
- (23) The Irish authorities estimate that, of the total portfolio identified for potential transfer to NAMA, approximately EUR 10 billion consist of interest roll-up. Therefore, NAMA estimates that the original principal balances on these loans were approximately EUR 72.5 billion.
- (24) The five prospective participating credit institutions would also have booked provisions for an amount of around EUR [...] billion as of 30 November 2009.
- (25) The estimated aggregate initial average loan to value (LTV) rate for these loans is approximately 77% i.e. the value of the real estate collateral at the time the loans were

⁸ It should be emphasised that this estimate may change at least for two reasons. First, in light of the definition of the "eligible bank assets" which will be prescribed by the Regulations under the NAMA Act, it is only when the total range of eligible assets has been prescribed that a definitive basis will exist for determining the total nominal value of assets which are eligible for transfer to NAMA. Second, depending on the final scope of participating financial institutions, the total nominal value of assets could also change. However the Act limits the total amount of bank assets that can be purchased to EUR 54 billion.

⁹ This number includes interest roll-up which is capitalised unpaid interest (for development loans) but excludes the mark to market of associated derivatives. This represents approximately 11.2% of the total assets of the 10 largest financial institutions based in Ireland (measured by total assets).

originated was EUR 94.2 billion¹⁰. The loans were made over a number of years and not all were made at the peak of the market, but at this stage no vintage breakdown of the portfolio has yet been provided to the Commission.

(26) The Irish authorities estimate that the purchase price to be paid to participating institutions will be EUR 54 billion. This means a transfer price approximately 15.00% higher than the current market value of the loans identified for transfer (estimated at EUR 47 billion), and a 35.00% discount on their loan nominal value.

(27) The following table summarizes the indicative information above.

	<i>In EUR billion</i>	<i>In % of nominal value</i>
Nominal value (incl. roll-up interest and excl. derivatives mark to market)	82.5	100.0%
Book split	52.5 L&D	100.0%
	30.0 Associated loans	
Net original balance (excluding roll-up interest)	72.5	86.8%
Transfer price	54.0	64.7%
Market value	47.0	56.3%

(28) The geographical spread of the property associated with the loan assets is: (i) Ireland (66.8%), (ii) Northern Ireland (6.2%), (iii) Great Britain (20.7%), (iv) USA (2.7%) and (v) other (3.6%).

(29) 40% of these loans are estimated to be cash-flow producing, and it is projected that these cash flows will be sufficient to cover interest payments on the State-guaranteed bonds issued by NAMA for the payment of the purchase price as well as NAMA's operating costs. 60% of the loans are not producing any cash flows either because they are investment loans in default or because they are development loans with interest roll-up backed by incomplete developments.

(30) In addition to loans, about 1,000 derivative positions (mainly interest rate swaps) attached to commercial loans will be purchased by NAMA at market value. The notional amount of these derivatives is EUR 14 billion and the market value as of 12 February 2010 is approximately EUR [...] billion. The mark-to-market of these derivatives is already taken into account in the expected nominal value of the portfolio of EUR [...] billion.

6. Structure and operations

NAMA

(31) NAMA has been established on a statutory basis, as a separate body corporate with its own Board and Chief Executive both appointed by the Minister for Finance, under the control of the NTMA.

¹⁰ i.e. EUR 72.5 billion divided by 77%.

- (32) The NTMA will provide NAMA with business and support services and systems, and will assign staff to NAMA as deemed necessary. NAMA will reimburse NTMA for the cost of the assigned staff. NAMA may engage the services of any expert adviser or other service provider it considers necessary.
- (33) The purposes of NAMA are to contribute to the achievement of the purposes of the Act by acquiring such eligible bank assets (EBA) from participating institutions as is appropriate, dealing with those assets expeditiously and protecting or otherwise enhancing the value of those assets in the interests of the State. From a set up point of view, NAMA, as a corporate legal entity, will arrange and supervise the identification and valuation of property-backed loans on the books of qualifying financial institutions in Ireland, but will delegate, under its control, the actual purchase and management of these loans to a separately created Special Purpose Vehicle (“the Master SPV”).

The Master SPV

- (34) NAMA will create a Special Purpose Vehicle (“the Master SPV”), which will be responsible for:
- The purchase, management and disposal of loan assets identified and valued by NAMA, and
 - The financing of such purchases through the issuance of debt securities for a total amount of maximum EUR 54 billion¹¹: these will consist of securities guaranteed by the Irish government (for 95% of the total consideration) and non-State guaranteed subordinated debt securities (for 5%). The latter may only be redeemed if the SPV makes a profit over its life¹². Bonds issued by the Master SPV will be 1 year floating rate note securities (FRN) extendible at maturity at NAMA's option. They will carry a semi-annual interest rate equal to the 6-month EURIBOR rate flat. The re-issuance at maturity will most likely be an extension of the maturity FRN. The terms and conditions will remain the same throughout their life. [...] ¹³. Furthermore for government guaranteed NAMA debt issuance greater than 1 year duration the margin over the equivalent maturity debt of Ireland will not exceed 20 basis points, intended to reflect the current spread between the yield on government bonds and that required on government guaranteed paper. If unfavourable market developments lead to a significantly wider gap than is currently the case between the yield on government bonds and that required on government guaranteed paper, the Irish authorities commit to seek approval of the Commission before modifying the margin of 20 basis points to reflect the wider gap.
- (35) The Master SPV will be a separate legal entity and will be jointly owned by private investors, who will own 51% of its ordinary equity¹⁴, and by NAMA, which will hold

¹¹ The Act specifically provides that the aggregate of the principal of all debt securities issued to enable the acquisition of eligible bank assets shall not exceed EUR 54 billion or such other amount as the Minister may specify by order.

¹² [...]

¹³ [...]

¹⁴ According to the Irish authorities, and based on a letter from Eurostat who issued on 16 October 2009 a preliminary view on the ESA95 accounting treatment of NAMA and the Master SPV, the acquisition and financing of the assets from participating credit institutions would be treated as off-balance sheet in the Irish budget.

the remaining 49% of its ordinary equity. The subscribed capital of the Master SPV is likely to be EUR 100 million.

- (36) The Master SPV will have its own Board, with members appointed by NAMA and the private investors. However, since the State (Minister for Finance) is guaranteeing the majority of the securities (equivalent to 95% of the purchase price consideration) issued by the Master SPV, NAMA representatives on the Board will maintain a veto over all decisions of the Board that could affect the interests of NAMA or of the Irish government¹⁵.
- (37) The Master SPV may create a number of subsidiary SPVs, each of which would be responsible for the loan book of an individual participating financial institution. Any such subsidiary SPV would be 100% owned by the Master SPV. The Master SPV and all the other subsidiary SPVs are NAMA group entities.
- (38) The Master SPV will be run with the objective of making a profit on the purchase and management of the assets. The profits earned by the SPV will be distributed to the shareholders according to the following arrangement, which reflects the fact that the debt issued by the Master SPV will be guaranteed by the Irish Government:
- The equity investors (NAMA and private investors) will be entitled to receive an annual dividend linked to the performance and profitability (taking account of all direct and indirect costs) of the Master SPV, capped at [...].
 - Upon the winding-up of the Master SPV, the equity investors (NAMA and private investors) will only be repaid their capital if the Master SPV has the resources. The private investors will receive a further equity bonus of maximum [...] of the capital (capped at EUR [...]) if the Master SPV makes a profit.
 - All other profits and gains of the Master SPV will accrue to NAMA.
- (39) If the Master SPV makes a loss in its lifetime or is wound-up, the equity invested in the majority private-sector owned Master SPV and any associated dividends will be lost.
- (40) NAMA or a NAMA group entity are allowed under the Act to borrow, with or without the guarantee of the Minister such sums (in addition to the maximum funds raised for the purchase of the assets) as are required for the performance of its functions up to Euro 5 billion¹⁶.

Reporting requirements

- (41) Under the Act, NAMA shall produce annual accounts to be reviewed by the Comptroller and Auditor General. Such annual accounts will be publicly available and will report in particular on the debt securities issued by NAMA. Furthermore, the Act provides that NAMA will prepare and make public quarterly, semi-annual and annual reports reporting on its operations, acquired assets and their status and financial performance.

¹⁵ Ultimately, NAMA has been set up to fulfil specific objectives listed in the Act (paragraph (33) describes the purposes of NAMA). Any use of NAMA's veto rights will be to ensure the fulfilment of those objectives and purposes.

¹⁶ For example to complete unfinished developments if deemed profitable.

The Irish authorities will monitor the functioning and the performance of NAMA on a regular basis.

7. Powers and rights of NAMA

- (42) The Act provides that NAMA shall have all the powers necessary or expedient for, or incidental to the achievement of its purposes and the performance of its functions. Consequently the Act grants NAMA extensive powers, rights and exemptions (i) to simplify certain administrative and legal procedures associated with the acquisition and the post acquisition management of such assets and (ii) to help it achieve the maximum recovery value for them.
- (43) In particular, the Act grants NAMA specific post acquisition powers aimed at making NAMA's access to the underlying real estate security (both physically and legally) easier and at allowing it to have close control over the process of realisation of such security in order to maximise recovery value. Such specific powers could be split across three broad categories as follows:
- i. Vesting orders and compulsory purchase orders. The right of NAMA to ask the Court for a vesting order enables it to avoid having to go through a fire sale of some underlying land assets. The compulsory right of purchase enables NAMA to compulsorily acquire land assets in situations where debtors might try to frustrate the realisation by NAMA of its own assets.
 - ii. Powers that already exist at common law or would be provided for as part of the contractual terms and conditions of the transaction entered into by a prudent commercial market operator. These powers include in particular, the right of NAMA to (among others)
 1. Unilaterally amend the language of loan contracts; and
 2. Dispose of the acquired assets in anyway NAMA thinks fit.
 - iii. Powers designed to address particular technical legal difficulties and issues peculiar to NAMA and its operations, in particular the right to (among others)
 1. Receive information on a borrower from the tax authorities and
 2. Be protected against potential claims from other creditors in cases where NAMA receives payments from an insolvent borrower in preference and ahead of such other creditors.
- (44) Some of the powers granted to NAMA are not available or go beyond those available to traditional market players operating on the real estate financing market in Ireland. According to the Irish authorities, such powers are essential for the discharge by NAMA of the obligations imposed on it by its statute. They are essential for NAMA's fundamental purpose of acquiring assets in order to address a serious threat to the economy and to the systemic stability of credit institutions in the State.

(45) Additionally, the Act includes provisions on specific treatment of NAMA's tax status affecting stamp duties, the Business Expansion Scheme, capital gains tax, income/corporation tax, relevant contract tax and value-added tax. According to the Irish authorities¹⁷, the tax treatment of NAMA is equivalent to other market operators, except for stamp duty, since NAMA will be exempt from stamp duty on the transfer of loans and the enforcement of security. However, if NAMA or a NAMA subsidiary is to acquire property other than via enforcement of security on a non-performing asset, a charge to stamp duty will apply.

8. Transfer process and valuation methodology

Transfer process

(46) The transfer process will be organised around the transfer of exposures to impaired borrower relationships as opposed to loans from a given institution. It is anticipated that the first tranche will include the 10-15 largest borrower exposures across all participating institutions. It is estimated that the largest 100 exposures will account for about EUR 38 billion in nominal value of the loans to be acquired by NAMA. It is intended to have the transfer process completed over the next seven months.

(47) The timing of transfer is expected to be as follows:

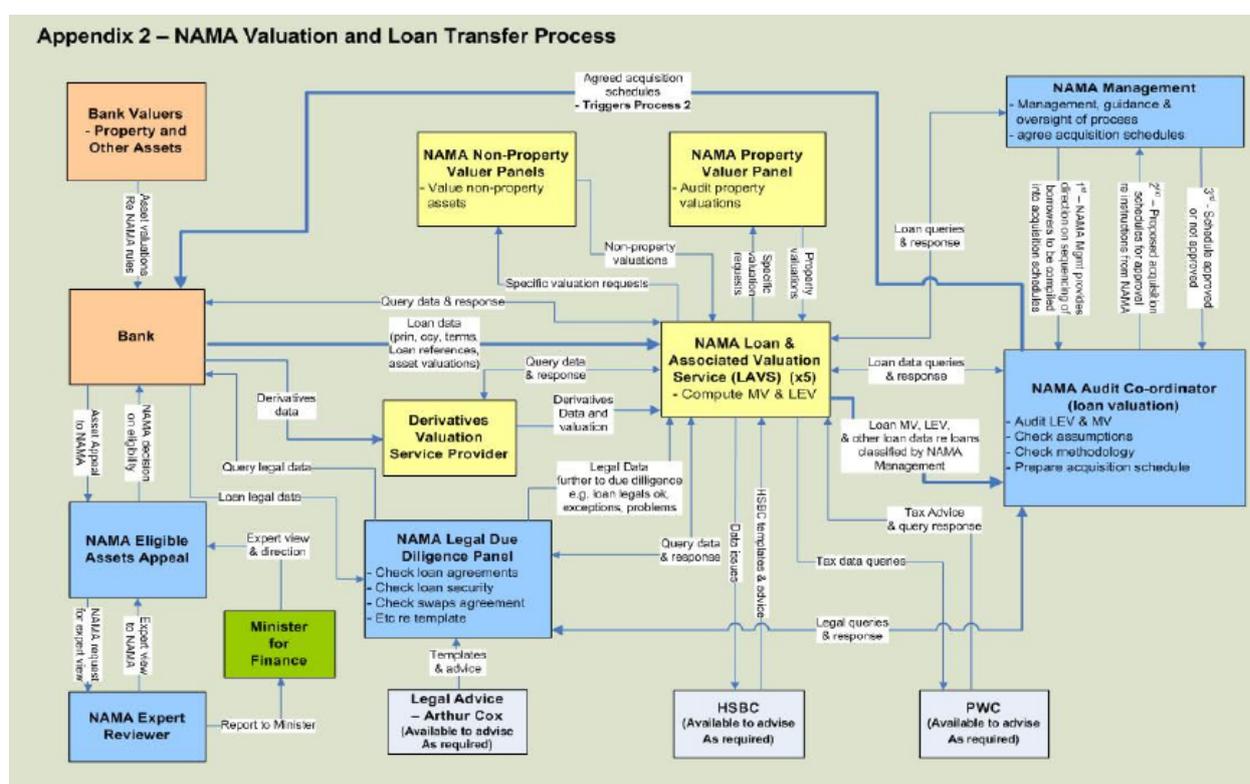
Period	Projected number of exposures (cumulative)	Projected book value of loans transferred (cumulative) , in EUR billion	Projected amount of issued securities, in EUR billion
Month 1	10	16	11.2
Month 2	35	24	16.8
Month 3	100	38	26.6
Month 4	300	50	35.0
Month 5	750	60	42.0
Month 6	1,200	70	49.0
Month 7	1,500-2,000	77	54.0

(48) Before the actual purchase of the loans by a NAMA group entity, a number of steps will have to be completed. These steps can be described as follows and are represented in the chart below:

- i. Identification of participating institutions;
- ii. Identification of all eligible bank assets by NAMA;

¹⁷ The Irish authorities have provided the Commission with an analysis of NAMA's tax status and treatment from PriceWaterhouseCoopers.

- iii. Provision by the participating institution of an asset information list which contains all the necessary items of information in order to value the loan;¹⁸
- iv. Provision by the participating institution of a legal and tax due diligence report;
- v. Determination of the current market valuation of all underlying property and assets by external valuers appointed and paid by the participating institution but with a duty of care to NAMA;
- vi. Determination by NAMA of the property long-term economic value, current market value and loan long-term economic value of the bank asset;
- vii. Valuation of all derivatives contracts attached to the eligible bank assets and transferred simultaneously;
- viii. Determination of the transfer schedule;
- ix. Purchase of the assets within 28 days of the transfer schedule.



- (49) A number of "checks and balances" provisions will allow NAMA to monitor the entire process and valuation obtained. In particular, steps are in place to allow for
- i. Checking the eligibility of the banks' assets;
 - ii. Checking the legal due diligence work done on the loans;
 - iii. Checking non-property and property valuations;

¹⁸ Banks will have to provide over 350 data fields on each asset transferred.

- iv. Checking the loan's valuation;
- v. Checking the overall process

(50) The Act also includes a clawback mechanism to ensure that any overpayment made by NAMA to a participating institution is repaid by the participating institution (see paragraph (69)).

Valuation Methodology

(51) The valuation methodology chosen by the Irish authorities and their advisors is derived directly from the methodology used to value non-performing assets. The fundamental premise is to evaluate the assets using a discounted cash flow method taking into account the timing and reliability of the cash flows coupled with an appropriate discount factor to arrive at a current valuation.

(52) The ultimate target of such cash flow valuation exercise is to determine the long-term economic value of the eligible bank asset which is defined as "the value that such asset (ie. the loan) can reasonably be expected to obtain in a stable financial system when the crisis conditions prevailing are ameliorated". The transfer price of the assets will be no greater than the long-term economic value of the bank asset, so determined.

(53) Four separate valuations will be provided:

- i. The current market value of the property or other collateral underlying the loans (the "Property CMV"), defined as "the estimated amount that would be paid by a willing buyer to a willing seller in an arm's-length transaction after proper marketing (where appropriate) where both parties act knowledgeably, prudently and without compulsion";
- ii. The long-term economic value (or real economic value) of the property or other collateral underlying the loans (the "Property LEV"), defined as "the value, as determined by NAMA, [...], that it can reasonably be expected to attain in a stable financial system when the crisis conditions prevailing [...] are ameliorated and in which a future price or yield of the property is consistent with reasonable expectations having regard to the long-term historical average";
- iii. The current market value of the transferred loan asset itself (the "Bank Asset CMV"), defined as "the estimated amount that would be paid by a willing buyer to a willing seller in an arm's-length transaction after proper marketing (where appropriate) where both parties act knowledgeably, prudently and without compulsion";
- iv. The long-term economic value (or real economic value) of the loan asset itself (the "Bank Asset LEV"), defined as "the value, as determined by NAMA [...], that it can reasonably be expected to attain in a stable financial system when the crisis conditions prevailing at the passing of this Act are ameliorated".

(54) Property valuations are indirect and direct inputs in the cash flow analysis used to determine the long-term economic value of the bank asset.

Property current market value (Property CMV)

- (55) Each property relating to a bank asset to be acquired by NAMA will be subject to an individual valuation carried out by a valuer as of a date specified by NAMA in advance of the acquisition. External independent professional real estate valuers will be required to prepare market valuation reports in accordance with the provisions of the Appraisal and Valuation Manual ("the Red Book") of the UK Royal Institution of Chartered Surveyors (or equivalent).
- (56) Whilst it is expected that all the properties securing the eligible bank assets will be independently valued, given the high number of loans, the market valuation process will be performed in two steps.
- i. Firstly, each participating institution will provide NAMA with the required data for the top 100 borrower relationship credit positions. NAMA will then determine from these the top 150 borrower relationship credit positions by size of exposure across all participating institutions. The underlying collaterals relating to these top 150¹⁹ borrower relationship credit positions will form the "core underlying assets", for which the valuers will provide Collateral CMVs. The data then collected would form a statistical basis for determining the Collateral CMVs of the remaining underlying assets (the "non-core underlying assets"). The statistical basis would be applied to establish an initial Collateral CMV of the non-core underlying assets, based on which an initial transfer price will be determined;
 - ii. Secondly, the valuers will prepare valuation reports for the non-core underlying assets over the next 12 months (i.e. post transfer of assets to NAMA in certain circumstances) in order to determine a final Collateral CMV of the non-core underlying assets. Any settlement amount (deriving from any difference between the initial Collateral CMV and the final Collateral CMV of the non-core underlying assets) will be clawed back by NAMA.
- (57) The valuers will be appointed and paid for by the participating institutions. To address potential conflicts of interest, four levels of control have been put in place:
- i. Participating institutions have to use a standard letter of instruction prepared by NAMA for instructing valuers. This letter sets out the parameters under which valuations should be performed;
 - ii. Each valuer owes a duty of care to NAMA;
 - iii. NAMA will appoint a panel of professional valuers to review and audit the valuations prepared by the valuers and provided by the institutions; and
 - iv. An audit coordinator will be appointed to audit the information provided by institutions in respect of land and other collateral to ensure compliance with the guidelines and consistency across all the participating institutions.

¹⁹ There is some overlap in the top borrower exposures of the participating institutions.

- (58) The asset information list to be provided by the participating institution for each eligible bank asset will be the basis for the valuation exercise. The assessment of the individual security will take into account the actual characteristics of the property including a detailed investigation of the development environment in terms of planning permission status, cost of carrying out development including fees and costs, supply of competing schemes, demand for proposed end product / space time scales, and general viability and risk assessment. Full transparency of the valuation methodology will be required in the valuation reports, with full disclosure of the inputs used in the valuation process.

Property long term economic value (Property LEV)

- (59) Once the Property CMV has been determined, the Property LEV can be determined using various adjustment factors, which will be uniformly applied to specific baskets of assets, initially broken down by city/region and asset type or other relevant categorisation. The adjustments will be made using various econometric and statistical tools that are yet to be determined but will likely include for example:

- the extent to which the price or yield of such assets has deviated from the long-term historical average;
- supply and demand projections by reference to the type of asset and its location;
- macroeconomic projections for growth in the gross domestic product and for inflation or deflation;
- demographic projections;
- land and planning considerations (including national, regional or local authority development or spatial plans) that may exert an influence on the future value of the asset concerned; and
- analyses on the extent to which existing land zoning and planning permissions granted and in force meet or exceed projected growth requirements.

- (60) The outcome of this process is the establishment of a long-term economic value matrix which will give the percentage of "uplift" to be applied to the current market value of properties on the basis mainly of the nature of this property and its location. This matrix will be used by NAMA to derive the long-term economic value of the property from its current market value. This matrix will however be subject to specific ceiling values, as stated in the Act, for the determination of the long-term economic values as follows :

- for any property other than land²⁰, Property LEV is equal to Property CMV;
- the LEV of a particular parcel of land cannot be more than 125% of the market value; and
- the LEV of the total portfolio of land assets of a participating financial institution cannot be more than 120% of the total market value.

²⁰ This includes for example, all other types of security that could be attached to a loan such as personal guarantees, art, share portfolios, wine collections; helicopters and life insurance policies.

Bank asset current market value (Bank asset CMV)

- (61) Once both the current market value and long-term economic value of the properties are determined, these values are used as inputs in the cash flow analysis used to calculate the current market value and the long-term economic value of the bank asset itself.
- (62) The bank asset CMV is determined through a discounted cash flow analysis, which models the cash flows expected to be received by NAMA for those assets and discounts them using a discount factor reflecting the current market value of the loan. Items taken into account when modelling the bank assets' expected cash flows are among others:
- i. the nature of the loan and its sources of repayment (for example, sale of the development once completed for development loan, or interest and rental payments for investment loans);
 - ii. the characteristics of the loan, (i.e. interest rate, original loan to value, maturity, etc.);
 - iii. the legal framework (i.e. relationship to the underlying property as security, strength of the security package, cross default clauses, covenant breaches, etc.); and
 - iv. the hedging structure, if any, of the loan and the market value of the hedging instruments used.
- (63) The underlying cash flows of each loan will be projected (including cash flows of the underlying collaterals to which the loans have access) and discounted in a specially built individual model. The market-based return used for discounting will reflect factors such as current loan-to-value, liquidity, perceived default risk (including of underlying tenant), potential interruption of cash flows, robustness of underlying asset valuations, likelihood of final repayment, interest rate risk, etc. Such discount rate may be estimated through comparisons with other asset classes, current lending/investment requirements for real estate assets and current trading conditions for senior/mezzanine and equity financings²¹.

Bank asset long-term economic value (Bank asset LEV)

- (64) The methodology for calculating the bank asset long-term economic value is the same as that for calculating the bank asset market value i.e. a discounted cash flow analysis of the loan's expected cash flows. The same variables are used in both valuation approaches. There is, however, a difference in the valuations which occurs through the different assumed values for the inputs. Key variables affecting the expected cash flows from the bank assets are the period over which the cash flows are expected to be received²², enforcement costs, income sources, hedging obligations and final settlement

²¹ Notwithstanding the above, if a loan is in default and its security is being enforced, its current market value should be more or less equal to the current market value of the property securing it, less any enforcement costs.

²² The Irish authorities intend to discount the cash flows over a period which is different from the loan remaining maturity. This period will depend on the current market valuation of the underlying property and the uplift (i.e. the prospect for recovery) granted when determining the LEV of the property. The Irish authorities will apply four "standard scenarios" as follows: assets with poor recovery prospects demonstrated with an uplift of less than 10.0% will be valued on average over three years; assets with better recovery prospects demonstrated by an uplift between 10.0% and 15.0% will be valued over 5 years, assets with an uplift between 15.0% and 25.0%

obligations, future lending obligations and funding costs (for incomplete developments which NAMA decides to complete).

- (65) Unlike the current market value of the bank asset, the long-term economic value of the asset will take into account the benefit of any ancillary security (for example, personal guarantees, and other corporate assets). Another key difference will reside in the discount rate used to discount the cash flows. For the determination of the long-term economic value of the bank assets, the Irish authorities propose to use a discount rate equal to the sum of the Irish government bond yield as of 21 December 2009 for the same maturity as that used for the asset cash flows (to reflect NAMA's cost of funding) plus a spread of 170 basis points.
- (66) The bank asset LEV resulting from such analysis will be the maximum potential price to be paid by NAMA for the transfer of the loans.
- (67) If the total credit exposure of NAMA to one relationship extends across more than one institution, the methodology provides for each loan to be evaluated on its own merits and individual security package. To the extent that more than one institution benefits from an existing security, the extent and relevance of the additional security would need to be considered in conjunction with each loan relying on such security on a pro rata basis based on the nominal value of the underlying loans. The necessary transparency and equal treatment is thereby provided to all institutions.

Transfer price

- (68) The maximum transfer price (or purchase price by NAMA) will be the bank asset's long-term economic value.

Clawback mechanisms

- (69) Because of the large number of assets, the transfer process will take place in two stages, with some assets being transferred without a valuation of the current market value of the underlying property. For these assets, the Act provides that if, following the completion of the relevant property valuation, the original transfer price turns out to be more than is due, the institution will repay to NAMA an amount equal to the overpayment.²³
- (70) Two additional risk-sharing mechanisms are envisaged under the scheme, which would provide NAMA with the ability to recoup some of the losses, if any were to be experienced during the lifetime of NAMA.
 - The first risk-sharing mechanism is the fact that NAMA will pay 5% of the transfer price of the acquired assets to the participating credit institutions in the form of subordinated debt securities. Repayments on such subordinated debt securities will only be made if NAMA does not make a loss over its lifetime. If losses occur, the repayment of the subordinated securities will be compromised and a commensurate loss (i.e. up to 5% of the transfer price of the assets) will be borne by the participating credit institutions.

will be valued over 8 years and finally bank assets for which the current market value of the property is greater than the outstanding balance of the loan, will be valued over the remaining maturity of the loan.

²³ See supra, valuation methodology for Property CMV.

- Secondly, the Irish authorities intend to introduce a levy on the participating financial institutions if, on the winding up of NAMA, there were to be a deficit.

9. Remuneration of the State

(71) The remuneration of the State is embedded in the discount factor used to discount the loan cash flows when determining the bank asset's long-term economic value. At present the Irish authorities intend to use a discount rate equal to the Irish government bond yield as of 21 December 2009 for the same maturity as that used to determine the assets cash flows plus 170 basis points which corresponds to a total expected remuneration of the State of EUR 4.59 billion²⁴.

III. THE POSITION OF IRELAND

(72) The Irish authorities acknowledge that the notified asset relief measure may contain elements of State aid.

(73) However, the Irish authorities consider the scheme is compatible with the internal market on the basis of Article 107(3) (b) TFEU²⁵ as it is necessary in order to remedy a serious disturbance in the Irish economy.

(74) The Irish authorities commit as follows :

- i. To notify each individual tranche of transferred assets. Such notifications will include detailed information regarding the assets transferred and their valuation.
- ii. To provide with each transfer a certificate from the audit coordinator and a letter from the relevant supervisory authority validating the valuation amount of impairments taken on the relevant assets;
- iii. That NAMA will claw back any excess payment from the relevant participating institution if the transfer price paid is estimated too high after the Commission's assessment of a notified transfer.
- iv. That the Minister for Finance will issue a Direction to the NAMA Board directing that all short-term government guaranteed debt issued by NAMA up to 1 year maturity will not exceed the equivalent pricing of government guaranteed issuance of the Housing Finance Agency. Furthermore for government guaranteed NAMA debt issuance greater than 1 year duration, the margin over the equivalent maturity debt of Ireland will not exceed 20 basis points, intended to reflect the current spread between the yield on Irish government bonds and that required for government guaranteed paper. If unfavourable market developments lead to a significantly wider gap than is currently the

²⁴ Assuming an average life of the loan portfolio of 5 years, the expected remuneration was calculated by HSBC as the result of the following : 54 billion x 1.70% x 5 = 4.59 billion

²⁵ With effect from 1 December 2009, Articles 87 and 88 of the EC Treaty have become Articles 107 and 108, respectively, of the Treaty on the Functioning of the European Union (TFEU). The two sets of provisions are, in substance, identical. For the purposes of this Decision, references to Articles 107 and 108 of the TFEU should be understood as references to Articles 87 and 88, respectively, of the EC Treaty where appropriate.

case between the yield on government bonds and that required on government guaranteed paper, the Irish authorities commit to seek approval of the Commission before modifying the margin of 20 basis points to reflect the wider gap.

- v. To submit a restructuring plan (or amend an already submitted restructuring plan as the case may be) for each participating institution within 3 months from their accession to the NAMA scheme; and
- vi. To provide a report to the Commission every 6 months on the functioning of the asset relief measure and on the development of the participating institutions' restructuring plans.
- vii. Concerning the use of NAMA's powers granted to it by the Act:
 - 1. The Irish authorities commit that NAMA will not use the power to request a vesting order (as per sections 152 to 156 of the Act) in the context of a syndicated loan without the agreement of the other syndicate members. Similarly, for any other mortgage on the property, the Irish authorities undertake that NAMA will get agreement of the holders of equivalent charges, in terms of ranking and priority, before using this power. The Irish authorities commit to include a clause in the code of conduct relating to non-participating institutions to this effect.
 - 2. The Irish authorities commit that NAMA will only exercise the general power to seek a compulsory purchase order contained in section 158(1)(a) of the Act in circumstances where there are issues concerning ransom strips or access or related issues and the particular facts or the circumstances involved do not clearly fall within the terms of any of the five other situations foreseen in subsections (1) and (2) of section 158. If, in the future, NAMA should consider in particular circumstances that reliance on Section 158(1)(a) would be necessary for purposes other than issues related to ransom strips, access or related issues, then NAMA will advise the Commission of its intention to utilise the provision in such circumstances and will consult with the Commission.
 - 3. The Irish authorities commit that NAMA will consult with the Commission on the appropriate use of the power to unilaterally amend contracts (as per section 102.3 of the Act) prior to its exercise;
 - 4. The Irish authorities commit that NAMA will address in the code of conduct relating to non-participating institutions, the use of power given to it under section 139 of the Act (allowing for the removal of limitations on the right of transfer of assets) in the context of a syndicated loan and where the rights of the members might be affected. Similarly the Irish authorities commit that NAMA will address in the code of conduct the

position of other loans on the property and ensure the rights of holders of those loans are not adversely affected.

5. The Irish authorities commit that NAMA will not use the power to request tax information (as per section 204 (3) of the Act) from the Revenue Commissioners;
6. The Irish authorities commit that NAMA undertakes to consult with the Commission before invoking section 228(2) as a defence to any claim that might be brought against NAMA and likewise to the fullest extent to which it is within NAMA's power, NAMA undertakes that it will only assert section 228(2) as a defence to any claim brought by the liquidator of an insolvent company where NAMA believes that another creditor of the company has behaved aggressively in securing the payment of monies owed to that creditor.
7. The Irish authorities commit that NAMA will report on a yearly basis to the Commission and to the Irish national competition authorities on the use of NAMA's post acquisition powers as specified in the document "Responses to questions from the European Commission dated 21st January, 2010", dated 4February 2010.

IV. SENATOR REGAN'S COMPLAINT

- (75) On 15 December 2009, Senator Eugene Regan lodged a formal complaint against some of the aspects of the intended operations and functioning of the NAMA scheme with the Commission²⁶. The services of the Commission met with Senator Regan on 25 January 2010. Following such meeting additional material was submitted by Senator Regan on 12 February 2010.
- (76) Senator Regan's submission was sent to the Irish authorities for comment on 28 January 2010. Comments were received back from the Irish authorities on 3 February 2010. The Commission received comments on this further submission on 18 February 2010.
- (77) In his submission of 15 December 2009, Senator Regan, on the basis of NAMA's draft business plan²⁷, raises the main following concerns and argues that in these aspects, NAMA does not accord with the basic principles of EU State aid policy:
 - i. The format, scale and scope of the proposed asset relief measure are disproportionate to the size of the Irish economy and budgetary resources and threaten the financial viability of the State itself. In particular the scope of eligible assets (i.e. the total amount of loans to be acquired and their concentration in the real estate market) is viewed as too wide;

²⁶ This complaint has been registered under case number CP 24 / 2010.

²⁷ Draft business plan announced by the Minister for Finance in October 2009.

- ii. Further, the scale and scope of NAMA and powers given to it may distort competition on the Irish real estate market;
- iii. The NAMA scheme does not provide for any mechanism for ensuring the maintenance of lending by banks to the real economy and no system for monitoring such lending;
- iv. On the basis of the business plan, it appears that the NAMA scheme would be put into operation prior to the approval by the European Commission;
- v. There is a general lack of ex-ante transparency or disclosure in particular in relation to impairments, upfront assessment and valuation of eligible bank loans;
- vi. The valuation methodology is viewed as unrealistic, in particular there is no disclosure of assumptions used to generate the LTEV. The valuation methodology does not appear to be based on a market-driven price discovery process or subject to a third party assessment;
- vii. The proposed NAMA scheme does not include an adequate burden sharing mechanism of the costs with participating institutions, which would allow for a better alignment of the Scheme with public policy interests. In particular the Scheme does not include any real claw back mechanism which would allow for the State to recover some of the losses from participating banks in the longer run;
- viii. The Scheme does not include any provision for an in-depth restructuring of participating banks. The Scheme does not include any provisions for better governance in the Irish banking sector (in particular with regards to dividend policies or executives' remuneration);
- ix. The NAMA Scheme is silent on the issue of any potential recapitalisation that participating institutions may need following the transfer of the assets; and
- x. The prospective participation of Anglo Irish Bank to NAMA is viewed as not necessary, as Anglo Irish Bank is not perceived by Senator Regan as an institution of systemic importance.

(78) The Commission has analysed the content of the complaint submitted by Senator Regan. It intends to address his points in the contents of this decision (paragraphs (134) to (140)).

V. ASSESSMENT

1. State aid character of the Scheme

(79) As set out in Article 107(1) of the TFEU, 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 or the production of certain goods shall,

in so far as it affects trade between Member States, is incompatible with the internal market.

- (80) The notified measures constitute aid to the participating institutions pursuant to Article 107(1) TFEU.
- (81) Firstly, the purchase of the assets is financed up to 95% by State guaranteed bonds. In current circumstances, it is highly unlikely that a market economy investor would have purchased the proposed eligible bank assets out of private funds on a comparable scale and on similar terms. Therefore, without such State guarantee, the measure could not be implemented. Therefore it is clearly financed albeit indirectly, through State resources²⁸.
- (82) Secondly, since this Scheme confers an economic advantage on beneficiaries and strengthens their position vis-à-vis their competitors in Ireland and in other Member States, these measures distort competition and affect trade between Member States. The advantage is selective since it benefits only beneficiaries under the Scheme and is provided through State resources.
- (83) Finally, point 15 of the Communication from the Commission on the treatment of impaired assets in the Community banking sector (the Impaired Asset Communication or IAC)²⁹ states that public asset relief measures are considered as State aid if impaired assets are purchased at a value above the market price. As described in paragraph (68), the anticipated transfer price will be the bank asset's long-term economic value which will be greater than the bank asset's current market value.
- (84) The Commission also notes that NAMA's stamp duty exemption on acquisition of the assets may also be viewed as additional State aid. The tax exemption alleviates NAMA from some costs and allows the scheme to take place for the direct benefit of the participating institutions. So the stamp duty exemption could also constitute an indirect benefit to the participating institutions. If NAMA was to be considered as an undertaking, its exemption from stamp duty upon acquisition may also be viewed as direct State aid to NAMA.

2. Compatibility

Applicability of Article 107(3)(b) TFEU

- (85) Article 107 (3)(b) TFEU enables the Commission to declare aid compatible with the internal market if it has the effect "to remedy a serious disturbance in the economy of a Member State". The *Communication from the Commission on application of State aid rules to measures taken in relation to financial institutions in the context of the current*

²⁸ The majority of NAMA shares will be held by private investors to avoid the consolidation of NAMA debt with Ireland's public debt (see paragraph (35)). However, the amount of equity capital invested by such private investors is very small compared to the amount of State guaranteed bonds (ie. EUR 51 million as opposed to EUR 51.3 billion) and NAMA, hence the finance minister will, through veto rights, keep control over NAMA's decisions and overall management. Therefore, NAMA's shareholding structure does not materially counterbalance the public nature of its funding sources.

²⁹ Communication from the Commission on the treatment of impaired assets in the Community banking sector – OJ C 72 of 26.03.2009, p.1.

*global financial crises*³⁰ (the Banking Communication) confirms and details the principles of the applicability of Article 107(3)(b) of the TFEU to any support measure for banks in the context of the global financial crisis.

- (86) The Commission acknowledged in its recent approval of a revised Irish guarantee scheme³¹ that the threat of a serious disturbance in the Irish economy continues and that measures supporting banks are suitable to address that threat. Further, the Commission considers that the present scheme concerns the entire Irish banking market and does not dispute the analysis of the Irish authorities that concerns remain over the asset quality of financial institutions in Ireland. Indeed, if these problems are not addressed, they will result not only in difficulties for the Irish banking sector but, owing to that sector's pivotal role in providing financing to the rest of the economy, they will also have a systemic effect on the Irish economy as a whole. Hence it finds that the scheme is apt to remedy a serious disturbance in the Irish economy.

Framework for evaluating compatibility

- (87) In line with the Banking Communication, in order for an aid or aid scheme to be compatible under Article 107(3)(b) TFEU, it must comply with the general criteria for compatibility under Article 107(3) TFEU. This implies that the measure has to be appropriate, necessary and proportionate.
- (88) More specifically, asset relief measures, irrespective of their exact nature, need to be assessed under the Impaired Assets Communication which provides guidance as for the methodologies concerning the valuation of the impaired assets, the necessary remuneration of the State for the asset relief provided and the procedural steps that are to be followed as well as the criteria that will be used to evaluate the State aid given to the banks as a result.

3. Assessment

- (89) The Impaired Assets Communication sets out criteria for the compatibility of such measures with the internal market. These criteria comprise (i) the appropriate identification of the problem and disclosure, (ii) the appropriateness of the remuneration and burden sharing, (iii) the alignment of banks' incentives with public policy objectives, (iv) the eligibility of assets, (v) the valuation of eligible assets, (vi) the management of assets subject to relief measures and (vii) the requirement of the assessment of a restructuring plan by the Commission.
- (90) The purpose of this decision is to assess all the elements of relevance of the notified asset relief measure under State aid rules as set out in the IAC. The Irish authorities commit however to notify each "tranche" of transferred assets, such notification to include detailed information on the assets transferred and their valuation³². The Irish authorities also commit to notify either a restructuring plan for each beneficiary institution within 3 months of its accession to the asset relief programme³³. The

³⁰ OJ C 270, 25.10.2008, p. 8

³¹ ELG Scheme, Commission Decision of 20.11.2009 Credit Institutions Eligible Liabilities Guarantee Scheme, in case N349/2009

³² Annex III to the Impaired Assets Communication.

³³ A fully fledged restructuring plan will have to be submitted to the Commission if the aid amount received through the asset relief measure represents at least 2% of the participating institution risk weighted assets.

Commission will reassess the aid granted in light of the adequacy of the actual notified asset transfers and restructuring plans.

- (91) Annex V of the Impaired Assets Communication states that any Commission approval of an impaired assets scheme will be granted for a period of 6 months. This limitation in time aims at preventing the granting of open-ended approvals for schemes whose terms were still subject to change). In the case of NAMA, the Commission notes that all the parameters of the scheme (which are being assessed in this decision) are already final in particular, eligible institutions, eligible assets, and the valuation methodology (including the State remuneration) and not subject to further revision. In light of the scale and complexity of the transfer process, the implementation of the scheme will take place over several months as indicated in paragraph. In this context the Commission considers appropriate not to limit the approval of the scheme to 6 months, in order to allow for its proper implementation.
- (92) With regard to issues pertaining to the valuation methodologies employed in the context of the asset relief scheme, the Commission has drawn on technical assistance provided by external experts under contract by the Commission and by experts from the European Central Bank.

Transparency and ex-ante disclosure

- (93) The Impaired Assets Communication requires that any bank participating in an asset relief scheme should (i) provide full ex-ante transparency and disclosure of impairments on the assets to be covered by the scheme (including the additional impairment and/or losses to be taken as a result of the participation to the scheme) and (ii) follow up any application to the scheme by a full review of that bank's activities and balance sheet with a view to assessing the bank's capital adequacy and its prospect for a return to future viability.
- (94) The Commission views positively that the incurred losses for the participating institutions from the asset transfer will be identified in advance of the asset transfer and that the valuation process for the eligible bank assets will be certified by recognised independent experts (Ernst & Young for the Financial Regulator and KPMG for NAMA), and validated by the relevant supervisory authority, the Financial Regulator. The valuation outcome per se will be certified by each independent loan valuer who will provide a certificate to the audit coordinator.
- (95) Further the Act provides that any data supplied by a participating institution to NAMA will have to be jointly certified by the chief executive officer and chief financial officer of the participating institution, who have a duty according to the Act "to act in utmost good faith".
- (96) Consequently, at this stage, the Commission is satisfied that, as a scheme, NAMA includes adequate transparency and ex-ante disclosure provisions. For each individual notification, the Commission therefore expects to receive a letter from the Financial Regulator validating the valuation process and the losses incurred by the relevant participating institution.
- (97) As for the full review of the bank's activities and balance sheet, the Commission expects for each participating institution to submit a restructuring plan, and for those institutions

benefiting from other aid measures, the inclusion of the impact of their participation in NAMA in the restructuring plans.

Burden-Sharing

- (98) The principle of burden-sharing as set out in the Impaired Assets Communication requires that banks ought to bear the losses associated with impaired assets to the maximum extent. Therefore, the assets should be transferred at a price that matches or stays below the real economic value.
- (99) The Impaired Assets Communication also explains that burden-sharing is achieved through an adequate remuneration of the scheme. The Impaired Assets Communication states indeed that any pricing of asset relief must include a remuneration for the State that takes account of the risks of future losses exceeding those that are projected in the determination of the "real economic value".
- (100) In the case of NAMA, as described in paragraph (68) above, it is intended that the assets will be transferred at a price which is no greater than the bank asset's long-term economic value. Further, as described in paragraph (71), the remuneration of the State is embedded in that purchase price as a margin added to the risk-free rate (Irish government bond yield for the relevant maturity) used to discount the assets' expected long-term cash flows.
- (101) The Commission views positively the commitment by the Irish authorities not to transfer the assets at a price greater than the real economic value of the bank asset. Further, the Commission, in paragraphs (113) to (122) below, validates the general methodology used to determine the assets' long-term economic value. In particular, the Commission agrees, that, to the extent that the discount rate and in particular the margin added to the risk-free rate is viewed as adequate, the long-term economic value so determined also includes an adequate remuneration for the State.
- (102) The Irish authorities will discount the asset cash flows at a rate equal to the Irish government bond yield as of 21 December 2009³⁴ for the maturity equal to that used for the relevant asset cash flows plus 170 bps. Based on the information available at this time on the portfolio, a reasonable estimate for the average initial risk margin of the loans is in the region of 200 basis points³⁵. Further, a reasonable estimate of expected losses on these loans at the time they were granted is around 30 basis points³⁶. Therefore, the Commission notes that a risk margin above the risk-free rate of 170 basis is a reasonable estimate for the remuneration that market operators would have required at the time of pricing³⁷ to cover unexpected future losses on such assets.
- (103) Consequently, the Commission views that NAMA provides an appropriate framework for an adequate burden-sharing of the costs of the measure between the State and participating institutions. The Commission also notes that, based on the information received on the risk weighted assets of the applicant institutions, that remuneration would also constitute adequate burden-sharing, if that remuneration was measured

³⁴ Date on which the Act was passed.

³⁵ NAMA draft business plan published in October 2009.

³⁶ Based on information provided by HSBC, experts for the Irish authorities.

³⁷ The loans to be acquired have been granted over several years prior to the outset of the financial crisis. As such, the Commission considers that the initial risk margin reflects "normalised market conditions".

against the regulatory capital relief obtained by the participating institutions through the scheme³⁸.

(104) Finally, the Commission notes that some additional burden-sharing may be embedded in the payment in the form of subordinated bonds of 5% of the transfer price. However, this form of burden-sharing could be triggered only in the unlikely scenario, where NAMA makes such high losses over its lifetime that it would not be able to recover the capital invested. The Irish authorities consider this situation extremely unlikely. Regarding the Irish authorities' intention to introduce a levy on the participating financial institutions if, on the winding up of NAMA, there were to be a deficit, it is not possible to judge its contribution to burden-sharing as neither the likelihood nor the characteristics of this levy can be estimated at this stage.

Alignment of banks' incentives with public policy objectives.

(105) Under section 5.3, the Impaired Assets Communication requires that within an impaired asset relief measure, banks' incentives be aligned with public policy objectives, through (i) a 6 month maximum enrolment window, (ii) mechanisms to ensure that banks most in need to participate do participate and (iii) appropriate behavioural constraints to, among other things, limit the impact on competition.

(106) The Act provides for an enrolment window limited to 60 days after the establishment date of the scheme. This window opened on 21 December 2009 and closed on 19 February 2010³⁹. The NAMA scheme is open to any credit institution and each application is assessed by the Minister, in consultation with the Governor and the Regulatory Authority on the basis of criteria that the Commission views as objective and non discriminatory (paragraph (12) and (13) and Annex I). The Commission also notes that 3 out of the 5 applicant institutions are among those that have already received material amounts of State aid, which demonstrates their need for joining the impaired assets scheme.

(107) Further, the Act includes a number of behavioural constraints in particular it provides that participating institutions may be required to restrict the balance sheet growth, to restrict take-over activities, to reduce balance sheet or to restrict or require consolidation and merger. The Commission notes that while the Act itself does not provide for additional constraints, it is anticipated that all the participating institutions will (if they have not already done so) submit a restructuring plan which will include behavioural constraints such as restrictions on executive remuneration, caps on dividends and coupons, other safeguards which ensure aid received is not used to the detriment of competitors and the obligation to provide credit to the real economy.

(108) The Commission, therefore, concludes that NAMA as a scheme includes adequate provisions to align participating banks' incentives with public policy interest and will further assess behavioural constraints in the context of the individual notifications and restructuring plans.

Eligibility of Assets

³⁸ Annex IV of the IAC stipulates that when identifying the necessary target return of an impaired asset relief measure, member states could be inspired by the remuneration that would have been required for recapitalisation measures to the extent of the capital effect of the proposed asset relief.

³⁹ Five institutions have formally applied (AIB, ENBS, BoI, Anglo Irish Bank and INBS).

(109) As regards the eligibility of the assets, section 5.4 of the IAC provides that asset relief measures require a clear identification of impaired assets and that certain limitations in relation to eligibility must apply to ensure consistency and prevent undue distortions of competition. The Impaired Assets Communication however further sets out that a balance needs to be found between meeting the objective of immediate financial stability and the need to ensure the return to normal market functioning, which would plead in favour of flexibility when identifying classes of assets. In particular, whilst the IAC cites as eligible assets those that have triggered the financial crisis (the IAC explicitly refers to US mortgage-backed securities), it also allows for the possibility to "extend eligibility to well-defined categories of assets corresponding to a systemic threat upon due justification, without quantitative restrictions"⁴⁰. In this context the IAC specifically mentions as one of those systemic threats, the burst of a bubble in the domestic real estate market

(110) As mentioned in paragraphs (15) to (19), the measure targets a specific type of assets, namely (i) all loans issued for the purchase, exploitation or development of land as well as loans either secured or guaranteed by land, and (ii) some of their associated commercial loans. Commercial loans are loans to the same borrowers which are interconnected to the land and development loans.

(111) The Commission recognises that the Irish financial system and domestic economy has been affected by the burst of a real estate bubble⁴¹ and agrees that as a consequence loans to the real estate sector are at the source of the principal uncertainties in relation to asset quality in the Irish financial system. Indeed, HSBC, the advisor of the Irish authorities, estimates that approximately 76% of the total non-performing aggregate loan exposure of the prospective participating credit institutions constitutes loans backed by land and property development and their associated commercial loans.

(112) On the basis of the above Ireland has developed a proportionate approach within the meaning of point 34 of the Impaired Assets Communication and the scope of assets to be included in the NAMA Scheme is in line with the eligibility requirements of the IAC.

Valuation

(113) Regarding valuation, the Impaired Assets Communication notes in section 5.5 that a correct approach to valuation is of key importance to prevent undue distortions of competition. At this stage, the Commission has only been provided with details of the intended valuation methodology and framework but has not yet received any detailed description, statistics or breakdown of the eligible assets. No actual asset valuation has been received either.

(114) The Commission will therefore assess the compatibility of the elements of relevance of proposed valuation methodology under State aid rules as set out in the IAC. Actual valuations will be assessed separately when detailed information on actual transfers will be notified⁴².

⁴⁰ See point 34 of Impaired Asset Communication.

⁴¹ It is estimated that Irish property prices have fallen by an average 50% since early 2007 across all the sectors and regions comprising NAMA exposures.

⁴² As per Annex V of the Impaired Asset Communication.

(115) First of all, the Commission views positively the generic approach chosen by the Irish authorities to complete two types of valuation, a current market value valuation and a long-term economic value valuation. As matter of fact, the Irish authorities are proposing to perform four valuations (see paragraph (53)):

- i. The property's current market value;
- ii. The property's long-term economic value;
- iii. The bank asset's current market value;
- iv. The bank asset's long-term economic value.

(116) The proposal to produce both a current market value of the transferred asset as well as a long-term economic value of such assets meets the requirements of the Impaired Assets Communication and so does, in principle, the proposal of the Irish authorities to set the transfer price of the assets at a maximum equal to the bank asset's long-term economic value.

(117) Concerning the methodology employed to determine the bank asset real economic value of those bank assets, the Commission agrees with the fundamental premise of the proposed valuation methodology which is the evaluation of the assets using a discounted cash flow method taking into account the timing and reliability of the cash flows coupled with an appropriate discount factor (see paragraph (51)). As such, this approach is also in line with the Impaired Asset Communication⁴³.

(118) Concerning the discount rate applied to the cash flows, the Irish authorities will discount the asset cash flows over 3 maturities (3, 5 and 8 years) depending on the recovery prospects (paragraph (64)) at a rate equal to the Irish government bond yield as of 21 December 2009 for the relevant maturity plus 170 basis points⁴⁴. Based on the information available (on the loan initial margin and expected losses), the Commission notes that the margin added to the risk-free rate is a reasonable estimate for the remuneration of unexpected losses that a market operator would have required for similar assets under normalised market circumstances (paragraph (103)).

(119) Concerning the determination of those assets' future cash flows and the assumptions used to model such future cash flows, the Impaired Assets Communication states that it should be based on observable market inputs and realistic and prudent assumptions⁴⁵. The Commission recognises that the valuation of land and development loans is a very complex exercise which involves first of all an in depth analysis of each asset's legal and economic characteristics, complex modelling and a relatively large number of assumptions.

(120) The Commission views positively the approach chosen by the Irish authorities to value each bank asset individually on a case-by-case basis, and in particular to perform an

⁴³ Point 40 of the IAC states that the Commission would consider a transfer value reflecting the underlying long-term economic value of the assets on the basis of underlying cash flows and broader time horizons as an acceptable benchmark indicating compatibility of the aid amount as the minimum necessary.

⁴⁴ The Irish government bond yields as of 21 December 2009 with a 3, 5 or 8 year maturity are 2.844%, 3.900% and 4.462% respectively, resulting in a total discount rate of 4.544%, 5.600% and 6.162% for each maturity respectively.

⁴⁵ IAC, annex IV.

individual valuation of each underlying real estate property, which is a critical input in the determination of the bank asset's valuation. Further, the envisaged process put in place by the Irish authorities will allow the Irish authorities to have an adequate understanding based on independent professional expert opinions of the current market value of the underlying property, the exact legal status of the bank asset (including all possible interconnections with other assets to the same borrowers which could have an impact on the cash flows to be received under the bank asset) and current performance of the asset (see paragraphs (55) to (58) for a description of the appointment of the valuers and approach to preparing valuation reports). The audit and claw back mechanisms put in place (see paragraph (69)) should ensure that the ultimate transfer price has been determined according to the agreed guidelines and methodology.

(121) Concerning the individual assumptions to be used in the modelling of the valuation to determine the bank asset's long-term economic value, the Commission will assess detailed information regarding the assets covered and their valuation when reviewing the individual notifications of the transferred tranches⁴⁶. However, the Commission agrees with the methodology described by the Irish authorities to the Commission for a number of key assumptions as follows:

- i. Perimeter of cash flows. The perimeter of cash flows eligible to repay the bank asset is a function of the legal status of the loan and of the interconnections it has with other loans to the same borrower. In this regard, it is critical to determine whether the loan is legally in default and the consequences thereof according to the terms of the underlying loan contract⁴⁷. The Commission agrees with the principle that the expected loan repayment cash flows should match the legal position of the loan and its right to additional cash flows, in particular the cash flows generated by the property itself (i.e. rental payments and sales proceeds) but will only assess the validity of this assumption in the context of concrete cases.
- ii. Time horizon over which the cash flows will be assessed. The Impaired Assets Communication stipulates that cash flows could be analysed over "broader time horizons"⁴⁸. In the case of land and development loans, the Commission agrees with the principle put forward by the Irish authorities that the determination of such time horizon should be derived from the property valuation performed by the external experts and from their assessment of its recovery prospects. The time horizon over which the real economic cash flows of the assets will therefore be determined as a function of the level of

⁴⁶ The Commission is and will be receiving technical assistance from external valuation experts to assess both the generic valuation methodology and the individual valuations.

⁴⁷ For example, if a loan is legally in default, this may result, depending to the terms of its contract, in NAMA being entitled to immediately enforce the underlying security (ie. the piece of real estate) and divert all the cash flows received from the underlying property (typically rental cash flows) to the repayment of the loan. Furthermore, depending on the nature of the interconnection a loan has with other loans to the same borrower, any excess on the enforcement of the security of one loan may be used for the repayment of another. The right of NAMA to receive such additional cash flows to use them to repay the bank asset (ie. cash flows in excess of the contractual interest and principal payments on the loan itself) will have a material impact on the repayment prospects and therefore on the valuation of the bank asset.

⁴⁸ IAC, point 40.

uplift above the current market value of the property that the external valuers deem achievable if the loans are being worked out over a longer period of time (paragraph (121)(iii)). Real economic cash flows will be determined and discounted over three main maturity assumptions as follows: (i) assets with poor recovery prospects as demonstrated by an uplift above CMV of 10% or less will be valued over 3 years, (ii) assets with medium recovery prospects between 10.0% and 15.0% uplift will be valued over 5 years and (iii) assets with recovery prospects justifying an uplift in excess of 15.0% (capped at 25.0%) will be valued over 8 years. Further, loans for which the CMV of the underlying property exceeds the nominal outstanding of the loan will be valued over their remaining maturity. The Commission considers that this methodology is in line with the principle of the Impaired Asset Communication that assets should be valued over a broader term horizon and that it uses prudent and realistic⁴⁹ assumptions for the work out periods over which the optimal recovery prospects for each asset are likely to be achieved.

- iii. Property long-term economic value. The Irish authorities have indicated their intention to derive the long-term economic value by applying an "uplift" factor on the current market value. The Commission views the process in place for the determination of the current market value as adequate to obtain an objective, independent and as fair as possible current market value for these assets. Concerning the uplift, the Commission understands that it will be determined on a case-by-case basis as a result of the in-depth analysis and review of the underlying property. For land assets that uplift will not exceed 25% individually and 20% for the portfolio of a participating institution as a whole⁵⁰. The exact level of uplift will however only be assessed in the context of actual valuations.
- iv. Assumptions related to partly completed developments. Valuing a partly completed development involves a number of additional assumptions to determine the expected profitability of the completed project as opposed to the partly developed land. The Irish authorities will mainly rely on the opinion of their external valuers to determine whether the loan backed by a fully developed land will be more valuable (after taking into account all the costs associated with the completion of the development) than as it currently stands. The Commission agrees with the principle of relying on experts' opinions, which the Commission believes will be provided in an independent and professional manner, but will assess all the assumptions involved in this exercise on the basis of the individual notifications.
- v. Enforcement costs. Due to the impaired nature of most of the assets (default of the loan itself or of an interconnected loan), NAMA will in most cases be entitled to become the direct owner of the underlying

⁴⁹ These assumptions have been validated by the market experience of the Irish authorities' and Commission experts.

⁵⁰ [...]

property. The seizure of the underlying property by NAMA could be achieved in a number of ways, including by legal enforcement. The costs associated with a full legal enforcement process are approximately 15.00%⁵¹. It is however very difficult to predict ex-ante the proportion of assets for which NAMA will have to go through a full legal enforcement process. The Irish authorities propose to apply enforcement costs of 5% to all the assets. This corresponds to over 50% of the non-cash flow producing loans incurring a 15% enforcement costs. The Commission considers, on the basis of the information available, that this is a reasonable and prudent assumption.

- vi. Other numerical assumptions. The cash flow modelling of land and development loans involves a number of other assumptions, such as assumptions related to rental cash flows (vacancy rate, re-rental rates etc...). The Commission agrees with the principle of such assumptions being important assumptions in the assessment exercise but will review them in light of actual asset valuations.

(122) The Commission views positively the valuation methodology which the Irish authorities intend to use to value the bank assets and finds it in compliance with the requirements of the Impaired Assets Communication. The assessment of the actual valuations will be performed when assessing each transfer notification. The Commission expects those valuations to follow the principles presented by the Irish authorities and described herein in paragraphs (113) to (121). Because of the large number of assets expected to be transferred, some assets might be transferred before the actual assessment of the relevant notification by the Commission has been performed. Any payment in excess of the long-term economic value of the assets, as determined following the Commission's assessment, will be clawed back by the Irish authorities from the relevant participating institution (paragraph (69))⁵².

Management of assets

(123) As regards the management of assets, section 5.6 of the IAC requires a clear functional and organisational separation between the beneficiary and its assets, notably as to their management, staff and clientele. The Communication states in that respect that this should prevent conflicts of interest.

(124) Under the proposed scheme, the bank assets will be acquired from participating institutions by NAMA and will therefore be removed from the balance sheets of the banks upon transfer. This ensures a clear functional and organisational separation between the participating institutions and the bank assets which is consistent with the provisions of the Impaired Assets Communication.

(125) The Act grants NAMA a number of powers, rights and exemptions deemed necessary, expedient for, or incidental to the achievement of its purposes and the performance of its function, i.e. acquiring such eligible bank assets from participating institutions as is appropriate and dealing with those assets expeditiously, protecting or otherwise

⁵¹ Market standard level validated by external experts.

⁵² This claw back mechanism is in line with the requirement of point 43 of the IAC

enhancing their value in the interests of the State. A number of these powers, rights and exemptions are beyond those available to market operators dealing on the Irish real estate market. In light of the scope and scale of the NAMA scheme in relation to the size of Irish real estate market, careful consideration must be given to the potential distortive effects of the use of such extended powers on competition on this market.

(126) The Commission acknowledges that the existence of NAMA and the scope and scale of its acquired assets are necessary to address the serious disturbance to the Irish economy created by the burst of the real estate bubble. The Commission further recognises that because of the scale of the scheme and the very large number of loans to be acquired, a number of exemptions and rights are necessary and justified to facilitate and expedite the acquisition process and to correct the impact of any obvious oversights which are likely to occur in a due diligence process of this scale and complexity. Importantly, none of these powers are taken into account in determining the value of the asset transferred.

(127) The Commission notes however that a number of powers, rights and exemptions are granted to NAMA for the management of the assets post acquisition with a view to help the agency achieve the maximum recovery value for the assets. Such powers, in particular when they are specific to NAMA and not available to market operators are potential sources of competition distortions. In its assessment, the Commission has in particular focused on those specific powers which it considers to be potentially more distortive. For those, the Commission has asked commitments from the Irish authorities as follows:

- i. Power to make an order vesting in NAMA the interest in land concerned of a chargor (sections 152 to 156 of the Act). This remedy would allow NAMA to hold the land concerned rather than putting it up for sale immediately and then would avoid flooding the market with fire sales. The Commission recognises that the ability to work out a loan and its security over a longer time horizon is central to the valuation process of the assets and in line with requirements of the Impaired Assets Communication. The Commission however relies for the use of this power on a commitment from the Irish authorities (paragraph ((74)vii.1)): NAMA will not use this power in the context of a syndicated loan without the agreement of the other syndicate members. Similarly, for any other mortgage on the property, the Irish authorities undertake that NAMA will get agreement of the holders of equivalent charges, in terms of ranking and priority, before using this power. The Irish authorities further commit to include a clause to this effect in the Code of Conduct relating to non-participating institutions to this effect.
- ii. Power to compulsory acquire land (sections 157 to 171 of the Act). NAMA is granted the right to ask the Court for a compulsory purchase order of a land in cases where certain debtors try to frustrate the objectives of NAMA. Such power is not available to a market operator and could potentially affect the valuation of properties owned by other parties. The Commission notes that the Act provides that an application to the Court for such an order may only be made if NAMA has first tried to acquire the land by agreement. Further, the

Commission relies on the commitment from the Irish authorities that NAMA will only exercise the general power to seek a compulsory purchase order contained in Section 158(1)(a) of the Act in circumstances where there are issues concerning ransom strips or access or related issues and the particular facts or the circumstances involved do not clearly fall within the terms of any of the five other situations set out in subsections (1) and (2) of sections 158 (paragraph (74)vii.2);

- iii. Right to unilaterally amend contracts (section 102(3) of the Act). The Act grants NAMA the right to unilaterally amend contracts. This power could potentially impact the position to other parties to the same contracts or parties which have interest in the same underlying asset or in a connected asset. The Commission notes positively that the Act provides that such amendment has to be a term as close as possible to the original term and further relies on the commitment from the Irish authorities that NAMA will consult with the Commission on the appropriate use of this power prior to its exercise;
- iv. Removal of limitations on transfer of assets (Section 139 of the Act). The right gives NAMA the ability to dispose of the assets as it thinks fit disregarding any limitations on the transfer of assets that the loan documentation may include. This could potentially negatively affect the interests of another party to the same agreement or to a party who has interest in the same underlying property. To mitigate this risk, the Commission relies on the commitment by the Irish authorities that NAMA will address in the Code of Conduct the use of such power in the context of a syndicated loan and where the rights of the members might be affected. Similarly the Irish authorities commit that NAMA will address in the Code of conduct the position of other loans on the property and ensure the rights of holders of those loans are not degraded.
- v. Power to request information from the Tax Authorities (section 204(3) of the Act). The Act grants the right to NAMA to receive information on a borrower directly from the tax authority. This right is not available to a normal market operator which could create distortions of information and negatively affect the interests of third parties. However, the Irish authorities commit that NAMA will not to use this power.
- vi. Finally the Act grants NAMA the right to invoke section 228(2) of the Act as a defence against any claim that might be brought against it pursuant to section 286 to the Companies Act 1963. This section basically gives the right to NAMA to receive payments from an insolvent company ahead of other creditors without the risk of seeing such payments invalidated by the Court under section 286 of the Companies Act 1963. The Commission views this power as potentially highly distortive as it directly affects other market competitors and third parties. The Commission however relies on the commitment from the Irish authorities that NAMA undertakes to consult with the

Commission before invoking section 228(2) as a defence to any claim that might be brought against NAMA and likewise to the fullest extent to which it is within NAMA's power, NAMA undertakes that it will only assert section 228(2) as a defence to any claim brought by the liquidator of an insolvent company where NAMA believes that another creditor of the company has behaved aggressively in securing the payment of monies owed to that creditor.

- (128) In addition, whilst the Commission recognises that the other post acquisition powers granted to NAMA by the Act are justified in the context of the objectives of the measure, the Commission still believes that the supervision of the use of those powers is necessary. Therefore, the Commission has required and obtained the commitment by the Irish authorities to report on a yearly basis on the use of such post acquisition powers to both the Commission and the Irish competition authorities (paragraph (74)vii.7). This commitment will allow the Commission and the Irish competition authorities to take any action they consider as adequate if they deem that NAMA's use of its powers has resulted in competition distortions.
- (129) Concerning NAMA's tax status, NAMA's stamp duty exemption upon acquisition may constitute additional (albeit indirect) State aid to the participating banks. Further, if NAMA was to be considered as an undertaking, its exemption from stamp duty upon acquisition could also be viewed as aid to NAMA itself. However, the Commission views the exemption from stamp duty for the acquisition of the assets as an integral part of the relief measure and as such necessary and appropriate to help the measure fulfill its objectives. Therefore, the Commission views it that if indeed NAMA's stamp duty exemption upon acquisition constituted direct aid to NAMA and/or indirect aid to the participating banks, such aid would be compatible by virtue of the compatibility of the scheme as a whole with Article 107 (3)(b) of the TFEU. The Commission however stresses the point that following acquisition, NAMA's operations will be subject to stamp duty like all other market operators.

Follow-up (restructuring plan)

- (130) As regards the need for an assessment of a beneficiary's balance sheet and activities section 6 of the IAC states that an application for aid by an individual beneficiary should be followed by a full review of that beneficiary's activities and balance sheet, with a view of assessing capital adequacy and the prospects for future viability.
- (131) Annex V to the IAC requires that a restructuring plan for each beneficiary has to be notified to the Commission within three months from its accession to an asset relief programme.
- (132) The Commission notes that 3 out of the 5 applicants are already benefit from other support measures and have already committed to submit restructuring plans. If their participation to NAMA is accepted, the Commission will assess those restructuring plans taking into account their participation to NAMA. For any other potential participating institutions, the Commission relies on the Irish authorities' commitment to provide a restructuring plan within 3 months from their accession to the NAMA scheme.

(133) Further, Ireland has committed to notify the transfer of assets to NAMA individually. In the situation where the Commission has taken a decision on the restructuring plan of an institution participating in the NAMA scheme before completion of the transfer of all its eligible assets to NAMA, and if following that completion it appears that the participating institution has received through NAMA more aid than initially anticipated in the restructuring plan, then such additional aid will be separately notified in accordance with EU State aid rules and assessed by the Commission in accordance with its Communication on "The return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules"⁵³. . .

Response to Senator Regan's complaint

(134) The Commission has assessed the content of Senator Regan's complaint. The Commission has found the NAMA scheme in compliance with the EU State aid rules concerning impaired asset relief measures for financial institutions.

(135) First of all, the Commission recalls that the implementation of the Scheme is conditional upon its approval by the Commission. Further, this decision of no objection applies to NAMA as a scheme. The Irish authorities have committed to separately notify each individual tranche of transferred assets (paragraph (74)i). Such notifications will include detailed information regarding the assets transferred and their valuation (including all underlying assumptions used to determine the asset's long-term economic value). The Commission will assess each separate notification and will in particular review and assess actual valuations of the transferred assets. The Irish authorities have committed to include in such notifications a certificate from the loan valuers and a letter from the relevant supervisory authority validating the valuation of the transferred assets (paragraph (74)ii). The letter from the relevant supervisory authorities will also validate the amount of impairments taken by the participating banks on the transferred assets. Additionally, the Commission relies on the commitment of the Irish authorities to claw back any excess payment that might become apparent after the Commission review if for practical reasons a transfer has occurred prior to the Commission decision (paragraph (74)iii).

(136) On the basis of and subject to the above mentioned commitments, the Commission has found that the proposed valuation methodology is in line with the requirements of its Impaired Asset Communication. In particular, the Commission has found that the cornerstone of the valuation process is the determination of the current market value of the underlying properties which will be performed by external valuers in an independent and professional manner. The Commission also points out that the uplift applied to the property's current market value to determine the property's long-term economic value (which is itself a key component of the bank asset's LTEV and hence of the transfer price) will also be independently determined by the independent valuers (paragraphs (121)iii).

⁵³ OJ C 195 of 19.8.2009, p. 9. For the avoidance of doubt, in this situation, the Commission would not question the accuracy of the total transfer price received by the participating institution from the State. This situation is therefore different from a situation where following an assessment of an individual transfer notification, the Commission is of the opinion that the transfer price paid is too high. In that case, the Irish authorities have committed to claw back any over payment from the participating institution. This process will not involve any further State aid notification.

- (137) Concerning the burden sharing aspect of the measure, the Commission recalls that the IAC considers as adequate burden sharing a transfer price at or below the long term economic value of the asset and an appropriate remuneration for the State. The Commission has found that both conditions were satisfied by the NAMA scheme (paragraphs (101) and (103)). This conclusion is reached without taking into account the 5% of the transfer price will be paid in the form of subordinated bonds (which would trigger burden sharing only in an extremely remote scenario), or the Irish authorities intention to introduce a levy on the participating financial institutions if, on the winding up of NAMA, there were to be a deficit (for which no assessment of the likelihood or conditions can be made at this point in time);
- (138) Concerning the format, scale and scope of the measure, the Commission firstly recalls that the choice of management arrangement for impaired assets is the responsibility of each Member State⁵⁴. Further, the eligibility criteria proposed by the Irish authorities for both participating institutions and bank assets are in line with the provisions of the IAC (paragraphs (106) and (112)). In particular, the Commission views the inclusion of the associated commercial loans as necessary to capture the entire exposure to the impaired borrower relationship as well as to help with aligning the measure with public policy objectives⁵⁵. Concerning the potential participation of Anglo Irish Bank in the Scheme, this participation will be assessed according to eligibility criteria for applicant institutions which the Commission has found to be objective and non-discriminatory.
- (139) Concerning the distortions of competition which could result from the scale of the scheme relative to the Irish real estate market as well as from the powers granted to NAMA, the Commission relies on the commitment from the Irish authorities to limit the use of those distortive powers described in paragraph (74)vii.1 to (74)vii.6 and to report on the use of post acquisition powers on a yearly basis to the Directorate General for Competition of the Commission as well as to the Irish national competition authorities ((74)vii.7).
- (140) Finally, the Commission recalls that the Irish authorities have committed to submit a restructuring plan for each participating institution within 3 months of their participation in the scheme. The Commission will assess such plans and reviews in light of the EU State aid rules and in particular of its *Communication on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules* (the Restructuring Communication)⁵⁶. That assessment will also take into account any recapitalisation needed following the participation in the NAMA scheme.

VI. DECISION

The Commission concludes that the introduction of the asset relief scheme for certain financial institutions in Ireland constitutes a State aid within the meaning of Article 107(1) TFEU.

⁵⁴ IAC, point 11.

⁵⁵ The inclusion of associated commercial loans will help NAMA maximise the recovery obtained on the entire impaired borrower relationship.

⁵⁶ OJ C 195, 19.08.2009, p. 9.

Since the above-mentioned measure fulfils the requirements of Article 107(3)(b) TFEU, as a scheme it is compatible with the internal market, with the result that the Commission raises no objections.

If this letter contains confidential information which should not be published, 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 publication of the full text of this letter to agree to the disclosure to third parties in the authentic language on the Internet site. http://ec.europa.eu/community_law/state_aids/state_aids_texts_en.htm.

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

European Commission
Directorate-General for Competition
State aid Greffe
B-1049 Brussels
Fax No: (+32)-2-296.12.42

Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-president of the Commission

Annex I

1. Eligible institutions

(141) The three factors under which eligibility of applicant credit institutions is assessed are further detailed below.

Factor 1 : Systemic importance

(142) In order to appreciate the systemic importance of the applicant credit institution, the Minister will first assess whether exclusion from participation will have a materially negative effect on the stability and proper functioning of the Irish financial system or the Exchequer. If the Minister concludes that an applicant credit institution qualifies under either of these factors it will be deemed systemic. Otherwise, before concluding that the institution is not deemed systemic, a marking scheme (see below) will be applied and if the institution does not score above 60%, it will not be deemed systemic.

(143) The marking scheme is made up of the following ten sub-criteria, for which a score ranging between 1 and 10 is granted.

- Level of deposits in the State (1 is 0% market share, 10 is dominant market position);
- Number of retail depositors in the State (1 is 0 depositors, 10 is dominant market position);
- Number of customer accounts in the State (1 is 0 customer accounts, 10 is dominant market position);
- Existence and scale of branch network in the State (1 is no branches, 10 is complete branch network);
- Position in Irish mortgage market (1 is no market participation, 10 is dominant market position);
- Position in Irish SME lending market (1 is no market participation, 10 is dominant market position);
- Position in other business lending market (1 is no market participation, 10 is dominant market position);
- Position in Irish consumer lending (1 is no market participation, 10 is dominant market position);
- Number of borrowers in Ireland (1 is no lending function, 10 is dominant market position);
- Role played in State's payment system (1 is no role in payment system, 10 is control over State's payment system)

Factor 2 : Available support, financial position of the institution and resources available to the Minister

- (144) The second assessment covers the following elements : (i) the support available to the applicant credit institution, (ii) the financial position of the applicant credit institution and its subsidiaries, (iii) the impact that a non-participation would have on the financial position of the applicant's group and (iv) the resources available to the Minister.
- (145) First, the support available to the applicant credit institution will be assessed under three categories, based on which the Minister will make a judgment following consultation with the Governor of the Central Bank and the Regulatory Authority on whether support for the institution is required :
- Liquidity support received, available, reasonably expected to be or have been available from (i) the Irish Government, (ii) any other Member State, and (iii) the parent company;
 - Capital support received, available, reasonably expected to be or have been available from (i) the Irish Government, (ii) any other Member State, and (iii) the parent company;
 - Asset relief support received, available, reasonably expected to be or have been available from (i) the Irish Government, (ii) any other Member State, and (iii) the parent company.
- (146) Second, the financial position of the applicant credit institution and its subsidiaries will be assessed based on a thorough review of financial data and stress testing. More particularly, the following elements will be reviewed : the liquidity position, the funding position, the capital position, the asset quality and risk exposures. The Minister will make a judgment following consultation with the Governor of the Central Bank and the Regulatory Authority on whether support for the institution is required.
- (147) Third, the impact that non-participation would have on the financial position of the applicant's group will be assessed based on the same above-mentioned elements, but to the extent that non-designation would impact on the applicant institution's group.
- (148) Finally, the factor to be applied by the Minister is an assessment of whether designation as a participating institution would be appropriate having regard to the resources available to him/her. Where a number of applications have been received and an assessment of the eligible assets of all applicants would result in the purchase of assets above the level of EUR 54 billion, the threshold set out in the Act, institutions will be ranked by the Minister taking account of the assessment above. Where insufficient resources are available, and taking account of the ranking in priority, the Minister may determine either to exclude the lowest ranking institution(s) or to purchase only a proportion of assets from those institutions.

Factor 3 : Compliance with all applicable obligations

- (149) This is a factual assessment only.

2. Eligible assets

(150) The classes of eligible bank assets may include :

- (a) credit facilities issued, created or otherwise provided by a participating institution
 - (i) for the purpose, whether direct or indirect and whether in whole or in part, of purchasing, exploiting or developing development land,
 - (ii) where the security connected with the credit facility is or includes development land,
 - (iii) where the security connected with the credit facility is or includes an interest in a company engaged in purchasing, exploiting or developing development land,
 - (iv) where the credit facility is directly or indirectly guaranteed by a company referred to in subparagraph(iii),
 - (v) directly or indirectly to a debtor who has provided security referred to in subparagraph (ii) or (iii), or
 - (vi) directly or indirectly to a person who is an associated debtor of a debtor to whom a credit facility described in any of subparagraphs (i) to (iii) has been provided,
- (b) credit facilities and classes of credit facilities (other than credit facilities referred to in paragraph (a)) relating to debtors or associated debtors of participating institutions (or classes of debtors or associated debtors of participating institutions) where the total amount of indebtedness in respect of such facilities to a participating institution is such that, in the opinion of the Minister, acquisition by NAMA is necessary for the purposes of this Act,
- (c) other rights arising directly or indirectly in connection with a credit facility described in paragraph (a) or (b) including
 - (i) a contract to which the participating institution is a party or in which it has an interest,
 - (ii) a benefit to which the participating institution is entitled, and
 - (iii) any other asset in which the participating institution has an interest,
- (d) bank assets associated with bank assets specified in paragraphs (a) and (b), and
- (e) any other class of bank asset of a participating institution the acquisition of which, in the opinion of the Minister, is necessary for the purposes of the Act.