EUROPEAN COMMISSION

Brussels, 23.11.2011
C (2011)7756 final corr.

PUBLIC VERSION

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COMMISSION DECISION

of 23.11.2011

ON STATE AID

No C 28/2010

implemented by Portugal

for the short-term export credit insurance scheme

(Only the Portuguese version is authentic)

(Text with EEA relevance)

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union (TFEU), and in particular the first subparagraph of Article 108(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to those provisions,[1]

Whereas:

(1) This decision concerns State aid put into effect by Portugal in the form of a short-term export credit insurance scheme (hereinafter 'the scheme').

1. PROCEDURAL ASPECTS

(2) On 12 January 2009 Portugal notified a short-term export-credit insurance scheme under section 5.1 of the Commission Communication 'Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis'[2] (hereinafter referred to as 'the Temporary Framework').

(3) Although the scheme was originally notified as short-term export-credit insurance for OECD countries, the scheme also covers domestic trade transactions.

(4) Insofar as the Portuguese authorities confirmed that the scheme was implemented as of January 2009, the Commission informed Portugal by letter dated 19 April 2010 that the scheme had been transferred to the Non-Notified aid registry.

[1] OJ C 111, 9.4.2011, p.46.

[2] OJ C 16, 22.1.2009, p. 1. The Commission has applied the Temporary Framework since 17 December 2008 and authorised the Portuguese 'Limited amounts of aid' scheme (case N 13/2009) on 19 January 2009 on the basis of the Temporary Framework.

(5) By letter of 27 October 2010, the Commission informed Portugal of the opening of an investigation under Article 108(2) of the TFEU in relation to the scheme.

(6) By letter of 29 November 2010, the Portuguese authorities sent their observations on the Commission's letter of 27 October 2010. They attached two letters from credit insurers (CESCE and COSEC) dated 22 November 2010 and 23 November 2010 respectively.

(7) The Commission's decision to initiate the procedure was published in the Official Journal of the European Union of 9 April 2011.[3] The Commission invited interested parties to submit comments on the scheme. No comments were received.

2. DESCRIPTION OF THE MEASURE

2.1. Objective

(8) The Portuguese authorities have alleged that the current financial crisis has resulted in an increased risk for commercial operations. This in turn has led to an increasingly conservative attitude on the part of credit insurers, reflected in the level of insurance cover for risks inherent in commercial operations.

(9) The objective of the scheme is to address a market failure due to the unavailability of credit insurance and to help restore confidence in the credit insurance market.

(10) Those aims are pursued through the provision of credit insurance coverage to exporters and to companies that are temporarily confronted with the unavailability of export insurance cover in the private market for transactions with buyers in OECD countries or for domestic transaction.

(11) According to the Portuguese authorities, the insurance sector has shrunk considerably since 2008, which resulted in the unavailability of cover. On 30 September 2010 the total value of the insured portfolio decreased by 32.84% between 31 December 2009 and 31 December 2009 and by a further 22.4% from 31 December 2009 to 30 September 2010. The total value of the insurance portfolio was down to EUR 15.9 billion in 2010 from EUR 30.6 billion at the end of 2008. The number of insured firms decreased from 3 709 at the end of 2008 to 2 290 in September 2010. Letters from insurers were also provided to justify the need for continuation of the scheme until the end of 2010, despite allegations in the letters that the maximum cover amount granted by the scheme would not be reached. Those letters explained the need for the scheme by referring to the increased risk of export credit insurance due to the general economic situation in times of recovery from the crisis, with a subsequent increase in prices and reduction of coverage from private insurers in certain sectors.

2.2. Legal basis

(12) The national legal basis for the scheme is Decree-Law No 175/2008 establishing the Finova of 26 August 2008 and Decree-Law No 211/1998 of 16 July 1998 laying down the rules applicable to mutual guarantee societies (as amended by Decree-Laws No 19/2001 of 30 January 2001 and No 309-A/2007 of 7 September 2007).

[3] OJ C 111, 9.4.2011, p.46.

2.3. Implementing body

(13) The scheme is implemented through the following private credit insurers active on the Portuguese market: COSEC, CESCE, COFACE and Credito y Caución.

2.4. Beneficiaries

(14) According to information submitted on 26 November 2010 by the Portuguese authorities, 399 beneficiaries were subscribed to the scheme at October 2010.

(15) The segmentation of the credit limits granted at October 2010 is reproduced in the following tables:

(16) Utilization by intermediary insurer:

Insurance company	**Beneficiaries**		**Credit limit in euro**	
	Number	**(%)**	**Value**	**(%)**
COSEC	273	68.42%	151 693 571	71.68%
Credito y Caución	43	10.78%	28 259 171	13.35%
CESCE	55	13.78%	24 747 850	11.69%
COFACE	28	7.02%	6 929 700	3.27%
Total	**399**	**100%**	**211 630 292**	**100%**

(17) Breakdown by market size in euros into domestic and export transactions in October 2010 :

	Credit limit effectively used[4]	
	Value (€)	**(%)**
Domestic trade transactions	137 175 542	73.20%
Export transactions	50 221 841	26.80%
Total	**187 397 383**	**100%**

(18) Breakdown by size of beneficiary:

Size of beneficiary	**Beneficiaries**		**Credit limit in euro**	
	Number	**(%)**	**Value (€)**	**(%)**
Big firms	126	31.58%	101 135 009	47.79%
Medium firms	158	39.60%	71 507 618	33.79%
Micro-/Small firms	115	28.82%	38 987 665	18.42%
Total	**399**	**100%**	**211 630 292**	**100%**

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[4] The total amount of credit limit granted is EUR 211.6 million, while the credit limit effectively used to cover trade operations was EUR 187.3 million.

2.5. Terms and conditions of application of the scheme

(19) The scheme covers commercial risks (such as insolvency and protracted default) linked to export transactions for periods of less than two years with OECD countries, and risks linked to domestic trade transactions.

(20) The public insurance operates as a risk-sharing facility ('a top-up') with private insurers. It is granted only as a supplement to the cover provided by a private insurer.

(21) The public insurance is granted, according to the Portuguese authorities, under exactly the same terms and conditions as the private insurance. Thus, the amount covered by the public insurance may never exceed the amount covered by the private insurer. However, the applicable insurance premium is equal to 60% of the premium charged by the private insurer. The average rate applicable under the scheme represented 0.21% of turnover, while the market rate charged by private insurers represented on average 0.36% of turnover in 2009. Even the average market rates – of 0.23% and 0.24% in 2007 and 2008 respectively – were higher than the average rate applicable under the scheme from 2009 onwards.

(22) In the event of occurrence of the insured event, any recovered amounts are divided between the State and the private insurer providing the basic cover, in proportion to the share of the total cover guaranteed, i.e. quota share. The recovery procedure is administered by the private insurer.

2.6. Duration

(23) The scheme was notified on 12 January 2009 for a duration from 1 January 2009 to 31 December 2010. No prolongation has been notified to the Commission.

2.7. Budget

(24) According to the information submitted to the Commission by the Portuguese authorities, the maximum guarantee per single beneficiary is EUR 1.5 million.

(25) According to the information submitted to the Commission by the Portuguese authorities, the overall budget of the scheme for both domestic and export transactions is EUR 2 billion.[5]

3. COMMISSION DECISION ON THE FORMAL INVESTIGATION PROCEDURE

(26) In its decision of 27 October 2010 initiating the formal investigation procedure, the Commission set out its preliminary assessment and expressed doubts as to the compatibility of the scheme with the internal market. The doubts expressed in that decision concerned:

- The application of the scheme to short-term export credit insurance, in which the pricing of the guarantee was below the level normally required pursuant to the Commission Communication on short-term export credit insurance[6] (hereinafter 'the Communication'). The Commission expressed doubts that the remuneration was necessary and proportionate to attain the objective, considering the potential distortions of competition that it implies.

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5 According to the notification of 12 January 2009.

6 OJ C 281, 17.9.1997, p.4.

- The application of the scheme to domestic transactions. The Commission expressed doubts as to the compatibility of the measure and again questioned the pricing of the guarantee provided.

4. COMMENTS BY PORTUGAL

(27) In their comments on the initiation of the formal investigation procedure, the Portuguese authorities argue that the Commission's claim that companies under the scheme benefit from an advantage that would otherwise not be available is not consistent with the objectives expressed in the Temporary Framework. To prove the market failure, the Portuguese authorities refer to the loss ratio, which had attained a record of 102% in 2008, despite the fact that the number of firms covered by insurance had decreased by 29.41% at the end of 2009 compared with the end of 2008 and by another 12.53% by the end of September 2010. The value of the insured portfolio had decreased by 32.84% at the end of 2009 compared to end 2008 and by another 22.36% at September 2010. Portugal also argues that other Member States have also adopted such schemes.

(28) As regards the selective nature of the advantage, Portugal argues that the scheme **is not selective**, but instead constitutes a measure of general character which does not entail any intra-sectoral or cross-sectoral discrimination. Portugal also deplores the absence of a definition by the Commission of what constitutes a general measure. According to Portugal, the absence of discrimination is proven by: (i) the application of the scheme also to companies from other Member States which are active in Portugal; (ii) the acceptance of applications to the scheme from all four insurers active in Portugal, all of which are held at least in part by foreign entities; (iii) the absence of a change of the financing needs during the crisis; (iv) the major beneficiary of the scheme, which in October 2010 was the segment of operations relating to the national market (73.2%); (v) the possibility of all firms operating in Portugal to use the scheme, independently of whether the nature of their activities is linked to trade in goods (the sectors 'construction', 'transport' and 'other services - excluding commerce' have benefitted from the scheme for the amounts of EUR 2 155 000, EUR 471 500 and EUR 4 580 000 respectively), although by their nature, export credits are mainly related to transactions in goods. Moreover, the **top-up model** would not be a source of discrimination, according to Portugal, as it does not prevent any firm from negotiating such a policy with a private insurer. The public authorities rely entirely on the risk assessment of the private insurers. Also, according to the Portuguese authorities, the **maximum limit** set per insurance does not prevent access to it by big firms, which have benefitted from the scheme (up to 47.79% in terms of value of operations, as opposed to 33.79% for medium-sized and 18.42% for small-sized firms, but only up to 31.58% in terms of number of beneficiaries, as opposed to 39.60% for medium-sized firms and 28.82% for small-sized firms). That maximum limit is designed to ensure that the State resources involved are proportional to the objectives pursued, and that risk is well diversified, while at the same time ensuring access to the scheme for a greater number of firms. The fact that the maximum amount of the scheme has not been used stands as a proof of the absence of discrimination for big firms, according to the Portuguese authorities. Finally, Portugal questions the link between the case law indicated by the Commission in point 36 of the decision to open the formal investigation procedure and the discrimination. It regrets that the Commission has not set out criteria that a measure must fulfil in order to be of a general nature.

(29) Portugal justified the **lower pricing** of the scheme compared to that of private insurance, arguing that an adverse selection can be observed as firms chose to ensure the less risky operations under the scheme, leaving the riskier operations for coverage by the private insurance. In that respect, the reasoning of the Commission would not be relevant, according to the Portuguese authorities, in the sector of export credit, where risk does not increase with the amount of the credit as it does for bank credits. The low risk is also shown, according to the Portuguese authorities, by the fact that at October 2010 the volume of claims accumulated in the scheme increased by only 0.26% of the total value of insurance contracted. Moreover, the pricing applied to the State guarantee corresponds, according to the Portuguese authorities, to the market pricing before the crisis and does therefore not entail an advantage for its beneficiaries.

(30) Further, according to the Portuguese authorities the scheme does not give rise to a distortion of competition between Member States, because: (i) it also covers national operations; (ii) the costs of insurance differ in the Member States, as shown by the different pricing of the insurance; and (iii) that type of service is unavailable on the market.

5. COMMENTS BY OTHER INTERESTED PARTIES

(31) Following the publication of the Commission Decision to open the formal investigation procedure in the Official Journal on 9 April 2011, the Commission received no comments from third parties.

6. ASSESSMENT

6.1. Qualification of the measures as State aid

(32) Article 107(1) TFEU states:

> *Save as otherwise provided in this Treaty, 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, be incompatible with the internal market.*

(33) In order for Article 107(1) TFEU to be applicable, there needs to be an aid measure imputable to the State which is granted by State resources, affects trade between Member States and distorts competition in the internal market by conferring a selective advantage on certain undertakings.

State resources

(34) As explained in the Commission decision of 27 October 2010 initiating the formal investigation procedure, the insurance is directly provided by the State and any losses stemming from the scheme affect the national budget. The scheme therefore involves State resources. The involvement of State resources is not contested by Portugal.

Selective advantage for insurers

(35) The Commission has analysed export credit insurance markets in its decisions on short-term export credit insurance schemes.[7] Premium rates in the short-term export credit insurance market are typically fixed in contracts for periods of at least one year. Therefore, any change in the pricing of the cover offered is effective only with a time lag. Further, the market practice is to adjust the supply of credit insurance by increasing or decreasing the amounts of credit offered and not by changing the rate charged on the cover. This practice has also been observed since the beginning of the financial crisis, as evidenced by the letters of refusal of cover sent by Portugal and the letters of refusal sent in other cases of short-term export credit insurance schemes.[8] In general, the letters of refusal from insurers do not offer exporters, as an alternative, a higher price for the cover of certain buyers. Evidence shows that as a consequence of the financial crisis, private insurers significantly reduced the cover offered, often withdrawing it altogether. Other data supplied by market operators confirm the above.[9] Thus, competition between insurers is based chiefly on quantities rather than prices. Through the measure, the State responded to demand not covered by the existing private operators. However, in a competitive market with no state intervention, a new operator would have responded to the demand by granting additional insurance cover. Consequently, the effect of the State's intervention was to protect the market positions of the private operators already active on the Portuguese market.

(36) Short-term export credit insurance is a product in which the insurer takes over the commercial and political risk of default by the buyer in a trade transaction. Banks also offer to take over the commercial risks of trade transactions through documentary credit and non-recourse factoring. Short-term export credit insurance offered by export credit insurance companies and documentary credit offered by banks are demand-side substitutes in the market for protection against the commercial risk of trade transactions. In the absence of State intervention, exporters might have resorted at least to some

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[7] See, in particular, Commission decision *Austrian short term export credit insurance* in case N 434/2009, OJ C/25/2010 of 2.2.2010, Commission decision *Export credits Denmark* in case N 198/2009, OJ C/179/2009 of 01.08.2009, Commission decision *Belgian short term export credit insurance* in case N 532/2009, OJ C/19/2010 of 26.01.2010, in Commission decision *Finnish short term export credit insurance* in case N 258/2009, OJ C/227/2009 of 22.09.2009, Commission decision *German short term export credit insurance* in case N384/2009, OJ C/212/2009 of 05.09.2009, Commission decision *Hungarian short term export credit insurance* in case N187/2010, OJ C/259/2010 of 15.09.2010, Commission decision *Luxembourg short term export credit insurance* in case N50/2009, OJ C/143/2009 of 24.06.2009, Commission decision *Lithuanian short term export credit insurance* in case N659/2009, OJ C/33/2010 of 10.02.2010, Commission decision *Latvian short term export credit insurance* in case N84/2010, OJ C/213/2010 of 06.08.2010, Commission decision *Dutch export credit insurance – reinsurance scheme* in case N409/2009, OJ C/270/2009 of 11.11.2009, Commission decision *Slovenian short term export credit insurance* in case N713/2009, OJ C/108/2010 of 28.04.2010.

[8] See in particular Commission decision *Belgian short term export credit insurance* in case N 532/2009, OJ C/19/2010 of 26.01.2010, Commission decision *Finnish short term export credit insurance* in case N 258/2009, OJ C/227/2009 of 22.09.2009, Commission decision *German short term export credit insurance* in case N384/2009, OJ C/212/2009 of 05.09.2009, Commission decision *Luxembourg short term export credit insurance* in case N50/2009, OJ C/143/2009 of 24.06.2009, Commission decision *Latvian short term export credit insurance* in case N84/2010, OJ C/213/2010 of 06.08.2010, Commission decision *Danish export credit insurance – reinsurance scheme* in case N409/2009, OJ C/270/2009 of 11.11.2009, Commission decision *Slovenian short term export credit insurance* in case N713/2009, OJ C/108/2010 of 28.04.2010.

[9] See *Credit insurance in support of international trade*, Fabrice Morel, Berne Union, 2010, http://www.berneunion.org.uk/pdf/Credit%20insurance%20in%20support%20of%20international%20trade.pdf.

extent to documentary credit (letter of credit) offered by banks.[10] Owing to the possible substitutability between short-term export credit insurance offered by insurers and the documentary credit offered by banks, the measure entails an advantage in favour of the sector of short-term export credit insurance, because it contributes to maintaining the market share of export credit insurers in the market for protection against the commercial and political risks of trade transactions. As banks are not eligible to apply for the scheme, under which public insurance is offered only as a supplement to the cover granted by private insurers, the advantage is selective.

(37) In the light of the foregoing, the Commission concludes that the measure confers a selective advantage on insurers.

Selective advantage for exporters and domestic trading companies

(38) Exporters and trading companies subscribing to the scheme pay a premium which is lower than the market premium. This leads to a strengthening of the position of the companies that benefit from the scheme compared to those who would potentially receive their coverage only from private insurers at a market price. The mere strengthening, through measures of a scheme, of the position of some market players compared to their competitors in a comparable situation, has been considered to constitute an advantage.[11] In the present case, strengthening of the position of those beneficiaries would not have been possible to the same extent without the intervention of the State.

(39) Furthermore, as affirmed by Portugal, cover is unavailable on the market, at least to the same extent, for the risks covered under the scheme. Thus companies benefiting from the scheme receive a double advantage in the form of access to insurance cover that would otherwise be unavailable: not only do they benefit from a lower premium than the market price, but they also benefit from the existence of the additional cover.

(40) The Portuguese scheme is de facto selective.

(41) An initial indication that the scheme is selective is that the companies that benefit from the measure are almost exclusively companies that trade in goods, while companies that provide services benefit much less from it. In the context of the formal investigation proceedings, the Portuguese authorities state that there are no legal obstacles preventing companies not involved in commercial activities to benefit from the scheme and that the sectors 'construction', 'transport' and 'other services - excluding commerce' have benefitted from the scheme. However, Portugal also admits that by their nature, export credit insurance mainly concerns transactions in goods. Companies that supply transport and other services accounted for only 2.4% of the insurance provided under the scheme at October 2010. Given that undertakings that supply services accounted for only 8 of a total of 361 undertakings that benefitted from the scheme and about 1.25% of the share of credit limits, it is clear that the measure in question essentially aided companies that trade in goods.

(42) There are other elements that show that the scheme is de facto selective.

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[10] See *The Report on Market Trends of Private Reinsurance in the Field of Export Credit Insurance,* European Commission, http://ec.europa.eu/competition/state_aid/studies_reports/export_credit_insurance_report.pdf.

[11] See judgment of the Court (Third Chamber) of 8 September 2011 in Case C-279/08 P, Commission v. Netherlands, not yet published.

(43) First, despite the claim of the Portuguese authorities that the scheme has a general character because the beneficiaries are defined by objective criteria which do not entail a discrimination against entities from other Member States, the conditions set under the scheme grant a certain margin of discretion in the choice of beneficiaries. The scheme follows a 'top-up' model, according to which only companies that have a credit limit with a private insurer are eligible for the scheme, while companies to which private credit insurers refuse cover completely are not eligible for the 'top-up'. The scheme leaves it entirely to the private companies to judge the eligibility for cover. In the absence of uniform and objective criteria for determining the risk entailed in the transactions which each exporter or trader carries out, the scheme grants private operators a degree of latitude in judging the creditworthiness of the companies that are eligible to apply for cover. The Court of Justice has considered that to be considered as non-selective, a measure should be based on a criterion of application which is objective, has no geographic or sectoral connotation, and is in keeping with the objective of the measure.[12] In the present case, the absence of objective criteria for the decision to grant private cover leads to potential discrimination between beneficiaries that are in a comparable factual situation.[13]

(44) Second, even if the criteria for access to the scheme were to be considered objective, the Court has held that the mere existence of objective criteria does not prejudge the selective nature of the measure where the measure has the effect of advantaging certain undertakings to the detriment of others. Thus, the Court has stated that '[t]he fact that the aid is not aimed at one or more specific recipients defined in advance, but that it is subject to a series of objective criteria pursuant to which it may be granted, within the framework of a predetermined overall budget allocation, to an indefinite number of beneficiaries who are not initially individually identified, cannot suffice to call in question the selective nature of the measure and, accordingly, its classification as State aid within the meaning of Article 92 of the Treaty [107(1) TFEU]. At the very most, that circumstance means that the measure in question is not an individual aid. It does not, however, preclude that public measure from having to be regarded as a system of aid constituting a selective, and therefore specific, measure if, owing to the criteria governing its application, it procures an advantage for certain undertakings or the production of certain goods, to the exclusion of others.'[14] Thus, according to the Court of Justice, State interventions should not be judged on their causes or aims, but on their effects.[15] In the case at hand, the scheme is de facto selective.

(45) Third, in order to be of a general nature, a measure must not only be based on objective and horizontal criteria, but must also not be limited either in time or in its field of application. The scheme, despite Portugal's insistence on its general character, is limited both in time and in its field of application, including by the very nature of the top-up model, as has been explained above in recital 43.

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[12] Judgment of the Court of First Instance of 10 April 2008 in case T-233/04 Kingdom of the Netherlands v Commission of the European Communities [2008] ECR II-00591, point 88.

[13] Judgment in case C-143/99 Adria-Wien Pipeline GmbH and Wietersdorfer & Peggauer Zementwerke GmbH v Finanzlandesdirektion für Kärnten[2001] ECR I-08365, point 41.

[14] Judgment of the Court of First Instance (Third Chamber, Extended Composition) of 29 September 2000 in case T55/99, Confederación Española de Transporte de Mercancias v. Commission , ECR II-3207, point 40.

[15] Judgment in case C-173/73 Italian Republic v Commission of the European Communities [1974] ECR 00709, point 13.

(46) Finally, the criteria under the scheme are not in conformity with the aim and logic of the measure.[16] Even if the scheme were to be applied in an objective manner by the private insurers, only companies which saw their cover reduced during the crisis would be eligible under the scheme. Companies for which private insurers have cancelled credit limits completely are excluded from the scheme. Therefore, despite the aim of the scheme to address an alleged unavailability of cover on the private market, it does not cover the companies which are most severely affected by the reduction of the private insurance capacity in the market. In that respect, the design of the measure is not appropriate to address the identified market failure

(47) On the basis of the foregoing considerations, the advantages conferred on the exporters and trading companies subscribing to the scheme are of a selective nature.

Effect on trade and distortion of competition

(48) Concerning the effect on trade, the scheme covers export transactions and domestic transactions in tradable goods.

(49) By covering domestic transactions, the scheme may potentially affect trade between Member States to the extent that it could appreciably distort trade flows, for instance by diverting economic activities from exports into domestic transactions.

(50) As regards the distortion of competition, according to the case law of the Court of Justice, the mere fact that the competitive position of an undertaking is strengthened compared to other competing undertakings, by giving it an economic benefit which it would not otherwise have received in the normal course of its business, points to a possible distortion of competition.[17]

(51) As the scheme applies to exports, including for other Member States, the measure clearly affects trade flows between Member States, as it facilitates the exercise of an export activity by beneficiaries.

(52) The scheme also affects trade insofar as it covers domestic transactions. It is well-established case-law that where aid granted by a Member State strengthens the position of a company compared with other competing companies in intra-Union trade, the latter should be considered affected by that aid. In this regard, the fact that an economic sector has been liberalised at the level of the Union could serve to determine that the aid has a real or potential effect on the competition and affects trade between the Member States. Additionally, it is not necessary that the beneficiary company itself be involved in the trade within the Union. Aid granted by a Member State to a company may contribute to maintaining or increasing the activity in the domestic market, with the result that companies established in another Member States have fewer opportunities to penetrate the market of the Member State in question. Furthermore, the strengthening of an undertaking which, until then, was not involved in intra-Union trade may place that undertaking in a position that enables it to penetrate the market of another Member State.[18]

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[16] Judgment of the Court of First Instance (Fifth Section, Extended Composition) of 10 April 2008 in case T233/04 Kingdom of the Netherlands v Commission of the European Communities [2008] ECR II-00591, point 88.

[17] See judgment in Case 730/79 Philip Morris Holland BV v Commission [1980] ECR 2671, point 11.

[18] See, in particular, Case C-222/04 Cassa di Risparmio di Firenze, ECR 2006, p. I-289, paragraphs 141-143, and the case-law cited therein.

(53) In the present case, the measure benefits companies active in various sectors open to trade within the European Union. Thus even advantages conferred on domestic transactions of companies active only in the Portuguese market affect trade between Member States.

(54) Moreover, the purpose of the measure is to support the commercial trading activities of companies established in Portugal as opposed to undertakings established in other Member States. The measure may, therefore, distort competition in the internal market.

Conclusion

(55) Consequently, this project constitutes state aid within the meaning of Article 107(1) of the TFUE. The aid may be considered compatible with the common market if it can qualify for one of the exceptions provided for in the Treaty.

6.2. Compatibility of the aid to insurers

(56) The Commission has laid down in its Communication conditions under which aid to insurers in the form of State-supported short-term export credit schemes is considered to be compatible. In the context of the financial crisis, the Temporary Framework sets out the conditions of application of the Communication.

(57) Point 2.5 of the Communication as amended[19] defines 'marketable risks' as the commercial and political risks relating to public and non-public debtors established in the countries listed in the Annex[20] to the Communication. Financial advantages in favour of export credit insurers that enter or cover a transaction qualified as a marketable risk are normally prohibited.

(58) Point 3.1 of the Communication states that factors that may distort competition between private and public or publicly supported export-credit insurers insuring marketable risks include de jure and de facto State guarantees of borrowing and losses. Such guarantees enable insurers to borrow at rates lower than the normal market rates or make it possible for them to borrow money at all. Furthermore, they obviate the need for insurers to reinsure themselves on the private market,

(59) As far as countries not listed in the Annex to the Communication are concerned, such risks are 'non-marketable' within the meaning of the Communication and public support for insuring them is not covered by the Communication.

(60) Point 4.2 of the Communication provides that 'marketable risks' cannot be covered by export credit insurance with aid from the Member States. However, point 4.4 of the Communication provides that under certain conditions, these risks can be temporarily covered by public or publicly-supported export credit insurers. In particular it states that risks incurred in respect of debtors established in countries listed in the Annex to the Communication are considered temporarily non-marketable only if it can be demonstrated that private insurance cover for the risks generally viewed as marketable is unavailable. Member States which wish to invoke that escape clause must provide a market report and produce evidence from two major, internationally recognised export credit insurers as well as a national credit insurer, both demonstrating the unavailability

[19] See corrigendum published in OJ C 217, 02.08.2001, p. 2.

[20] The list includes EU and OECD countries.

of cover for the risks in the private insurance market. Moreover, the publicly-supported export credit insurer must, as far as possible, align its premium rates for such non-marketable risks with the rates charged elsewhere by private export credit insurers for the type of risk in question and provide a description of the conditions which the public export credit insurer intends to apply in respect of such risks.

(61) In order to speed up the procedure, the Temporary Framework simplified, until 31 December 2010, the proof that Member States need to produce to demonstrate the unavailability of cover. To that end, Member States had to submit evidence supplied by a large internationally recognised private export credit insurer and a national credit insurer or by at least four well-established exporters in the domestic market. The Temporary Framework was prolonged until 31 December 2011.[21]

Unavailability of cover

(62) Portugal submitted a number of letters from exporters which show that they have been refused cover for a number of transactions. Nevertheless, the Commission has not found sufficient proof of the unavailability of cover in the letters provided by the Portuguese authorities. The reasons provided in those letters for refusal are either confidential or explicitly state that refusal is due to the customer's poor liquidity and financial position, which is a normal business practice in a properly functioning insurance market. Portugal provided data, in its reply to the Commission decision of 27 October 2010 initiating the formal investigation procedure, that shows a decline in the number of firms taking up insurance (there is a 29.41% decline up to the end of 2009 compared with the previous year, and of another 12.53% up to September 2010), as well as a decline in the value of the insured portfolio (32.84% decline at the end of 2009 compared with the previous year, and of another 22.36% until September 2010). However, of the two letters from private insurers provided by Portugal pointing to the unavailability of cover in the private market, one of them (from CESCE, dated 22 November 2010) states that the financing needs of firms have also diminished due to the decrease of the buying markets. Therefore, the alleged reduction of insured volumes is not sufficient proof of the unavailability of cover on the market.

(63) Moreover, if indeed cover is unavailable in the private market and it then becomes available when the State grants a partial coverage, it could constitute a sign that the insurers have received State aid. As that market adjusts mainly by quantity not by prices, as explained in recital 35, the availability of credit deriving from the state aid allows the operators already present on the market to maintain their position.

Alignment of premium rates with rates charged by private credit insurers

(64) The rates charged under the scheme represent 60% of the rate charged by a private insurer to cover the same client. Further, contrary to the allegations of Portugal, the risk transferred to the State under the scheme can be considered higher than the risk covered by the private insurer on a stand-alone basis. It should be recalled that the risk of default increases when the insured amount increases. Thus, with a larger amount of insurance cover the exporter would accept to conclude more commercial transactions with a given buyer. The total volume of transactions could exceed the capacity to repay of the buyer.

(65) The Portuguese authorities consider that the risk of additional transactions is lower, considering that an exporter which obtained limited cover would first insure the riskiest

[21] OJ C6, 11.1.2011, p.5.

buyers; with increased cover, the exporter would progressively insure buyers that are less risky. However, that argument overlooks the fact that credit limits are granted per buyer, and therefore the exporter does not have the choice to exclusively use the entirety of the limit granted for the least credit-worthy buyers.

(66) Moreover, the argument of the Portuguese authorities that the additional transactions insured are of lower risk than the transactions insured by the private insurer would lead to the conclusion that the private insurers accept, for a given level of premium, a higher risk, while they refuse to cover transactions with lower risk for the same level of premium. If that argument was correct, a rational private insurer would insure more transactions, which would increase their premium income while decreasing the risk. In other words, the argument of the Portuguese authorities would point to an irrational behaviour of private insurers, who would agree to insure a riskier part of the portfolio instead of the less risky part. Therefore that argument cannot be accepted.

(67) As a result of the increased risk covered by the measure, the State assumes exposure to a higher expected ultimate loss than the private insurer, when granting and pricing the initial cover on a stand-alone basis. Therefore, in the case of a top-up scheme where the decision to extend the cover is taken only after the premium for the initial credit insurance limit has been set, the price of the top-up must reflect a higher risk of possible excess cover. The argument of the Portuguese authorities, according to which firms would operate an adverse selection which would ensure that the riskier operations would be covered by private insurance, is not supported by any concrete data nor by the known market practice. The most common form of private short-term credit insurance (whole turnover policy) requires that whole portfolio of credited sales is covered under the policy. Thus, the insured company is prevented from insuring their risks selectively. The Commission considers that the price of supplementary insurance should have taken into account the higher level of risk assumed. The pricing should therefore have been higher than the price charged for the base cover by the private insurers.

(68) In the present case, the rates charged under the scheme are lower than the current rates in the export credit insurance market, which is confirmed by Portugal in its reply to the Commission decision of 27 October 2010 initiating the formal investigation procedure. That pricing is also lower than the 2007 and 2008 market rates. For that reason, the argument brought forward by the Portuguese authorities, according to which the pricing corresponds to the market rates before the crisis, is also not confirmed. Moreover, the price should also take into account the level of risk assumed. Therefore, the pricing should in fact be higher than the market price.

(69) In the light of the foregoing, the scheme as applied to insurers is incompatible with the Communication and the Temporary Framework.

6.3. Compatibility of the aid to exporters and domestic trading companies

6.3.1. COMPATIBILITY OF THE MEASURE AIMED AT SHORT-TERM EXPORT CREDIT INSURANCE

(70) Article 107(3)(c), applicable under normal market circumstances, and Article 107(3)(b) of the TFEU, applicable in periods of serious disturbance in the economy, allow aid to be considered compatible with the internal market under certain conditions.

(71) The Commission recalls that according to case law, Article 107(3)(b) of the TFEU must be applied restrictively and must tackle a disturbance in the entire economy of a Member State.[22]

(72) In line with the principles set out in the Temporary Framework (paragraph 5.1), as prolonged until 31 December 2012, in order to be deemed compatible, aid measures must fulfil the following criteria:

a. *Appropriateness:* The aid must be well-targeted in order to be able to effectively achieve the objective of remedying a serious disturbance in the economy. It would not be the case if the measure were not appropriate to remedy the disturbance.

b. *Necessity:* The aid measure must, in its amount and form, be necessary to achieve the objective. Thus, it must be of the minimum amount necessary to reach the objective, and take the form most appropriate to remedy the disturbance. In other words, if a lesser amount of aid or a measure in a less distortive form were sufficient to remedy a serious disturbance in the entire economy, the measure in question would not be necessary. That analysis is confirmed by settled case law of the Court of Justice.[23]

c. *Proportionality*: The positive effects of the measures must be properly balanced against the distortions of competition, in order for the distortions to be limited to the minimum necessary to reach the measures' objectives. Article 107(1) of the TFEU prohibits all selective public measures that are capable of distorting trade between Member States. Any derogation under Article 107(3)(b) of the TFEU which authorises State aid must ensure that such aid is limited to what is necessary to achieve its stated objective.

Appropriateness

(73) As explained in recital 46, the design of the scheme excludes companies which are hardest hit by the crisis and therefore it is not appropriate to address the alleged market failure of unavailability of private cover.

Necessity and proportionality: alignment of premium rates with rates charged by private credit insurers

(74) As stated above in recital 62, although the information provided by Portugal indicates strains in the private credit insurance market, it fails to prove an unavailability of cover. Therefore the necessity of the State intervention cannot be established.

(75) As explained in recitals 21 and 64, the rates charged under the scheme represent 60% of the rates charged by private insurers to cover the same client.

(76) As explained above in recitals 65 to 67, in the case of a top-up scheme where the decision to extend the cover is taken only after the premium for the initial credit insurance limit has been set, the price of the top-up must reflect a higher risk of possible excess cover.

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[22] See for instance judgment of the Court of First Instance in joined cases T-132/96 and T-143/96 Freistaat Sachsen, Volkswagen AG and Volkswagen Sachsen GmbH v Commission of the European Communities [1999] ECR II-3663, paragraph 167.

[23] See judgment in Case 730/79 Philip Morris Holland BV v Commission [1980] ECR 2671, point 17. This principle was recently reaffirmed by the judgment in case C-390/06 Nuova Agricast Srl v Ministero delle Attività Produttive [2008] ECR I-02577, point 68.

(77) The objective to provide the allegedly unavailable insurance cover could also be achieved through a scheme priced in such a way as to reflect the underlying risk assumed by the State. Therefore, the pricing of the scheme based on a premium lower than the premium which would be charged by the market for similar risks is not proportionate to the objective of the scheme.

(78) In view of the above, the export credit insurance part of the scheme cannot be considered to be compatible aid to exporters under Article 107(3)(b) of the TFEU and the Temporary Framework.

(79) Regarding Article 107(3)(c), all the arguments in respect of appropriateness, necessity and proportionality are equally pertinent in the compatibility analysis under Article 107(3)(b). Therefore the aid to export credit insurers under the scheme affects trade conditions to an extent contrary to the common interest.

6.3.2. *COMPATIBILITY OF THE SCHEME IN RELATION TO DOMESTIC TRADE INSURANCE OPERATIONS*

(80) As regards the application of the scheme to domestic transactions, domestic trade insurance below market price could divert trade transactions away from exports in favour of domestic transactions and have a major impact on imports. Therefore, under normal market conditions State support in favour of domestic trade operations is strictly forbidden. However, subparagraphs (c) and (b) of Articles 107(3) of the TFEU allow aid to be considered compatible with the internal market under certain circumstances. In that context, the Communication and the Temporary Framework set criteria for the compatibility of aid measures for short-term export credit insurance. However, those texts do not cover domestic trade transactions.

(81) Nevertheless, Portugal notified the scheme in the context of the current financial crisis under the Temporary Framework. Therefore it must be established whether, in view of the far-reaching consequences of the current economic crisis, the scheme could be regarded as compatible directly under Article 107(3)(b) of the TFEU. If not, then it must be analysed whether the measure can be deemed compatible under Article 107(3)(c).

(82) Concerning compatibility under Article 107(3)(b) of the TFEU, that provision enables the Commission to declare aid compatible with the internal market if it aims 'to remedy a serious disturbance in the economy of a Member State'.

(83) The Commission reiterates that Article 107(3)(b) of the TFEU needs to be applied restrictively and must tackle a disturbance that effects the entire economy of a Member State.[24] It also recalls that, as stated above in recital 73, the measure must fulfil the principles of appropriateness, necessity and proportionality.

(84) The measure was put in place in the context of the current financial crisis and is limited in time.

(85) The Commission has received letters from exporters and private insurers indicating a reduction in insurance cover for domestic transactions The Portuguese authorities argue that the loss ratio has increased to 102%. However, that observation is not conclusive since the increase follows a constant trend since 2004, as shown in the observations

[24] See for instance judgment of the Court of First Instance (Second Chamber, extended composition) in joined cases T-132/96 and T-143/96 Freistaat Sachsen, Volkswagen AG and Volkswagen Sachsen GmbH v Commission of the European Communities [1999] ECR II-3663, point 167.

provided by the Portuguese authorities. That constant increase in the loss ratio even before the outbreak of the financial crisis may point, not to a market failure in domestic trade financing, but rather to a structural problem in the market. Therefore, the Commission has not found evidence that the scheme is appropriate to address a serious disturbance in the economy and considers the scheme cannot be declared compatible under the Temporary Framework or Article 107(3)(b).

(86) Concerning the compatibility of the measure under the Communication and Article 107(3)(c), the aim of the scheme is to address the unavailability of cover in the insurance market. However, being a top-up scheme which leaves some degree of latitude in the choice of the beneficiary to private insurers, the scheme potentially excludes companies from cover which are in a comparable factual situation to the companies covered, but were more affected by the crisis. Such excluded companies would have had insurance cover completely withdrawn as opposed to only partially cancelled. Moreover, the measure not only provides additional cover to beneficiaries, it also provides an advantage in terms of pricing, given that the premiums are below market rates. As already noted, the rates charged under the scheme represent 60% of the rates charged by a private insurer to cover the same client, while the fact that the cover limit is extended to double the initial limit implies a higher risk not reflected by the premium. The level of the pricing under the scheme is not justified in view of the need to address the unavailability of insurance cover. The scheme is not proportionate to achieving its stated objective given the potential distortions of competition.

(87) The Commission therefore concludes that the State aid granted to domestic trade insurance operations does not fulfil the conditions under subparagraphs (b) or (c) of Articles 107(3) of the TFEU and is incompatible with the internal market.

7. CONCLUSION

(88) In the light of the foregoing, the Commission concludes that the scheme grants State aid within the meaning of Article 107(1) TFEU which cannot be declared compatible with the internal market.

8. RECOVERY

(89) According to Article 14(1) of Council Regulation (EC) N° 659/1999,[25] where negative decisions are taken in cases of unlawful aid, the Commission shall decide that the Member State concerned shall take all necessary measures to recover the aid from the beneficiaries. Only aid which is incompatible with the internal market shall be recovered.

(90) The purpose of recovery is to restore the situation that existed prior to the granting of the aid. It is achieved once the incompatible aids are repaid by the beneficiaries, which therefore forfeit the advantages which they enjoyed over their competitors The amount to be recovered should be such as to eliminate the economic advantage given to the beneficiaries.

(91) For the exact quantification of the amount of aid, as no appropriate market price is available for remuneration of the State cover, a proper benchmark has to be defined. As

25 Council Regulation No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 (now Article 88) of the EC Treaty, OJ L 83, 27.03.1999, p. 1.

set out in the first indent of point 4.2 of the Commission Notice on guarantees,[26] the 'cash grant equivalent' of a loan guarantee in a given year can be calculated in the same way as the grant equivalent of a soft loan. Hence the aid amount can be calculated as the difference between a theoretical market rate and the rate obtained thanks to the State guarantee after any premiums paid have been deducted.

(92) In respect of the aid to insurers, the advantage takes the form of the preservation of the market share of the insurers. In the absence of aid, cover could have been provided by another market player. In particular, as explained above in recital 35, competition in the market is based mainly on quantities and not on prices. Furthermore, market practice is to fix an average price for the entire portfolio which is then to be insured with the same insurer[27] to avoid cherry picking by the insured company. Cherry picking could occur if the insured company paid an average price only for clients with high risk and did not insure the lower risk clients or insure low risk clients with another insurer. Therefore, if another market player had provided cover to the exporters for the entire requested credit limits even at a higher price, exporters would probably have moved their entire insurance policies to the alternative cover provider. The advantage in monetary terms is the profit margin realised on the volume insured by each private insurer decreased by the costs associated to this volume. These elements, translated into the profits realised by the private insurers participating in the scheme over the period over which top-up cover was provided by the State, would have been recorded by another market player in the absence of the scheme. The aid in favour of the insurers is therefore quantified as the profits realised by the insurers participating in the scheme over the period it was in place as a result of their cover of individual exporters and domestic trading companies subscribing to the scheme. The advantage for the clients subscribing to the scheme should be calculated at the level of each individual insurer participating in the scheme and in case of profit exceeding the de minimis amount it should be recovered.

(93) In respect of the exporters, the beneficiaries should have paid remuneration for the State cover under market conditions. The aid amount should therefore be calculated as the difference between that actual market rate, adapted for the change in the level of risk. The Commission has developed a method for the calculation of the amount to be recovered (explained in the Annex to this Decision) based on reasonable assumptions and on common market practice. Under that method, a theoretical market price for the cover granted by the State is equal to 110% of the price (in terms of premium rate) charged by the private insurer in the case of each individual exporter. As the price charged under the scheme is 60% of the premiums charged by the private insurer, the amount to be recovered in each transaction is equal to the amount charged by the State under the scheme multiplied by 5/6.

(94) The amount referred to in recital 93 constitutes the amount to be recovered, plus the recovery interest effectively accrued on that amount from the date on which the aid was made available to the beneficiaries (date of the individual guarantees) until its actual recovery. The recovery interest shall be calculated on a compound basis in accordance with Chapter V of Commission Regulation (EC) No 794/2004 of 21 April 2004

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[26] Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees, OJ C 155, 20.06.2008, p.10.

[27] This market practice is based on the predominant use of whole turnover products instead of single risk products.

implementing Council Regulation (EC) No 659/1999,[28] as amended by Regulation (EC) No 271/2008.

(95) The present decision shall be implemented immediately, in particular in respect of the recovery of all the individual aids granted under the scheme with the exception of the aids that fulfil the conditions laid down by Regulations adopted pursuant to Articles 1 and 2 of Commission Regulation (EC) No 994/98 or by any other approved aid scheme up to the maximum aid intensity or de minimis limits applicable to this type of aid.

HAS ADOPTED THIS DECISION:

Article 1

The State aid involved in the short-term export-credit insurance scheme in application of Decree-Law No 175/2008 establishing the Finova of 26 August 2008 and Decree-Law No 211/1998 laying down the rules applicable to mutual guarantee societies of 16 July 1998 (as amended by Decree-Law No 19/2001 of 30 January 2001 and Decree-Law No 309-A/2007 of 7 September 2007), unlawfully granted by Portugal, in breach of Article 108(3) of the Treaty on the Functioning of the European Union, is incompatible with the internal market.

Article 2

Individual aid granted under the scheme referred to in Article 1 which, at the time the aid is granted, fulfils the conditions laid down by a Regulation adopted pursuant to Article 1 of Regulation (EC) No 994/98 or by any other approved aid scheme is compatible with the internal market, up to the maximum aid intensities or de minimis limits applicable to this type of aid.

Article 3

1. Portugal shall recover the incompatible aid referred to in Article 1 from the beneficiaries.

2. The sums to be recovered shall bear interest from the date on which they were made available to the beneficiary until their actual recovery.

3. The interest shall be calculated on a compound basis in accordance with Chapter V of Regulation (EC) No 794/2004, as amended by Regulation (EC) No 271/2008.

4. Portugal shall immediately abolish the scheme referred to in Article 1 and cancel all outstanding payments of aid under the scheme referred to in Article 1 with effect from the date of notification of this Decision.

[28] OJ L 140, 30.4.2004, p.1.

Article 4

1. Recovery of the aid grated under the scheme referred to in Article 1 shall be immediate and effective.

2. Portugal shall ensure that this decision is implemented within four months following the date of notification of this Decision.

Article 5

1. Within two months following notification of this Decision, Portugal shall submit the following information to the Commission:

   (a) The list of beneficiaries that have received aid under the scheme referred to in Article 1 and the total amount of aid received by each of them;

   (b) The total amount (principal and recovery interest) to be recovered from each beneficiary;

   (c) A detailed description of the measures already taken and planned to comply with this Decision;

   (d) Documents demonstrating that the beneficiaries have been ordered to repay the aid.

2. Portugal shall keep the Commission informed of the progress of the national measures taken to implement this Decision until recovery of the aid referred to in Article 1 has been completed. It shall immediately submit, on simple request by the Commission, information on the measures already taken and planned to comply with this Decision. It shall also provide detailed information concerning the amounts of aid and recovery interest already recovered from the beneficiaries.

Article 6

This Decision is addressed to the Portuguese Republic.

Done at Brussels, 23.11.2011.

For the Commission,

Joaquín ALMUNIA
Vice-President

Notice

If the decision 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 the decision. Your request specifying the relevant information should be sent by registered letter or fax to:

EUROPEAN COMMISSION
Directorate-General for Competition
State aid Greffe
Joseph II 70 3/225
B-1049 Brussels
Fax No: + 32.2.296.12.42

Annex on pricing of top-up trade insurance cover

Premiums for insurance cover are set in such a way as to cover at least the expected loss and the administrative costs. Therefore the minimum premium acceptable for a sound economic operator can be expressed as follows:

$PR = \mathrm{Pr}\,ob \times ExpectedLoss + adm = \mathrm{Pr}\,ob \times (ExposureAtDefault - \mathrm{Re}\,\mathrm{cov}\,eryAmount) + adm$,
where:

PR – premium charged by the private insurers on the stand-alone basis;

Prob – probability of the insured event;

Recovery Amount – expected amount of recovery, based on historical market data;

adm – administrative costs. For the sake of simplicity, in this analysis administrative costs are assumed to be equal to zero (). This assumption does not affect the outcome of the analysis because administrative costs are not a decisive component for setting the premium level. If reliable data on administrative costs are available, the variable can easily be included in the analysis.

(ExposureAtDefault – the maximum loss amount to which an institution would be exposed in case of the default of its counterpart.)

In the following, the subscript '0' designates a variable in the absence of (or prior to) the State intervention, and the subscript 'S' designates a variable with the State intervention.

From the formula above, it can be seen that:

$$\frac{PR_S}{PR_0} = \frac{\mathrm{Pr}\,ob_S\,(Exposure_S - \mathrm{Re}\,\mathrm{cov}\,eryAmount_S)}{\mathrm{Pr}\,ob_0\,(Exposure_0 - \mathrm{Re}\,\mathrm{cov}\,eryAmount_0)}$$

By definition:

$$\mathrm{Re}\,\mathrm{cov}\,eryRate = \frac{\mathrm{Re}\,\mathrm{cov}\,eryAmount}{Exposure}$$

or $\mathrm{Re}\,\mathrm{cov}\,eryRate \times Exposure = \mathrm{Re}\,\mathrm{cov}\,eryAmount$

The expression is transformed as follows:

$$\frac{PR_S}{PR_0} = \frac{\mathrm{Pr}\,ob_S \times Exposure_S\,(1 - \mathrm{Re}\,\mathrm{cov}\,eryRate_S)}{\mathrm{Pr}\,ob_0 \times Exposure_0\,(1 - \mathrm{Re}\,\mathrm{cov}\,eryRate_0)}$$

A feature of the measure under scrutiny is that the cover under the scheme is at most equal to or lower than the cover provided by the private (base) insurer in the absence of State aid (that is, that the State supported cover is at most equal to the cover provided by the private insurer).

Assuming for the moment that the State supported cover is exactly equal to the cover provided by the private insurer, the following relation results: $Exposição_S = 2 \times Exposição_0$.

In that case the expression is transformed as follows:

$$\frac{PR_S}{2PR_0} = \frac{\Pr ob_S (1 - \operatorname{Re}\operatorname{cov} eryRate_S)}{\Pr ob_0 (1 - \operatorname{Re}\operatorname{cov} eryRate_0)}$$

The consequences of what is known in the industry as 'over-crediting' on the correct pricing of a trade insurance cover are explained below. Over-crediting is observed both at the level of the probability of default and at the level of the recovery rate.

– Probability of default

The probability of default increases with the trading activity of the buyer. Trade credit and bank loans are imperfect substitutes: in particular, both can be used to expand the activity of the buyer/borrower. Therefore, as in the case of bank loans, increased trade credit creates a risk of over-crediting, i.e. the buyer expands his activity beyond what is economically efficient. In the terms of the formulas presented, over-crediting can be expressed as:

$$\Pr ob_S \succ \Pr ob_0$$

That situation would in particular arise in cases where the exporter is the main supplier of the buyer. In that case the economic activity of the buyer increases proportionately to the trade transaction concluded with the insurer exporter and thereby increases proportionately to the amount of credit cover granted.

– Recovery ratio

Owing to the increase in credit exposure, the amount to be recovered also increases. However, given that the recoverable amount depends on the hypothetical liquidation proceeds, this theoretical recoverable amount is capped by the amount of the assets that the buyer (or the liquidation administrator) can sell to cover the trade credit liability and, as the amount of assets is finite, the recovery rate would increase less than proportionately to the increase of credit cover.

$\operatorname{Re}\operatorname{cov} eryRate_S = \operatorname{Re}\operatorname{cov} eryRate_0 \times \alpha$, where:

$0.5 \leq \alpha \leq 1$ (α =0.5, if the recovery amount does not increase at all where the exporter is granted the State's top-up for a transaction with a certain buyer; α =1 in the theoretical case where the recovery amount increases at the same pace as the total credit limit received by the exporter for the transaction with a certain buyer.)

Given the above, it can be concluded that $PR_S \succ 2PR_0$.

Therefore, the premium to be paid on the State cover is higher than the premium paid to the private insurer for the initial cover.

A premium of 110% of the premium paid for the initial cover can be considered to factor in to an adequate extent the increase in the probability of default and the decrease in the recovery rate. Such level of premium would be consistent with the pricing in the market. Under approved export credit schemes, the increases in premia from one category of risk to another were in the range of 25-50%.[29]

If $Exposure_S \prec 2 \times Exposure_0$, PR_S decreases proportionally (but is always higher than PR_0). In order to take that factor into account, recital 93 of the Decision envisages quantification of the amount to be recovered in each transaction as the amount charged by the State multiplied by 5/6, based on the following reasoning. In each transaction the State charges 60% of the rate charged by the private insurer, whereas the market price would have been 110% of the rate charged by the private insurer. Therefore, the market premium is calculated by dividing the premium effectively paid to the State by 60% and multiplying it by 110%. From that premium the amount already paid to the State should be subtracted in order to arrive at the amount to be recovered.

$$\Pr emiumPaid \times \frac{110\%}{60\%} - \Pr emiumPaid = \Pr emiumPaid\,(\frac{110\%}{60\%} - 1) = \Pr emuimPaid \times \frac{5}{6}$$

[29] See for instance the Commission decision concerning Finnish short term export credit insurance in case N 258/2009, OJ C 227, 22.09.2009, p.1.