



EUROPEAN COMMISSION

Brussels, 22.12.2011
C(2011) 10068 final

Subject: State aid SA.33571 (2011/N) – Rescue aid to NORD/LB - Germany

Sir;

1. PROCEDURE

- (1) On 21 April 2011, Germany informally approached the Commission regarding the envisaged implementation of recapitalisation measures in favour of NORD/LB ("Kapitalmaßnahmen" or the "capital measures").
- (2) Between May and September 2011, the Commission sent three information requests to Germany, insisting inter alia on a company evaluation.
- (3) On 6 September 2011, Germany submitted a documentation of the envisaged recapitalisation measures, including a company evaluation by an external consultant, aiming to ensure the compliance of the measure with market rules. The Commission subsequently sent two information requests related to the valuation.
- (4) Germany notified the recapitalisation measures covered by this decision to the Commission by letter of 16 December 2011, registered with the Commission on the same date.
- (5) For reasons of urgency, Germany accepts that exceptionally the decision is adopted in English.

Seiner Exzellenz Herrn Guido WESTERWELLE
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2. DESCRIPTION

2.1 Beneficiary

- (6) The NORDDeutsche Landesbank Girozentrale group ("NORD/LB" or the "bank") is a German Landesbank which serves as the central institution of the savings banks in the *Länder* of Niedersachsen, Sachsen-Anhalt and Mecklenburg-Vorpommern. The NORD/LB Group is comprised of NORD/LB which has participations in following entities: Bremer Landesbank (92.5% ownership); NORDDeutsche Landesbank Luxembourg S.A. (100% ownership), which in turns owns 100% of NORD/LB Covered Finance Bank; Braunschweigische Landessparkasse (a fully-owned subsidiary of NORD/LB); NORD/LB Asset Management (100%); and Deutsche Hypothekenbank (100%).
- (7) Before the measures subject to this notification came into effect, NORD/LB had the following ownership structure: the Land Niedersachsen (41.75%), the Land Sachsen-Anhalt (8.25%), the Sparkassenverband Niedersachsen (SVN) (37.25%), the Sparkassenbeteiligungsverband Sachsen-Anhalt (SBV) (7.53%) and the Sparkassenbeteiligungszweckverband (SZV) (5.22%). SVN, SBV and SZV will hereinafter be referred to "the Savings Banks' Associations".
- (8) The bank offers a wide range of financial services to its private, corporate and institutional customers and public authorities. The main areas of focus of NORD/LB are real estate banking, corporate and project finance, ship and aircraft financing, and asset management, as well as retail, private and corporate banking.
- (9) On 30 September 2011, NORD/LB had a balance-sheet total of EUR 228.7 billion (EUR 228.6 billion per 31 December 2010).
- (10) On 8 April 2011, the European Banking Authority (EBA) announced that it would use a benchmark of Common Equity Tier 1 (CT1)¹ of 5% against which it would assess banks in the EU-wide stress test in June 2011.
- (11) The EBA only included commercial instruments of the highest quality in that CT1 definition.
- (12) To enable NORD/LB to pass the stress test, its owners decided in the shareholders' meeting ("Trägerversammlung") of 27 April 2011 to strengthen the bank's capital. For that purpose, they decided to provide the capital measures with the main aim of converting the silent participations and other capital instruments held by Land Niedersachsen and its wholly-owned subsidiary into core capital with the nominal value of EUR 1067 million and of providing an additional share capital increase by Land Niedersachsen of around

¹ That definition is based on EBA's own definition of Core Tier 1, which differs in a number of points from the Tier 1 definition in the current EU legislation in the Capital Requirements Directive (CRD) comprising Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions, OJ L 177, 30.6.2006, p.1 and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions (recast), OJ L 177, 30.6.2006, p. 201 with subsequent amendments.

EUR 600 million. Subsequently, the Savings Banks' Associations participated for around EUR 100 million in the latter capital increase, thus reducing the participation of the Land Niedersachsen to around EUR 500 million.

- (13) On 25 May 2011, Land Niedersachsen approved a law allowing for the capital measures². As a consequence, NORD/LB passed the EBA stress test with 5.6% CT1 ratio. However, NORD/LB had to commit to EBA to implement the capital measures by 31 December 2011 at the latest.
- (14) On 27 April 2011, the 'Trägerversammlung' of NORD/LB in principle agreed the capital measures, leaving open its concrete terms and conditions.
- (15) On 18 August 2011 the 'Trägerversammlung' agreed on the terms and conditions of the capital measures on the basis of a company evaluation carried out by an external consultant. That decision was modified by decisions of 23 November 2011 and 15 December 2011. The implementation of the capital measures is subject to the approval of the European Commission.
- (16) A further EBA exercise was carried out in October 2011. The criteria for that exercise were set in September 2011 and stipulated that the CT1 as a percentage of RWA had to reach 9% including a sovereign buffer. The results of the October 2011 exercise were published on 8 December 2011.³ Banks are expected to build those buffers by 30 June 2012 in order to reach 9% of CT1. For NORD/LB, EBA observed a capital shortfall of EUR 2489 million⁴.

2.2 The capital measures

- (17) The capital measures consist of an increase of the CT1 through both capital conversion and capital increase measures. More specifically, they contain following measures:
 - (i) Termination and repayment of the silent participation of Land Niedersachsen of around EUR [...] million;
 - (ii) Termination and repayment of two silent participations of its wholly-owned subsidiary Hannoversche Beteiligungsgesellschaft mbH (hereafter "HanBG") of around EUR [...] million;

² Gesetz über Kapitalmaßnahmen zugunsten der Norddeutschen Landesbank.

³ In light of the sharp increase in systemic risk triggered by the sovereign debt crisis in the euro area, the EBA has designed a recapitalisation exercise, covering large EU banks, which aimed at providing a further, temporary capital buffer for the banks involved.

⁴ Source: EBA website-Results of the 2011 EU Capital Exercise. However, that shortfall is caused to a certain extent by EBA's decision to move the deadline for the implementation of the measures forward to 30 September 2011, instead of 1 December 2011, as initially agreed. Thus, the capital measures committed in April 2011 had not been accepted by EBA at the time of the latest recapitalisation exercise. Notwithstanding that factor, the need for additional capital to meet the capital shortfall identified by the latest recapitalisation exercise cannot be excluded.

* Secret business

- (iii) Repayment of subordinated loans ('Nachrangmittel') held by HanBG of around EUR [...] million;
 - (iv) Repayment of a special loan ('besonderes Darlehen') by Land Niedersachsen of around EUR [...] million; and
 - (v) Repayment of a special capital injection (besondere Kapitaleinlage) of around EUR [...] million.
 - (vi) The conversion of all of the amounts mentioned in points i) to v) above into CT1
 - (vii) In addition, a capital injection in cash of around EUR 600 million (made up of around EUR 500 million from Land Niedersachsen and around EUR 100 million from the Savings Banks' Associations, of which around EUR [...] million result from a conversion of capital investments (*Genussscheine*) into CT1).
- (18) The Land Sachsen-Anhalt does not hold silent participations, while the Savings Banks' Associations do so only for a limited amount. Hence, they will not participate in the conversion of silent participations. The Land Sachsen-Anhalt will not participate in the capital injection at all. Initially, the Savings Banks' Associations did not intend to participate in the capital increase either. Later in the process, in November 2011, the Savings Banks' Associations decided to participate with a total of around EUR 100 million and thus reduce the initially planned participation of the Land Niedersachsen from around EUR 600 million to EUR 500 million.
- (19) The shareholders agreed to postpone the implementation of a part of the capital measures, equivalent to EUR 279 million, for reasons of budgetary law, to 2 January 2012.
- (20) In sum, the capital measures described in the recital (17) above consist of several elements which result in the conversion of silent participations and other capital instruments held by Land Niedersachsen and its 100% subsidiary, HanBG, into CT1, totalling EUR 1067 million as well as an additional core capital increase of both Land Niedersachsen for the amount of EUR 500 million and the Savings Banks' Associations for the amount of EUR 100 million.
- (21) That increase of the CT1 of EUR 1667 million is composed of nominal share capital (Stammkapital) of EUR [...] million and the corresponding issuance premium (Agio) of EUR [...] million. The Agio is defined as difference between the nominal value of shares and the amount actually paid in. Subsequently, the Stammkapital will amount to EUR 1493 million; the total issuance premium to EUR 3037 million and the total paid in capital to EUR 4531 million.⁵
- (22) As a result of the capital measures, the voting rights have been accordingly revisited. The voting rights following the capital measures are as follows: Land Niedersachsen receives around 56.03% of the voting rights; Land Sachsen-Anhalt around 5.99%, SVN around 28.36%, SBV around 5.68 % and SZV around 3.94 %.

⁵ Before the capital measures, the Stammkapital was made up of EUR 1085 million and an issuance premium (Agio) of EUR 1779 million, or a total Kernkapital of EUR 2864 million.

- (23) As a result, the Land Niedersachsen becomes the majority shareholder. It will be in a position to nominate 6 of the 18 members of the supervisory board, of which 6 are nominated by the employees. Having the majority of votes in the shareholders' meetings means among others that it can e.g. achieve acceptance on a possible change of the bank's bylaws, appoint the Chairman of the Board and decide on the allocation and distribution of profits.
- (24) The exact allocation of the voting rights is based on the assessment conducted by an external consultant, who conducted a valuation of NORD/LB based on the Net Present Value, a generally accepted valuation methodology. That methodology determines the net present value (NPV) of the expected future cash flows, discounted to the (present) valuation date.
- (25) The key assumptions in the valuation are: a CT1 ratio of NORD/LB of [...] %; a discount rate of [...] % up to and including 2015 and [...] % thereafter.
- (26) More specifically, the discount rate (Kapitalisierungszinssatz) was calculated by taking into account the adverse effects on the financial markets caused by the ongoing financial crisis. Its value is [...] % for the period until 2015 and [...] % (before growth) from 2016 on. The components of the discount rate are a risk-free interest rate (angemessener risikofreier Basiszinssatz) of [...] % based on a recommendation of the IDW⁶ and a risk premium for NORD/LB of [...] % (until 2015) and [...] % (from 2016 on). The latter was calculated with a Beta-factor of [...] (until 2015) and [...] (from 2016 on) multiplied by a market risk premium of [...] % (which is in the middle of the band ranging from [...] % to [...] % recommended by the IDW).
- (27) As a result, the external consultant determined a company value of EUR [...] million as of 30 June 2011 (valuation date) which was adjusted to EUR [...] million as of 1 December 2011. 1 December 2011 was the initially envisaged date for the implementation of the capital measures.
- (28) From the valuation, it follows that the relation between company value (EUR [...] million) and present nominal share capital (Stammkapital) (EUR [...] million) is [...] %. That ratio defines how the capital measures of EUR 1667 million will be split among nominal share capital (Stammkapital) and Agio. In that case, the Agio has a value of EUR [...] million. Voting rights accrue only to the nominal value of shares (Stammkapital) and the Agio does not receive any remuneration.

3. GERMANY'S POSITION

- (29) Germany requests urgent temporary approval of the measures in order to comply with the capital requirements as set out by EBA. If the measures are not approved before the end of the year it would not meet the expectations of the capital markets.

⁶ Institut der Wirtschaftsprüfer.

- (30) Germany cannot exclude that the conversion of silent participations and other capital instruments of Land Niedersachsen and the additional share capital increase of Land Niedersachsen constitute State aid under the current circumstances.
- (31) In any event, in view of the risk that the failure of the bank to comply with the EBA requirements would entail for Germany's financial system, Germany argues that the measures are compatible with the internal market under Article 107(3)(b) TFEU.
- (32) Germany submits that the increase of the ordinary share capital will be carried out at market terms. In order to give the capital providers a sufficient remuneration, the voting rights and the associated share of dividends have been properly adjusted.
- (33) Germany committed to notify an in-depth restructuring plan within six months from the date of the present rescue decision.
- (34) Germany committed that until a final decision on the restructuring aid is taken, NORD/LB will make payments on hybrid capital instruments only if it is under a legal obligation to do so and does not use reserves or special reserves as defined by §340(f)/(g) of the German Commercial Code to this end.
- (35) Germany also commits that NORD/LB must not use the granting of the measures or any advantages over competitors arising there from for advertising purposes.

4. ASSESSMENT

4.1. Existence of State Aid

- (36) According to Article 107(1) TFEU, State aid is any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods, in so far as it affects trade between Member States.
- (37) The qualification of a measure as State aid requires that the following conditions are met: a) it must be financed by a Member State or through State resources; b) it must grant an advantage liable to favour certain undertakings or the production of certain goods; c) the measure must distort or threaten to distort competition; d) and the measure must have the potential to affect trade between Member States.
- (38) The capital measures are granted by the shareholders of NORD/LB. All shareholders are either public entities such as regions or municipalities or are owned by them (the savings banks). The Commission recalls that it has already established in its case practice that means provided by savings banks associations are resources directly or indirectly controlled by public authorities⁷. As all shareholders of NORD/LB are thus either directly

⁷ See point 64 of the Commission Decision of 29 September 2010 in case C32/2009, *Restructuring of Sparkasse KölnBonn*, OJ L 235, 10.09.2011, p.1; point 29 of the Commission Decision of 30 April 2008 in case NN 25/2008, *WestLB risk shield*; Commission Decision of 1 October 2008 in case C43/2008, *WestLB risk shield*, OJ C 322, 17.12.2008, p.16; and Commission Decision of 12 May 2009 in case C43/2008, *WestLB risk shield*.

or indirectly attributable to the State,⁸ the Commission concludes that the measures stem from State resources.

- (39) The capital measures allow NORD/LB to obtain capital in a financial and economic crisis situation where it would have been very difficult to find such capital on the market. While it is not excluded that a shareholder of a bank would convert its silent participation, given that such capital will lose its regulatory quality in the medium-term and provided that the new shares offer a sufficient return, it is not evident that private shareholders would provide significant amounts of additional capital. In any event, unlike in the present case, a market economy investor would not have agreed, even in principle, on the measures in April 2011 unless it was already in receipt of and had analysed a company evaluation. Therefore, the Commission considers that the capital measures would not have been provided by a market economy investor. The capital measures must therefore be regarded as providing an advantage to NORD/LB. Moreover, the resulting advantage is selective since it only benefits one bank.
- (40) Given that NORD/LB is and will be active in the financial sector, which is open to intense international competition, any advantage from State resources to the bank has the potential to affect intra-Union trade and to distort competition. The measures therefore constitute State aid within the meaning of Article 107(1) TFEU.

4.2. Compatibility

- (41) Article 107(3)(b) TFEU empowers the Commission to find that aid is compatible with the internal market if it is intended "to remedy a serious disturbance in the economy of a Member State". The Commission has acknowledged that the global financial crisis can create a serious disturbance in the economy of a Member State and that measures supporting banks are apt to remedy that disturbance. That assessment has been confirmed in the Recapitalisation Communication⁹ and the Restructuring Communication.¹⁰ The Commission still considers that requirements for State aid to be approved pursuant to Article 107(3)(b) TFEU are fulfilled in view of the reappearance of stress in financial markets. The Commission confirmed that view by adopting the 2010 Prolongation Communication¹¹, which prolongs until 31 December 2011 the application of State aid rules to support measures in favour of banks in the context of the financial crisis. The Commission has since extended the application of those rules beyond 31 December 2011.¹²

⁸ See in that respect for example Commission decision of 30.6.2009 in case C 17/2009, LBBW, OJ 2009 C 248, 10.16.2009, p. 7, recital 40.

⁹ Communication from the Commission – The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition, OJ C 10, 15.1.2009, p. 2.

¹⁰ Commission communication on the return to viability and the assessment of the restructuring measures in the financial sector in the current crisis under the State aid rules, OJ C 195, 19.8.2009, p. 9.

¹¹ Communication from the Commission from 1 January 2011, of State aid rules to support measures in favour of bank's in the context of the financial crisis, OJ C 329, 7.12.2010, p. 7.

¹² Communication from the Commission on the application, from 1 January 2012, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 356, 6.12.2010, p. 7.

- (42) In respect of the German economy that analysis has been confirmed in the Commission's approval of various measures undertaken by the German authorities to combat the financial crisis.¹³
- (43) Any uncertainty regarding the fulfilment of regulatory requirements could directly affect the financial markets and thus the entire economy of a Member State. In light of the current fragile situation of the financial markets, the Commission continues to base its assessment of State aid measures in the banking sector on Article 107(3)(b) TFEU.
- (44) On the basis of Article 107(3)(b) TFEU, the general principles applicable for State aid granted to financial institutions are set out in point 15 of the Banking Communication¹⁴. Accordingly, the aid must be appropriate to achieve the objective of remedying a serious disturbance in the economy, limited to the minimum necessary in view of the objective pursued, and proportionate to minimize negative spill-over effects on competitors, other sectors and other Member States.
- (45) The Recapitalisation Communication¹⁵ translates those general principles into specific compatibility conditions.
- (46) In order to be compatible the aid must first be appropriate. The aim of the aid is to eliminate the threat to the stability of the German economy stemming from any solvency problems of NORD/LB. The Commission considers that the aid instruments chosen by the German authorities, i.e. the conversion of a silent participation into common equity and the additional provision of equity capital via a recapitalisation is an appropriate means to address NORD/LB's solvency problems. The aid is consequently designed to prevent any infringement of the EBA capital requirements by moving the capital ratios of NORD/LB above the required minimum.
- (47) It can secondly be considered that the capital measures are necessary to meet the new regulatory requirements. The capital ratios of NORD/LB would have otherwise not been sufficient to prevent regulatory action which the supervising authority, Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin), could have taken. Given the current economic circumstances, to that end the capital ratio might need to be well above present regulatory minimum requirements laid down by German law.
- (48) Moreover, a limitation of the aid to the minimum is supported by a commitment of Germany ensuring that NORD/LB will not release reserves in order to record a profit and thereby pay coupon to hybrid capital holders.

¹³ Commission Decision of 20 December 2011 in case SA.29590, *Bad Bank for WestLB*, not yet published and Commission decision of 29 September 2011 in case SA.29338, *Restructuring of HSH Nordbank AG*, not yet published.

¹⁴ Communication on the application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis, OJ C 270, 25.10.2008, p. 8.

¹⁵ Communication from the Commission - Recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition, OJ C 10, 15.1.2009, p. 2.

- (49) Finally, in order to be proportionate the Commission must assess whether the remuneration for the aid was adequate to limit the distortions of competition to the minimum. In that respect, the Commission considers that the Recapitalisation Communication provides the appropriate framework for assessment.
- (50) As regards common equity, the Annex to the Recapitalisation Communication recalls that "Ordinary shares are remunerated by uncertain future dividend payments and the increase of the share price (capital gain/loss), both of which ultimately depend on the expectations of future cash flows/profits. [...]. For non-quoted banks, as there is no quoted share price, Member States should come to an appropriate market-based approach, such as full valuation." Moreover, the German rescue scheme implementing that rule for Germany provides that "In the case of ordinary shares, the Federal Government will demand a discount on the price prevailing before the capital increase was announced." Point 8 of the recent *Communication from the Commission on the application, from 1 January 2012, of State aid rules to support measures in favour of banks in the context of the financial crisis*, which will only be applied as of 1 January 2012, stipulates that the discount should be sufficient.¹⁶
- (51) Germany has determined a company value as described above in point (27). On that basis Germany submits that the shareholders should have obtained an increase of shares and increased dividend payments flowing from the receipt of the shares.
- (52) The Commission has not had sufficient time and means to assess the submitted valuations. A final conclusion of the appropriate remuneration will therefore be left for the restructuring assessment. The conclusion that the measures were necessary to meet the regulatory requirements is hence without prejudice to the question whether the price paid by the shareholders subscribing to the capital increase appropriately reflects their respective fair shares of the value of the bank. In the present case, the Commission needs to assess whether the voting rights received and the attached entitlement for a percentage of the profits is adequate. It is clear that any additional advantage inherent to remuneration below that required by the State aid rules will need to be taken into account in the restructuring phase.¹⁷
- (53) Furthermore, the Commission notes positively that NORD/LB has agreed not to advertise the fact that it received State aid.
- (54) In sum, the Commission concludes that the aid measures are appropriate to rescue NORD/LB in the short-term and will for the time being not entail an undue distortion of competition. The Commission however reiterates that it needs to be provided with a restructuring plan at the latest six months from the date of the present decision and that the approval of the aid is limited until the Commission takes a final decision on the restructuring plan, which Germany will submit within 6 months .

¹⁶ OJ C 356, 6.12.2010, p. 7.

¹⁷ Similar. Commission decision of 29.5.2009 in case N 264/2009 (ex-PN 59/2009) – Rescue aid to HSH Nordbank AG, OJ C 179/2, 1.8.2009, p. 3. and Commission decision of 20.9.2011 in case SA.29338 – Restructuring of HSH Nordbank AG, not published yet.

4.3. Conclusion

- (55) In view of the elements set out above, it can be concluded that the capital measures of EUR 1667 million in favour of NORD/LB can be temporarily approved as rescue aid until the Commission takes a final decision on the restructuring plan, which Germany will submit within 6 months. .

5. DECISION

The Commission observes that the recapitalisation measures in favour of NORD/LB consisting of a conversion of silent participations and other capital instruments held by Land Niedersachsen and of its wholly-owned subsidiary, Hannoversche Beteiligungsgesellschaft mbH, for a nominal amount of EUR 1067 million into core capital and the additional share capital increase of Land Niedersachsen and Savings Banks' Associations of EUR 600 million constitute State aid within the meaning of Article 107(1) TFEU. They fulfil the requirements of Article 107(3)(b) TFEU and are temporarily compatible with the internal market for reasons of financial stability until the Commission takes a final decision on the restructuring plan, which Germany will submit within 6 months. The Commission has accordingly decided not to raise objections against the implementation of the measures.

Germany exceptionally accepts that the decision be adopted in the English language.

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

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Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President