The European Commission's Decision-making on State Aid for Financial Institutions—Good Regulation in the Absence of Good Governance?

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Introduction

Since the beginning of the financial and, later, the sovereign debt crisis, EU Member States have granted numerous aids for the rescue and restructuring of financial institutions. Like any other State aid, rescue and restructuring aids for financial institutions need to comply with the EU State aid regime. Article 107 (1) TFEU provides a general prohibition of State aid. However, under exceptional circumstances, State aid is (TFEU art.107(2)) or may be permitted if it is considered compatible with the internal market (TFEU art.107(3) or art.106(2)) subject to the Commission's approval sanctioned by a pre-approval implementation ban (stand still) under TFEU art.108(3). While general rescue and restructuring aid has been traditionally approved under TFEU art.107(3)(c) and the Community Guidelines on State aid for rescuing and restructuring firms in difficulty[1] (the "Rescue and Restructuring Guidelines"), the financial and sovereign debt crisis has triggered off the application of TFEU art.107(3)(b), i.e. compatible aid to remedy a serious disturbance in the economy of a Member State. However, the Commission's exclusive authority to permit State aid under TFEU art.108(3) according to these exceptions has been preserved.[2] State aid measures in favour of financial institutions during the financial and sovereign debt crisis with which the Commission has been confronted comprise, inter alia, State guarantees as well as granting of credit, the purchase of voting or non-voting shares of ailing banks for the purpose of recapitalisation[3] or hybrid capital and the acquisition of risk positions, especially impaired assets, and the installation of bad banks.[4] Faced with such different instruments of State aid for the rescue and restructuring of financial institutions during the crisis, the Commission has developed a distinct set of crisis rules since 2008. This article examines how the Commission applies the EU State aid rules, in particular TFEU art.107(3)(b), to State aids for financial institutions during the crisis, thereby shaping the post-crisis architecture of the financial sector.

Legal framework of the EU State aid control in the financial sector

Before adopting a series of specific communications to remedy the consequences of the crisis between October 2008 and July 2009, the Commission applied the same rules, the Rescue and Restructuring Guidelines, to aids for firms of all sectors other than the coal and steel sectors.[5] However, in the aftermath of the collapse of Lehman Brothers in September 2008, the Commission qualified the crisis as a serious disturbance in the economy of the Member States within the meaning of TFEU art.107(3)(b), thereby acknowledging that State aid for financial institutions suffering from the crisis is not primarily a mean to help the ailing financial institution itself, but serves to combat systemic risks and to prevent a severe disruption of the financial system and the economy as a whole.[6]

The Commission's Communications on the application of article 107(3)(b) TFEU to State aid granted to financial institutions during the crisis

The Commission has issued a number of specific communications on the application of TFEU art.107(3)(b) to State aid granted to financial institutions during the crisis. Those communications are:

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[1] [2004] OJ C244/2.

[2] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.28.

[3] *Allied Irish Banks/Educational Building Society and Irish Life & Permanent Group Holdings* (SA.33296).

[4] The *CEPS Task Force Report*, October 2010) (pp.8–9) differentiates between four main forms of State aid to the financial sector: (1) guarantees for bank deposits, bank bonds or all bank liabilities, (2) equity support to strengthen the capital base of financial institutions, (3) creation of a bad bank in which banks get a delay to reimburse their creditors until the financial system normalises and assets recover and (4) nationalisation of banks, whereas the latter itself is not a form of State aid; it is rather the capital injection in a bank in trouble that forms State aid.

[5] Pesaresi and Mamdani, "Latest Developments in the Rules on State Aid for the Rescue and Restructuring of Financial Institutions in Difficulty" [2012] *European State Aid Law Quarterly* 767.

[6] In no. I.2. and I.3. of its Communication 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 [2011] OJ C 356/7, the Commission indicated that it considered that the requirements for State aid to be approved pursuant to art.107(3)(b) of the Treaty were still fulfilled and would continue to be fulfilled beyond the end of 2011.

- the Communication on the application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis (the "Banking Communication")[7];
- the Communication on the recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition (the "Recapitalisation Communication")[8];
- the Communication on the treatment of impaired assets in the community banking sector (the "Impaired Assets Communication"),[9] all three of the latter concerning the compatibility prerequisites of the main types of State aid, which are guarantees on liabilities, recapitalisations and asset relief measures;
- the Communication on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules (the "Restructuring Communication")[10] setting out the particular features for restructuring and viability plans in the specific context of crisis-related State aid granted to financial institutions under TFEU art.107(3)(b);
- the Communication on the application, from January 1, 2011, of State aid rules to support measures in favour of banks in the context of the financial crisis (the "First Prolongation Communication")[11] extending the Restructuring Communication—the only one of the four aforementioned Communications with a specified expiry date—on amended terms; and
- the Communication on the application, from January 1, 2012, of State aid rules to support measures in favour of banks in the context of the financial crisis (the "Second Prolongation Communication"),[12] extending the Restructuring Communication beyond December 31, 2011 and supplementing "the Recapitalisation Communication by providing more detailed guidance on ensuring adequate remuneration for capital instruments that do not bear a fixed return; [explaining] how the Commission will undertake the proportionate assessment of the long-term viability of banks in the context of the banking package; and [introducing] a revised methodology for ensuring that the fees payable in return for guarantees on bank liabilities are sufficient to limit the aid involved to the minimum"[13].

By setting out the principles under which the Commission assesses State aid for financial institutions during the financial crisis, those crisis-specific rules for the financial sector outline the Commission's scope for imposing conditions (1) subject to which an aid may be considered compatible with the internal market and (2) to safeguard compliance with the decision to be monitored pursuant to art.7(4) of Council Regulation (EC) 659/1999,[14] which provides procedural rules for State aid. Although the Commission's communications are non-binding ("soft law"), they provide an "authoritative guide (...) to the Commission's methodology and would certainly be taken into consideration by the European Courts in exercising their judicial review function."[15]

Key principles of State aid control in the financial sector

The Commission's assessment of State aids for financial institutions during the financial crisis as set out by the abovementioned rules distinguishes between rescue aid and restructuring aid.[16] Rescue aid is designed as short-term aid "to give the beneficiary the necessary breathing space to develop a detailed restructuring or liquidation plan"[17]. Therefore it is granted in principle for a period of no longer than six months, whilst restructuring aid is usually granted for a longer period of time to enable its beneficiary to implement its restructuring or liquidation plan. With regard to the compatibility assessment under TFEU art.107(3)(b), both forms of aid need to comply with three key principles, which base on the (general) Rescue and Restructuring Guidelines of the Commission, but have been modified with regard to the particularities of the financial sector during the crisis[18]:

[7] [2008] OJ C270/8.
[8] [2009] OJ C10/2.
[9] [2009] OJ C72/1.
[10] [2009] OJ C195/9.
[11] [2010] OJ C329/7.
[12] [2011] OJ C356/7.
[13] No. I.5. of the Second Prolongation Communication.
[14] [1999] OJ L83/1.
[15] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.31.
[16] Pesaresi and Mamdani, "Latest Developments in the Rules on State Aid for the Rescue and Restructuring of Financial Institutions in Difficulty" (2012) *European State Aid Law Quarterly* 767, 768.
[17] Pesaresi and Mamdani, "Latest Developments in the Rules on State Aid for the Rescue and Restructuring of Financial Institutions in Difficulty" (2012) *European State Aid Law Quarterly* 767, 768.
[18] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.41; Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145; Pesaresi and Mamdani, "Latest Developments in the Rules on State Aid for the Rescue and Restructuring of Financial Institutions in Difficulty" (2012) *European State Aid Law Quarterly* 767, 768.

1. It needs to be shown that the beneficiary can achieve long-term viability without State aid within a reasonable period of time.
2. Shareholders and hybrid capital holders need to contribute through bans on dividends or coupon payments and limitations on the repurchase of capital instruments; and additionally, the aid needs to be adequately remunerated by the beneficiary ("burden sharing" as a mean to limit State aid to the minimum necessary and to minimise the State's, i.e. the taxpayers' burdens). This concept of "burden sharing" has been designed to replace the "50 per cent own contribution" under the Rescue and Restructuring Guidelines in order to avoid contagious fire sales of assets by the beneficiary.[19]
3. Beneficiaries need to provide measures like capacity reductions and divestments going beyond those required to ensure the beneficiary's viability to limit the distortions of competition caused by the aid to the minimum necessary. Compared to the traditional concept of compensatory measures as established by the Rescue and Restructuring Guidelines, this requirement includes "a greater focus on market competition conditions rather than compensation of competitors as well as the development of behavioural measures for situations where sufficient divestments could not be found without threatening viability"[20] to "ensure an effective restructuring of the banking sector while maintaining an adequate flow of credit to the real economy (both within and beyond the domestic markets of the banks that received aid)"[21] in regard of the interconnectedness of financial institutions across the EU and beyond. This reflects an important evolution in the State aid clearing practice of the Commission and its objectives in the past four years: At the beginning of the financial crisis, the main focus was on rescuing banks by providing liquidity and reinforcing the capital base, while today State aid measures approved by the Commission aim at the recovery of the long-term viability of the aid recipient or—if long-term viability without State aid cannot be achieved within a reasonable period of time—its liquidation.[22]

The Commission's practice of controlling State aid for financial institutions

Though the key principles that underpin the EU State aid regime and its implementation by the Commission are clearly pronounced in the Commission's communications and its case practice, applying them in practice is rather difficult due to highly speculative ex ante assessments, in particular under the conditions of the evolving sovereign debt crisis. What, for example, is the strictest minimum contribution of a (sovereign debt infected) State-aided financial institution, its shareholders and hybrid capital holders to restructuring costs? What conditions can the Commission impose on an aid-recipient? The Commission assesses and answers those questions on a case-by-case-basis due to the different structures, business models, sizes and operating areas of State-aided financial institutions. Yet, there are certain basic considerations that the Commission consistently applies. Those are adequate remuneration, dividend and/or coupon payment ban and price leadership ban.[23] What differs are the degrees of downsizing and the core market reduction by, for example, divesting non-core subsidiaries.[24]

Restructuring aid

In general, the Commission will only consider an aid to be compatible with the internal market on the basis of TFEU art.107(3)(b) if the aid is presented within a restructuring plan that is apt to restore the financial institution's long-term viability whilst ensuring burden sharing and limiting distortion of competition in the relevant markets. To ensure the latter, the Commission may impose conditions and obligations according to art.7(4) of Regulation 659/1999 or ask for appropriate optional commitments by the beneficiary. Most of such measures aim at reducing the business activities of the beneficiary.[25] In 2011, for example, the Commission approved aid by the Greek State for the Agricultural Bank of Greece (ATE), the fifth largest banking group in Greece having approximately 6 per cent of total bank assets in Greece, considering the restructuring plan of ATE not only apt to restore the bank's long-term viability, but also apt to ensure ATE shares the burden of its

[19] Pesaresi and Mamdani, "Latest Developments in the Rules on State Aid for the Rescue and Restructuring of Financial Institutions in Difficulty" (2012) *European State Aid Law Quarterly* 767, 768.
[20] Pesaresi and Mamdani, "Latest Developments in the Rules on State Aid for the Rescue and Restructuring of Financial Institutions in Difficulty" (2012) *European State Aid Law Quarterly* 767, 768.
[21] Pesaresi and Mamdani, "Latest Developments in the Rules on State Aid for the Rescue and Restructuring of Financial Institutions in Difficulty" (2012) *European State Aid Law Quarterly* 767, 768.
[22] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.
[23] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.15.
[24] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.15.
[25] Soltész, "Von der Beihilfekontrolle zur Neugestaltung des Marktes—Schafft die Kommission eine ‚bessere Bankenwelt'?" (2010) *Wirtschaft und Wettbewerb* 743, 748.

restructuring and to limit distortion of competition in the Greek retail banking market by committing to reduce its overall assets by 25 per cent during the restructuring period through sales, the run-off of certain securities portfolios and reduction of total loan balances.[26]

The degree of balance sheet reduction of State-aided financial institutions, however, differs considerably. Whilst the Commission was content with the reduction of the State-aided bank's overall assets by 25 per cent in the ATE case, for example, the degree of downsizing and the core market reduction has been considerably higher in other State aid cases as the Hypo Real Estate (HRE) case[27] shows: The banking group HRE faced a severe liquidity shortage in 2008 as the interbank lending markets dried up in the aftermath of the Lehman Brothers bankruptcy. After the nationalisation of HRE in 2009, the Commission cleared a restructuring aid for HRE on July 18, 2011 judging the restructuring plan of HRE and its core bank Deutsche Pfandbriefbank (Pbb), which is essentially active in public investment and real estate finance, apt to restore Pbb's long-term viability whilst ensuring that the bank and its former owners adequately contribute to the restructuring costs and that distortion of competition will be adequately mitigated by phasing out all business activities of the HRE other than the activities of its core bank Pbb, so that Pbb's adjusted balance sheet size at the end of 2011 would be about 85 per cent smaller than HRE group's balance sheet size at the end of 2008.

Liquidation aid

Regarding State aid for the liquidation of ailing banks, the Commission basically focuses on the question whether the aid is limited to what is necessary to carry out an orderly winding-up of the bank. Therefore, safeguards have to be implemented that those parts of the bank which are not sold will not pursue any new activities but merely phase out on-going operations in order to limit potential distortions of competition. On those conditions, the Commission authorised aid by the Danish State for the liquidation of the Eik Bank, until 2010 the biggest financial institution in the Faroe Islands with significant retail and corporate banking activities in the rest of Denmark.[28] The bank entered into the Danish scheme for the winding-up of financial institutions in distress and some of its activities were offered for sale in a public tender while others were transferred to the publicly owned Danish Financial Stability Company (FSC), to be either sold or liquidated within a maximum of five years.

Rescue aid

Rescue aid is only approved temporarily and it is in general subject to the submission of a revised restructuring plan with the final approval of the measure being conditional on the restructuring plan's compliance with the abovementioned three key principles of State aid for financial institutions during the financial crisis: (1) a return to long-term viability of the bank; (2) adequate participation in the restructuring costs by shareholders and hybrid capital holders ("burden sharing"); and (3) proper measures to limit the distortion of competition created by the State aid.[29]

Involvement of the beneficiary

While the Commission focuses on the compliance with the three aforementioned key principles, the concrete phrasing of details of restructuring lays in the hand of the beneficiary and its Member State. However, the Commission's control does go further than merely receiving and assessing restructuring concepts presented by the Member States and the beneficiary. Restructuring plans are often the result of close communications and negotiations between the Commission, the Member State granting aid and the beneficiary. Thus, restructuring plans are only—and yet at least—in very broad terms based on proposals worked out between the State-aided financial institution and the Member State concerned. In the HRE case,[30] for example, Germany notified the first version of the restructuring plan in 2009. As the Commission had doubts on the bank's viability, the adequacy of the measures addressing burden sharing and the limitation of distortion of competition, it opened an in-depth investigation. In the course of that investigation, the restructuring plan was finally agreed on by all parties including the Commission and finally updated in June 2011. However, the Commission itself generally emphasises that many if not all measures taken in a single case (e.g. radical divestments like in the ING case) have usually been proposed by the beneficiary itself.[31] In any case, the beneficiary and the Member State, which can usually better assess the feasibility of a measure, have at least the prerogative of first initiative and of first proposal in formulating commitments.[32] However, it may turn out to be difficult to comply with divestments agreed on or imposed by the Commission due to the present market circumstances, especially due to the risks of contagious fire sales of assets. The Commission has proven flexibility in handling divestment obligations and behavioural measures that it had imposed, accepting, for example, proposals to modify contagious or impracticable

[26] SA.31154 (N429/2010).
[27] SA.28264.
[28] SA.31945.
[29] SA.33216; Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.32.
[30] SA.28264 (ex C 15/2009 and N 196/2009).
[31] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.40 with regard to the ING, KBC and Lloyds cases.
[32] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.

divestment obligations.[33] It is nevertheless important to underline that neither the TFEU nor the Council Regulation 659/1999 constitute any legal basis for "hearings" of recipients of aid or their competitors by the Commission, although in practice, the Commission is usually willing to receive written submissions by interested third parties including aid recipients or to hold meetings.[34] Yet, the notification procedure remains a bilateral procedure between the Commission and the Member State concerned. The degree of involvement of a financial institution that shall receive State aid is at the discretion of the Commission and the Member State concerned regardless of how useful such participation would be with regard to the complex economic and case-specific issues to be solved when granting restructuring, liquidation or rescue aids to ailing financial institutions.[35]

Execution of divestment obligations

EU State aid law conforming execution of divestment obligations is driven by the key principle of market economy price maximising. This principle derives from the market economy investor (market vendor) principle, which excludes the presence of State aid if State sales are on (hypothetical) private vendor terms. Although TFEU art.107(1) addresses the Member States, not strictly private undertakings, those principles apply to State aid driven divestment procedures requested by the commission as condition subject to which an aid may be considered compatible with the internal market pursuant to TFEU art.107(3)(b).[36] This is based on the assumption that the best price achievable at the market will ensure the beneficiary's contribution to the restructuring, so that in turn, the State aid contribution is limited to the necessary minimum. Moreover, divestment at the best achievable price also ensures that the buyer does not gain any benefits under unusual market terms from a divestment which might not have been initiated if not imposed by the Commission, thereby avoiding unnecessary distortions of competition by such divestment. To achieve the objective of price maximising, the Commission draws on two key principles as confirmed by the General Court: (1) the conduct of an open, transparent, unconditional and non-discriminatory tender; and (2) the acceptance of the highest bid after the tender.[37]

EU State aid law requirements on tendering procedures

Difficulties to divest under the market tendering terms as requested by the Commission and the General Court may not only arise from the crisis market environment, but also from the formal requirement of conducting an open, transparent, unconditional and non-discriminatory tender, which applies to divestments of subsidiaries or other businesses by State-aided institutions.[38] The Commission and the General Court have developed rather formalised requirements for tendering procedures under the terms of EU State aid law,[39] although the typical private vendor would never subscribe to such a high degree of formalisation.[40] Due to gambling strategies of potential purchasers, a formalised tender might even be counterproductive to the objective of achieving the highest price in the market. This issue is particularly sensitive with regard to the basic principles of openness and transparency, which might appear to be a market ideology driven myth in the real world of gambling strategists among the bidders. Therefore, a private vendor wishing to maximise the price would conduct a structured (tender) procedure using the expertise of an investment bank or other agencies, which, at least in the initial phase, directly contact potential bidders upon terms of confidentiality and selectively negotiate with them, in order to gain, in favour of the vendor, information on, inter alia, bidders' financial reliability, strategic alliances (bidders' cartels), substantial or procedural preferences.[41] Such a structured procedure can help to maximise the price, even if it does not comply with the principles of an open, transparent, unconditional and non-discriminatory tender. Thus, the Commission and the General Court should handle the prerequisites imposed on tendering or sales procedures more private-vendor-like flexible to avoid unnecessary exacerbation of divestment obligations, which, indeed, risk to reduce the price of assets.[42]

The requirement of accepting the highest bid

The General Court's judgment in the *Burgenland* case[43] emphasises the imperative of accepting the highest bid after a tender within a privatisation procedure. Due to the troubled internal market and acquisition restrictions for State aid supported institutions, the highest bidder might come from a third state making it difficult to judge its financial and transactional reliability.[44] Nevertheless, the

[33] SA.34539.
[34] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.31.
[35] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) pp.31, 32.
[36] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.
[37] General Court, *Land Burgenland and Austria v Commission* (T-268/08 & T-281/08), judgment of February 29, 2012, not yet reported.
[38] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.
[39] General Court, *Land Burgenland and Austria v Commission* (T-268/08 & T-281/08).
[40] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.
[41] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.
[42] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.
[43] General Court, *Land Burgenland and Austria v Commission* (T-268/08 & T-281/08).
[44] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.

Commission and the General Court follow a very restrictive approach in affirming non-feasibility of a divestment to the highest bidder.[45]

The concept of burden sharing

While the requirement of long-term viability without State aid after a reasonable period of time ensures that State aid is only granted as a remedy for a serious disturbance in the economy of a Member State or—in the case of the current crisis—of the Member States as a whole and not as a restructuring aid to financial institutions that are ailing due to non-crisis related difficulties, the concept of burden sharing provides for a maximised contribution to the restructuring costs by the aid recipient, thereby making sure that State aid is limited to the minimum necessary.

How can the burden of restructuring be shared conforming to EU State aid law?

The restructuring aid to NORD/LB[46] cleared by the Commission's decision of July 25, 2012 implies a rather flexible concept of burden sharing. Besides adequate remuneration of the public authorities that granted the aid, NORD/LB will also use the aid to strengthen its capital in the coming years by respecting a ban on dividends and hybrid coupon payments as well as on acquisitions during the restructuring period and by divesting profitable subsidiaries. Moreover, the NORD/LB will follow a cost-optimisation programme. Finally, a reduction of total assets by 15 per cent in 2016 in comparison with the end of 2011, restrictions of some business activities, divestments of non-core subsidiaries and behavioural commitments limit the distortions of competition created by the restructuring aid. The Commission's approach, however, appears more generous in that case than the clearance decision of July 25, 2012 suggests at first sight once taking into account that the clause of accessoriness between the ban on dividends and coupon payments under the silent partnership contract had been withdrawn the day before the Commission's decision of July 25, 2012, on July 24, 2012.[47] That accessoriness clause under the silent partnership contract excluded payments on T1 coupons in the case of a ban on dividends as imposed by the Commission's decision of July 25, 2012. Since the withdrawal of that accessoriness clause, payments on T1 coupons are allowed during the restructuring period of the bank in spite of the dividend ban. This eases the hybrid capital holders' contribution to the restructuring costs by a more near-term return on these hybrid restructuring investments.[48] Payments on T1 coupons might be justified (despite the dividend ban) only in the case of the hybrid capital holders' pure public status as a State aid donor (without any competitive functions as an undertaking). By contrast, if the hybrid capital holder is a public savings bank, i.e. an undertaking in highly competitive (retail) markets, the ban on coupon payments must not be compromised in order to avoid any watering down of regulatory coherency of the concept of burden sharing.

"Freeloader" asymmetries in burden sharing

Moreover, the NORD/LB case vividly demonstrates an asymmetry in burden sharing, that can be found in other cases as well and is yet unresolved. After the successful restructuring period, an asymmetry between the shareholder's ratio in the equity capital qualifying for dividends and their ratio in the contribution to the restructuring costs may arise from an unadjusted application of the usual dividend payment scheme under corporate law providing for an equal distribution of dividends to all shareholders of the same category of voting or non-voting (preferential) shares regardless of the individual shareholder's extra-contribution to the restructuring costs during the restructuring period. Thus, shareholders ("freeloaders") who have contributed less than others (e.g. less than the aid granting public shareholder/hybrid capital holder) might receive a disproportional share of the profit by virtue of (unadjusted) regular dividend payment schemes compared to their input during the restructuring period. In the case of NORD/LB, for example, the savings banks ("Sparkassen") own 38 per cent of the equity and bear less than 7 per cent of the restructuring costs, while the States of Lower Saxony and Saxony-Anhalt contribute much more to the restructuring costs. Yet, after the successful restructuring period, i.e. after the withdrawal of the ban on dividends, the savings banks will receive dividends according to their ratio of 38 per cent of the equity regardless of them bearing less than 7 per cent of the restructuring costs.[49] To eliminate such "freeloader" asymmetries in burden and profit sharing, EU State aid control would be well advised to develop and implement a concept which ensures the proportional correlation of a shareholder's contribution to burden sharing and his post-restructuring dividends and capital gains.[50] In doing so, due regard must be given to the circumstance that—following the Commission's approach—contributions to the restructuring costs do not only embrace a transfer of resources, but also the risk of short-term as well as long-term dilutions of a shareholder's earning rights.[51] However, the approval of coupon payments (by contrast to the dividend ban) in favour of public hybrid capital holders in their role as

[45] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 146.
[46] SA.34381, see IP/12/838.
[47] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 147.
[48] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 147.
[49] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 147.
[50] Koenig and Soltész, "Regulierung durch EU-Beihilfenrecht in der Finanz-und Staatsschuldenkrise" (2013) *Wertpapier-Mitteilungen* 145, 147.
[51] In the NORD/LB case, for example, the Commission stated that the dilution suffered by the shareholders following the recapitalisation, together with a ban on dividend and hybrid coupon during the period of restructuring, also contribute to an appropriate burden sharing of the restructuring costs (IP/12/838).

restructuring aid donors does not adequately remedy the aforementioned asymmetry in burden sharing, at least not according to an adequate adjustment under market economy investor terms.

Re-privatisation

The requirement of a market economy investor return that proportionally correlates to the ratio of burden sharing raises the question when Member States should sell back shares acquired for the purpose of recapitalisation during the crisis to the private market. The answer is: as soon as the market has stabilised, Member States concerned have to abide the momentum for a market economy investor sale, i.e. not sell back shares earlier as it seems at least likely ex ante for a market economy investor to make a reasonable risk adjusted profit. Of course, the market economy investor momentum can only be temporised with the assistance of an investment bank's expertise. Thus, the governments' political promise that their aid measures are merely temporary, and that the ultimate objective is to return the State-aided institution as soon as possible completely to the private sector is scrutinised under the market economy investor test.[52] However, the State aid law scrutiny of the market economy investor momentum of sale as such does "in no way prejudice the rules in Member States governing the system of property ownership" according to TFEU art.345. In case of re-privatisation, EU State aid law merely requires a market economy remuneration of the State capital invested, but does not impose an obligation on Member States to re-privatise a financial institution that has been partly or totally nationalised during the crisis, unless otherwise agreed in the context of a State aid procedure[53] and in conformity with TFEU art.345.

Conclusions ...

In spite of the exceptional circumstances of the financial and sovereign debt crisis, in particular the vast number of State aids granted and assessed since the beginning of the crisis, the Commission has succeeded in integrating the crisis-related State aid measures into the "classical" schemes de lege lata under arts 107 (1) and (3) sanctioned by the pre-approval implementation ban (stand still) under TFEU art.108(3). This success story is due to the Commission's flexible and pragmatic approach through legally non-binding communications on the Commission's intended application of the State aid rules combined with a sophisticated consensual and at the same time regulatory approach during the crisis while avoiding—for most decisions—judicial review by the European Courts,[54] thereby strengthening the level playing field for financial institutions in the post crisis internal market. However, the Commission's assessment of State aids for financial institutions during the crisis does go further than a mere legal control of compliance with EU State aid law. The compatibility assessment under TFEU art.107(3)(b) allows the Commission for a remarkable scope of discretion and economic appreciation in determining the form and content of national restructuring measures by the Member States, in particular by imposing divestment obligations and behavioural measures on the aid recipient to limit distortions of competition. Those obligations and measures will sustainably govern the aid recipients future business operations and growth agenda, thereby influencing and shaping the entire or at least great parts of the present and, more important, the post crisis financial sector. Even if the Commission contests the assertion of its subtle regulatory approach, there are obvious parallels with the Commission's merger policy striving for regulatory coherency of behavioural or structural conditions imposed by the approval decision with special regard to interdependent market structures, i.e. neighbouring, upstream and downstream markets, from a ratione temporis as well as from a ratione materiae perspective.

... and Philosophy

Notwithstanding the allegations of legal conservatism, under the crisis conditions, the thin line between *instant* emergency *law* making and interpretation has vanished, and under these conditions, the Commission has done a brilliant job all in all. Indeed, the Commission has exercised good regulation in the absence of good governance by sovereign debtors and financial institutions. Or to put it in modern platonic terms: EU State aid law regulation stems from the kingdom of thought, whereas public and corporate good governance stems from the reign of political and corporate feasibility!

[52] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.21.
[53] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.22.
[54] Lannoo, Sutton and Napoli, "Bank state aid in the financial crisis—fragmentation or level playing field?" (A Centre for European Policy Studies (CEPS) Task Force Report, October 2010) p.34.