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Competition Law in a Crashed Economy: State Aid to the Financial Sector

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Faced with the credit crisis the European Commission has relaxed the EU state aid rules by accepting rescue aid to systemic banks. When the first panic was over, it however put into place a strict legal framework for assessing restructuring aid, requiring banks that received substantial asset relief to cut deeply into their balance sheet. The authors examine this legal framework and in particular the legal basis of the restructuring measures the Commission seeks to impose.

1. Introduction

Competition law is aimed at ensuring free competition on the market to the benefit of consumers. In essence, competition law is based on the presumption that 'the market' is always right. But what if there is no market, or only a market that is seriously disturbed as a result of panic, irrational behaviour and a total loss of confidence? Is it in these circumstances possible at all to apply the competition rules or should these rules be temporarily stalled?

Market distortions may be caused by antitrust violations (cartel arrangements and abuse of dominant position),[1] by mergers between companies enhancing their market power following the merger,[2] or by financial aid granted by governments.[3] In the last decade, competition policy has increasingly been influenced by economic thinking.[4] An approach focusing on market power and economic effects is aimed at establishing what really happens or is likely to happen on the market. It may, on balance, reduce the scope of the EC treaty provisions that prohibit anti-competitive behaviour.[5] This may explain why the Commission has only cautiously introduced more economics into its competition policy.

A similar tension between the need to be realistic and the desire to maximize own powers is at the heart of the topic discussed in this article. Of the three branches of competition law (anti-trust, mergers and state aid), state aid clearly is the most political one. The state aid rules are broadly brushed compared to the other two fairly technical areas. In addition, the Commission has a very wide discretion in applying exceptions to the prohibition of state aid. The exceptional circumstances that followed the collapse of Lehman Brothers forced the Commission to adapt its policy on state aid in favour of the financial sector, while remaining firmly determined to have the final say on what aid is allowed. In numerous speeches on the credit crisis Competition Commissioner Neelie Kroes stated that competition law is not the cause of the financial crisis but part of the solution.

In this article, we will explain how the Commission is applying the state aid rules to national measures to support systemic banks. We will analyse the specific legal framework the Commission has put into place with a view to restoring financial stability while at the same time sustaining the level playing field between financial institutions. This 'crisis framework' consists of a series of communications which set the rules of the game, even if they are not formally binding.

2. The General Legal Framework

According to Article 87(1) EC 'state aid' is any aid granted by a Member State or through state resources in any form whatsoever which distorts or threatens competition, by favouring certain undertakings, in so far as it affects trade between Member States. This definition encompasses five conditions: (i) a financial advantage; (ii) from state resources; (iii) granted to certain undertakings (as opposed to measures of a general nature), having the effect; of (iv) distorting competition; and (v) having an impact on intrastate trade.

Measures taken in the financial crisis in favour of banks normally meet those conditions. This holds true of a) recapitalisation measures, b) guarantee schemes covering liabilities and c) back-up facilities transferring illiquid or impaired assets. It is not *a priori* given that such measures involve the granting of a financial advantage. Indeed, how does one establish that the State has paid a price above market price for a capital injection when the market is completely disturbed? In a situation of market failure the 'private investor test'[6] is not a particularly helpful instrument. Likewise, a guarantee to cover liabilities not necessarily qualifies as state aid. This may depend *inter alia* on the premium paid in return. Finally, the transfer of illiquid assets will not necessarily be a state aid

1. Articles 81 and 82 EC.
2. Regulation 139/2004, *OJ* 2004, L 24/1.
3. Articles 87 and 88 EC.
4. This is also true for state aid policy, following the State Aid Action Plan of 2005 (COM(2005)107 final of 07.06.2005).
5. In state aid cases, economic effects are discussed principally in the context of the exceptions to the general prohibition of state aid. See José Luís Buendía Sierra & Ben Smulders, *The limited role of the 'refined economic approach' in achieving the objectives of State aid control – Time for some realism'*, (Liber Amicorum Francisco Santaolalla), Alphen aan den Rijn: Kluwer Law International 2008.
6. The 'private investor test' assesses whether the State paid more for the transaction than a reasonable private investor would have paid. If this is the case, a financial advantage is granted.

when the portfolio also contains an 'upside' for the State, in the form of profit generating assets on top of an adequate fee. One may nonetheless assume that the Commission will consider all measures in favour of banks in the present crisis to constitute state aid and, consequently, to fall within its power to scrutinize these measures on their compatibility with the internal market.

State aid measures must be notified to the Commission before they may be implemented ('the stand-still principle').[7] The Commission has in principle two months to take a decision in which it may establish that the contemplated measure a) does not involve aid, b) that it does involve aid that is compatible with the internal market, or c) that further investigation is required.[8] In the last case, the Commission will open a formal procedure in which it will invite interested parties to submit observations, normally within one month. The formal procedure will end in a) an approval of the aid, b) a conditional approval or c) a prohibition.[9] In the last hypothesis, sums that have been paid must be recovered.[10] In case of a conditional approval, the Commission authorizes the measure under a series of conditions and obligations, which have normally been negotiated between the Commission and the Member State, for example restructuring measures in order to reduce the balance sheet of the beneficiary of the state aid. If the Commission approves a state aid it will generally do so on the basis of the general exception contained in Article 87 (3)(c) EC, when the aid facilitates the development of certain economic activities, provided the amount of aid is proportionate to the objective pursued. The Commission's policy as regards rescue and restructuring measures is outlined in the 2004 Rescue and Restructuring Guidelines[11] ('the R & R Guidelines'), which are based on Article 87(3)(c) EC. Because of the serious distortions of competition that can arise from R & R aid, the Commission normally approves such aid only under very strict conditions: the eligible undertaking has to be in difficulties[12] and the aid must be appropriate, proportionate and restricted to the minimum. The last three requirements are refined into several sub-requirements: aid may only be granted once in ten years to the same undertaking (the so-called 'one time, last time principle'), the undertaking has to contribute own financial means (at least 50% of the restructuring costs – the so-called 'burden sharing'), and the undertaking has to offer 'compensatory measures', which can take the form of divestments or closure of certain branches.

3. The Inadequacy of the General Legal Framework

In a *first phase* of the crisis (roughly from summer 2007 until October 2008), the Commission still applied the R & R Guidelines, in cases like *IKB, Sachsen Landesbank* and *Northern Rock*. When the crisis rapidly deteriorated in late September 2008, the Commission was closely involved, albeit informally, in discussions on the take-over of banks that had got into serious difficulties such as *Fortis*. In those days of survival, the Commission's prime objective was not to be sidelined in the political tsunami of rescue measures and, in particular, to avoid that the crisis was used to create new national champions. It is fair to say that the Commission had its part in the negotiations that took place in that turmoil.

Soon afterwards, the Commission put into place a legal framework with a view to structuring the various measures that Member States were on the point of taking in order to support systemic banks. The Commission also undertook to vet state aid measures at an unknown speed, if necessary within 24 hours. The general legal framework was not adequate to handle the problems raised by the exceptional nature of the financial crisis, in particular because the credit crunch affected also financially sound banks that could not be considered to be in difficulties within the meaning of the R & R Guidelines, but which had difficulties in financing their everyday business once the interbank market had come to a halt. The conditions set out in the R & R Guidelines were too strict and procedures too slow to allow for an immediate and adequate response to a crisis of this magnitude.

Thus, in the *second phase* of the financial crisis, the Commission had recourse to Article 87(3)(b) EC. This provision contains a possible ground for approving 'aid to [...] remedy a serious disturbance in the economy of a Member State'. In order for Article 87(3)(b) EC to apply, the whole economy of a Member State has to be affected by the disturbance.[13] Despite the fact that this provision has to be narrowly interpreted and that it had been applied only once (back in the 1980's), the Commission has used it as a basis for approving almost all of the rescue aid measures in favour of financial institutions, mostly for an initial period of 6 months.[14]

In order to clarify eligibility criteria and to enhance legal certainty, the Commission issued a series of communications which together make up for 'the crisis framework': the 'Banking'[15], 'Recapitalisation'[16], 'Impaired Assets'[17] Communications, which all aim specifically at the financial sector. Thus, the Commission gradually refined the crisis framework. In its

7. Article 88(3) EC.
8. See Article 4(2), (3) and (4) of Regulation (EC) 659/1999.
9. A positive, a conditional or a negative decision. See Article 7(3),(4) and (5) of Regulation (EC) 659/1999.
10. Article 14 of Regulation (EC) 659/1999.
11. Communication from the Commission – Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty, *OJ* 2004, C 244/2.
12. Which in short means that the undertaking is almost on the verge of liquidation. See for a detailed description the R & R Guidelines, points 9-13.
13. Joined cases C-57/00 P & C-61/00 P (*Freistaat Sachsen and Volkswagen*) (2003) ECR I-9975, para 98. The Commission enjoys a wide discretion when assessing the seriousness of the disturbance because of the complex economic and social nature of such an assessment.
14. See M. Hall, 'Competition Law and the Credit Crunch: Do the Usual State Aid Rules Still Apply?' Practical Law Company 22 January 2009, p. 3 and T. Jestaedt & J. Wiemann, 'Anwendung des EU-Beihilfenrechts in der Finanzmarktkrise – Wettbewerbspolitisches Regulativ, Hemmschuh oder Feigenblatt?', *Wirtschaft und Wettbewerb* 2009/6, p. 606.
15. Commission Communication – The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis, *OJ* 2008, C 270/8.
16. Commission Communication – The recapitalization of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition, *OJ* 2009, C10/2.
17. Commission Communication on the treatment of impaired assets in the Community Banking Sector, *OJ* 2009, C 72/1.

own view, the R & R Guidelines and the crisis framework complement each other; the R & R Guidelines are therefore not entirely set aside.[18]

The European economy is currently in the *third phase*, where the Commission examines whether all the Member States' measures (insofar they have not yet been definitely approved) were proportionate. The emphasis is now on finding long term solutions regarding impaired assets. The Commission has launched formal investigation procedures with regard to several banks.[19] A fourth communication of 22 July (the 'Restructuring Communication')[20] elucidates how restructuring plans should be devised in order to strike the right balance between achieving a bank's long term viability and the prevention of undue distortions of competition.

4. Summary of the Crisis Framework[21]

The Commission pursues, just like under the R & R Guidelines, to maintain a level playing field[22] and tries to prevent subsidy races between Member States.[23] Therefore, crisis State aid must be appropriate, indispensable and proportionate to fulfil the objective pursued.

The *Banking Communication* of October 2003 focuses on guarantees and guarantee schemes covering liabilities. It lays down principles for other crisis instruments (recapitalisation, asset relief and winding up) that would later be covered by the three remaining Communications.[24] There should be a non-discriminatory access to aid and the eligibility criteria must be objective as well.[25] The Commission also states that State support must be limited in time and scope, that there should be an adequate contribution from the private sector and that both behavioural restrictions (for example, no advertising that bank received aid) and structural adjustments (such as divestitures) are required to minimize competitive distortions.

The *Recapitalisation Communication* of December 2008 sets outs that three different objectives can be used to invoke Article 87(3)(b) EC: restoration of financial stability, ensuring lending to the real economy and preventing insolvency.[26] It specifies that the measures should be reviewed after six months.

The main aim of the *Impaired Assets Commission* of February 2009 is to ensure a level playing field through a co-ordinated Community approach concerning certain aspects of asset relief.[27] This Communication seeks to remove uncertainty as to the size of the losses from impaired assets transferred to governments. Those assets mostly concerned American overrated mortgage portfolios. To that effect, a valuation methodology at Community level will have to be established.[28]

The *Restructuring Communication* primarily sets out how Member States should devise restructuring plans. Financial stability is still the prime objective, but the Commission tries to preserve the level playing field by demanding compensatory measures and appropriate burden sharing.[29] In sum, this Communication lays out the measures needed to ensure a smooth return to financial stability.

5. Main Features of the Crisis Framework

5.1. *Scope*

The scope of the crisis framework is limited to the financial sector because other sectors do not have such an immediate impact on the (real) economy.[30] Some banks are too big to fail. Initially, it seemed unclear whether Article 87(3)(b) EC (and hence, the crisis framework) could also be applied to non-systemic banks.[31] It seemed logical to apply a narrow approach because there has to be a link between the disturbance of Member State's economy and the distressed bank.[32] However, the Commission found it arbitrary to allow the application of Article 87(3)(b) EC 'in case Member States were taking action as regards the entire sector or big systemic

18. This is explicitly acknowledged in point 10, 42 and 49 of the Banking Communication and point 44 of the Recapitalisation Communication, whereas the Impaired Assets Communication only indirectly refers to the R & R Guidelines in point 49.
19. Commission Decisions C 15/2009 (*Hypo Real Estate*) of 07.05.2009; C 11/2009 (*Fortis Bank*) C 124/19; C-10/2009 (*ING*) of 31.03.2009; C 16/2009 (*Bayern Landesbank*) of 30.04.2008; C 18/2009 (*KBC*) of 30.06.2009 and C 17/2009 (*West Landesbank*) of 30.06.2009.
20. Commission Communication on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid, *OJ* 2009 C 195/9.
21. Again we limit ourselves to the measures concerning aid to the financial sector. The Commission has also temporarily relaxed a number of its general state aid instruments, to help 'the real economy'. See the Communication published in *OJ* 2009, C 83/1.
22. Again, this is corroborated by the Communications; see the Recapitalisation Communication point 8, the Impaired Assets Communication point 37 and the Restructuring Communication, point 2.
23. See also the Recapitalisation Communication points 8, 11, 16, 19, 35 (footnote 2), the Impaired Assets Communication, points 4 and 36 (footnote 19), the Restructuring Communication, points 2 and 29 and the Temporary Framework point 1.1, 3rd paragraph. The term 'level playing field' is not mentioned in the Banking Communication.
24. Recapitalisation measures are dealt with in chapter 4 and asset relief is briefly broached in point 40 of the Banking Communication. Asset relief is to be understood as clearing the balance sheet of a bank from assets whose value has greatly diminished or cannot be estimated. The rationale behind this is to restore confidence in inter-banking lending by rendering a bank's financial status more transparent.
25. Point 16 and 18 of the Banking Communication.
26. Points 4-6 of the Recapitalisation Communication.
27. Point 13 of the Impaired Assets Communication.
28. *Ibid* point 37. However, this assessment seems extremely difficult. The Commission has submitted an invitation to tender in order to assist the Commission in the assessment of asset relief measures as well as the refinement and development of the valuation principles and to provide training to Commission officials in relation to topics within his field of expertise. See COMP/2009/D5/014.
29. *Ibid* point 29.
30. Point 11 of the Banking Communication.
31. B.J. Drijber, 'Mededingingsrecht als luxeprobleem', *Markt & Mededinging* 2008/5, p. 412. The Ecofin Council stated that it agreed to support systemic financial institutions. See press release of the Council of 07.10.2008, p. 6. The Banking Communication stated rather vaguely (point 5) that its purpose was to 'provide guidance on the criteria relevant for the compatibility with the Treaty of general schemes as well as individual cases of application of such schemes and ad hoc cases of systemic relevance.'
32. R. Luja, 'State Aid and the Financial Crisis: Overview of the Crisis Framework', *European State Aid Law Quarterly* 2009/2, p. 145-160, p. 147.

banks, while smaller banks would still need to revert to Article 87(3)(c) [EC]'.[33]
The Impaired Assets Communication is not limited to toxic assets but covers the wider notion of 'illiquid assets'.[34] Those various concepts are not anywhere precisely defined. It is up to the Member States to decide which categories of assets will be relieved. However, the wider the scope of the asset relief, the deeper the commitments and restructuring measures will have to be.[35]

5.2. *Temporality*

The crisis framework only creates a temporal derogation to the normal R & R State aid regime because a medium/long-term goal is the return to normal market conditions.[36] Member States are under the obligation to review their measures (general and individual) at least every six months.[37] Access to asset relief schemes should in principle only be open within a six-month time window in order to accelerate the recovery of the financial market. Member States should also devise a cut-off date for assets that entered the balance sheet at a certain point in time, prior to the announcement of the relief programme. This will reduce the risk of banks engaging in irresponsible investments and thus preventing moral hazard. That does not alter the fact that the restructuring period may last for a longer period than the maximum under the R & R Guidelines (five instead of three years).[38]

5.3. *Healthy and Distressed Banks*

Concerning the financial soundness of financial institutions, the Commission distinguishes between illiquid but otherwise well-run banks, and banks with endogenous problems (also called 'fundamentally unsound banks'). These will be required to substantially restructure their business and offer compensatory measures in order to limit distortions of competition.[39]
The Impaired Assets Communication however dropped the distinction between fundamentally sound banks and distressed banks, because this label was putting too much of a stigma on presumed 'unsound banks'.[40] While it rightly abandoned the distinction between 'fundamentally sound' and 'fundamentally unsound', the Commission still may use as counterfactual (what would have been the situation had the aid not been granted?) the presumption that a bank would have gone bankrupt. Such a counterfactual will determine to an important extent the 'depth' of the restructuring required.

5.4. *Private Sector Contributions*

In line with the R & R Guidelines, the Commission expects a serious contribution from the bank and its shareholders to keep the aid amount to the minimum, whether the measure consists of a guarantee or of a recapitalisation measure. This is first and foremost expressed in a remuneration amount that comes as close as possible to the market price, or – in the absence thereof – what could be considered a market price.[41]
An additional contribution should take place and a restructuring plan or a liquidation plan must be notified in case a State guarantee is activated. Moreover, the Commission demands a significant participation (i.e. more than 30%, but less than the 50% applied under the R & R Guidelines) of private investors to offset distortions of competition.[42]
The same holds true for asset relief. The starting point is that banks should bear the losses incurred by impaired assets themselves and remuneration should also take place upfront. Claw-back clauses could be a means to ensure payment at the earliest moment possible, in case banks are not able to remunerate *ex ante*. However, later payment should lead to a higher contribution of the bank and its shareholders. No fixed burden-sharing thresholds are applied, as the Restructuring Communication makes clear.

5.5. *Exit Strategies*

A very important feature of the crisis framework is the requirement of exit strategies for Member States, which should encourage a swift return to normal market conditions. Therefore, an add-on on top of the initial remuneration paid to the State, an increase over time of the remuneration, an increase through call-options or a restrictive dividend policy could be considered by the Member States as an additional incentive for banks to repurchase their shares.[43]

5.6. *Compensatory Measures*

Compensatory measures are essentially synonymous for restructuring measures. Restructuring is the price a bank pays in order to compensate for the aid it received. Compensation is needed to ensure that the aid is proportionate. There is a clear link between burden sharing and compensatory measures.

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33. See Report from the Commission, State Aid Scoreboard – Spring 2009 Update – Special Edition on State Aid Interventions in the Current Financial and Economic Crisis from 08 April 2009 COM/2009/164), p. 10. For example, the Roskilde Bank, the 8th largest bank of Denmark, was recognized as a systemic bank.
34. A too narrow approach could be insufficient to restore market confidence. Point 32 of the Impaired Assets Communication.
35. *Ibid*, point 36.
36. This is in compliance with the Council conclusions of 07.10.2008, p. 7. See the Banking Communication, points 12, 24, 28-29 and 35, the Recapitalisation Communication points 10, 20, 31-34 (within this framework the temporality is expressed by sufficient exit incentives) and the Impaired Assets Communication, point 53 (here, temporality is expressed by the return to long-term viability, which implies that banks can survive without any state support). As regards the temporal scope of the Restructuring Communication it has to be noted that it is only valid until 31.12.2010.
37. This is called a viability review. See the Banking Communication, point 24, the Recapitalisation Communication, point 40, the Impaired Assets Communication, annex V and the Restructuring Communication, point 8.
38. Point 15 of the Restructuring Communication.
39. See points 14, 33, 35 of the Banking Communication. Thus, this approach applies to guarantee as well as recapitalisation measures. Hall mentions that most of the schemes target at healthy banks, see Hall 2009, p. 5. The Recapitalisation Communication adds that the Commission will only clear the recapitalisation of a distressed bank provided this bank will either undergo an in-depth restructuring under the R & R Guidelines or will be winded up. See point 44.
40. Point 17 of the Impaired Assets Communication states that the Communication equally applies to all banks irrespective of their individual situation.
41. Points 25-26 and 38-39 of the Banking Communication. Again this principle applies to guarantees and recapitalisations.
42. Points 19 and 21 of the Recapitalisation Communication.
43. Points 31-34 of the Impaired Assets Communication.

Indeed, the lower the remuneration paid to the State, the higher the compensation has to be.
The Restructuring Communication gives strict guidance as to how a restructuring plan should be structured. A comparison with different options like a break-up or absorption by a third party is required. In addition, the planned restructuring results have to be tested under a worst case and a base case scenario.[44] This will enable the Commission to assess the proportionality of the measure.
Structural measures like divestment of business branches could be required, depending on the level of distortion that is brought about by the relief. Factors that determine the compensatory measures' scope are: total aid amount, volume of impaired assets benefiting from the measure, proportion of losses resulting from the asset, general soundness of the bank, risk profile of the relieved assets, quality of risk management, solvency ratio levels in the absence of aid, market position of the beneficiary and distortions of competition from the bank's continued market activities including in its 'domestic market' and impact of the aid on the structure of the banking sector.[45]
In comparison to the R & R Guidelines, the rules on restructuring under the crisis are in some respects more flexible. Yet, 'in-depth restructuring' is systematically required for banks which would have gone bankrupt without the aid *and* for banks that received asset relief that equals more than 2% of their total risk weighted assets.[46]

5.7. *Behavioural Remedies*

A prominent feature is the use of behavioural obligations, e.g.: no acquisitions in certain business areas for a number of years, no 'price leadership', no advertising with State aid, and in particular not with government shareholding.[47] It is submitted that such measures should not go so far as to hamper competition. The Impaired Assets Communication also identifies behavioural safeguards,[48] that may take the form of compulsory credit provisions financed by the capital effect of the relief, or a restriction on dividend policy and a cap on executive remuneration.[49] This is indeed the kind of measures the Commission imposed amongst others in its decision on the capital injection to *ING*.[50]

6. Two examples: *Fortis* and *ING*

6.1. *Fortis*

The Dutch State purchased *Fortis Bank Nederland* ('*FBN*'), it provided to FBN a credit facility and it purchased long-term loans. Subsequently, the State bought the activities of ABN AMRO that were controlled by *FBN*.[51] The Commission found that the first measure did not constitute State aid to *FBN*, but the other three did. The second and third measures were assessed under the Banking Communication, whereas the fourth measure was assessed under the Recapitalisation Communication. Although the second and the third measure were appropriate to address the crisis, they were not proportionate, as the Netherlands asked a fee amount that was lower than the amount recommended by the European Central Bank. In addition, neither a time-window for drawing loans nor a fixed end date was envisaged nor had any of the behavioural safeguards mentioned in the Banking Communication been implemented.
Concerning the fourth measure, the risk-profile of *FBN* could not be assessed because the Dutch authorities were said to have not provided sufficient information. Therefore, the question whether *FBN* was a healthy or a distressed bank could not be answered. In any case, the Recapitalisation Communication required a viability/restructuring plan, which had not been submitted in time. Precisely in order to restore and preserve viability, the Dutch government intends to merge ABN AMRO and *FBN*. This intention gave rise to a clash with Commissioner Kroes who insists on a correct implementation of the remedies linked to the approval of the take-over of parts of ABN AMRO by *FBN* that took place back in October 2007. Otherwise the Commission is unwilling to accept the integration of the two banks, in spite of ABN AMRO and *FBN* having become much smaller players on the market. As long as no solution has been found the Commission will 'withhold' a final state aid decision.

6.2. *ING*

ING received an increase in core tier 1 capital of € 10 billion in 'virtual equity' in October 2008 and an illiquid assets back-up facility (IABF) for its Alt-A portfolios in February 2009. The first measure was approved for six months in a 'non-objection decision', in which the Commission 'took note' of a series of behavioural remedies.[52] The Dutch authorities got six months to present a 'credible' viability plan. The legal basis for the approval was Article 87(3)(b) EC.
The second measure triggered a formal investigation procedure.[53] The Commission does not investigate the entire measure in depth, but only the valuation of the Alt-A assets and the corollary thereof, the burden sharing. In its decision opening the formal procedure, the Commission emphasised that '[t]he main aim of valuation is to establish the real economic value, given that this value represents the benchmark level in that a transfer of impaired assets and at this value indicates compatibility of aid ensuring the relief effect by exceeding current market value but keeping the aid amount to the minimum necessary.'[54] The Commission was of the preliminary view that the independent expert, who had been commissi-

44. *Ibid*, point 13.
45. Point 59 of the Impaired Assets Communication.
46. Points 54-55 of the Impaired Assets Communication.
47. Points 27 and 38 of the Banking Communication. See also the decisions in *Commerzbank* (Case N 244/2009) and *Fortis* (footnote 53).
48. Point 9 of the Impaired Assets Communication.
49. *Ibid* points 30-31. The cap on bonuses is obviously part of a wider discussion.
50. Formally the Commission only took note of these commitments measures, since Article 4(3) of Regulation 659/1999 has no legal basis for transforming such commitments into formal conditions.
51. Commission Decision C 11/09 (*Fortis Bank Nederland*), *OJ* 2009, C 124/19.
52. Commission Decision N 528/2008 (*ING*), *OJ* 2008, C 328/9.
53. Commission Decision C 10/2009 (*ING*), *OJ* 2009, C 158/13.
54. *Ibid*, point 63.

oned by the Dutch authorities to assess the value of the assets, had been overly optimistic about the prospects of the loans.[55] In any event, the Commission found that it had not been given all the information it needs to verify that the estimation was correct. Despite these perceived shortcomings, the Commission approved the aid for six months because the measure complied with a number of conditions of the Impaired Assets Communication and with due considerations for the need to preserve financial stability. Again the legal basis for this was Article 87(3)(b) EC. This temporary authorization was recently renewed for another six months.[56]

In the meantime, there have been discussions between the Commission on the one hand and the Netherlands, *ING* and the Dutch Central Bank on the other hand about the required compensatory measures. The viability plan required under the first decision on the recapitalisation has become part of the requirement to present a restructuring plan under the second decision. Indeed, although *ING* is considered by the Netherlands as a fundamentally sound institution (the problems it encountered stemmed from its American portfolios) it got government support twice and the IABF transaction involves more than 2% of the total risk weighted assets.

7. Some miscellaneous questions

In spite of the communications many uncertainties are still surrounding the assessment of individual cases under the crisis framework. This may be unavoidable for a set of specific rules that must also fit into the general legal framework of the EC Treaty. In this section we will briefly discuss some of these questions.

First, it is not entirely certain that the Court of First Instance would accept the interpretation given of Article 87(3)(b) EC. There are no precedents of cases in which this provision was applied this way, for the simple reason that this crisis is unprecedented. The exceptional circumstances in a way forced the Commission to 'reinvent the law'. It cannot be entirely excluded that, in a case brought by an affected third party, the Court will be *'plus communautaire que la Commission'* and annul a positive decision based on Article 87(3)(b) EC.

Secondly, the exact relation between the R & R Guidelines and the specific communications remains troublesome. There is a tension between the 'logic' behind the application of Article 87(3)(b) EC and the more traditional approach underlying the R & R Guidelines. Article 87(3)(b) EC is predominantly used for aid to intrinsically healthy banks that are faced with unexpected and exogenous difficulties, whereas the R & R Guidelines are principally meant to be applied to structurally unsound companies having endogenous difficulties. Although the Commission acknowledges that there is a difference between section (b) and (c) of Article 87(3) EC, the crisis framework deviates only marginally from the R & R Guidelines.

By the same token, one may wonder how the Commission exactly applies the proportionality test, in other words how it assesses the size of the structural measures that are needed to remove distortions of competition allegedly caused by a state aid. It is far from easy to establish such distortions. In practice, the Commission simply presumes a distortion once it finds a financial advantage, without making any attempt to quantify the distortion in economic terms. When applying Article 87(3)(b) EC the Commission may arguably be required to identify the amount of aid necessary to remedy the market failures resulting from the financial crisis. If the aid does not exceed that amount, it is questionable whether structural compensatory measures are needed at all.

Thirdly, it is unclear how far the Commission can go in asking structural remedies. If the yardstick is a return to a situation of undistorted competition, on what basis would the Commission decide what assets must be sold? Initially, the Commission seems to have favoured divestments in other Member States, which is somewhat surprising from an internal market perspective. Subsequently, it started asking banks to cut deeply into their domestic operations. It is submitted that the Commission should give reasons why it holds that specific restructuring measures are needed to restore a situation of undistorted competition. Restructuring demands should in our view not be used as a policy tool for reshaping the banking landscape. In any event, after having implemented all restructuring measures, a bank must still have sufficient flesh on the bones. If precisely the most viable and profitable parts were to be sold, restructuring might have the opposite effect of returning to long-term viability.

8. Final observations

The Commission may be given a large amount of credit for the expedient way in which it handled highly complex transactions and for the clarity it has sought to bring through its various communications. It has shown that also in exceptional circumstances it knows how to play its part on the institutional scene, while accepting that a crisis situation raises exceptional problems that call for adapted solutions. We have also observed that uncertainties remain, in particular how the Commission in the current phase of the crisis construes the causal link between the distortions it perceives and the restructuring it requires. As regards sound financial institutions in an unsound market, the Commission should continue to apply Article 87(3)(b) EC, rather than slip back to the old approach of the R & R Guidelines for aid to unsound companies in sound markets.

So far the Commission's 'credit crisis law' has not been tested in court. Apparently, only very few third parties submit observations following the opening of formal investigation procedures. Competitors may be afraid that tomorrow it will be their turn: *'Hodie tibi, cras mihi'*. If the Commission were to adopt a negative decision, an appeal is however likely to follow.

We conclude with a somewhat more political observation. As we all know, the prime cause of the crisis was the devaluation of US mortgage portfolios, in which European banks would probably not have invested so massively had they not been

55. Its decision does not reveal whether it disposes itself of an alternative and more convincing valuation, taking due account of the 'upside' of the transaction for the Dutch State.
56. Decision of 15 September 2009. The Commission claimed that it still has not received sufficient information and expressed 'additional doubts' as regards the valuation of the asset relief.

under a statutory duty to invest American savings into American instruments. In the US, the bursting of the housing bubble has led the government to create the Troubled Asset Relief Program under which financial institutions could access up to $ 700 billion in funds. Unlike their EU counterparts, American beneficiaries of federal government support would not appear to have to undergo any form of restructuring. What is more, there is in principle nothing under EU competition law to stop Citibank (to name just one financial institution that has received US government support) from acquiring substantial assets from an EU bank forced to divest, whereas that same EU bank is not allowed to do substantial acquisitions in the near future, not even in the US. Designed to prevent 'financial competition' between EU Member States, the EU state aid rules will therefore act as a straightjacket, weakening the market position of some of the largest EU banks at a global level.