EUROPEAN COMMISSION

Brussels, 28.06.2010
C(2010)4402 final

Subject: State Aid N 257/2010 – Denmark
Third extension of the Danish guarantee scheme on new debt

Madam,

I. PROCEDURE

1. On 23 January 2009 Denmark notified a guarantee scheme (hereafter "the scheme"), which was approved by Commission decision of 3 February 2009 in State aid case N 31a/2009 (hereinafter "the original decision")[1]. On 10 July 2009 the Danish authorities notified a request to extend the scheme, which was approved on 17 August 2009 in State aid case N 415/2009[2]. On 15 January 2010 Denmark notified the Commission a further request to extend the scheme, which was approved on 1 February 2010 in State aid case N 20/2010[3].

2. After preliminary exchange of information between the Commission and the Danish authorities, on 17 June 2010 Denmark notified a third extension of the scheme for additional six months from 1 July 2010 until 31 December 2010. Denmark accepts exceptionally that the decision is adopted in the English language.

3. The request for extension regarding the guarantee scheme does not relate to the general State guarantee authorised by the Commission on 10 October 2009 in State aid case NN51/2008[4].

II. DESCRIPTION

[1] OJ C 50, 3.2.2009, p. 3.
[2] OJ C 227, 22.9.2009, p. 2.
[3] OJ C 57/3, 9.3.2010, p. 3.
[4] OJ C 273, 28.10.2008, p. 2.

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1. The objective of the scheme

4. In response to the ongoing exceptional turbulence in global financial markets, Denmark brought forward a guarantee scheme for credit institutions, designed to restore the stability of the financial system and to remedy a serious disturbance to the Danish economy. In particular, the scheme aimed at restoring confidence and encouraging interbank lending through the granting of State guarantees to new short- and medium-term debt issuance.

2. Description of the original scheme

5. Institutions eligible to participate in the scheme are credit institutions (i.e. banks and mortgage credit institutions) fulfilling the solvency requirements fixed by the Danish Financial Supervisory Authority (hereinafter the FSA).

6. Debt instruments that can be guaranteed under the scheme are all newly issued short- and medium-term loans, including commercial papers, senior unsecured bonds, supplementary securitized capital covered bonds, and new loans covering existing debts. Subordinated debt falls outside the scope of the scheme. The duration of the guarantee depends on the underlying loan's maturity, but in any case is not longer than three years.

7. The beneficiary must pay a fee on the guarantee based on the Recommendations of the European Central Bank[5].

8. Denmark confirms that the overall maximum budget of the scheme is DKK 600 billion (EUR 80 billion).

3. The continued necessity of the scheme

3.1. Operation of the scheme to date

9. According to the notification and the six-monthly reports on the use of the scheme, 32 banks had applied for an agreement in principle to benefit from the State guarantee under the scheme for a total amount of approximately DKK 262 billion (EUR 35.3 billion). Of these, 25 have effectively used the scheme by issuing guaranteed bonds for a total amount of approximately DKK 106 billion (EUR 14.3 billion).[6]

3.2. Extension of the scheme

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[5] Recommendations on Government Guarantees on Bank Debt of the European Central Bank of 20 October 2008.

[6] Danske Bank A/S has issued bonds amounting to approximately EUR 5.3 billion, FIH Erhvervsbank – EUR 3.6 billion, BRFkredit A/S – 1.1 billion, Vestjysk Bank A/S – 0.7 billion, Spar Nord Bank A/S – EUR 0.6 billion, Sparekassen Sjaelland – EUR 0.4 billion, Eik Banki P/F, Arbejdernes Landsbank A/S, P/F BankNordik, Den Jyke Sparekasse, Max Bank A/S - EUR 0.3 billion each, Sparekassen Himmerland A/S, Skjern Bank A/S, Sparekassen Vendsyssels, Ostjydsk Bank A/S - EUR 0.2 billion each, Aarhus Lokalbank A/S, Diba Bank A/S, Sparekassen Farso, Sparekassen Ostjylland A/S - EUR 0.1 billion each, Sparekassen. Tonder Bank A/S, Vordingborg Bank A/S - EUR 0.04 billion each, Hvetbo A/S - 0.03 billion, Vorbasse-Hejnsvig Sparekasse, Dronninglund Sparekasse - EUR 0.02 billion each, Basisbank A/S - EUR 0.01 billion.

10. The Danish authorities are planning to extend the window for issuing debt instruments under the scheme until 31 December 2010.

11. Denmark introduces amendments to the extended scheme concerning pricing conditions (an increase in the guarantee fee), viability review requirements and an additional reporting obligation, which are in line with the updated compatibility conditions for the renewal of guarantee schemes[7]. All other conditions of the original scheme remain unchanged.

III. POSITION OF DENMARK

12. The Danish authorities are of the opinion that the guarantee scheme provides important support to the credit institutions and it is a useful tool in the transition period to more normal market conditions. Denmark points out that the normalisation of the Danish money market is still lagging behind that of the euro money market and the banks' access to market funding is still affected by the crisis.

13. In its letter dated 31 May 2010 the Danish Central Bank states that the availability of the guarantee scheme is still required. The Danish Central Bank acknowledges that overall the banking sector has improved its liquidity situation over the past year. However it considers it important that the credit institutions continue to have the opportunity to apply for individual State guarantees until the end of 2010.

14. In addition, Denmark commits to charge beneficiary banks a guarantee fee that is higher than under the pricing formula recommended by the ECB in October 2008 at least by:
    - 20 basis points for banks with a rating of A+ or A[8],
    - 30 basis points for banks rated A-[9], and
    - 40 basis points for banks rated below A-. Banks without rating will be considered to belong to the category of banks with a BBB rating.[10]

15. Denmark also undertakes to present a viability review for every bank that is granted guarantees on new or renewed liabilities as from 1 July 2010 and for which at the time of the granting of new guarantees the total outstanding guaranteed liabilities (including guarantees accorded before 1 July 2010) exceed both a ratio of 5% of total liabilities and the total amount of EUR 500 million[11]. The viability review will be communicated to the Commission within three months of the granting of guarantees and will comply with the principles set out in the Restructuring Communication[12]. In particular, it will cover the solidity of the funding capacity of the bank concerned; where necessary and in any event where requested by the Commission in case of doubt, a liquidity stress test will be carried out. No separate viability review has to be presented for banks that are already in restructuring or

7 http://ec.europa.eu/competition/state_aid/studies_reports/phase_out_bank_guarantees.pdf

8 Or A1 and A2 depending on the rating system employed.

9 Or A3 depending on the rating system employed.

10 In the case of divergent assessments by different rating agencies the relevant rating for the calculation of the fee increase should be the higher rating. The material time for the rating in the determination of the guarantee fee is the day on which the guarantee is granted in relation to a specific bond issuance by the beneficiary.

11 Currently it corresponds to approx. DKK 3.7 billion.

12 The 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 rules, OJ C 195, 19.8.2009, p. 9.

obliged to present a restructuring plan or subject to a pending viability review at the time new guarantees are granted.

16. In addition to the existing commitments concerning reporting obligations, Denmark undertakes to submit to the Commission a concise mid-term review on the operation of the support scheme by 15 October 2010 at the latest.

17. Denmark undertakes to maintain the commitments made since the introduction of the support scheme and confirms that all other conditions as defined by the original decision remain unchanged.

IV. ASSESSMENT

18. In its decision of 3 February 2009, the Commission concluded that the support scheme constitutes State aid within the meaning of Article 107(1) TFEU. However, it found that the measures were compatible with the internal market under Article 107(3)(b) TFEU, because they were apt to remedy a serious distortion of the Denmark economy. To this end, the Commission had assessed the appropriateness, necessity and proportionality of the measure.

19. The Commission observes that the extension of the scheme is a response to the continuing financial difficulties that Denmark, as most Member States, continues to experience. Since the objective of the measure is to provide short- and medium-term financing to financial institutions which are unable to obtain funds on the financial markets, it is important to ensure the availability of the guarantee scheme as long as the global financial crisis continues.

20. Although access to funding for banks has gradually improved in most funding markets over the past year and is no longer a systematic and generalized problem, markets have not yet fully returned to entirely normal functioning. Against this background and taking into account the residual fragility of recovery process and the possibility of setbacks in that process, the continuation of a support scheme can be deemed necessary to ensure financial stability as confirmed by the letter from the Danish Central Bank and the Ministry of economic and business affairs. The Commission therefore considers that the extension of the scheme for a further six months is appropriate and necessary to remedy a disturbance of the Danish economy.

21. On the basis of the above, the notified extension of the support scheme does not alter the Commission's previous assessment in the decision of 3 February 2009 and the extension decisions of 17 August 2009 and 1 February 2010.

22. As regards the specific features of the guarantee scheme, in assessing the request for the extension the Commission has to balance its positive effects for financial stability with the distortions of competition and the delay in the return to a normal functioning of the financial markets that the extension entails. Guarantee schemes should contain minimum exit incentives, and a gradual alignment to market conditions should take place in order to minimise negative spill-over effects on competitors and other Member States.

23. The gradual stabilisation of the market situation and the resulting reduction of the risk premium for unguaranteed debt have brought about a first step towards an

alignment with market conditions, whilst providing an exit incentive for the sounder institutions. Lower-rated banks for which bond issuances with a government guarantee still hold considerable economic benefits have become the prime users of guarantee schemes.

24. It is necessary to minimise distortions across banks in the internal market and avoid the risk of State aid dependence. There should therefore be an adjustment of the terms on which banks may retain for the time being the possibility of accessing government guarantees schemes.

25. On the basis of these considerations, the prerequisites for the compatibility of guarantee schemes with Article 107(3)(b) TFEU that have been established by the Banking Communication[13] and the Commission's subsequent decisional practice continue to apply but need to be complemented by requirements aimed at achieving two objectives.

26. First, banks should be incentivised to scale down or terminate their recourse to government guarantees by means of pricing rules that bring the funding costs of beneficiary banks closer to market conditions and thereby reduce distortions of competition. This should be achieved by an increase in the guarantee fee[14] in comparison with the ECB recommendations of October 2008 that amounts at least to 20 basis points for banks with a rating of A+ or A[15], 30 basis points for banks rated A-[16], and 40 basis points for banks rated below A-[17].

27. Second, the use of guarantee schemes should not enable banks with structural weaknesses in their business models to postpone or avoid the necessary adjustments. To this end, the Member State concerned should present a viability review for any bank that requests new guarantees under a scheme which take or keep the total amount of the bank's outstanding guaranteed liabilities above 5% of the bank's total liabilities and above the absolute amount of EUR 500 million[18]. The viability review should be presented on the basis of the parameters established in the Restructuring Communication within three months of the granting of the guarantees[19]. The viability review will either confirm the bank's long-term viability without State support or show that farther-reaching restructuring is required.

28. The Commission considers that the notified extension until 31 December 2010 of the State guarantee scheme complies with the requirements set out above and is compatible with the internal market. In particular, the Commission notes positively that the Danish authorities have brought the original scheme fully in line with these requirements and provided commitments concerning new pricing conditions (an increase in the guarantee fee) and viability review requirements (see point 14 and 15 above).

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13 Communication from the Commission - 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.

14 For liabilities of all eligible maturities.

15 Or A1 and A2, depending on the rating system employed.

16 Or A3, depending on the rating system employed.

17 Banks without rating will be considered as having a BBB rating.

18 See footnote 10.

19 Except where the bank concerned is already in restructuring or subject a pending viability review on the basis of a restructuring or viability plan; in those circumstances the award of additional State aid will be assessed within the framework of the ongoing restructuring/viability review process.

29. As regards the combination of this guarantee scheme with other aid measures, as indicated in the Annex to the Restructuring Communication, any restructuring plan should contain all State aid received as individual aid or under a scheme during the restructuring period and all such aid needs to be justified as satisfying all criteria prescribed by the Restructuring Communication (i.e. return to viability, own contribution by the beneficiary and limitation of competition distortion). Accordingly, once a Member State is under an obligation to submit a restructuring plan for a certain aid beneficiary, the Commission needs to take a view in its final decision as to whether any aid granted during the restructuring period satisfies the criteria required for the authorisation of restructuring aid. To this end an individual *ex ante* notification is necessary.

30. Furthermore, the Commission recalls that based on point 16 of the Restructuring Communication, if aid not initially foreseen in a notified restructuring plan is necessary for the restoration of viability, this additional aid cannot be granted under an approved scheme but needs to be subject to individual ex ante notification and any such further aid will be taken into account in the Commission's final decision on that bank.

31. In addition to the above, Denmark agrees to provide the Commission with a concise mid-term review of the operation of the scheme by 15 October 2010 in addition to the pre-existing reporting requirements and to complement its future reports on the operation of the scheme with updated available data on the cost of comparable (nature, volume, rating, currency, etc.) non-guaranteed and guaranteed debt issuances. This will allow the Commission to assess the appropriateness, necessity and proportionality of possible further extension of the scheme beyond 31 December 2010 and the conditions for such extensions. Any further extension will require the Commission's approval and will have to be based on a review of the developments in financial markets and the scheme's effectiveness.

V. DECISION

The Commission concludes that the extension of the scheme until 31 December 2010 does not alter its previous assessment in the original decision of 3 February 2009 (State aid case N 31a/2009) and subsequent extension decisions of 17 August 2009 (State aid case N 415/2009) and 1 February 2010 (State aid case N 20/2010) that the measures under the scheme are compatible with the internal market. Therefore, since it fulfils the conditions to be considered compatible with internal market under Article 107(3)(b) TFEU the Commission has decided not to raise objections. The Commission notes that Denmark accepts exceptionally the adoption of the decision in the English language.

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Yours faithfully,

For the Commission

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