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C(2013) 5036 final

<p>In the published version of this decision, some information has been omitted, pursuant to articles 24 and 25 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus [...].</p>		<p style="text-align: center;">PUBLIC VERSION</p> <p>This document is made available for information purposes only.</p>
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**Subject: State Aid SA.36869 (2013/N) – Portugal
Prolongation of the Portuguese guarantee scheme for credit institutions
H2 2013**

Sir,

I. PROCEDURE

1. By decision of 29 October 2008 in case NN 60/2008¹ ("the original decision") the Commission raised no objection against the granting of State aid until 31 December 2009, on the basis of the Portuguese Guarantee Scheme ("the scheme").
2. On the basis of subsequent notifications, the Commission approved the prolongation of the scheme in its decisions of 22 February 2010 in State aid case N 51/2010², 23 July 2010 in State aid case N 315/2010³, 21 January 2011 in State aid case SA.32158⁴, 30 June 2011 in State aid case SA. 33178⁵, on 21 December

¹ Commission Decision of 29 October 2008 – State aid NN60/2008, OJ C 9, 14.01.2009 and Corrigendum, OJ C 25, 31.01.2009.

² Commission Decision of 22 February 2010 – State aid N51/2010, OJ C 96, 16.04.2010.

³ Commission Decision of 23 July 2010 – State aid N315/2010, OJ C 283, 20.10.2010.

⁴ Commission Decision of 21 January 2011 – State aid SA.32158, OJ C 111, 9.4.2011.

⁵ Commission Decision of 30 June 2011 – State aid SA.33178, OJ C 344, 24.11.2011.

S. Ex.^a o Ministro dos Negócios Estrangeiros
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2011 in State aid case SA. 34034⁶, 27 June 2012 in State aid case SA.34958⁷ and on 17 December 2012 in State aid case SA.35743⁸.

3. On 1 July 2013, Portugal notified an eighth extension of the scheme until 31 December 2013. Further information was provided by exchange of electronic mails on 19 June and 1, 4 and 23 July 2013.
4. For reasons of urgency, the Portuguese authorities exceptionally accept that the Commission decision be adopted in the English language.

II. FACTS

II.1. Description of the scheme

Legal basis and budget

5. To stabilise the financial market, Portugal passed law 60-A/2008 of 20 October 2008⁹ and its implementing provisions, *Portaria* n° 1219-A/2008 of 23 October 2008¹⁰, *Portaria* n° 946/2010 of 22 September 2010¹¹ and *Portaria* n° 80/2012 of 27 March 2012¹².
6. The total budget of the prolonged scheme is EUR 24.12 billion¹³.

Objective of the Guarantee Scheme

7. In response to the ongoing exceptional turbulence in the global financial markets, Portugal brought forward a measure designed to preserve the stability of the financial system and to restore the confidence in the economy. In particular, the scheme aims to support the access to liquidity of solvent credit institutions in Portugal in the context of the financial crisis.

Description of the Guarantee Scheme

8. The beneficiaries of the scheme are all credit institutions incorporated in Portugal, including subsidiaries of foreign banks with registered office in Portugal. Only institutions which are solvent for the purposes of Portuguese law may benefit from the scheme.
9. Under the approved *Portaria* n° 80/2012, the scheme covers the issuance of non-subordinated debt with a minimum maturity of three months and a maximum maturity up to five years. In case of guarantees on the issuance of covered bonds (on mortgages and on the public sector), the maturity can go up to seven years.
10. The remuneration for guarantees on liabilities will be calculated in accordance with the formula set out in the 2011 Prolongation Communication¹⁴, and as described in

⁶ Commission Decision of 21 December 2011 - State aid SA.34034, OJ C 99, 03.04.2012.

⁷ Commission Decision of 27 June 2012 - State aid SA.34958, OJ C 246, 15.8.2012.

⁸ Commission Decision of 17 December 2012 – State aid SA.35743, OJ C 36, 17.12.2013.

⁹ Diário da República, 1.ª série, n.º 203.

¹⁰ Diário da República, 1.ª série, n.º 206

¹¹ Diário da República, 1.ª série, n.º 185.

¹² Diário da República, 1.ª série, n.º 62.

¹³ Article 134(2) of the 2013 Portuguese State Budget.

the Commission Decision in State aid case SA.34958¹⁵. The indicative guarantee fees for the period 1 August 2013 to 31 December 2013 can be found in Annex II and are based on an updated sample of European banks established by the Commission on 15 May 2013.

11. A detailed description of the scheme has been provided in recitals 5 to 21 of the original decision.

Operation of the Guarantee Scheme up to 21 April 2013

12. The Portuguese authorities submitted a report on the operation of the scheme on 1 July 2013. As of 21 April 2013, the total amount of outstanding guarantees was EUR 16.225 billion, while EUR 5.25 billion have already been reimbursed.

III. POSITION OF PORTUGAL

13. On 1 July 2013 Portugal notified to the Commission a request to extend the scheme until 31 December 2013.
14. The Portuguese authorities submit that the prolonged scheme constitutes State aid within the meaning of Article 107(1) of the Treaty on the Functioning of the European Union ("TFEU"), but is of the view that the proposed prolongation is compatible with the internal market on the basis of Article 107(3)(b) TFEU as it is necessary in order to remedy a serious disturbance in the economy of Portugal.
15. Portugal submitted a letter by the Bank of Portugal¹⁶ further supporting the need for the proposed prolongation of the scheme to safeguard the stability of the financial system in Portugal, because prevailing market conditions do not allow for a termination of the scheme.
16. In particular, according to the Bank of Portugal, the scheme needs to be prolonged for a number of reasons. First, the Memorandum of Understanding ("MoU")¹⁷ signed between the Portuguese Government on the one hand, and the International Monetary Fund, the European Commission and the European Central Bank on the other hand, foresees measures for the banking sector which include the maintenance and the reinforcement of the scheme. Secondly, the Bank of Portugal considers that, notwithstanding the return of the Portuguese State to the market for medium- and long-term debt and the return of two Portuguese financial institutions to the international debt market, it cannot conclude that there is a total reestablishment of market access conditions for the Portuguese banking system as a whole to the capital markets given that some adverse effects of the sovereign risk crisis still persist. Although the scheme has not been used in the last year the Bank of Portugal thinks that its availability may prove to be relevant to enhance the ability of the Portuguese financial institutions to access the capital markets in the future.

¹⁴ Communication from the Commission on the application, from 1 January 2012, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 356, 6.12.2011, p. 7.

¹⁵ Recitals 13 to 16. See footnote 7.

¹⁶ Letter of the Bank of Portugal of 26 June 2013.

¹⁷ Portugal, "Memorandum Of Understanding On Specific Economic Policy Conditionality", 17 May 2011, http://ec.europa.eu/economy_finance/eu_borrower/mou/2011-05-18-mou-portugal_en.pdf

17. In line with the requirements of the 2011 Prolongation Communication, Portugal provided an indicative fee (estimation) for each financial institution eligible to benefit from those guarantees. The estimation was based on an application of the scheme's remuneration formula and recent market data. The indicative fees are set out in Annex II.

IV. ASSESSMENT OF THE MEASURE

IV.1. Existence of State Aid

18. According to Article 107(1) TFEU, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.
19. For the reasons indicated in the original decision, the Commission considers that the Scheme constitutes State aid within the meaning of Article 107(1) TFEU, because it concerns the provision of State resources to a certain sector, i.e. the financial sector, which is open to intense international competition.¹⁸ Therefore, any advantage from State resources to a financial institution affects intra-Union trade and therefore threatens to distort competition. The measures therefore constitute State aid within the meaning of Article 107(1) TFEU. Nothing in the prolonged scheme alters that assessment.

IV.2. Compatibility

20. Under the scheme, Portugal intends to provide aid in the form of guarantees in favour of credit institutions.
21. Given the exacerbation of tensions in sovereign debt markets that has taken place since 2011, the Commission considers it appropriate to examine the measure under Article 107(3)(b) TFEU.
22. Article 107(3)(b) TFEU empowers the Commission to find that aid is compatible with the internal market if it is intended "to remedy a serious disturbance in the economy of a Member State". The Commission has acknowledged that the global financial crisis can create a serious disturbance in the economy of a Member State and that measures supporting banks are apt to remedy that disturbance. That assessment has been confirmed in the Recapitalisation Communication¹⁹ and the Restructuring Communication.²⁰ The Commission still considers that requirements for State aid to be approved pursuant to Article 107(3)(b) TFEU are fulfilled in view of the reappearance of stress in financial markets. The Commission confirmed that view by adopting the 2010 Prolongation Communication²¹, which prolonged until 31

¹⁸ Original decision, recitals 23 to 25.

¹⁹ Commission Communication – Recapitalisation of financial institutions in the current financial crisis: limitation of the aid to the minimum necessary and safeguards against undue distortions of competition, OJ C 10, 15.1.2009, p. 2.

²⁰ Commission communication on the return to viability and the assessment of the restructuring measures in the financial sector in the current crisis under the State aid rules, OJ C 195, 19.8.2009, p. 9.

²¹ Communication from the Commission on the application, from 1 January 2011, of State aid rules to support measures in favour of bank's in the context of the financial crisis, OJ C 329, 7.12.2010, p. 7.

December 2011 the application of State aid rules to support measures in favour of banks in the context of the financial crisis. The Commission has since extended the application of those rules beyond 31 December 2011 under the 2011 Prolongation Communication.

23. The Commission does not dispute the position of the Portuguese authorities that the prolongation of the scheme is still necessary for reasons of financial stability. Consequently, the Commission finds that the scheme aims at remedying a serious disturbance in Portugal's economy.
24. Therefore, the Commission continues to base its assessment of State aid measures in the banking sector on Article 107(3) (b) TFEU.

Appropriateness

25. The objective of the scheme is to temporarily offer appropriate measures to establish backstops for the financial system in a timely and efficient manner, where financial institutions face difficulties in obtaining sufficient funding. The Commission observes that the continuing crisis has eroded confidence in the creditworthiness of counterparties, which results in difficulties in obtaining necessary funding on the financial markets. Hence, a backstop mechanism by the Member State, which in case of urgency ensures that the financial sector would have access to funding, is an appropriate means to strengthen the financial institutions and thus to restore market confidence.

Necessity

26. With regard to the scope of the measure, the Commission notes positively that Portugal does not change the size of the guarantee scheme, keeping at EUR 24.12 billion and that the scheme applies until 31 December 2013.
27. The Commission notes that Portugal has committed to follow the pricing and other conditions for State guarantees as laid down in the 2011 Prolongation Communication which requires, in particular, the application of a new pricing method based largely on market data. That new pricing formula takes into account the greater differentiation by risk of banks' credit default swap (CDS) spreads in recent times, by referring to median CDS spreads over a three-year period ending one month before the granting of guarantees. Increases in CDS spreads in recent years are partially due to influences that are not specific to individual banks, in particular the growing tensions in sovereign debt markets for Member States in difficulty and an overall increase in the perception of risk in the banking sector. However, the new pricing formula isolates the intrinsic risk of individual banks from changes in CDS spreads of sovereigns, notwithstanding the fact that sovereign spread is itself considered as a component of the price determination.
28. Since the beginning of the sovereign crisis the CDS of Member States in difficulty have rocketed. The CDS of the large banks located in those Member States have increased in line with those of their sovereign. The very high CDS of large banks in programme countries do not seem to primarily reflect their intrinsic risk profile, but are mainly driven by the sovereign risk. That linkage can lead to a situation in which the application of the guarantee pricing formula based on the individual CDS spread of the bank results in an excessively expensive guarantee, which is not justified by the risk profile of the bank. Therefore, it seems appropriate to consider the CDS

spreads of individual banks located in the countries subject to a financial assistance programme as temporarily non-representative of the intrinsic risk of that bank.

29. On the basis of the above observation, the Commission does not object to Portugal's intention to determine the guarantee fee for banks which still have a traded CDS on the basis of the CDS of the sample of Union banks in the "BBB- and lower" rating category. The Commission will review its assessment of the macro-economic situation and appropriateness of that exceptional pricing mechanism whenever a further prolongation of the scheme is notified.
30. Therefore, the Commission considers the measure as limited to the minimum necessary.

Proportionality

31. As regards proportionality, Portugal committed to present a restructuring plan, within two months of the granting of the guarantees, 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. This ensures that the use of the scheme will not enable banks with structural weaknesses in their business models to postpone or avoid the necessary adjustments.
32. Second, the Commission notes that Portugal has committed to a number of behavioural safeguards such as ban on advertisement referring to the State support and ban on any aggressive commercial strategies, which would not take place without the State support. Such safeguards help ensure that the participating institutions do not misuse the received State support to expand their activities.
33. Finally, the Commission welcomes that Portugal undertakes to submit individual restructuring or liquidation plans, within two months, for banks which cause the guarantee to be called upon.
34. As regards the combination of the scheme with other aid measures, the Commission recalls that, as indicated in the Annex to the Restructuring Communication, the restructuring plans to be submitted should contain all State aid received as individual aid or under a scheme during the restructuring period.
35. Furthermore, based on paragraph 16 of the Restructuring Communication, the Commission recalls that should further aid not initially foreseen in a notified restructuring plan be necessary for the restoration of viability, it 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 Communication's final decision on that bank.

Monitoring

36. Commission welcomes that Portugal undertakes to present every three months a report on the operation of the scheme and on guaranteed issuances, and to complement it with updated available data on the cost of comparable (nature, volume, rating, currency) non-guaranteed debt issuances.

Conclusions on the compatibility of the aid measure

37. The amended Portuguese guarantee scheme for banks remains an appropriate, necessary and proportionate measure to remedy a serious distortion of Portugal's economy and does not alter the Commission's previous assessment in the original decision of 29 October 2008 and the prolongation decisions of 22 February 2010, 23 July 2010, 21 January 2011, 30 June 2011, 21 December 2011, 27 June 2012 and 17 December 2012. In light of the commitments set out in Annex I the notified prolongation complies with the requirements set out above and is compatible with the internal market pursuant to Article 107(3)(b) TFEU.
38. In line with the Commission's decisional practice the Portuguese guarantee scheme can therefore be prolonged until 31 December 2013. Any further prolongation 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. CONCLUSION

The Commission has accordingly decided:

- to consider the aid to be compatible with the internal market.

Portugal exceptionally accepts that the present decision be adopted in the English language, for reasons of urgency.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

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

European Commission
Directorate-General for Competition
State Aid Greffe
B-1049 Brussels
Fax No: +32-2-296 12 42

Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President

Annex I

Commitments

With regard to the notification of the prolongation of the Portuguese guarantee scheme for credit institutions H1 2013, Portugal made the following commitments:

- (a) to grant aid measures under the scheme only to solvent credit institutions which have no capital shortfall²²; banks which have already received approved rescue aid at the date of entry into force of the 2013 Banking Communication, i.e. before 1 August 2013, but have not yet obtained a final approval of the restructuring aid, can also receive support under a scheme without individual notification. In such case an update to the restructuring plan has to be submitted if the restructuring plan had not already provided for the envisaged guarantee measure.
- (b) to grant the guarantees under the scheme only for the new issuance of senior debt (subordinated debt is excluded);
- (c) to provide guarantees only on debt instruments with maturities from three months up to five years (or a maximum of seven years in the case of covered bonds) and to limit the guarantees with a maturity of more than three years to one-third of the total outstanding amount of guarantees granted to the individual bank;
- (d) to determine the minimum remuneration level of the State guarantees under Article 4 of Portaria No 1219-A/2008 of 23 October 2008 (as amended by Portaria No 80/2012 of 27 March 2012), in line with the formula set out in the Commission's 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 (C(2011) 8744 final, p. 7);
- (e) to communicate to the Commission, within three months following each issuance of guaranteed bonds, the actual fee charged;
- (f) that any credit institution that is granted guarantees on new liabilities or on renewed liabilities for which, at the time of the granting of the new guarantee, the total outstanding guaranteed liabilities (including guarantees accorded before the date of this decision) exceed both a ratio of 5% of total liabilities and the total amount of EUR 500 million will be required to present a restructuring plan within two months of the granting of the guarantees;
- (g) that any institutions which cause the guarantee to be called upon will be required to submit individual restructuring or liquidation plans²³, within two months from such event;

²² "No capital shortfall" according to the most recent Union-wide capital exercise (the 2011 European Banking Authority ("EBA") capital exercise required at least a capitalisation of 9% as defined by EBA) or other equivalent national exercises by the national supervisory authority.

²³ The plan must be prepared on the basis of the parameters established in the Commission Communication on the return to viability and the assessment of the restructuring measures in the financial sector in the current crisis under the State aid rules (the "Restructuring Communication"), OJ C 195, 19.8.2009, p. 9.

- (h) to impose a ban on advertising referring to State support by the beneficiaries of the scheme and to prevent them from employing any aggressive commercial strategies which would not take place without the support of the Portuguese government;
- (i) to report on the operation of the scheme and on guaranteed issuances by 15 October 2013 (for the period 1 July to 30 September 2013) and by 15 January 2014 (for the period 1 October to 31 December 2013) at the latest
- (j) to complement reports on the operation of the scheme with updated available data on the cost of comparable non-guaranteed debt issuances (as regards nature, volume, rating, currency).

Annex II

Indicative guarantee fees as of 15 May 2013	
Institute	Premium per institute (basis points)
Banco Comercial Português, S.A.	[...]*
Banco Espírito Santo, S.A.	[...]
Caixa Geral de Depósitos, S.A.	[...]
Banks without CDS spread	[...]

* Confidential information.