



EUROPEAN COMMISSION

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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 [...].

PUBLIC VERSION

WORKING LANGUAGE

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Subject: State aid NN 49/2008 - Belgium

NN 50/2008 – France

NN 45/2008 – Luxembourg

**Emergency aid to Dexia in the form of a guarantee for bonds and
liquidity assistance**

Dear Sirs,

I have the honour to inform you that the European Commission has decided not to raise any objections to the above-mentioned state aid.

1. PROCEDURE

- (1) On 30 September 2008 the authorities of Belgium, France and Luxembourg (hereinafter 'the Member States concerned') publicly announced the implementation of the capital increase described in Section 2.2 of this letter (hereinafter 'the capital increase'). On 9 October 2008 the Member States concerned announced the implementation of the guarantee described in Section 2.3 (hereinafter 'the guarantee').

1.1. Information communicated by the Belgian authorities

- (2) By email of 2 October 2008, registered as received by the Commission on the same day, the Belgian authorities informed the Commission of the measures they had taken in relation to the capital increase, asking the Commission 'to consider this letter as a notification of the state aid elements inherent to the operation'.

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Belgium sent information relating to the guarantee on 9, 17 and 30 October, 3, 5, 6 and 7 November and between 12 and 19 November.

- (3) On 1 October 2008, Belgium forwarded to the Commission a letter from the Banque Nationale de Belgique justifying the urgency of the measures taken by Belgium in relation to the capital increase. In an email dated 14 October 2008, Belgium undertook to submit a plan for the Dexia Group, within six months of 3 October 2008, setting out in detail the measures aimed at ensuring its long-term viability. The plan will take account of the measures taken on 3 and 9 October 2008.
- (4) By letters dated 8 and 13 October, Belgium informed the Commission of a liquidity assistance (hereinafter 'LA') operation launched by the Banque Nationale de Belgique (hereinafter 'BNB') to tackle the temporary liquidity problems faced by Dexia Banque Belgique. Belgium kept the Commission informed of the amounts used for this operation.

1.2. Information communicated by the French authorities

- (5) By letter of 1 October 2008, registered as received on the same day, the French authorities submitted information to the Commission on the capital increase, but added that this was just a factual description sent to the Commission departments for information purposes which did not constitute a state aid notification and did not prejudice the legal description that the French authorities would give to the matter in question. By letter dated 13 October 2008, the French authorities informed the Commission of the implementation of the guarantee. Further information was provided on 10 November 2008.
- (6) On 2 October 2008, France forwarded to the Commission a letter from the Banque de France justifying the urgency of the measures taken by France in relation to the capital increase. By letter dated 13 October 2008, France also undertook to forward to the Commission, by 2 April 2009 at the latest, evidence of the viability of the activities of the Dexia Group and, where appropriate, the operational measures capable of ensuring a return to long-term viability.

1.3. Information communicated by the Luxembourg authorities

- (7) By email dated 1 October 2008, registered as received by the Commission on the same day, the Luxembourg authorities (using the form for state aid notifications) informed the Commission of the measures it had taken in favour of Dexia Banque Internationale Luxembourg SA, a subsidiary wholly controlled by Dexia SA, concerning the capital increase. The Luxembourg authorities stressed that they considered that these measures did not constitute state aid and that therefore they were only informing the Commission for reasons of legal certainty. By email dated 13 October 2008, the Luxembourg authorities informed the Commission of the guarantee. Further information was provided on 6 November 2008.
- (8) On 10 October 2008, Luxembourg forwarded to the Commission a letter from its Financial Sector Supervisory Committee justifying the urgency of the measures taken by Luxembourg in relation to the capital increase. By letter dated 2 October 2008, Luxembourg undertook to notify a liquidation plan or a restructuring plan for Dexia within six months from the authorisation of the aid.

1.4. Receipt of a complaint from a Dexia competitor

- (9) On 4 November 2008, a Dexia competitor operating on the Belgian market submitted two complaints to the Commission against the aid received by Dexia. The competitor considers that the aid measures are not compatible with the common market and alleges that Dexia used the aid to distort the financial market, in particular regarding interest rates offered to depositors.

2. DESCRIPTION OF THE AID MEASURES AND SCOPE OF THIS DECISION

2.1. The beneficiary

- (10) Dexia is a financial group active in the banking and insurance sectors. The parent company, Dexia SA, is a limited company incorporated in Belgium and listed on the Euronext Paris and Euronext Brussels stock exchanges. Its stock market value was €1.7 billion on 30 June 2008.
- (11) Dexia was formed in 1996 by the merger of Crédit Local de France and Crédit Communal de Belgique. It specialises in loans to local authorities (but it also has 5.5 million private customers).
- (12) Before the implementation of the measures set out in this letter, the ownership structure of Dexia was broken down as follows:

Company	Share of the capital
Arcofin	18,08 %
Holding Communal	17 %
Caisse des Dépôts et Consignations	11,89 %
Ethias	6,37 %
CNP Assurances	2,00%
Staff on payroll	3,92%
Free float	40,74%

2.2. Capital increase

- (13) On 28 September 2008, the Board of Directors of Dexia noted the deterioration in market conditions and the financial difficulties faced by some financial institutions. Given their impact on Dexia, the Board of Directors decided, on 29 September 2008, to swiftly proceed with a capital increase of €6.4 billion.
- (14) Having secured the agreement of various investors prepared to take part in the reserved capital increase, including the Belgian, French and Luxembourg authorities, the principle of and arrangements for a reserved capital increase were unanimously approved at an ensuing meeting of the Board of Directors on 30 September 2008.

- (15) The capital increase was accompanied by a removal of the pre-emptive rights of existing shareholders in accordance with Belgian company law and Dexia's statutes (this removal was apparently dictated by the need for immediate intervention). Therefore, in accordance with Belgian legislation, the issue price for new shares must be at least equal (in this case equal) to the average closing price of Dexia shares over the 30 calendar days preceding the day of the launch of the issue, namely €90. A total of 606 million new shares will be issued in this way.
- (16) The French authorities stress that the issue price reflects Dexia's value over the last six months. Whatever the reference period used over this period, the capital increase occurs at a rate which is always within the bracket constituted by the average rate +/- the standard deviation.
- (17) According to information from the Belgian authorities, the €6 billion capital increase by the Belgian and French shareholders, consisting in the issue of ordinary Dexia SA shares, became definitive on 3 October 2008. The underwriting of this reserved capital increase is broken down as follows.
- (a) Belgium:
- the Belgian State is investing €1 billion in Dexia SA;
 - the Flemish Region is investing €500 million in Dexia SA;
 - the Walloon Region is investing €350 million in Dexia SA;
 - the Bruxelles-Capitale Region is investing €150 million in Dexia SA;
 - Holding Communal SA is investing €500 million in Dexia SA;
 - Arcofin SC is investing €350 million in Dexia SA;
 - Ethias is investing €150 million in Dexia SA.
- (b) France:
- The French State is investing €1 billion in Dexia SA. This contribution will be managed by the Agence des Participations de l'Etat;
 - the Caisse des Dépôts et Consignations (CDC) group is investing €1.71 billion in Dexia SA;
 - CNP Assurances is investing €228 million in Dexia SA.

The Luxembourg State has undertaken to invest €376 million in Dexia Banque Internationale Luxembourg SA, in the form of convertible bonds with a maturity of three years, interest of 10% a year and conversion to ordinary shares on terms to be agreed.

2.3. The guarantee

- (18) By an agreement concluded on 9 October 2008, the Member States concerned decided to set up a guarantee mechanism for Dexia¹. It is a joint and non-several guarantee extended by Belgium (60.5%), France (36.5%) and Luxembourg (3%). The guarantee covers all financing obtained by Dexia SA and its subsidiaries Dexia Banque Belgique, Dexia Banque Internationale Luxembourg SA and Dexia Crédit Local from credit institutions and institutional depositors, and the bonds and debt instruments issued by Dexia to institutional investors, provided these financing measures, bonds or securities fall due before 31 October 2011. The guarantee covers the debt issued during six months from the entry into force of the guarantee agreement referred to below. It is renewable by mutual agreement for one year.
- (19) Moreover, financing which can be covered by the guarantee is limited to €150 billion, corresponding to all the financing issued before 9 October 2008 and falling due before 31 October 2009.
- (20) The guarantee is also the subject of an agreement between Dexia and the three Member States; it sets out the terms of the guarantee, including its remuneration (the agreement of 9 October provided for a remuneration 'reflecting the advantage thus obtained by the Dexia Group entities concerned based on normal market conditions'). The remuneration of the guarantee will consist of a commission that Dexia will have to pay every month on the *pro rata temporis* amount outstanding calculated as follows:
- for bonds with a fixed maturity of less than one month, including deposits at notice, the commission will be equal to 25 basis points on an annual basis, to be increased to 50 basis points after 15 February 2009;
 - for all other covered bonds with a maturity of up to 12 months or with an indefinite maturity, the commission will be equal to 50 basis points on an annual basis;
 - for all covered bonds with a maturity strictly exceeding one year, the remuneration of the guarantee will be equal to 50 basis points on an annual basis, plus the lower of the following two values, applied to each covered bond: either the median value of the Dexia five-year CDS spreads over a period starting on 1 January 2007 and ending on 31 August 2008 (provided that these spreads are representative), or the median value of the five-year CDS spreads during the same period for all credit institutions with a long-term credit rating equivalent to that of Dexia.

In each case, the commission is calculated on the average amount of the outstanding covered bonds with the maturity in question and covered by the guarantee during the previous month.

¹ More precisely for Dexia SA, Dexia Banque Internationale Luxembourg, Dexia Banque Belgique and Dexia Crédit Local France, or their issuing vehicles.

2.4. The LA operation

- (21) The LA operation is provided by the BNB in cooperation with the Banque de France. [...] * The credits granted by the BNB are covered by a guarantee from the Belgian State (with retroactive effect) pursuant to the Law of 15 October 2008 on measures to promote financial stability and introducing in particular a state guarantee on credits granted and other operations conducted in the context of financial stability and the Royal Decree of 16 October 2008, in implementation of Article 117A of the Law of 2 August 2002 on the supervision of the financial sector and financial services.

2.5. The sale of the FSA subsidiary

- (22) On 14 November 2008 Dexia announced the existence of a new \$16.9 billion guarantee extended by the Belgian and French Governments for the financial products of the FSA subsidiary, following Dexia's decision to sell the insurance part of FSA. FSA is not covered by the guarantee set out in the agreement as described in Section 2.3 above.

2.6. Scope of this Decision

- (23) This Decision covers only the guarantee issued under the agreement of 9 October 2008 which is the subject of the agreement described in Section 2.3 above, and the LA operation described in Section 2.4. The other measures will be examined separately in a subsequent decision.

3. ASSESSMENT OF THE COMMISSION

3.1. Existence of state aid within the meaning of Article 87(1) of the Treaty

- (24) The Commission is required to examine the aid measures using the criteria of Article 87(1) of the Treaty. The Commission considers that the measures at issue are selective since they only concern one undertaking, namely the Dexia group. Given Dexia's size and importance on the Belgian, French and Luxembourg markets and the fact that, without the aid, the group could have faced insolvency, which would have significantly changed the structure of the banking sector in all three countries, the Commission considers that the measures at issue affect trade between Member States and distort or threaten to distort competition. The aid measures include state resources and are clearly imputable to the Member States concerned.
- (25) As regards the advantage criterion, France considers that the guarantee does not constitute state aid. It points out in particular that the guarantee will be subject to a suitable rate of interest, similar to what it would be under normal market conditions. The other Member States have not expressed their views on this issue.

* Business secret.

- (26) The Commission notes that according to the information it has received, the rate of remuneration of the guarantee was not specified at the time it was granted; it was determined later on at a level in line with the recommendations of the European Central Bank of 20 October 2008, as in other cases or schemes investigated by the Commission² which are nevertheless considered to be aid measures. The Commission also notes that the reason for this guarantee was that Dexia no longer had access to short- or long-term financing on the interbank or capital markets. Given these circumstances, the Commission cannot consider that the guarantee is remunerated at a market rate. As regards the argument of the French authorities, the Commission stresses the fact that a remuneration must be assessed not with regard to any 'normal' functioning of the market but by taking into consideration the circumstances which existed at the time of the operation.
- (27) The Commission therefore considers that the guarantee represents state aid in favour of Dexia.

3.1.1. The LA operation

- (28) As regards the LA operation, the Commission has already made clear that where a Member State or a central bank reacts to a banking crisis with general measures open to all comparable market players (i.e. lending to all market players on equal terms), such general measures are often outside the scope of the state aid rules and do not need to be notified to the Commission. Dedicated support to a specific financial institution may also be found not to constitute aid in specific circumstances.
- (29) In this case, the Commission has noted that the BNB benefits from a guarantee from the Belgium State for the LA operation (even though this guarantee is not dedicated to this operation) pursuant to the Law of 15 October 2008 on measures to promote financial stability and introducing in particular a state guarantee on credits granted and other operations conducted in the context of financial stability, and that the operation also forms part of other measures, including the capital increase and guarantee measures. Belgium pointed out that the information concerning the LA operation 'supplemented' its capital increase notification, and that the BNB's operation was discretionary.
- (30) Given this background, the LA operation does not fulfil the criteria to avoid classification as state aid, as defined in paragraph 51 of the Communication from the Commission on the application of state aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis³. As a result, and notwithstanding Dexia's pledges, the Commission considers that the operation entails state aid.

3.2. Legality of the aid

- (31) Article 88(3) of the Treaty provides that the Member States shall inform the Commission, in sufficient time to enable it to submit its comments, of any plans

² See for instance Aid N 512/2008 – Germany – Rescue package for financial institutions in Germany.

³ OJ C 270, 25.10.2008.

to grant or alter state aid. In the case at issue, the Commission notes that the Member States concerned agreed on 9 October to implement the guarantee. While the information presented to the Commission in this respect took the form of a notification (as in the case of Belgium) or was submitted using the notification forms, it was submitted after the aid had been implemented and the notifications cannot therefore be considered to be valid.

- (32) The Commission therefore concludes that the aid measures were implemented in violation of Article 88(3) of the Treaty.

3.3. Legal basis of the compatibility analysis

- (33) The Belgian authorities invoke Article 87(3)(b) of the Treaty, which provides that 'aid ... to remedy a serious disturbance in the economy of a Member State' may be considered to be compatible with the common market. The Belgian authorities rely on the assertion that a collapse of Dexia would lead to a serious disturbance in the Belgian economy. France quoted paragraphs 87(3)(b) and 87(3)(c) in the event that the Commission should consider that the operation constitutes aid. Luxembourg does not mention any legal basis on which to assert the compatibility of their aid measures with the common market.
- (34) Let us first examine the relevance of the legal basis invoked by Belgium. The Commission will first of all present the arguments of the Belgian authorities on the difficulties faced by Dexia (Section 3.4) and the repercussions of a collapse of the bank on the Belgian economy (Section 3.5), and then draw its conclusions with regard to the applicability of Article 87(3)(b) of the Treaty (Section 3.6).

3.4. Difficulties faced by Dexia

- (35) The Belgian authorities have made the following observations.
- (36) Dexia's difficulties should be seen in the light of the international financial crisis at the time when the aid was granted. Dexia is heavily exposed to bank counterparties, the solvency of which deteriorated over the days preceding the granting of the aid. These positions give rise to a risk of significant losses which would affect Dexia's rating (which is crucial for obtaining lines of credit). For example, Dexia has assessed the losses incurred following the bankruptcy of Lehman Brothers at around €350 million. Dexia also has significant exposures in high-risk banks or countries, such as American, Irish, Icelandic or Turkish banks.
- (37) Moreover, the fall in stock markets led to significant losses on Dexia's securities portfolio, in particular during the third quarter. An amount of €7 billion in negative AFS reserves was set aside to account for unrealised losses on assets. There were strong fears that these unrealised losses might escalate and need to be realised, with a direct impact on the capital. This would affect Dexia's accounting capital (€15.639 billion on 30 June 2008) to the tune of one half.
- (38) Dexia was also undermined by the holding of precarious assets by its American subsidiary Financial Security Assurance (FSA), which specialises in credit enhancement. FSA has a high exposure to the US property market, which has been experiencing an unprecedented crisis since the summer of 2007. Since the first quarter of 2008, FSA has sustained losses which have been constantly revised upwards ever since as a result of the continued deterioration of the US

property market. On 30 June 2008, FSA transferred reserves worth \$1 billion to its exposure to the US property market (amounting to \$18.2 billion). Additional reserves are expected to be registered in the results of the third quarter. FSA has developed an asset management activity consisting mainly in the reinvestment of the excess liquidity of local authorities in the form of contracts guaranteeing to depositors an amount in capital and the payment of interest. This liquidity was invested mainly in assets linked to the US property market and in particular in sub-prime assets (\$7.6 billion out of a total portfolio of \$17.3 billion on 30 June 2008). The value of this portfolio dropped sharply in 2008, creating a substantial divergence with 'deposits' (divergence of \$4.3 billion on 30 June 2008). The deterioration in FSA's rating could have given rise to the possibility of depositors immediately withdrawing their holdings, thereby forcing FSA to sell these invested assets and incur a significant capital loss. Such loss crystallisation would have led to a severe deterioration in the creditworthiness of Dexia, which in June 2008 had set up a line of liquidity of \$5 billion for the asset management activity in order to avoid having to sell impaired assets. Moreover, the rating agency Moody's would probably have downgraded FSA's rating, thereby increasing the pressure on Dexia. FSA's extremely difficult situation forced Dexia to contemplate extreme scenarios (termination of activity or, as was announced subsequently on 14 November, sale) so as to limit the group's exposure. Such scenarios would have given rise to substantial additional losses.

- (39) Generally, the financial crisis has led to a major lack of confidence in banks, which is mainly reflected in an extreme scarcity of liquidity within the banking system. Dexia finances itself mainly in the short term on the financial markets by selling bonds to investors or borrowing money from other banks. Fears concerning whether or not Dexia can maintain its solvency have intensified the group's liquidity problems. These problems have had a direct impact on the activity of Dexia, which has encountered problems in placing issues guaranteed by loans to local authorities. For instance, at the beginning of September, Dexia was forced to cancel [...]. Dexia also wished to use [...]. Market conditions prevented it from using this source of financing.
- (40) This loss of confidence was also reflected at the level of private customers who started to withdraw [...] their holdings from Dexia in Belgium and Luxembourg during the course of Monday 29 September.
- (41) During the course of Monday 29 September 2008, the markets lost all confidence in Dexia:
- Unsecured interbank funding was practically non-existent at the beginning of the day.
 - During the day, the non-guaranteed interbank market was made unavailable to Dexia; Dexia's signature was no longer accepted on the repo collateral market and Dexia had to resort to the ECB's 'discount window' for an amount of €[100-400] million in order to remedy its liquidity situation. Dexia also approached the Banque Nationale de Belgique and the Banque de France to subscribe to a collateralised line of liquidity amounting to €[10-25] billion.

- Abnormal withdrawals also started to take place in Luxembourg and Belgium, severely jeopardising the liquidity of the Dexia Group (amounts outstanding represented €[50-100] billion, of which €[20-60] billion was liable to be paid on request).
 - The financial rating agency Standard & Poor's announced that they were downgrading Dexia's long-term debt rating from 'AA' to 'AA-'.
- (42) These various elements created a huge loss of confidence on the markets. On 29 September 2008, the Group's quoted shares fell by nearly 30% in one day. Since January 2008, the Group's quoted shares have fallen by nearly 59%. Against this background, Dexia could not survive without a massive recapitalisation to remedy its critical liquidity situation and restore the confidence of the market and the interbank system. The ordinary share recapitalisation by the Belgian and French shareholders was announced on 30 September 2008 and took place on 3 October.
- (43) Despite the increase in capital, Dexia was faced with a context of generalised mistrust on the financial markets and the drying-up of its refinancing possibilities on the interbank market.
- (i) Dexia shares continued to fall and lost 27% in five days, with an increase in value on the stock market which then amounted to approximately €6.4 billion, injected at the time of the recapitalisation.
 - (ii) On 8 October 2008, the rating agency [...].
 - (iii) Dexia no longer had access either to short-term unsecured refinancing on the interbank market or to long-term financing on the capital markets.
 - (iv) Dexia had to cope with important drawings from the lines of liquidity open to US municipalities and the public sector; at the same time, the flow of withdrawals in the retail networks continued.
 - (v) Dexia subscribed to lines of liquidity from the BNB and the Banque de France.
- (44) Taken together, these elements led to a major liquidity crisis such as to jeopardise Dexia's ability to continue to operate. It was therefore crucial to take significant measures to reopen access for Dexia to institutional financing mechanisms. This is the backdrop against which the guarantee was announced on 9 October 2008 and subsequently set up; the purpose was to provide reassurance to Dexia customers with regard to the protection of their deposits and the bank's liquidity.

3.5. Risks for the Belgian economy

- (45) Dexia is a major player on the - heavily concentrated - Belgian banking market. Because of its origins, Dexia is the public sector's bank of reference. It holds a pre-eminent position in the area of management of Belgian local and regional authority funds, in which Dexia holds a market share of [30-50]% (end of

August 2008). Dexia is also by far the largest provider of credit to local and regional authorities with a market share of [50-70]%.

- (46) At that time, Dexia held [10-20]% of the deposit accounts that Belgian households had in Belgian banks, making it one of the top three banks in Belgium as regards retail banking with around [1-5] million clients in Belgium. Its market shares in households loans were [10-25]% for mortgages and [10-25]% for consumer credit. As regards loans to undertakings other than financial undertakings, Dexia held [10-25]% of deposits and [10-25]% of credits. As regards financial institutions other than banks, Dexia held [5-12]% of deposits and [20-30]% of credits. At the end of June 2008, the balance of the deposit accounts held by all Belgian households with Dexia totalled €[25-40] billion.
- (47) The Belgian authorities also argued that Dexia held an important position on the international interbank market. At the end of June 2008, Dexia Group's interbank loans amounted to approximately [2-5]% of the debts due to banks for the EU banking sector. The other Belgian banks made up the largest part of its interbank loans ([15-20]%) but this sector also had a strong international dimension (for instance, interbank loans with the UK and France represented [15-20]% and [10-15]% respectively).
- (48) Belgium considers that Dexia's position on the Belgian market and on the interbank market leaves no doubt as to the dramatic consequences that bankruptcy would have had given the circumstances that prevailed at the time when the aid was granted. It considers that a grave loss of public confidence would have ensued (real risk of a bank run) which in turn would have triggered an acute crisis of confidence in the entire banking system (at both Belgian and international level), in particular because financial links between financial and banking institutions are so intertwined. This risk was compounded by the high volatility of the financial markets.
- (49) Belgium also points out that jeopardising Dexia would have put some of Dexia's shareholders with important roles to play in the Belgian economy in a disastrous situation, in particular:
- Holding Communal (17% of its capital on 30 June 2008), whose shareholders are the Belgian municipalities and which is an essential financing vehicle for local authorities;
 - the ARCO Group (18% of its capital on 30 June 2008), which is a cooperative holding with over 800 000 private shareholders from wide sections of the population;
 - Ethias (6% of its capital on 30 June 2008), the third largest insurance company in Belgium, all classes combined, with a 13.1% market share (over one million persons insured).

3.6. Assessment of the Commission

3.6.1. Applicability of Article 87(3)(b) of the Treaty

- (50) Article 87(3)(b) of the Treaty provides that 'aid ... to remedy a serious disturbance in the economy of a Member State' may be considered to be

compatible with the common market. Settled case-law shows that this Article must be interpreted strictly and that the aid in question must aim to remedy a serious disturbance affecting the economy of the Member State as a whole.

- (51) In the light of the considerations set out in paragraphs 36 to 44, the Commission notes that at the time when the aid at issue was granted, Dexia was faced with very severe difficulties which raised fears for Dexia's short-term survival.
- (52) It should therefore be assessed whether the suspension of Dexia's business activities would have led to a serious disturbance in the Belgian economy as a whole. The Commission notes in this respect that Dexia held a pre-eminent position in the local authority financing sector. Dexia is also a very important retail bank with [10-20]% of Belgian household deposits. In the economic context which prevailed at the time when the aid was granted, which was marked by an acute crisis in the American and European banking sectors (near standstill of the interbank lending market and proliferation of banks facing severe difficulties, leading to either buyouts by competitors, state intervention or bankruptcy), it was reasonable to conjecture that the suspension of Dexia's business activities would have been capable of largely paralysing all activities which were dependent on Belgian local authorities and of creating a crisis of confidence among Belgian households vis-à-vis the banking sector as a whole, resulting in a run on other banks established in Belgium. In the context of the international banking crisis, the sudden closure of a bank as important as Dexia would also acutely increase foreign banks' mistrust of Belgian banks, which would have the effect of cutting off any possibilities of borrowing – even very short term – on the interbank market. This latter effect, combined with the bank run, would mean that Belgian banks would not be in a position to finance themselves, leading to several of them filing for bankruptcy. The banking business would then be lastingly paralysed.
- (53) On the basis of the arguments set out in points 45 to 49 above and of the preceding analysis, which is based on the combination of the size of Dexia, its large presence in certain sectors of activity and the exceptional conditions on the financial market at the time when the aid was granted, the Commission considers that since the purpose of the aid measure was to avoid Dexia's bankruptcy, the aid measure was such as to remedy a serious disturbance in the Belgian economy as a whole. The Commission had already considered, in its communication of 13 October 2008 (hereinafter 'the Communication')⁴, that the current conditions on the financial markets, and their potential consequences for the economies of the Member States, meant that Article 87(3)(b) could serve as a legal basis for approving aid measures aimed at resolving this systemic crisis. It therefore considers that the compatibility of the aid must be examined on the basis of Article 87(3)(b) of the Treaty.
- (54) The same goes for France's aid measure, which was aimed at the same entity as Belgium's aid measure, namely Dexia. As for Luxembourg's aid, the Commission notes that it was granted in coordination with Belgium and France and that its purpose was to save Dexia as a whole and not just its Luxembourg subsidiary. It is therefore also apt to remedy a serious disturbance in the Belgian economy. The aid measures granted by France and Luxembourg can therefore also be examined

⁴ Idem.

on the basis of Article 87(3)(b) of the Treaty. As a result, it is not necessary to determine whether or not the closure of Dexia would lead to a serious disturbance in the economies of France or Luxembourg.

3.6.2. *Conditions for compatibility under Article 87(3)(b) of the Treaty*

- (55) In accordance with the Communication, it should be emphasised that in order to be compatible under Article 87(3)(b) of the Treaty, an individual aid award or an aid scheme must comply with the general compatibility criteria under Article 87(3)(c) of the Treaty read in the light of the general objectives of the Treaty and in particular Articles 3(1)(g) and 4(2) thereof, which implies compliance with the following conditions.
- (56) First of all, the aid must be a suitable means for reaching the desired end, namely to remedy a serious disturbance in the economy of a Member State as a whole.
- (57) The aid must also be necessary, i.e. its amount must not exceed what is strictly necessary to achieve the desired aim and it must take the form most appropriate for remedying the identified serious disturbance in the economy. Any aid exceeding this minimum amount is not necessary for remedying the serious disturbance and cannot therefore be authorised under Article 87(3)(b) of the Treaty. In other words, if another aid measure involving a smaller amount or less likely to distort competition (for instance a temporary and limited guarantee instead of a capital injection) would have been sufficient to remedy the disturbance in the economy, the measure is not necessary. This is confirmed by settled case-law⁵.
- (58) Lastly, the aid must be proportionate, meaning that the distortion of competition it gives rise to or threatens to give rise to must be balanced against its positive impact. The distortion of competition must therefore be limited to what is strictly necessary to achieve the desired effect. Indeed, as indicated in Articles 3(1)(g) and 4(1) and (2) of the Treaty, the Community has a system for ensuring that competition in the internal market is not distorted. In accordance with this principle, Article 87(1) of the Treaty prohibits, as a general principle, any selective measure which could form an obstacle to trade between Member States. Any aid authorised by way of derogation from this general principle under Article 87(3)(b) of the Treaty must therefore be limited to what is strictly necessary to achieve its objective.
- (59) The three points above are general principles of Community state aid rules which apply to all aid approved under Article 87(3). The Commission notes that in this case the remedy to the serious disturbance takes the form of aid measures to an undertaking which, in the absence of such measures, could have been left short of liquidity and forced to close down. In the Community guidelines on state aid for

⁵ Judgment in Case 730/79, *Philip Morris* [1980] ECR 2671. This case-law was recently confirmed by the Court in Case C-390/06, *Nuova Agricast v Ministero delle Attività Produttive*, [2008] ECR I-2577: 'As is clear from Case 730/79 *Philip Morris/Holland v Commission* [1980] ECR 2671, paragraph 17, aid which improves the financial situation of the recipient undertaking without being necessary for the attainment of the objectives specified in Article 87(3) EC cannot be considered compatible with the common market.'

rescuing and restructuring firms in difficulty⁶ (hereinafter 'the Guidelines'), which are referred to in the Communication, the Commission explained how it applies the above general principles in the case of aid aimed at rescuing or restructuring firms in difficulty. The Commission draws on the principles set out in the Guidelines and specifies certain criteria to be used to assess measures taken with regard to financial institutions in the context of the global financial crisis, and in particular recapitalisation and guarantee arrangements.

3.7. The Commission's assessment of the measures in favour of Dexia

3.7.1. Is the aid appropriate?

- (60) Belgium indicated as early as 29 September 2008 that Dexia had launched intensive discussions with the government, reference shareholders and regulators in order to develop solutions to restore the group's viability. Dexia had initially considered whether to allow minority shareholders to participate in the increase of its capital. However, a market-based operation of the kind involving preferential rights had become inconceivable given the attacks on its listed securities and the fact that the reference shareholders had indicated that they were financially incapable of committing themselves to taking on a share of the increase in capital at the level of what was needed to rescue the group. It was in this very volatile context that the Member States concerned decided to grant the aid. Indeed, only government intervention could provide a solution of sufficient scope and speed to ensure Dexia's survival.
- (61) Despite the increase in capital announced on 30 September, the combination of the elements referred to in paragraph 43 created a major liquidity crisis such as to compromise the group's ability to continue to operate. It was therefore crucial to take significant measures to reopen access for Dexia to institutional financing mechanisms. The Commission already noted in its Communication that the drying-up of interbank lending due to an erosion of confidence between financial institutions could justify guaranteeing certain types of interbank deposits and even short- and medium-term debt instruments, to the extent that such debts are not already adequately protected by existing investor agreements or other means. The guarantee follows the same logic in the particular case of Dexia. As regards the LA operation, the Commission has also recognised that Member States may wish to supplement the guarantee or recapitalisation plans with other forms of liquidity support.
- (62) In the light of the above, the Commission considers that the aid measures at issue were appropriate to ensure Dexia's survival.

3.7.2. Necessity of the aid

- (63) The guarantee is the result of Dexia's assessment of the evolution of its liquidity needs over a time span of 1 day to 24 months, on the premise of crisis scenarios as experienced since the beginning of October, in particular:

⁶ OJ C 244, 1.10.2004, p. 2.

- no unsecured refinancing in the short-term (no interbank loans) or in the long-term (impossibility of issuing bonds);
 - drawings on lines of liquidity open to US local authorities and the French public sector;
 - use of emergency lines at central banks involving significant amounts;
 - gradual attrition of deposits of retail customers in a climate of generalised mistrust, further increasing the group's liquidity needs;
 - no commercial production (freeze on new loans to local authorities).
- (64) The envisaged scenarios suggest that these crisis situations would inevitably make it impossible for Dexia to cope with the additional need for unsecured financing, despite using lines of liquidity at central banks.
- (65) Only the kind of benefits a state guarantee can yield for its short-term wholesale financing operations and medium-term bond financing could enable the group to regain adequate cover of its financing needs sufficiently quickly. The scope of the guarantee therefore covers a financing volume with a maximum maturity of three years, equivalent to the maturity of all the financing taken out or issued by Dexia before the date on which the guarantee was granted and falling due before 31 October 2009. The guarantee is therefore restricted to Dexia's refinancing needs. Dexia has undertaken to reduce its dependence on very short-term financing once the guarantee agreement is signed, committing itself in particular:
- provided market conditions allow, to make all necessary efforts to change the structure of its financing covered by covered bonds so that covered bonds with a maturity of less than one month do not represent more than 50% of the group's bonds with a maturity of less than one month at the time when the agreement is signed;
 - in any case, to ensure that covered bonds with a maturity of less than one month do not represent more than 75% of bonds with a maturity of less than one month at the time when the agreement is signed.
- (66) The Commission therefore considers that the guarantee is limited to what is necessary for the continuation of its activities.
- (67) As regards the LA operation, the penalising rate means that this source of liquidity is called on only if needed. Since the guarantee was granted, it has been used much less. The Commission can therefore accept that even though this measure does contain state aid, the measure is limited to what is necessary for the continuation of Dexia's activities.

3.7.3. *Proportionality of the aid*

- (68) Limiting the guarantee to a financing volume with a maximum maturity of three years equivalent to all the financing taken out or issued by Dexia before the date on which the guarantee was granted and falling due before 31 October 2009 means that the measure covers Dexia's refinancing needs over a specific future period and can therefore hardly be used to increase Dexia's position on the markets upon which it operates.

- (69) As regards the duration of the instruments covered by the guarantee, the measure in favour of Dexia is aligned on the Communication and only involves instruments falling due on 31 October 2011 at the latest, namely with a maximum maturity of slightly over three years. Indefinite contracts are covered until 31 October 2009.
- (70) As regards the period during which the guarantee can be called in, the measure provides that any instrument or contract issued between 9 October and a date of six months from the signing of the guarantee agreement can be covered. It is assumed that contracts with an indefinite maturity, such as sight deposits, which existed on 9 October 2008, were concluded on that date and are covered by the guarantee. The Commission also notes that, as mentioned in paragraphs 3, 6 and 8, the Member States have undertaken to submit a plan for Dexia within six months. Given these circumstances, the Commission confines itself to giving an opinion on these measures for this period⁷.
- (71) The remuneration of the guarantee was fixed largely in line with the recommendation of the European Central Bank. Provided this remuneration is set below 50 basis points (for bonds with a fixed maturity of less than one month, including deposits at notice, for a period until 15 February 2009), the Member States have provided a justification of this reduced rate, in terms of both a reduced value for Dexia and a commercial necessity given the existing financing profile at the time when the agreement came into force. The Commission therefore accepts that the rate represents an adequate contribution from the beneficiary.
- (72) In order to avoid undue distortions of competition, Dexia has ruled out the possibility of using its status as a bank with a state guarantee for some of its commitments for commercial advertising to third parties other than beneficiary third parties, and of using the guarantee for purely arbitrage transactions or in any advertising campaign highlighting the existence of the guarantee. The Member States concerned have confirmed that Dexia has also undertaken to limit the growth of its balance sheet (compared with the situation on 30 June 2008) to whichever is the highest between (i) the average growth of the Belgian, French and Luxembourg GDPs in 2007, (ii) the average annual balance sheet growth of the Belgian, French and Luxembourg financial sectors over the period 1988-2007 and (iii) the balance sheet growth of the European financial sector over the period from April to September 2008. Dexia has also undertaken not to offer deposit remuneration conditions to private individuals that would be among the three most attractive rates offered by the ten banks with the highest market share of retail deposits in each of the three Member States taken individually. As regards deposits at notice, for which a reduced rate of remuneration of the guarantee of 25 basis points was exceptionally agreed, Dexia has undertaken that the average amount of these deposits will not exceed €4 billion, which is the average amount in constant euros observed between 1 January 2007 and 31 August 2008. The Commission considers that these commitments address the allegations made in the two complaints referred to in Section 1.4 above, without prejudice to the

⁷ For guarantee arrangements, the Commission requests that Member States undertake to provide a restructuring plan for any beneficiary for which the guarantee is called in. Since such undertakings have already been given for Dexia, such a request would be devoid of purpose in this case.

possibility for the complainant to exercise its rights for the period when the aid was not authorised.

- (73) The penalising rate of the LA operation means that the measure is an expensive source of liquidity which is therefore unlikely to give Dexia an undue advantage for its operations.
- (74) The Commission is therefore of the view that the aid is proportionate.
- (75) It should be noted that the Commission will review the proportionality of the measures in favour of Dexia once it has received the plan(s) that the Member States have undertaken to provide within a period of six months. The Commission notes in particular that the guarantee agreement provides that if changes are needed in order to ensure that the agreement is in line with the EU rules on state aid, the Member States reserve the right to amend the agreement and/or to adjust their joint guarantee accordingly.

3.8. Conclusion regarding compatibility

- (76) The Commission considers that, as an emergency rescue measure, the aid satisfies the conditions laid down above and is compatible with the common market on the basis of Article 87(3)(b) of the Treaty. It accordingly authorises the aid for a period of six months.
- (77) After this initial period during which the aid is authorised as an emergency rescue measure, the Commission will have to reassess it, this time as a structural measure. It will then check that the aid is in line with the three general principles defined above and, in the application of these principles, it will take account of the conditions set out in the Guidelines. In this regard the Commission notes in particular that in order to continue to benefit from the derogation provided for in Article 87(3)(b) of the Treaty, this emergency rescue aid will have to be followed by:
- either a restructuring plan that ensures a return to long-term viability for the company. Indeed, if the measure is not effective in the long term, it will require further aid measures and will not achieve the desired affect, namely to remedy a serious disturbance in the Belgian economy;
 - or a plan organising the orderly liquidation of all or part of the financial institution's assets, thereby avoiding the negative effects described above.
- (78) This authorisation of the aid as an emergency rescue aid measure may be renewed at the duly justified request of the Member States concerned if the crisis in the banking sector continues.

4. CONCLUSION

The Commission has decided not to raise any objections to the state aid measures implemented by Belgium, France and Luxembourg in favour of Dexia. This decision is applicable for a period of six months from 3 October 2008 (date of implementation of the

first measure). This period may be renewed at the duly justified request of the Member States concerned if the crisis in the banking sector continues. If a plan for the restructuring or liquidation of the recipient is submitted in line with the undertakings given by the three Member States, this period will be automatically extended until the Commission takes its decision on the plan.

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: http://ec.europa.eu/community_law/state_aids/index.htm.

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

European Commission
Directorate-General for Competition
State aid Registry
SPA 3 - 6/5
B-1049 Brussels
stateaidgreffe@ec.europa.eu

Yours faithfully,

For the Commission

Neelie KROES
Member of the Commission