# Société de Prise de Participation de l'État (SPPE) (FR GFC)

Devyn Jeffereis[1]

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**Abstract**

As the Global Financial Crisis deepened, the bankruptcy of Lehman Brothers on September 15, 2008 and ensuing contagion began affecting the French economy and financial system (Xiao 2009 – pp. 16). France experienced declines in major economic indicators such as GDP, household consumption, and investment (Annual Report 2008 – pp. 16). In addition, the ensuing credit crunch in financial markets resulted in the seizing up of various lending markets (Xiao 2009 – pp. 15). Due to conservative business practices, a consolidated market structure, and a sound regulatory framework, the French banks were relatively better situated than their European counterparts to weather the crisis (Xiao 2009 – pp. 3-4) (Conac 2010 – pp. 304). However, the French authorities instituted a precautionary recapitalization scheme in order to "restore market confidence" in these institutions (State Aid N 613 2008 – pp. 3) (Conac 2010 – pp. 310). The French government created the *Société de Prise de Participation de l'État* (SPPE), a limited liability company that it wholly owned, in October 2008 (SPPE Annual Report 2009 – pp. 7). It initially participated in the global bailout of Dexia, a struggling Belgian-based European bank, and then began performing precautionary recapitalizations to the broader French banking system (SPPE Annual Report 2009 – pp. 7). In order to finance itself, the SPPE issued government guaranteed debt to inject capital into financially sound banks (Annual Report 2009 – pp. 45) (State Aid N 613 2008 – pp. 2). Banks applied to receive funds from the SPPE during two separate rounds in exchange for behavioral commitments, such as lending growth and limits on executive compensation (State Aid N 613 2008 – pp. 8-10) (Annual Report 2009 – pp. 45). From December 11, 2008 through the first half of 2009, the government injected more than €20 billion into six major French banking groups in the form of preference shares and subordinated debt (Conac 2010 – pp. 311) (State Aid N 613 2008 – pp. 3) (State Aid N 29 2009 – pp. 2, 5). The recipients of capital injections, with the exception of Dexia, paid back all capital and interest owed to the SPPE by May 19, 2011, resulting in a net profit of €0.8 billion (Senate 2011).


**Keywords**: Titres super subordonnés à durée indéterminée (TSS), Preference shares, French banks, Precautionary recapitalization, two phase injection, voluntary

[1] Research Associate, Yale Program on Financial Stability (devyn.jeffereis@yale.edu)

# SPPE Capital Injections (France)

## At a Glance

Following the bankruptcy of Lehman Brothers on September 15, 2008 and ensuing contagion, the French economy and financial industry began experiencing strain (Xiao 2009 – pp. 16). In response, the French government created a limited liability company, which it wholly owned, called the *Société de Prise de Participation de l'État* (SPPE) in October 2008 (SPPE Annual Report 2009 – pp. 7). It initially participated in the global bailout of Dexia, a struggling Belgian-based European bank, and then began performing precautionary recapitalizations to the broader French banking system (SPPE Annual Report 2009 – pp. 7). In order to finance itself, the SPPE issued government guaranteed debt to inject capital into financially sound banks (Annual Report 2009 – pp. 45) (State Aid N 613 2008 – pp. 2). The participant banks received voluntary capital injections in exchange for a number of behavioral commitments, including executive compensation and lending targets (State Aid N 613 2008 – pp. 2, 8-10). These commitments aligned with its stated goal to "increase lending to the real economy by 3% to 4% per year" and "achieve an average increase of 0.5% in each banking group's Tier One capital" (Annual Report 2009 – pp. 45).

| Summary of Key Terms | |
|---|---|
| **Purpose:** To "increase lending to the real economy by 3% to 4% per year" and "achieve an average increase of 0.5% in each banking group's Tier One capital" (Annual Report 2009 – pp. 45). | |
| **Announcement Date** | October 20, 2008 |
| **Operational Date** | December 11, 2008 |
| **End of Issuance Window** | August 30, 2009 (extended from June 8, 2009) |
| **Legal Authority** | Article 6 of the LOI no. 2008-1061 du 16 octobre 2008 de finances rectificative pour le financement de l'économie |
| **Peak Utilization** | €10.5 billion (1st Phase)<br>€11.85 billion (2nd Phase) |
| **Participants** | Société Générale, BNP Paribas, Groupe Crédit Agricole, Groupe Crédit Mutuel, Groupe Caisses d'Epargne, Groupe Banques Populaires |
| **Administrators** | Commission Bancaire (CB); Agence France Trésor (AFT); Agence des Participations de l'État (APE) |

The first injection of €10.5 billion consisted of deeply subordinated debt called *Titres super subordonnés à durée indéterminée* (TSS) and provided capital to six major French banking groups on December 11, 2008 (Conac 2010 – pp. 311). For the second injection, banks were allowed to issue either newly available preference shares (core Tier 1 Capital) or the TSS used in the first injection (non-core Tier 1 Capital), depending on the quality of capital specific banks required (State Aid N 29 2009 – pp. 8). The French government also allowed banks to exchange TSS issued during the first injection for the newly available preference shares (State Aid N 29 2009 – pp. 4). Throughout the first half of 2009, the French government injected €11.85 billion into four of the original six banks (DE LA CRISE FINANCIÈRE A LA CRISE ÉCONOMIQUE – pp. 61). The recipients of capital injections, with the exception of Dexia, paid back all capital and interest owed to the SPPE by May 19, 2011, resulting in a net profit of €0.8 billion (Senate 2011).

## Summary Evaluation

The SPPE successfully increased Tier 1 ratios of participating banks, provided protection from liquidity and solvency risks, and allowed banks to raise capital in private markets (Annual Report 2009 – pp. 45). In addition, all recipients of capital injections, with the exception of Dexia and the newly merged BCPE, paid back their shares by December 2009 (Conac 2010 – pp. 314). BCPE paid back all capital and interest owed to the SPPE by May 19, 2011, resulting in a net profit of €0.8 billion from the intervention, not including the Dexia stake (Senate 2011). However, there is disagreement regarding whether the behavioral commitments that the French government demanded in return for capital injections were sufficiently onerous (Conac 2012 – pp. 338) (Jabko and Massoc 2012 – pp. 571).

**Contents**

# I. Overview

### Background

The French financial system had been large and complex in the years prior to the financial crisis, accounting for 10% of the global banking system and 5% of global capital markets (Xiao 2009 – pp. 3). Due to its substantial size, it was integral to the European and international banking system (Xiao 2009 – pp. 3). The primary players within this market were a few large universal banks that provided a wide array of financial services (Xiao 2009 – pp. 3). For example, six French banking groups, Société Générale, BNP Paribas, Groupe Crédit Agricole, Groupe Crédit Mutuel, Groupe Caisses d'Epargne, and Groupe Banques Populaires, represented over 80% of France's net banking income (State Aid N 613 2008 – pp. 3). With the exception of HSBC, foreign banks were unable to penetrate this concentrated market (Xiao 2009 – pp. 3). Although it is important to note that mergers and acquisitions across European borders often muddled the national affiliations of banking groups (Xiao 2009 – pp. 3).

In general, the French banking sector was better situated during the financial crisis in comparison to their European neighbors due to a number of structural reasons (Conac 2010 – pp. 304). Since the major banks adhered to a universal business model, providing a wide range of services, they had a stable source of funding through deposits (Conac 2010 – pp. 305). They also had high capital ratios and less exposure to subprime lending (Conac 2010 – pp. 305). Alternatively, French consumers, stemming from cultural norms, were hesitant to accrue debt (Conac 2010 – pp. 306). Stringent usury laws protected these consumers, making risky lending more difficult (Conac 2010 – pp. 307). French banks also provided home equity lines of credit to consumers later than in the US, which limited the domestic credit expansion in housing (Conac 2010 – pp. 308). From a regulatory perspective, although the Commission Bancaire (CB), the main French bank regulator, did liberalize its supervision immediately before the crisis, it required banks to hold better quality capital above Basel-dictated standards (Conac 2010 – pp. 306-307) (Xiao 2009 – pp. 15). In particular, the CB limited banks holding of non-core Tier 1 Capital to 25% of Core Tier 1 Capital, which was lower than neighboring countries (Conac 2010 – pp. 307). The CB raised this ceiling to 35% in November 2008 so banks could take full advantage of the injections (State Aid N 613 2008 – pp. 4).

France's favorable position required unique interventions tailored to their specific needs. As the crisis deepened, the bankruptcy of Lehman Brothers on September 15, 2008 and contagion of the global financial crisis began impacting the French economy (Xiao 2009 – pp. 16). French GDP growth fell from 2.3% in 2007 to 0.3% in 2008, the worst rate in 15 years (Annual Report 2008 – pp. 16). Similar to the rest of the Euro Area, France experienced substantial declines in major economic indicators, with household consumption decreasing from 2.4% growth in 2007 to 0.9% in 2008 and investment slowing from 6.5% in 2007 to 0.4% in 2008 (Annual Report 2008 – pp. 16). In financial markets, the collapse of Lehman sparked turmoil across the globe (Xiao 2009 – pp. 15). This shock resulted in the seizing up of various lending markets including interbank, senior unsecured, securitized, and covered bond (Xiao 2009 – pp. 15). The credit crunch led to declining equity prices, increased volatility, and widening spreads which required government intervention across the globe, including France (Xiao 2009 – pp. 15).

## Program Description

Following a Group of 7 industrialized nations (G7) meeting on October 10, 2008, which focused on guiding principles for action during the financial crisis, the French government pursued a dual approach to aid their banking system that included *the Société de financement de l'économie française* (SFEF) and *Société de Prise de Participation de l'État* (SPPE) (Annual Report 2008 – pp. 33, 35). The SFEF provided French banks with medium and long-term financing when difficult to find in private markets (Annual Report 2008 – pp. 35). The French government created the SPPE in October 2008 as a limited liability company to perform recapitalizations (SPPE Annual Report 2009 – pp. 7). Its first injection was €1 billion toward the international bailout of Dexia SA, a troubled Belgium-based bank with operations across Europe, in return for a 5.7% stake in the company (SPPE Annual Report 2009 – pp. 7) (State Aid NN 50 2008 – France – pp. 4). As the financial crisis spread in the fall of 2008, even relatively healthy French banks faced issues stemming from a global "flight-to-quality" and credit crunch (Xiao 2009 – pp. 15). In December 2008, SPPE began a broad recapitalization scheme for French banks in order to ensure they continued lending to the economy (Annual Report 2008 – pp. 35). Even though the banks that received assistance were sound, with the exception of Dexia, the SPPE attempted to "restore market confidence" in these institutions (State Aid N 613 2008 – pp. 3). At the time, markets were putting substantial pressure on banks, which could have resulted in reduced lending and negative impacts on the overall French economy (State Aid N 613 2008 – pp. 3). This case will focus on the bank recapitalization conducted by the SPPE.

The French National Assembly passed a law giving the SPPE the authority to recapitalize banks on October 16, 2008 (LOI n. 2008-1061 2008). Market expectations, stemming from the announcement of assistance by the Dutch government to ING, sped up the public announcement of this plan, which occurred on October 20, 2008 (Lagarde Testimony 2008 – pp. 286). The French government then submitted an outline of the program to the European Council on December 3, 2008, which approved it on December 8, 2008 (State Aid N 613 2008 – pp. 1). The SPPE performed two rounds of capital injections, €10.5 billion in December 2008 and €11.85 billion during the first half of 2009, bringing the total intervention to €22.35 billion (Conac 2010 – pp. 310) (Annual Report 2009 – pp. 45). Through these actions, the government hoped "to increase lending to the real economy by 3% to 4% per year" and "achieve an average increase of 0.5% in each banking group's Tier One capital" (Annual Report 2009 – pp. 45). The SPPE funded itself by issuing state-guaranteed debt (State Aid N 613 2008 – pp. 2).

The first injection of €10.5 billion occurred on December 11, 2008 and was provided to Société Générale (€1.7 billion), BNP Paribas (€2.55 billion), Groupe Crédit Agricole (€3.0 billion), Groupe Crédit Mutuel (€1.2 billion), Groupe Caisses d'Epargne (€1.1 billion), and Groupe Banques Populaires (€.95 billion) (See Figure 1 for an outline of the SPPE injections) (Conac 2010 – pp. 311) (State Aid N 613 2008 – pp. 3). All these banking groups applied to receive capital and were not obligated to do so (State Aid N 613 2008 – pp. 3). Although the budget for the scheme was €21 billion, the EC authorized the SPPE to inject €10.5 billion in the first round, with the option for banks to subscribe to a second injection in 2009 if market conditions continued to worsen (State Aid N 613 2008 – pp. 4).

The capital used for the first injection consisted of deeply subordinated debt securities commonly found in French markets, known in French as *Titres super subordonnés à durée indéterminée* (TSS) (State Aid N 613 2008 – pp. 3). The TSS were more like equity than the subordinated debt that U.S. banks typically issue, in that they were perpetual, or matured after 99 years, and loss-absorbing. For this reason, they qualified as non-core Tier 1 Capital (State Aid N 613 2008 – pp. 4, 18) (Jabko and Massoc 2012 – pp. 570). The TSS issued to the SPPE paid a penalty interest rate. The CB partly based the interest rate on each bank's average credit default swap spread or credit rating, to reflect individual bank's relative riskiness. In addition, the nominal amount banks owed on redemption increased each year, to encourage banks to redeem as quickly as possible (State Aid N 613 2008 – pp. 8). In return for the injection of government capital, banks were required to adhere to a number of behavioral constraints, including limitations on executive compensation and commitments to increase their lending (State Aid N 613 2008 – pp. 8-10). However, these commitments were not legally binding or backed by sanctions; instead, the CB relied on the reputational damage of noncompliance (State Aid N 613 2008 – pp. 10). The CB limited TSS issuance to 35% of a bank's total Tier 1 capital.

On January 21, 2009, the French authorities submitted to the European Commission an amendment to the original application describing the terms of its second round of capital injections (State Aid N 29 2009 – pp. 1). In this round, banks would have the option of issuing TSS (with the same characteristics as before) or preference shares (State Aid N 29 2009 – pp. 1). The EC approved the amendment on January 28, 2009 allowing banks to issue €11.85 billion of TSS or preference until August 30, 2009 (State Aid N 29 2009 – pp. 1, 9).

The beneficiary banks were required to issue preference shares that had similar characteristics to TSS, such as Tier 1 Capital, non-voting, and loss-absorbing (State Aid N 29 2009 – pp. 4). However, the preference shares were a form of equity and bore losses before the TSS. As such, they qualified as core Tier 1 Capital. There were no limits placed on dividends by the participating banks, however the CB prioritized dividend payments to preference shares held by the SPPE over ordinary shareholders (State Aid N 29 2009 – pp. 9). They could account for up to 50% of the share capital of an unlisted company and 25% of the share capital of a listed company, higher than the limits for TSS (State Aid N 29 2009 – pp. 4). Since preference shares were more subordinate, and therefore riskier, their remuneration was higher than the TSS (State Aid N 29 2009 – pp. 10).

Banks could use the funds raised from issuing preference shares to redeem TSS they had issued in the first injection (Annual Report 2009 – pp. 45). Only BNP Paribas took advantage of this provision. It issued €5.1 billion of preference shares and used approximately half of those funds to repurchase TSS, resulting in a net issuance of €2.55 billion (DE LA CRISE FINANCIÈRE A LA CRISE ÉCONOMIQUE – pp. 61). Of the six banks that participated in the first injection, Société Générale (€1.7 billion), BNP Paribas (€5.1

billion), Groupe Caisses d'Epargne Groupe (€1.1 billion), and Banques Populaires Groupe (€.95 billion) participated in the second injection. Crédit Agricole and Groupe Crédit Mutuel declined to participate (See Figure 1 for an outline of the SPPE injections) (DE LA CRISE FINANCIÈRE A LA CRISE ÉCONOMIQUE – pp. 61).

**Figure 1: Outline of SPPE Injections**

| Financial Institutions | First Injection | Second Injection |
|---|---|---|
| Société Générale | 1.7 | 1.7 |
| BNP Paribas | 2.55 | 5.1** |
| Groupe Crédit Agricole | 3.0 | - |
| Groupe Crédit Mutuel | 1.2 | - |
| Groupe Caisses d'Epargne | 1.1 | 1.1 |
| Groupe Banques Populaires | .95 | .95 |
| Total | 10.5 | 11.85* |

(Source: DE LA CRISE FINANCIÈRE A LA CRISE ÉCONOMIQUE – pp. 61)

*Note: The French government injected an additional €3 billion to assist in the merger of Groupe Caisses d'Epargne and Groupe Banques Populaires

** BNP used approximately half of the funds from the €5.1 billion preference shares issued in the second injection to redeem TSS issued during the first injection, resulting in a net second injection amount of €2.55 billion

### Outcomes

Following the first injection, the Tier 1 Capital ratio of each beneficiary bank increased by approximately 0.5%, as planned (State Aid N 29 2009 – pp. 3). The second injection increased each bank's Tier 1 Capital by an additional 0.5% (Annual Report 2009 – pp. 45). Participating banks could exit the scheme by buying back the shares or debt at any time, subject to the CB's consent (State Aid N 29 2009 – pp. 4). Due to the costly nature of the securities, along with improved economic and financial conditions, most participants repurchased their TSS and preferred shares by December 2009 (Annual Report 2009 – pp. 49) (Conac 2010 – pp. 314). The only exception was the newly merged Groupe Caisses d'Epargne and Groupe Banques Populaires (BCPE) (Conac 2010 – pp. 314). Following the final repayment of capital by BCPE on March 23, 2011 and its payment of 2010 dividends on May 19, 2011, the SPPE intervention during the Global Financial Crisis was closed (Senate 2011). In total, interventions through the SFEF and SPPE would result in a net profit of €2.7 billion, with the SPPE (not including its Dexia stake) accounting for €0.8 billion of that total (See Figure 2 for the assets held by the SPPE) (Senate 2011).

However, the SPPE did not close following the redemption of the capital injections as it continued to house shares of Dexia. The SPPE went on to participate in the second international Dexia bailout in 2012 (Dexia Annual Report 2018 – pp. 6) (Jabko and Massoc 2012 – pp. 573). According to the Dexia 2018 Annual Report, the SPPE still held 196,658,798 shares (46.81%) at the end of 2018, as the company continued to liquidate (Dexia Annual Report 2018 – pp. 190).

**Figure 2: Assets Held by the SPPE**

| Type of Assets | Issuers | Amount (as of October 22, 2009) | Amount (as of June 6, 2011) |
|---|---|---|---|
| Titres super subordonnés à durée indéterminée (TSS) | Groupe Banques Populaires | €1.95 billion | - |
| | Groupe Banques Populaires – Groupe Caisse d'Epargne merger group | €1.2 billion | - |
| | Groupe Caisses d'Epargne | €2.1 billion | - |
| | Groupe Crédit Agricole | €3.0 billion | - |
| | Société générale | €1.7 billion | - |
| Preferred Shares | BNP Paribas | €5.1 billion | - |
| | Société générale | €1.7 billion | - |
| | Groupe Caisses d'Epargne | €3.0 billion | - |
| Ordinary Shares | Dexia | €0.6 billion | €0.3 billion |

(Source: Assets Held by SPPE)

# II. Key Design Decisions

## 1. The SPPE was part of a two-pronged approach aimed at recapitalizing banks and providing refinancing assistance.

In response to the Global Financial Crisis, the French Government created two schemes, the *Société de financement de l'économie française* (SFEF) and *Société de Prise de Participation de l'État* (SPPE), to aid their banking sector through refinancing assistance and capital injections (Annual Report 2008 – pp. 35). The SFEF was a special purpose vehicle majority owned by France's leading banks that provided financing in exchange for collateral (Annual Report 2008 – pp. 35).[2] In order to fund itself, the financing vehicle issued bonds guaranteed by the French government (Annual Report 2008 – pp. 35). The SPPE, a limited liability company wholly owned by the French government, was financed by short-term debt guaranteed and issued by the French government and subscribed to subordinated debt or preference shares issued by banks (SPPE Annual Report 2009 – pp. 7) (Annual Report 2008 – pp. 35).

## 2. The legal basis for the SPPE was Article 6 of the LOI no. 2008-1061 du 16 octobre 2008 de finances rectificative pour le financement de l'économie.

On October 10, 2008, the Group of 7 industrialized nations (G7) created five principles to guide government action during the financial crisis (Annual Report 2008 – pp. 33). One of the guiding principles which directly applied to the SPPE involved "recapitalising public

[2] See Fang 2019 for more information on the Societe de Financement de l'Economie Francaise (SFEF)

and private financial institutions where required" (Annual Report 2008 – pp. 33). Following the G7 meeting, the French presidency of the EU hosted a summit of the euro area on October 12, 2008 where euro area leaders collectively agreed on the need for emergency measures (Jabko and Massoc 2012 – pp. 569). The French government then convened an emergency legislative procedure on October 16, 2008 to pass their own plan. Article 6 of the Law n ° 2008-1061 of October 16, 2008 to rectify finance for the financing of the economy was adopted within one week and allowing for the creation of both a recapitalization and refinancing program (Conac 2010 – pp. 299) (LOI n. 2008-1061 2008).

### 3. The European Commission approved the SPPE under Article 87(3)(b) of the EC Treaty as permitted state aid but required some changes to the plan.

Prior to approving the SPPE, the European Commission (EC) was required to determine whether the scheme represented state aid (State Aid N 613 2008 – pp. 13-14). If the EC concluded the SPPE was state aid then it would have an anti-competitive impact on the common market and require further legal scrutiny (State Aid N 613 2008 – pp. 13-14). According to Article 87(1) state aid is defined below:

> "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, insofar as it affects trade between Member States, be incompatible with the common market" (State Aid N 613 2008 – pp. 13).

Although the French government argued that the scheme did not constitute state aid, ultimately the EC disagreed (State Aid N 613 2008 – pp. 13-14).

As a result, the SPPE had to be approved under Article 87(3)(b), which affirms that state aid "may be considered to be compatible with the common market: (b) aid […] to remedy a serious disturbance to the economy of a Member State" (State Aid N 613 2008 – pp. 14). The EC determined that the SPPE was permitted under this provision as the program was well targeted ("in the case in point, to remedy a serious disturbance in the economy of a Member State"), necessary, and proportionate (State Aid N 613 2008 – pp. 14-16). The French government initially allocated €40 billion for the SPPE, but the EC revised this budget to €21 billion following its approval of the plan (Annual Report 2008 – pp. 35). Furthermore, the EC implemented a two-stage intervention that would only allow the second injection if markets conditions warranted it, along with a six-month application window (State Aid N 613 2008 – pp. 17). The EC described these measures as an "additional safeguard against excessive intervention by the State" (State Aid N 613 2008 – pp. 17).

### 4. The French government accelerated communications of the plan's details following the capital injection of €10 billion to ING by Dutch authorities.

On October 19, 2008, the Dutch government announced that it would inject €10 billion of nonvoting preferred shares into ING (Jolly 2008). This followed the announcement of TARP, a $700 billion package announced by the United States (Jolly 2008). ING described the funds as "a strong buffer to navigate the current market and economic environment" (Jolly 2008). As a result, markets expected comparable schemes aimed at improving capital ratios by other countries (Conac 2010 – pp. 310). In particular, these injections from various national authorities had "raised the bar for capital ratios" and led people to believe "there are new capital standards in the market" (Jolly 2008).

Christine Lagarde, the French Minister of the Economy, Industry and Employment, testified on October 22, 2008 to the French National Assembly Finance Committee that the impetus behind announcing the plan on October 20, 2008 was the Dutch intervention. She explained that market expectations for similar plans by other European countries following the Dutch government's October 19 announcement weighed heavily on banks' share prices during the morning of October 20, 2008 (Lagarde Testimony 2008 – pp. 286). In response, the French government decided to remove the uncertainty and announce the plan that night (Lagarde Testimony 2008 – pp. 286). Lagarde clarified that the plan had been in the works for several days and the Dutch announcement did not affect the details of the plan, but changed the application schedule (Lagarde Testimony 2008 – pp. 290).

The SPPE communicated its operations through the issuance of annual reports and the Agence des Participations de l'État (APE), the French government shareholding agency, absorbing its financial statements (SPPE Annual Report 2009 – pp. 17). The SPPE also had to report on the implementation of the bank rescue plan to Parliament and the EC after the first six months (LOI n. 2008-1061 2008) (State Aid N 613 2008 – pp. 10-11).

### 5. The French State was the SPPE's sole shareholder and contracted certain management duties to government agencies and third parties.

The French government created the SPPE as a simplified joint stock corporation (*Société par actions simplifiée*) and limited liability company with the French government as its only shareholder (SPPE Annual Report 2009 – pp. 7) (Conac 2010 – pp. 310). It had no employees and awarded no compensation to its directors or executive management (SPPE Annual Report 2009 – pp. 17). In order to manage its assets, the SPPE delegated roles to government and external agencies. For example, Ernst & Young performed an external audit of the SPPE financial statements in accordance with applicable French law for the year ended December 31, 2010 (SPPE Annual Report 2010 – pp. 1-2). The Agence France Trésor (AFT), the government agency responsible for managing public debts, managed debt issuances by SPPE, including the handling of margin calls and hedging foreign exchange exposures (SPPE Annual Report 2009 – pp. 8). As previously mentioned, the APE absorbed the SPPE financial statements into its balance sheet (SPPE Annual Report 2009 – pp. 17). The Commission Bancaire (CB), the primary regulator for both banks and investment firms, performed functions such as assessing potential participants and approving bank applications for exiting the program (State Aid N 613 2008 – pp. 2, 6).

### 6. The SPPE funded itself by issuing short-term, state guaranteed bonds.

The SPPE funded itself by issuing debt guaranteed by the state. These bonds were irrevocable, unconditional, first demand (an added form of protection in which the creditor is guaranteed repayment regardless of other transactions), and ensured through the *Caisse* *de la Dette Publique*[3] (French Public Debt Fund), a fund that backs the creditworthiness of the French government in financial markets, and available in any OECD currency (State Aid N 613 2008 – pp. 2) (SPPE Financing Program). The Minister for the Economy dictated the specific characteristics for each funding operation, such as duration and guarantee size (State Aid N 613 2008 – pp. 2). SPPE bonds primarily consisted of short-term notes because yields on short-term debt were significantly lower, and therefore cheaper, than longer-term debt (Conac 2010 – pp. 310). Also, banks had a strong motivation to redeem capital injections quickly (Conac 2010 – pp. 310).

**7. The application to receive SPPE injections was open to credit institutions satisfying set criteria.**

The French authorities outlined a set of criteria for credit institutions, including foreign subsidiaries operating in France, in order to qualify for capital injections under the SPPE (State Aid N 613 2008 – pp. 2). The criteria were based off of the Article 87(3)(b) provision (see KDD 3) that the program was approved under. The credit institutions satisfying the following criteria applied for recapitalization by the SPPE.

i. Authorized in France and supervised under the French Monetary and Financial Code
ii. Comply with the own funds [regulatory capital] requirement in the French Monetary and Financial Code
iii. In a financial position to be able to guarantee its long term viability and to present a positive economic situation in accordance with the criteria normally used in the banking sector
iv. Previously concluded an agreement with the State fixing the consideration provided for by law; and
v. Institutions where a severe and sudden reduction in their activity would have a serious impact on the French economy (State Aid N 613 2008 – pp. 2).

The CB examined and approved individual bank applications based on the above qualifications (State Aid N 613 2008 – pp. 2). Ultimately, six French banking groups applied to receive funds and all were approved (State Aid N 613 2008 – pp. 2-3).

**8. The capital injection program relied on voluntary participation by eligible credit institutions.**

The SPPE focused on providing funds to a large number of financially sound banks rather than rescuing near-bankrupt institutions (Jabko and Massoc 2012 – pp. 570). The intervention was a precautionary measure to shore up capital ratios and spur lending to the French economy (Conac 2010 – pp. 310). Therefore, there were no legal requirements or sanctions enacted to compel banks to receive funds (Jabko and Massoc 2012 – pp. 570) (State Aid N 613 2008 – pp. 10). The CB was responsible for reviewing and approving these applications (State Aid N 613 2008 – pp. 2). The participants, which represented over 80% of France's net banking income, included Société Générale, BNP Paribas, Groupe Crédit Agricole, Groupe Crédit Mutuel, Groupe Caisses d'Epargne, and Groupe Banques Populaires

[3] More information on the Caisse de la Dette Publique (French Public Debt Fund) can be found here

(State Aid N 613 2008 – pp. 3). HSBC France was eligible to receive funds through the scheme, but declined to apply (State Aid N 613 2008 – pp. 3).

Some of the six participating institutions, including Société Générale, publicly expressed hesitation regarding the capital injections (Conac 2010 – pp. 311-312). Conac (2010) cites this reluctance as evidence that the program was not necessarily voluntary—in other words, the government was pressuring banks to accept the funds Conac 2010 – pp. 312). He states, "By forcing all major French banks to participate into the scheme, the Government prevented the market from identifying a weaker one and creating a panic" (Conac 2010 – pp. 312). This issue also arose during Christine Lagarde's testimony on October 22, 2008 when Dominique Baert, a member of the French National Assembly Finance Committee, expressed concern about providing funds to non-struggling institutions. He questioned whether providing capital to all institutions hid those who really needed it from the markets. (Lagarde Testimony 2008 – pp. 291).

**9. The SPPE instituted a two-phase capital injection process.**

The EC approved the initial injections along with the option for a second installment of an identical amount under matching conditions should market conditions continue to deteriorate (State Aid N 613 2008 – pp. 4). Approximately a month and a half after the EC approved the initial plan on December 8, 2008; the French government notified the EC of a second installment on January 21, 2009 (State Aid N 29 2009 – pp. 1) (Conac 2010 – pp. 313). The EC approved the second installment on January 28, 2009, noting that the market conditions that led to the first installment still prevailed (State Aid N 29 2009 – pp. 1, 9). The CB calculated both injection amounts to increase the Tier 1 ratios of participating banks by 0.5% (State Aid N 613 2008 – pp. 16-17). In total, the two installments brought the initial budget to €21 billion (State Aid N 613 2008 – pp. 4).

**10. The first capital injection consisted of deeply subordinated, hybrid debt securities.**

On December 11, 2008, the SPPE injected €10.5 billion into six French banks through a subordinated-debt security called Titres super subordonnés à durée indéterminée (TSS) (Conac 2010 – pp. 311) (State Aid N 613 2008 – pp. 3). TSS were hybrid debt securities with a maturity of 99 years (or perpetual) and were commonly issued by French banks prior to the crisis (State Aid N 613 2008 – pp. 4). Lagarde characterized them as halfway between debt and capital in her testimony (Lagarde Testimony 2008 – pp. 286).

For these securities to qualify as Tier 1 they needed to fulfill Basel requirements of permanent type, subordination ranking placing the bearers just before shareholders (including preference shares), and able to absorb losses (State Aid N 613 2008 – pp. 4). The CB categorized TSS as non-core Tier 1 and had a ceiling of 35% of total Tier 1 Capital (State Aid N 613 2008 – pp. 4).

Additional requirements included:

i. Maturity of 99 years or perpetual
ii. Two-phase remuneration
iii. Subordination level over shareholders and to holders of the issuer's equity securities
iv. Subordination level below holders of bond instruments

v. Obligatory interest payments following remuneration of capital shareholders
vi. Loss absorbing; and
vii. Reimbursement at any time, pending approval by the CB (State Aid N 613 2008 – pp. 4-6).

There were a number of reasons behind the French government's decision to limit injections to TSS instead of more subordinated securities such as ordinary or preference shares. Since participating banks were solvent and healthy, injections of better quality capital were not necessary; it also could have sent a negative signal to the markets that the banks receiving capital were in a worse situation than initially disclosed (Conac 2010 – pp. 310). In addition, ordinary and preference shares would have been more expensive, required an extraordinary shareholders meeting, and French banks did not commonly use preference shares (Conac 2010 – pp. 310-311).

Lagarde explained that the decision to use TSS was because the injection of higher-quality capital was not justified, as the recipients were strong, well-managed, well-supervised and had the added support of robust retail businesses (Lagarde Testimony 2008 – pp. 288). Therefore, the increased costs and negative signaling effects associated with higher-quality capital would be counterproductive (Lagarde Testimony 2008 – pp. 288). She also highlights that TSS closely aligns with the goals of the program as it facilitates financing of the economy without taking equity stakes and attempting to reorient activity (Lagarde Testimony 2008 – pp. 288).

**11. Participant banks remunerated the TSS in two phases and redeemed them a penalty rate that increased yearly.**

The TSS used the below formulas to calculate interest payments, it paid the fixed rate for the first five years followed by the variable rate (State Aid N 613 2008 – pp. 4).

i. *Fixed Rate*: BTAN[4] five years + 300bps + 5 x CDS[5]
ii. *Variable Rate*: EURIBOR + 250bps + 5 x CDS (State Aid N 613 2008 – pp. 7)

Given the BTAN was approximately 3% prior to the December 11, 2008 issuance, the rate dictated by the above fixed rate formula was around 8%, varying slightly depending on the participating bank (State Aid N 613 2008 – pp. 8). According to Lagarde, 8% was the approximate rate that French banks paid during 2008 to raise this type of debt (Lagarde Testimony 2008 – pp. 288).

This remuneration structure provided stability, included a market rate, accounted for each institution's individual credit profile, and represented a penalty remuneration rate in comparison to an improved market (State Aid N 613 2008 – pp. 7). In order to classify the issued funds as Tier 1 Capital there could not be a leap in rates for these securities compared to market conditions (State Aid N 613 2008 – pp. 7). Therefore, the French government implemented an initial fixed-rate period to provide the required stability

[4] BTAN=average rate on the 5-year government bonds during the 20 days preceding the issue

[5] CDS=average value of the 5-year CDS spreads for the specific beneficiary institution over the period from 1 January 2007 to 31 August 2008 (if unavailable, the average five-year CDS in the beneficiary institution's credit rating category was used)

(State Aid N 613 2008 – pp. 7). As EURIBOR is a widely accepted market benchmark, its inclusion expanded the liquidity for these securities on the secondary market (State Aid N 613 2008 – pp. 7). The rate reflected each participant's risk profile by referencing the CDS spreads for the beneficiary institution while multiplying that spread by five to account for the subordination level of the security (State Aid N 613 2008 – pp. 8). These high rates also motivated beneficiaries to withdraw from the scheme quickly as the rates would likely prove relatively higher than those available in improved market conditions (State Aid N 613 2008 – pp. 8).

An additional feature of the injections was a nominal annual increase of the amount to be redeemed (State Aid N 613 2008 – pp. 8). Similar to the remuneration rate, this yearly increase acted as an incentive to exit the scheme quickly once market conditions improved (State Aid N 613 2008 – pp. 8). Under this arrangement, the nominal amount would increase to 1% if redeemed between the first and second year and to 3% between the second and third year. It then would increase by an additional 2% annually until the seventh year, reaching a maximum of 11% (Conac 2010 – pp. 312-313) (State Aid N 613 2008 – pp. 8).

**12. For the second injection, the CB gave banks the option of issuing TSS or preference shares.**

On January 21, 2009, the French authorities submitted an amended capital injection scheme to the EC (State Aid N 29 2009 – pp. 2). Under this updated proposal, the CB allowed banks to choose between two different securities for the second round of capital injections: the TSS securities approved on December 8, 2008, or newly introduced preference shares (State Aid N 29 2009 – pp. 2-3). These preference shares were on equal footing with ordinary shares in terms of liquidation as well as going concern basis and were not subject to Tier 1 Capital limits due to their core Tier 1 Capital classification (although they were limited to 50% of share capital for unlisted companies and 25% for listed companies) (State Aid N 29 2009 – pp. 3-4). However, the preference shares were non-convertible, non-voting, and had priority for dividend payments over ordinary shareholders (State Aid N 29 2009 – pp. 4). The issuing bank could buy back these shares, subject to the consent of the CB, at the highest of either 110% of the current price of the shares or the 30-day average price of the shares prior to the buyback date (State Aid N 29 2009 – pp. 4).

The CB introduced preference shares during the second round of capital injections due to logistical reasons that centered on Tier 1 Capital limitations (Conac 2010 – pp. 313). Partly due to the first round of injections, most banks had reached the 35% ceiling of Tier 1 Capital imposed on non-core Tier 1 securities, therefore limiting the beneficiaries' ability to issue more TSS (Conac 2010 – pp. 313). The preference shares would solve this issue by increasing Tier 1 Capital overall and subsequently allowing more TSS to be included in the Tier 1 ratio (Conac 2010 – pp. 313). They also allowed banks to increase their Core Tier 1 Capital ratios, which was positive for the banking system over the long-term (State Aid N 29 2009 – pp. 8).

In order to allow participants to take full advantage of the amendment, French authorities gave banks that received the first injection the option of repaying TSS with the proceeds from issuing preference shares (State Aid N 29 2009 – pp. 4). BNP Paribas pursued this strategy by issuing €5.1 billion of preference shares and using approximately half of those funds to repurchase TSS from the first injection (DE LA CRISE FINANCIÈRE A LA CRISE ÉCONOMIQUE – pp. 61).

### 13. The remuneration on preference shares was set higher than TSS.

The remuneration for preference shares issued during the second capital injection was set at the higher of:

i. Entry (fixed) rate for TSS increasing 25 bps annually, applied to the actual number of preference shares.
ii. The rate equal to 105% of the dividend per ordinary share for the 2009 financial year, divided by the unit issue price for preference shares (increasing to 110% for the 2010 financial year, 115% for 2011-2017, and 125% for 2018) (State Aid N 29 2009 – pp. 10-11)

Based on market conditions at the time, the above formulas resulted in an entry rate of 8% (State Aid N 29 2009 – pp.3 ). Although the entry rate was equal to TSS, these rates were deliberately costlier over time to reflect a greater degree of subordination and risk (State Aid N 29 2009 – pp. 11). In comparison to the TSS's average annual return for the first five years, the preference shares remuneration would be higher by at least 0.85% (State Aid N 29 2009 – pp. 11).

### 14. The French government requested and received an additional €500 million into the merged Caisses d'Épargne and Banques Populaires entity.

In addition to adding preference shares to the second injection, the French government increased the budget by €500 million to bolster the merged Caisses d'Épargne and Banques Populaires' Tier 1 ratio by 50 basis points (State Aid N 164 2009 – pp. 2). Although Caisses d'Épargne and Banques Populaires individually received €1.1 billion and €.95 billion, the French authorities felt further capital was required as the merged entities would consolidate all of their risk-weighted assets but only a portion of their share capital (DE LA CRISE FINANCIÈRE A LA CRISE ÉCONOMIQUE – pp. 61) (State Aid N 164 2009 – pp. 5). The EC approved the increase in budget and the merged BCPE entity received the additional €3 billion following its merger on July 31, 2009 (SPPE Annual Report 2010 – pp. 12) (State Aid N 164 2009 – pp. 9).

### 15. The French government amended the terms of the preference shares to further encourage quick redemption.

The French government notified the EC of an amendment to the updated January 28, 2009 scheme on March 16, 2009, prior to any issuance of preference shares under the plan (State Aid N 164 2009 – pp. 1, 5). It created a more powerful incentive for banks to exit the program quickly (State Aid N 164 2009 – pp. 1, 5). The changes were twofold, increasing remuneration and creating a jump in redemption costs on June 30, 2013 (State Aid N 164 2009 – pp. 5-6). The remuneration on preference shares was the higher of two rate formulas (See KDD 13) (State Aid N 29 2009 – pp. 10-11). The amendment modified the first rate, adding the dictated .25% premium from 2009 instead of 2010 (State Aid N 164 2009 – pp. 5).

Previously, banks were able to repurchase their preference shares at the higher of two rates regardless of redemption date (See KDD 12) (State Aid N 29 2009 – pp. 4). The revised plan created a jump in redemption costs on June 30, 2013 through the below structure.

*Prior to June 30, 2013 (highest of the below two values)*

i. The current value increased by the accrued coupon
ii. The average stock market price over the 30 days preceding the repurchase

*Following June 30, 2013 (highest of the below two values)*

i. 110% of the current value increased by the accrued coupon
ii. The average stock market price over the 30 days preceding the repurchase (State Aid N 164 2009 – pp. 5).

**16. Participating banks adopted a number of behavioral commitments in exchange for funds, administered by a Credit Mediator and a unit of the CB that monitored lending at the local level.**

Beneficiaries of the SPPE capital injections were expected to commit to the below behavioral requirements.

i. Limitations on compensation to senior executives and market operators (traders)
ii. Seeking to maintain an annual growth rate of 3-4% of overall lending to the French economy
iii. Performing case-by-case solutions for clients that are struggling to repay certain loans
iv. Striving to finance local authorities' investment requirements
v. Not engaging in unfair practices (such as using the capital-injection as an advertisement)
vi. No repurchasing of shares for the duration of the SPPE's holding of TSS; and
vii. Monthly presentation of a report on lending volume and trends (State Aid N 613 2008 – pp. 8-10)

**It is important to note that the CB did not back the credit monitoring and mediation by sanctions (State Aid N 613 2008 – pp. 10). The CB feared that the threat of punishment could harm the market; instead, it relied on the reputational damage of noncompliance (State Aid N 613 2008 – pp. 10). The CB also did not put limitations on the payment of dividends, only ensuring that the participants prioritized dividend payments to preference shares held by the SPPE over ordinary shareholders (State Aid N 29 2009 – pp. 9).**

The participating banks agreed to restrictions on executive compensation prior to the first capital injection (State Aid N 613 2008 – pp. 8). These limits included banning severance payments to executives of failed institutions or individuals who quit and providing a compensation policy to regulators for "market operators", such as traders (State Aid N 613 2008 – pp. 8-9). According to the Banque de France, in response to this assistance, "In early

2009, the top managers of the country's leading banks unanimously waived their bonuses for 2008" (Annual Report 2008 – pp. 35).

The credit-growth requirement was particularly important, as increased lending to the overall economy was a stated goal of the program, along with enhancing Tier 1 Capital (Annual Report 2009 – pp. 45). To facilitate credit growth and ensure compliance, the CB instituted an oversight framework that aligned with the program, including a national credit mediator that arbitrated issues for companies suffering credit issues (State Aid N 613 2008 – pp. 9). The primary goal of this mediator was to "to ensure that no business had to face its financial problems alone, to ensure that banks lived up to their commitments and to provide information and advice to the government" (Annual Report 2009 – pp. 48). The network of *département*[6]-level BdF heads acted as regional mediators, performing an initial proceeding that prioritized companies struggling in the previous six months, indicating they were victims of the overall economic downturn (Annual Report 2009 – pp. 48) (State Aid N 613 2008 – pp. 9). If the involved parties did not reach a solution either the regional mediator or company could appeal the case to the national mediator (State Aid N 613 2008 – pp. 9). The national credit mediator received 2,500 applications in the first two months of its existence and 20,000 by the end of 2009 with an acceptance rate of 84% (Annual Report 2009 – pp. 48). From the introduction of the program to the end of 2009, the credit mediation mechanism resulted in more than €2 billion in loans to over 9,000 business, safeguarding an estimated 160,000 jobs (Annual Report 2009 – pp. 48).

Additionally, the French government took steps to supervise banks at the local level, ensuring that loan increases aligned with predetermined targets. Two units performed this monitoring, an operational-monitoring unit and *département* committee for financing the economy (CDFE) (State Aid N 613 2008 – pp. 10). The *département préfet*[7] was responsible for constructing the operational-monitoring unit and the regional mediator served on it (State Aid N 613 2008 – pp. 10). The CDFE contained representatives from banking networks in the individual *département*, the OSEO[8], BdF, and other local economic agencies (State Aid N 613 2008 – pp. 10). This committee had three objectives; inform local economic agencies of national level initiatives, evaluate the *département*-level situation to restore the business lending market, and monitoring bank-lending commitments at the local level (State Aid N 613 2008 – pp. 10).

## 17. The application period to receive funds from the SPPE was from December 8, 2008 to August 30, 2009.

Originally, the application period to receive funds was supposed to last for six months, from December 8, 2008 to June 8, 2009, however the CB extended the deadline to August 30,

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[6] The département is a regional level of government in France, there are 96 in the metropolitan area and 5 overseas – more information can be found here

[7] Prefets are officials that represent the state in each département – more information can be found here

[8] The OSEO is a French agency that aims to promote SMEs – more information can be found here

2009 (State Aid N 29 2009 – pp. 9). The extension was due to the requirement that a bank hold an extraordinary general meeting of its shareholders to authorize the issuance of preference shares (State Aid N 29 2009 – pp. 9). The French authorities also cited uncertain market conditions as support for the extended application period (State Aid N 29 2009 – pp. 5).

Banks were able to redeem the TSS or preference shares issued under the scheme at any time, subject to the approval of the CB (State Aid N 29 2009 – pp. 4) (State Aid N 613 2008 – pp. 6).

**18. The CB increased the non-core Tier 1 Capital ceiling to allow banks to participate.**

On November 3, 2008, the CB decided to increase the ceiling of non-core Tier 1 Capital to 35% after some banks already reached the previous limit of 25% (State Aid N 613 2008 – pp. 4) (Conac 2010 – pp. 312). This allowed banks to take full advantage of the capital injections provided by the SPPE (Conac 2010 – pp. 312).

# III. Evaluation

The Banque de France (BdF) found that the interventions it orchestrated were successful (Annual Report 2009 – pp. 45). It argued that, "the streamlined structure" constructed in order to increase own funds allowed the government to customize its actions to support banks (Annual Report 2009 – pp. 45). The BdF also viewed the SPPE and SFEF as instrumental in protecting French banks from liquidity and solvency risks during the turbulence that occurred between September 2008 and March 2009 (Annual Report 2009 – pp. 45).

A number of academic analyses evaluated the SPPE and SFEF intervention. An IMF working paper by Xiao (2009) examined the effect of the French support plans on the financial sector by analyzing market information and balance sheets prior to and immediately following the announcement of both the SPPE (only the first injection) and SFEF schemes (Xiao 2009 – pp. 17). The study found that following the French support plan announcement, banks' credit risk, as measured by credit default swap spreads, decreased substantially. There was a varied impact on equity prices: the gross effect on equity prices was positive, but after controlling for benchmarks and beta (overall market movements), the adjusted impact was negative (Xiao 2009 – pp. 18).

Conac (2010) concluded that the French rescue was an overall success, arguing that even though the French financial sector was relatively less impacted by the crisis, the rescue plan was speedily implemented and ultimately profitable (Conac 2012 – pp. 338). He also cites the French authority's ability to achieve management changes and limitations on compensation, as well as active communications that "promote its agenda on banking regulation and bankers' compensation" (Conac 2012 – pp. 338). Conversely, Conac (2010) found that the major failure of the program was not leveraging the opportunity to pass a law, similar to the laws passed in Germany, which allowed for nationalizing or assuming control over an ailing financial institution (Conac 2012 – pp. 339).

Jabko and Massoc (2012) found that the rescue plan had two unique elements. First, France constructed new entities to take on specific roles during the crisis – the entities did not explicitly bail-out failing firms, instead they provided general support to the entire industry (Jabko and Massoc 2012 – pp. 569). Compared to other countries that engaged in massive rescue plans for near-bankrupt institutions, the SPPE and SFEF provided funds among all major French banks (Jabko and Massoc 2012 – pp. 570). Similarly, the use of preference shares and TSS resulted in an indirect intervention instead of substantial equity stakes in individual banks (Jabko and Massoc 2012 – pp. 570).

Jabko and Massoc (2012) argued that the French authorities requested comparatively little from the beneficiaries in exchange for assistance. They noted that the aid was not compelled; no sanctions were levied; the lack of voting rights for the shares meant the government had no oversight of management; executive compensation limits were not legally binding; and no limitations were placed on dividend payments (Jabko and Massoc 2012 – pp. 571). Due to this relatively moderate approach, Jabko and Massoc (2012) concluded that the plan was "exceptionally generous, beyond the requirements of the situation" (Jabko and Massoc 2012 – pp. 571).

The Cour des Comptes[9] (Court of Audit), the supreme body for auditing the use of public funds in France, issued a 2013 Annual Report that reviewed government interventions during the financial crisis, including the SPPE, in order to provide recommendations going forward (Cour des Comptes 2013 – pp. 23). These recommendations included:

i. Provide an annual statement disclosing the impact of bank support plans, including the SPPE and SFEF, on the French State
ii. Incorporate a breakdown of credit provided to local and regional authorities apart from 'local public administrations' into existing credit report
iii. Integrate a permanent compensation monitoring unit into the Prudential Supervisory Authority, a department of Banque de France, and implement an a priori approach to supervising compensation structures for executives and board members
iv. Implement a provision requiring credit establishments to subject the compensation budgets for executives and board members to an advisory shareholders' vote at a general meeting (Cour des Comptes 2013 – pp. 23).

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[9] More information on the Cour des Comptes (Court of Audit) can be found here

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