STATE AIDS (BANKS): THE GERMAN BANKS CASES

Subject: State aids

Industry: Banking (particularly German banking, though there are substantial implications for banking interests throughout the European Community)

Parties: German banks and special credit institutions

Source: Commission Statement IP/02/634, dated 26 April 2002

(Note. The Commission justly deserves credit for the progress it has made in dealing with the problem of state support for German banks, particularly in the light of Treaty provisions designed to offer some protection for the status quo. For true believers in free competition, the help given by some of the Member States to banks with more national prestige than economic foresight has always gone against the grain; and it seemed to be a step back in time when the original EEC Treaty was amended with the apparent aim of condoning some of the traditional support systems for banks in Germany. It looks as though the Commission is close to an agreement on ways in which competitive conditions will prevail. While not wishing to play down the Commission's success, it has to be pointed out that the transitional provisions are remarkably generous and the exceptions to the termination of the guarantees surprisingly wide.)

"The road is now clear to making the German system of State guarantees for public banks compatible with the State aid rules of the EC Treaty, thereby removing a longstanding distortion of competition at the heart of Germany's and Europe's financial system". In these words the Competition Commissioner Mario Monti commented on the German Government's official and definitive undertaking to implement the agreements reached with the Commission on the two forms of guarantees, the maintenance obligation and the guarantee obligation (see the end of this report for the definitions). To that effect, the German authorities undertook to put in place by the end of 2002 all necessary legislation both at the Federal and at the Provincial level.. The changes concern the Provincial banks, savings banks and special credit institutions.

"After two years of intensive negotiations, we are, at last, on course for a definitive solution to the issue of State aid in the form of guarantees to all of Germany's public banks", Mr Monti commented. "This subject had poisoned for a long time the domestic debate in Germany as well as the climate between the German authorities and the Commission. Germany's acceptance represents a milestone in our efforts to ensure a level playing field in the financial services sector. This development will also be beneficial to the competitiveness of the German and European economy, which requires the allocation of financial resources to be efficient, while certain types of government interventions tend to distort it, as experience has shown repeatedly. The change will not be abrupt, since we have agreed on transitional arrangements. But it will be a significant change, and a salutary one for the German taxpayer, the other German and non-German banks competing in the market, and in the end also for the German public banks themselves. Shielding them from market pressures would not, in the long run, have been in their own interest."

"This case is of great significance particularly in four respects", Mr Monti pointed out: "It shows that the Commission acts against all those forms of State aid, which are incompatible with the EU rules, whether they are in the open or are hidden ones such as guarantees; that we remain vigilant about State support to the banking sector, as we have been already in a number of other cases; that the Commission fulfils its role of guardian of the treaties with equal determination towards all Member States, large and small; finally, that it is perfectly possible to achieve compliance with State rules without putting in question the public nature of undertakings". Mr Monti also paid tribute to the efforts of the negotiating teams on both sides - the German team being headed by State secretary Caio Koch-Weser - who were involved in the highly complex discussions. "This has not been an easy task, not least because it involved both the federal Government and the Provinces, and I salute the efforts made by Germany to conform to State aid rules in such a crucial sector... Without the acceptance by the German authorities of a full and timely implementation of the necessary changes, the Commission would have had to pursue its legal procedure until the end".

The Commissioner recalled the strong initial resistance to the Commission's action, making a reference to further cases involving State guarantees. "It is interesting to note that, once the scope and motivation of our initiative had been fully understood, as well as our determination to ensure compliance with Community law, the public banks themselves came up with the outline of a solution which then became the basis for our discussions with Germany. I hope that this will be reflected upon by our interlocutors in future discussions about similar support schemes in certain other Member States." It is recalled that the Commission recently took the first step to bring the Austrian system of State guarantees in favour of certain public banks into line with the Treaty rules and that guarantee schemes in other Member States are currently being examined to determine whether they must also be altered or discontinued. It is also recalled that enforcement of State aid rules in the banking sector already took place in several cases, in particular concerning French and Italian banks.

Background

After starting negotiations in February 2000, the Commission adopted a decision on 8 May 2001, proposing to the German Government so-called "appropriate measures" to make the guarantee systems compatible with the State aid rules of the EC Treaty. In July 2001, the German authorities fully accepted the proposed appropriate measures, on the basis of an understanding between Commissioner Monti and State-Secretary Koch-Weser on the key principles of a solution as well as on the process and the timing, including transitional arrangements. Further discussions were, however, necessary to clarify important aspects, in particular regarding the application of State aid rules to the special credit institutions and the "grandfathering" of the guarantee obligation. After these had been successfully concluded, the Commission on 27 March 2002 amended its above-mentioned decision to reflect fully the measures to be taken by Germany, as agreed by the Commission. Germany in turn formally accepted on 11 April 2002 this new Commission decision. Provided the measures are correctly implemented, this acceptance puts an end to the State aid case.

Reminder of the main changes to the guarantee system

For provincial banks and savings banks, the guarantee obligation will be abolished; and the maintenance obligation will be replaced by a normal owner relationship between the owner and the public financial institution concerned. Liabilities existing on 18 July 2001, the date of acceptance by the German authorities of the Commission's recommendation of 8 May 2001, will continue to be covered by the guarantee obligation until their maturity runs out. There will a transitional period which will last until 18 July 2005, during which the maintenance and guarantee obligations can be kept in their present form. On the final date of this transitional period any liability still existing then and created after 18 July 2001 will continue to be covered by guarantee obligations on condition that its maturity does not go beyond 31 December 2015.

As regards special credit institutions, [here the Commission's Statement is unintelligible, but appears to mean that:] the use of advantages peculiar to the maintenance guarantee and other State guarantees relevant to the State aid rules is allowed for the performance of promotional tasks at the request of the State in certain areas such as the financing of small and medium-sized enterprises, infrastructure, environment-friendly investment, housing as well as co-operation with developing countries. Promotional tasks are to be specified in the legal texts. The activities of the special credit institutions, which are not in line with the State aid rules, must be either discontinued or hived off to legally independent subsidiaries without State support. The time limit for prescribing the legally binding legislative framework for special credit institutions (such as the promotional exceptions) is 31 March 2004. The hiving off must be achieved by 31 December 2007; and, in the interest of capital markets, the understanding makes clear that the application of the general State aid rules to an individual promotional activity will not have an effect on the continuance of the State guarantees as such.

Definitions

The "maintenance obligation" (*Anstaltslast*) means that the public owners (such as the Federal State, the Provinces and the municipalities) of the institution are responsible for securing the economic basis of the institution and its function for the entire duration of its existence. The obligation does not confer any rights on creditors. The "guarantee obligation" (*Gewährträgerhaftung*) on the other hand, confers a right on creditors. It stipulates that the guarantor will meet all liabilities of the bank, which cannot be satisfied from its assets. Neither guarantee is limited in time or in amount. Also, the credit institutions do not have to pay for them. ■