THE CREDIT CRISIS AND THE COMMUNITY EFFORTS TO DEAL WITH IT

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Abstract: *The article provides a brief overview of the role of State aid control during the credit crisis. Throughout this period the Commission has played an impressive role in applying the EU state aid rules with an unprecedented speed. The Commission has done this by approving a great number of individual state aid measures on the one hand, and by issuing general measures in the form of several specific communications. There is no doubt that the control of state aid has had a positive effect on the competitive conditions in the banking sector. The Commission's decisions also give rise to some more critical comments. These decisions have had a major impact on the beneficiary banks, especially because of the conditions that were imposed on them. The Commission's action raises important issues of legal protection, which will be discussed in this article. It is far too early in the day to provide a clear picture of the question whether due process has been duly observed by the Commission. Appeals of the decisions have only just been lodged, thus it will take several years before the view of the Community courts will provide answers.*

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1. INTRODUCTION

The credit crisis continued in 2009 although it abated somewhat in the second half of that year. In 2010 we seem to be on the way to a modest recovery. In particular, Germany shows an export driven recovery. Nevertheless, the massive state aid operations that were undertaken by the Member States have resulted in an intensive effort in Brussels to control the effects thereof. It will take quite a while before the dust of this major operation has settled.

This article will provide a brief overview of the role of State aid control for the financial sector.[2] Throughout this period the Commission has played an impressive role in applying the EU state aid rules with an unprecedented speed. The Commission has done this by approving a great number of individual state aid measures, on the one hand, and by issuing general measures in the form of several specific communications. There is no doubt that the control of state aid has had a positive effect on the competitive conditions in the banking sector.

The Commission's decisions also give rise to some more critical comments. These decisions have had a major impact on the beneficiary banks, especially because of the conditions that were imposed on them. Therefore, the Commission's action raises important issues of legal protection which will be discussed in this article. It is far too early in the day to provide a clear picture of the question whether due process has been duly observed by the Commission. Appeals of the decisions have only just been lodged thus it will take several years before the view of the Community courts will provide answers. These issues will be discussed in Section 4.

2. BACKGROUND

In September 2008, some major financial institutions in the USA (in particular Lehman Brothers), Germany, Ireland[3] and the UK defaulted. This had an unexpectedly rapid knock-on effect on the banking system in Europe. In the weekend of 27 and 28 September, the Belgian and Dutch ministers of finance met in an effort to avert the imminent collapse of the Fortis bank. Both governments provided an important capital injection,

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2 For a brief general overview see the article by Commissioner Neelie Kroes (until January 2010 responsible for competition policy): Kroes, 2010.

3 The Irish government's unilateral decision to offer full guarantees to all bank creditors was widely criticized in particular in the UK for forcing the hand of other Member States and undermining the solidarity across the EU.

which was agreed in close coordination with the Belgian and Dutch central banks. Soon thereafter the Dutch part of Fortis and ABN AMRO was nationalized. The following weekend, the Belgian and French governments met to discuss the problems of Fortis, Dexia and BNP. In the weekend of 11 and 12 October 2008, the French President Nicolas Sarkozy invited the heads of government of the Euro-group and the President of the European Central Bank to a meeting in Paris to discuss the banking crisis; this group is after all responsible for maintaining the value of the euro. He also invited the British Prime Minister Gordon Brown for a brief meeting before the actual talks within the Euro-group commenced. In the end, Gordon Brown was also invited to stay and participate in the Euro-group talks. The main outcome of the meeting was an agreement among the participating Member States to provide guarantees for their national banking sector. Three large Member States, the UK, France and Germany pledged 450 billion, 320 billion and 400 billion. Other Member States made equally impressive pledges. At that time there were no Community funds involved. Later the Commission proposed funds to be made available to the financial sector. A day later, on 13 October, the Commission called a meeting for competition policy experts in an attempt to build a consensus for the application of the competition policy rules. The application of the state aid rules was a necessary complement to the national measures propping up the financial viability of their banks.

3. STATE AID

3.1. Introduction

In the past two years the Commission has approved a large number of rescue operations for banks.[4] The Commission did so after an unusually short expedited examination period.[5] Some decisions were adopted in two days. The

4 The Commission provided a first overview in the IP of 4 Dec. 2008, "State aid: Overview of national rescue measures and guarantee schemes". Such overviews are published regularly on the website of DG Comp.

5 It should be recalled that the preliminary examination period for notified State aid according to Article 4(5) of Reg. 659/1999 is 2 months. The formal investigation period is another 18 months, which may be extended by common agreement according to Article 7(6) of Reg. 659/1999. Given their impact on competition and their complexity, the decisions in the financial sector would normally have been taken only after the opening of the formal procedure. By contrast, the decisions on the financial crisis were taken within 2 weeks: Decision K(2008) 6422, N 512/2008, Credit institutions in Germany; C(2008) NN 48/2008, Guarantee scheme for banks in Ireland; C(2008) 6616, N 524/2008, Guarantees for banks in the Netherlands. The decision in the case of C(2008) 6936, N 528/2008 Aid for the ING Bank was taken after 3 weeks, because additional information was needed. Other decisions were adopted within 2 days: e.g.

Commission's special task force for State aid in the financial sector worked flat out, including the weekends, during the autumn of 2008. Afterwards, it also adopted several communications. The following section 3.2. will give an overview of the Commission's general measures. Section 3.3. will discuss the Commission's individual decisions.

3.2. The Commission's general measures

Between October 2008 and July 2009, the Commission adopted a series of general measures tackling the specific issues in the context of the credit crisis and in particular the financial sector. The Commission continues to review and adapt the regime in accordance with the development of the economic situation.[6] The general measures are summarized below in chronological order. They provide valuable insights on how the Commission intends to apply the state aid rules to Member States' measures aimed at supporting the financial sector in the credit crisis.

On 13 October 2008, the Commission adopted the Communication on the application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis (the "Banking Communication").[7] The priority then was to restore the confidence and proper functioning of the banking sector, as the interbank lending market collapsed after the fall of *Lehman Brothers*. In the Banking Communication, the Commission laid down basic rules and principles to evaluate the compatibility of government measures in the financial sector with the

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C(2008), N 507/2008, Financial support measures to the Banking industry in the UK; C(2008), N 533/2008, Support measures for the banking industry in Sweden; C(2008) 6989, N 567/2008, Guarantee scheme for banks in Finland. Some measures were not notified i.e. Denmark case NN 51/2008, OJ 2008, C 273/2, but approved after the Commission contacted the Danish Government. The Commission approved, originally not notified, State aid for Irish banks in decision C(2008) 6059, NN 48/08. After intensive contacts with the Commission, the Irish authorities submitted the finalized scheme on 12 Oct., addressing issues raised in the discussions (see MEMO/08/615). The Commission found the revised scheme to be compatible with EU State aid rules, because it was an appropriate means to remedy a serious disturbance in the Irish economy (Art. 87(3)(b) EC), while avoiding unnecessary distortions of competition. In particular, it now provides for non-discriminatory access to banks with systemic relevance for the Irish economy, regardless of their origin, fair remuneration of the guarantee, is limited in time and contains appropriate safeguards to avoid abuses. The Irish measures are therefore now in line with the guidance just issued by the Commission (see IP/08/1495).

6 The Commission sent two questionnaires to the Member States concerning the application of the Temporary Framework in July 2009 and March 2010. It also began to prepare the phasing out of government guarantee rules. See the working document of DG Competition published on 30 April 2010: the application of state aid rules to government guarantee schemes covering bank debt to be issued after 30 June 2010.

7 Adopted on 13 October 2008 and published on 25 October 2008, OJ C 270, p. 8–14.

requirements of Article 107(3)(b) of the Treaty on the Functioning of the European Union (TFEU). The scope of the government measures includes aid in the form of guarantees, recapitalization, controlled winding-up of the financial institutions and the provision of other forms of liquidity assistance. Procedurally, all approvals are subject to the condition of review after six months. Member States have to submit a report for that purpose which should indicate a clear path towards exit from reliance on state aid.

On 5 December 2008, the Commission adopted the Communication on the recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition (the "Recapitalisation Communication").[8] Many Member States considered using capital injections to ensure the "lending to the real economy"[9] and the injection measures varied widely in nature, form and conditions. The Recapitalisation Communication intended to address the demand from the Member States and individual beneficiaries for further guidance on the compatibility of those measures with the competition rules. In the meantime, it built on and continued to develop the principles indicated in the Banking Communication. The Commission's approach follows the well-known principles of the guidelines for rescue and restructuring.[10] The Recapitalisation Communication is in line with the recommendations of the European Central Bank. It is based on the principle that State support for banks should not provide the recipients of aid with an artificially advantageous competitive position over banks not receiving aid. The legal basis for the communication is also Article 107(3)(b) TFEU[11], "aid to remedy a serious disturbance in the economy of a Member State". The procedural conditions follow those of the "Banking Communication." The approval is subject to the

8 Adopted on 5 December 2008 and published on 15 January 2009, OJ C 10, p. 2-10.

9 Recapitalisation Communication, paragraph 3.

10 OJ 2004, C 244/2.

11 The Commission has used Article 107(3)(b) as a legal basis before. The dismal performance of the Italian economy in the early 1970's prompted the Commission at the time to authorize the Italian government to grant "conservation aid" under Article 87, paragraph 3(b) to firms facing grave problems (see Second Report on Competition Policy, April 1972, pts. 120 and 123). Similarly, when as a result of the oil crisis of 1973 all Member States were hit by a severe economic recession, during the following years - and with the Commission's blessing - substantial aid programs were implemented in order to allow important industrial sectors (shipbuilding, textiles etc) to tide over the crisis (Fifth Report on Competition Policy April 1976, pts. 130-133). To our knowledge, since that period no further use has been made of the derogation provision of paragraph 3(b) in relation to conjunctural aid measures.

condition of review after six months. Member States have to submit a report for that purpose.

On 17 December 2008, the Commission adopted the Communication on the Temporary framework for State aid measures to support access to finance in the current financial and economic crisis (the "Temporary Framework").[12] While the previous communications addressed to specific issues in banking sector, the Temporary Framework set out a general regime for a coordinated European approach for national subsidy measures to all sectors. It implemented the general principle indicated in the European economic recovery plan.[13] As the impact of the economic crisis continued to unfold and spread, the Commission recognized the delicate balance between ensuring "maximum flexibility for tackling the crisis while maintaining a level playing field and avoiding undue restrictions of competition" [14] and the importance to ensure the sufficient and affordable access to finance. The Temporary Framework lists the existing instruments specifying compatible aids. Moreover, it provides more flexible and simplified rules for Member States to grant aid under higher limits on grants, credit guarantees, loans and risk capital. Subsequently, the Commission amended the limits in the Temporary Framework in February, October and December 2009. It also conducted consultations for the necessity of the application of the Temporary Framework in July 2009 and March 2010.[15]

On 25 February 2009, the Commission adopted the Communication on the Treatment of impaired assets in the Community banking sector (the "Impaired Assets Communication").[16] The State guarantees and recapitalisation measures adopted so far were yet to improve the lending market and the investors' confidence. The evaluation and location of the impaired assets was identified as one of the essential elements for restoring confidence. In addition, there were also the longer-term considerations to ensure the viability and budgetary sustainability of the banking sector. The

12 Adopted on 17 December 2008 and published on 22 January 2009, OJ C 16, p.1; consolidated version published on 7 April 2009, OJ C83.

13 Communication from the Commission to the European Council, COM(2008) 800.

14 Section 1.1, the Temporary Framework.

15 See the website of DG Competition for further details: http://ec.europa.eu/competition/recovery/publications.html.

16 Adopted on 25 February 2009 and published on 26 March 2009, C 72, p. 1-22.

Impaired Assets Communication provides guidance on the States assets relief measures. It is based on the principles of transparency and disclosure, adequate burden-sharing between the State and the beneficiary and prudent valuation of assets based on their real economic value. It also established the same supervision, review and report procedure as the previous communications.

On 23 July 2009, the Commission adopted the Communication on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules (the "Restructuring Communication").[17] It complements the previous three communications: the Banking Communication, the Recapitalisation Communication and the Impaired Assets Communication. Together they establish the foundation for the assessment of State intervention under State aid rules in the context of economic crisis. After all, the subsidies are temporary measures for urgent circumstances and the ultimate goal is to restore the long-term viability of the financial sector without State support. The Restructuring Communication clarifies the requirements for the restructuring aid, in particular the need to have adequate burden sharing between the bank, its shareholders and the State, and stressed that the measures should minimise the distortion of competition.

However, the Restructuring Communication seems to lose sight of a crucial distinction. It no longer makes a clear distinction between banks that are fundamentally sound and those that are not. The Commission seems to jump immediately to the conclusion that restoration of long-term viability will for *all banks* have to include restructuring. It should be stressed that restoring long-term viability does not necessarily require restructuring. Whereas before the financial crisis a certain level of viability would have been sufficient, this level will now have to be raised. Accordingly, the financial viability of the banks that do not meet the new standards will have to be upgraded. The aid exempted by Article 107(3)(b) is designed to help the banks to meet this new standard. Once this standard has been reached the viability will be restored. It is therefore remarkable that the Restructuring Communication seems to equate such restoration viability with restructuring such as a break-up or absorption by another bank. It is by no means self evident that restoration of viability will have to lead to restructuring.

17 Adopted on 23 July 2009 and published on 19 August 2009, OJ C 195, p. 9.

Another important feature of the Commission's communications is the shift in methodology. The rescue and restructuring rules only provided for structural conditions. By contrast, the Restructuring Communication provides for structural as well as behavioural conditions.[18] This is also borne out in the individual decisions discussed in the next section.

3.3. The Commission's individual decisions

3.3.1. *Introduction*

During the past two years, the Commission has taken a large number of decisions in individual cases. As speedy approval was essential, the Commission took most of these decisions under Article 108(3) TFEU that is the preliminary procedure. These decisions normally provided that the Member State had to submit a restructuring plan within six months. The follow-up decisions have been taken under the formal procedure of Article 108(2) TFEU. From a substantive perspective, the decisions have been taken under Article 107(3)(b) TFEU. As will be explained below, this legal basis for taking exemption decisions has only been used once in the past, the usual legal basis is Article 107(3)(c) TFEU.

According to the latest public available statistics, between October 2008 and 31 March 2010, the Commission took 161 decisions for the financial sector based on Article 107(3)(b) TFEU. Among those, 78 decisions were related to approximately 40 financial institutions and 83 decisions were related to approximately 40 schemes.[19]

The amount involved in the measures is also significant. The latest published figure of the total Member States' measures approved by the Commission in the period of the financial crisis is € 4 131.1 billion. It includes schemes and ad hoc interventions. The Commission also provided a breakdown into schemes and ad hoc cases as follows:[20]

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18 Jaeger, 2010: 578-579.

19 See the Report on recent developments on crisis aid to the financial sector - Spring 2010 Update, 26 May 2010, COM(2010) 255.

20 See the Report on recent developments on crisis aid to the financial sector - Spring 2010 Update, 26 May 2010, COM(2010) 255.

	Amount	% of EU-27 GDP[21]
Schemes aproved by the Commission:	3 181 billion EUR	25 %
Of which guarantee schemes	2 747 billion EUR	22 %
Of which recapitalisation measures	338,2 billion EUR	2,7 %
Of which asset relief interventions	54 billion EUR	0,4 %
Of which liquidity measures other than the guarantee schemes	41,9 billion EUR	0,3 %
Ad hoc interventions in favour of individual financial institutions	950,1 billion EUR	7,6 %

As will be clear from the above summary, it is impossible to even try to give an overview of the Commission's individual decisions. Instead, this section will discuss the Commission's approach in taking individual decisions. It will do so by discussing one individual decision in particular. This approach provides insight into the detailed nature of the Commission's intervention. It will very briefly mention some other decisions.

3.3.2. *Some individual decisions*

In the fall of 2009, the Commission adopted several decisions on the restructuring of major banks, ING, discussed below in more detail, Lloyds[22], KBC[23] and Northern Rock[24]. Earlier the Commission approved aid for the Royal Bank of Scotland[25] and Landesbank Baden-Wuertenberg.[26] All measures concerned the injection of one tier capital and recapitalisation involving several billions. The measures were approved after an adequate restructuring plan had been submitted. They were assessed along the lines of the Commission's communication on impaired assets. In all cases the approval was subject to important conditions. Often in the form of divestitures and

21 GDP by Member State, in € million, 1992-2008.

22 N 428/2009.

23 N 602/2008, N 360/2009 and C 18/2009.

24 C 14/2008.

25 N 422/2009 and N 621/2009.

26 C 17/2009. See on these measures Casteele, 2010.

the hiving off of non-core business activities. The restructuring measures also addressed excessive pre-crisis expansion.

3.3.3. *The Commission decision on ING's Illiquid Assets Back Facility and restructuring plan*[27]

FACTS

In order to understand this very complex state aid operation, it is important to understand that the ING state aid operation consisted basically of two measures taken by the government of the Netherlands. First, in the context of the turmoil on the financial markets in September/October 2008, the Dutch State injected, on 11 November 2008, EUR 10 billion of Core Tier 1 capital (the "CTI Transaction") in ING. This aid measure was provisionally approved by the European Commission on 12 November 2008 for a period of six months. The validity of the measure was automatically prolonged with the submission of a restructuring plan, until the Commission reached its decision on the plan.

Second, in January 2009, the Dutch State agreed to take over the economic risk relating to a part of some of ING's impaired assets. This measure was provisionally approved by the European Commission on 31 March 2009 (the "IA measure"), whereby the Dutch State committed itself to submit a restructuring plan concerning the applicant.

In October 2009, ING and the Dutch State concluded an amendment to the original CTI transaction in order to allow an early repayment of half of the CTI capital injection. A final version of ING's restructuring plan was submitted to the Commission on 22 October 2009. For obvious reasons the restructuring plan comprised both state aid measures.

On 18 November 2009, the Commission adopted a decision in which it approved the aid for ING's illiquid assets back-up facility, subject to the restructuring commitments listed in Annex I and II of the decision. Annex II contains the most important conditions and will therefore be cited in full below. Only in this way the reader will be able to fully appreciate the impact of the conditions to which the approval of the aid was subjected.

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27 No C 10/2009 of 18.11.2009. The facts have been taken from the website of DG COMP/State aid/cases. The Commission has taken five decisions in connection with the two state aid measures.

Annex II to the Commission decision of 18.11.2009 on the state aid No C 10/2009 implemented by the Netherlands for ING's Illiquid Assets Back-Up Facility and Restructuring Plan[28]

"As regards the restructuring aid the following commitments have to be respected:

a) As regards balance sheet reductions, the commitment for divestment of insurance, ING Direct US and other units to be divested before end of 2013:

- ING will reduce 45% of its balance sheet compared to 30 September 2008 by the end of 2013 and will divest a list of units as described in point 57, in particular Insurance and ING Direct US, [...].
- These figures refer to projections that do not take into account the possible impact of organic growth and exclude additional increases due to potential new regulatory requirements, such as for example if banks are required to hold significantly larger liquidity buffers due to new EU-wide regulations. Such requirements could increase the balance sheet significantly beyond the current organic growth projections.
- ING will not have a restriction on organic (that is to say not related to acquisitions) growth of the balance sheet of its businesses. [...]. In the future, ING will have a general policy to use its growth in funds entrusted by customer mainly to grow in lending to the real economy (corporates and consumers) and decrease its exposure to higher risk asset classes within US CMBS and US RMBS. [...].[29]
- With respect to units ING commits to sell (as listed in recital 57), if a divestment of any such unit has not taken place by 31 December 2013 (for example on the basis of a final binding sale agreement having been entered into), the Commission may where appropriate or due to exceptional circumstances, in response to a request from the Netherlands, grant an extension of this time period.[30] The Commission may also in such a case (i) request the Netherlands to appoint one or

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28 Published at the Website of DG Comp under the case number. Note this is the Non Confidential version. For obvious reasons the more interesting and revealing confidential version is not available.

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30 In particular, whenever a divestment is being undertaken by an IPO process which has commenced and significant (30% or more) share placements have been made prior to the end of the divestment period, the Commission (in consultation with the Netherlands, ING and the Trustee) shall actively consider allowing the entity more time to place remaining shares.

more (divestiture) trustee(s)[31], preselected and proposed by ING (and subject to the Commission's approval), […].
- Whenever the Netherlands seeks an extension of a time period, it shall submit a request to the Commission no later than one month before the expiry of that period, showing good cause. In exceptional circumstances, the Netherlands shall be entitled to request an extension within the last month of the time period.

b) The Netherlands furthermore commits that ING will adhere to an acquisition ban:

- ING will refrain from acquisitions of financial institutions for a certain period. These commitments will apply for the shorter period of three years starting from the date of the Commission decision or up to the date on which ING has fully repaid the Core-Tier 1 securities to the Netherlands (including the relevant accrued interest of Core-Tier 1 coupons and exit premium fees). ING will also refrain, for the same period, from any (other) acquisition of businesses that would slow down the repayment of the Core-Tier 1 Securities to the Netherlands.
- Notwithstanding this prohibition, ING may, after obtaining the Commission's approval, acquire businesses, in particular if this is essential in order to safeguard financial stability or competition in the relevant markets.

c) The Netherlands furthermore commits that ING will adhere to a price leadership ban:

- Without prior authorization of the Commission, ING will not offer more favourable prices on standardized ING products (on markets as defined below) than its three best priced direct competitors with respect to EU-markets in which ING has a market share of more than 5%.
- This condition is limited to ING's standardized products on the following product markets: (i) retail savings market, (ii) retail mortgage market, (iii) private banking insofar it involves mortgage products or saving products or (iv) deposits for SME's (SME defined according the definition of SME as customarily/currently operated by ING in its business in the

31 It is accepted that different trustees may be appointed with respect to different regions and/or business.

relevant country). As soon as ING becomes aware of the fact that it offers more favourable prices for its products than its three best priced competitors, ING will as soon as possible adjust, without any undue delay, its price to a level which is in accordance with this commitment.

- This condition will apply for three years starting from the date of the present Decision or up to the date on which ING has fully repaid the Core-Tier 1 securities to the Netherlands (including the relevant accrued interest of CT1 coupons and exit premium fees), whichever is shorter. A monitoring trustee preselected and proposed by ING, will be appointed by the Netherlands to monitor this condition. The monitoring trustee is subject to the Commission's approval.
- Moreover, to support ING's long-term viability, ING Direct will refrain, without prior authorisation of the Commission, from price-leadership with respect to standardised ING products on the retail mortgage and retail savings markets within the EU, for the shorter period of three years from the date of the present Decisions or up to the date on which ING has fully repaid the Core-Tier 1 securities to the Netherlands (including the relevant accrued interest of Core-Tier 1 coupons and exit premium fees). As soon as ING becomes aware of the fact that it has become the price leader on a retail mortgage or retail savings markets within the EU, ING will adjust its price to a level which is in accordance with this commitment as soon as possible without any undue delay.
- A monitoring trustee preselected and proposed by ING, will be appointed by the Netherlands to monitor this condition. The monitoring trustee is subject to the Commission's approval.

d) The Netherlands commits to a number of detailed provisions as regards the carve-out of WUH/Interadvies:

- ING will create a new company for divestment in the Netherlands, which will be carved out from its current Dutch retail banking business. The result has to be that this carved-out new company is a viable and competitive business, which is stand-alone and separate from the businesses retained by ING and that can be transferred to a suitable purchaser. This new company will comprise the business of the WUH/Interadvies banking division, which is currently part of the Dutch insurance operations, and the Consumer Credit Portfolio of ING Bank. WUH/Interadvies is an ING business unit under the umbrella of

Nationale Nederlanden Insurance unit. It is (predominantly) a mortgage bank operating on the basis of its own banking licenses. It is a viable 'standalone' player, having its own sales force for customer service and an independent organisation with a solid underlying income. The carve-out will be carried out under the supervision of the Monitoring Trustee in cooperation with the Hold-separate Manager. In this context, during the carve-out period, the Monitoring Trustee may recommend to ING such inclusions into the Divestment Business of tangible and intangible assets (related to the Divestment Business) as he considers objectively required to ensure full compliance with ING's above mentioned result oriented obligations and in particular the viability and competitiveness of the divestment business. If ING disagrees with the Monitoring Trustee about the objective requirement to include such tangible or intangible assets to ensure the viability and competitiveness of the Divestment Business, ING shall inform the Monitoring Trustee in writing. In such a case, ING's executive management and the Monitoring Trustee shall, within […], hold a meeting with a view to reaching a consensus. If no consensus is reached, ING and the Monitoring Trustee shall jointly appoint, without undue delay, an independent third party with expertise in the financial sector (the "Expert") to hear the parties' arguments and mediate a solution. If no such solution is reached, the Expert shall decide, within […] from its appointment, on the objective requirement to include the relevant related tangible or intangible assets into the Divestment Business to ensure its viability and competitiveness, and the parties shall accept the Expert's decision in this respect and will act accordingly. Issues relating to a disagreement shall be mentioned in the report of the Monitoring Trustee to the Commission.

- ING is committed to ensuring optimal divestment conditions by making a business plan, creating an internet platform and dedicating sales capabilities for the carved out entity. Also, it will make payment capability available (on commercial terms) if the buyer so requests. In addition, ING will assist in creating a Treasury function and ensure funding for two years post-divestment, whereas ING's funding support will gradually decline in those two years. ING's funding support to the WUH business will be based on internal funding transfer prices. ING intends to apply to the Netherlands for State guaranteed funding up to an amount of EUR […] billion for the funding of the WUH business.

In that case, the Dutch authorities commit to notify this measure separately.

- Moreover, ING will refrain for an interim period […] from actively soliciting customers of the WUH business for products that the WUH-business is supplying to these customers on the date of adoption of the present Decision.
- ING will seek to carve-out the WUH business […]. After the carve-out period […], ING will hold-separate the WUH business and seek to divest this business […][32].
- A monitoring trustee and hold-separate manager will be appointed within […] after the date of the present Commission Decision […] and a Divestiture trustee will be appointed […]. All trustees will be appointed by the Netherlands and preselected and proposed by ING. The trustees are subject to the Commission's approval.

e) The costs of all trustees appointed during the restructuring process will be borne by ING.

f) For restoring viability, the Netherlands commits that ING will adhere to the following:

- ING commits to orientate its non-deposit funding towards longer term funding once markets revert to less stressed conditions by issuing more debt instruments with a maturity more than 1 year. […].
- ING endeavours to eliminate its double leverage (using core debt as equity capital in its subsidiaries) as soon as possible and commits to do so at the latest by […]. The double leverage is automatically eliminated if and when ING Group reverts to being a regulated bank.

g) Regarding the deferral of coupons and calling of Tier 1 and Tier 2 securities the Netherlands commits that ING will adhere to the following:

- If a rights issue of more than is needed to repay 50% of the Core Tier 1 securities, including the relevant accrued interest and the exit premium fee, ING will not be obliged to defer coupon payments on hybrids on 8 and 15 December 2009[33] and any coupon payments on hybrids thereafter.

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32 […]

33 Provided that it is clear that part of the proceeds of the rights issue will be used for the coupon payments.

- If such a rights issue does not take place and ING was loss-making in the preceding year, ING will be obliged to defer hybrid coupons, insofar as ING has the discretion to do so, for the three years starting from the date of the Commission decision or up to the date on which ING has fully repaid the Core- Tier 1 securities to the Netherlands (including the relevant accrued interest of Core-Tier 1 coupons and exit premium fees), whichever is shorter.
- The Dutch authorities understand that the Commission is against State aid recipients remunerating own funds (equity and subordinated debt) when their activities do not generate sufficient profits[34] and that the Commission is in this context in principle against the calling of Tier 2 capital and Tier 1 hybrids. ING regrets the misunderstanding regarding the calling of a lower Tier 2 bond on 14 October 2009. The calling of Tier 2 capital and Tier 1 hybrids will in the future be proposed case by case to the Commission for authorisation, for the shorter period of three years starting from the date of the present Decision or up to the date on which ING has fully repaid the Core-Tier 1 securities to the Netherlands (including the relevant accrued interest on Core-Tier 1 coupons and exit premium fees).

h) The Netherlands commits that ING will refrain from mass marketing invoking the recapitalisation measure as an advantage in competitive terms.

i) The Netherlands commits that ING will maintain the restrictions on its remunerations policies and marketing activities as previously committed to under the agreements concerning the Core-Tier 1 securities and illiquid assets back-up facility.

j) ING and the Netherlands commit that the progress report about the implementation of the restructuring plan will be provided every six months to the Commission as of the date of the present Decision.

k) The Dutch authorities commit that the full execution of ING's restructuring will be completed before the end of 2013."

34 See paragraph 26 Commission Communication on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under State aid rules (Restructuring Communication).

APPEALS

The Commission decision has been appealed by the Netherlands government, as well as by ING respectively (case T-29/10 and T-33/10). The General Court has joined the two cases. The Central Bank of the Netherlands has intervened in the second case. In view of the intensive involvement of the Central Bank during the procedures, it is surprising that the Commission objected to the intervention. The President of the third chamber of the General Court ruled, in very clear language, that the intervention of the Central Bank is admissible.[35]

ING raised the following pleas[36]:

By means of its application, the applicant seeks partial annulment of the decision of 18 November 2009 on the state aid No C 10/2009 (ex N 138/2009) implemented by the Netherlands for the applicant's Illiquid Assets Back-Up facility and Restructuring Plan insofar as it allegedly (i) qualifies the amendment to the CTI transaction as additional aid in the amount of EUR 2 billion, (ii) has subjected the approval of the aid to the acceptance of price leadership bans and (iii) subjected the approval of the aid to restructuring requirements that go beyond what is proportionate and required under the Restructuring Communication.

The applicant submits that the contested decision should be partially annulled on the following grounds:

On the basis of its first plea, relating to the amendment to the CTI transaction, the applicant claims that the Commission:

(a) infringed Article 107 TFEU, in finding that the amendment to the Core Tier transaction between the applicant and the Dutch State constituted State aid; and that it

(b) infringed the principle of care and Article 296 TFEU resulting from a failure to carefully and impartially examine all the relevant aspects of the individual case, to hear the persons concerned and to provide adequate reasoning for the contested decision.

On the basis of its second plea, relating to the price leadership ban for ING and ING Direct, the applicant submits that the Commission:

35 Order of 14 July 2010. The order of the president of the third chamber of the General Court notes that the Central Bank has a clear interest in the issues raised in the appeal.

36 The text is taken from DG Comp's website: http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_C10_2009. The Dutch government raised similar arguments.

(a) infringed the principle of sound administration as a result of not having carefully and impartially examined all relevant aspects of the individual case and that it moreover violated the duty to provide adequate reasoning for the decision;

(b) infringed the principle of proportionality by making the approval of the aid measure conditional upon price leadership bans which are not adequate, necessary or proportionate;

(c) infringed Article 107(3)(b) TFEU and misapplied the principles and guidelines set out in the Restructuring Communication.

On the basis of its third plea, relating to disproportionate restructuring requirements, the applicant contends that the decision is vitiated by:

(a) an error of assessment, since the Commission wrongly calculated the absolute and relative aid amount and violated principle of proportionality and sound administration by requiring excessive restructuring without having carefully and impartially examined all the relevant facts provided to it; and

(b) an error of assessment and inadequate reasoning by deviating from the Restructuring Communication when assessing the required restructuring.

4. PROCEDURE AND LEGAL PROTECTION

4.1. Introduction

In order to understand the application of the exemptions of Article 107(3) TFEU, it is important to remember that this provision allows the Commission a considerable margin of discretion. This is reflected in the words "may be considered compatible with common market" in the heading of this provision.[37] The Commission has in the course of its decisional practice based on the exemptions of Article 107(3) TFEU gradually developed criteria for applying the provisions of this Article. These criteria have subsequently been tested before the ECJ and more recently also the CFI. On the basis of these tested criteria the Commission subsequently drafted Communications providing guidance. These have normally been discussed with the Member States and provide therefore the framework for the application of the exemption provisions of Article 107(3) TFEU. It is important to remember that communications do not have the same status as legislation. Communications bind the Commission but it retains the power

37 Paragraph 17 of the ECJ judgment in case 730/79 Philip Morris v. Commission.

to amend or repeal them. Communications cannot impliedly be amended by the Commission.[38] Member States are bound by Communications in so far as they agreed to their contents. Communications are subject to review by the Community courts as to their compatibility with primary Community law, secondary law, as well as with the general principles of Community law.

The recent application of state aid rules in the banking sector is based on Article 107(3)(b) TFEU. It is important to note that there is no body of case law defining the relevant criteria to be applied under this provision. The initial approach of the Commission was to adapt the existing rescue and restructuring (r&r) rules developed under the provision of Article 107(3)(c) TFEU to the new situation. In its first two Communications, it noted that the exemption of Article 107(3)(b) TFEU shall only apply to illiquid but otherwise fundamentally sound financial institutions. Aid to banks not satisfying this criterion will be assessed under the rescue and restructuring communications. The r&r communication addresses situations where an individual firm is no longer able to compete in the market. It is rescued because the continuation of the firm serves to save jobs in sectors or regions with serious unemployment. Therefore the r&r guidelines provide for restructuring operations. Restructuring is necessary because otherwise the firm would go bankrupt or would have to receive disproportionate amounts of aid causing distortion of competition. By contrast, aid designed to remedy a serious disturbance in a sector of the economy is intended to raise the general level of standards applicable in the industry. That calls for raising sector wide standards rather than measures designed to increase the performance of the individual firm. Sector wide standards are by their very nature behavioral rather than structural.

It is important to note that restructuring measures in the financial sector will necessarily impact on the basic tasks of the central banks and prudential supervisors. The text of Article 127 TFEU makes it clear that the ECB and central banks have a crucial role to play in the supervision of the financial sector. According to Article 127.2 TFEU their task is i.a.:

– to define and implement the monetary policy of the Community;
– to promote the smooth operation of payment systems.

According to Article 127(5) TFEU, the ECSB shall contribute to the smooth conduct of policies pursued by the competent authorities relating

38 Case C-313/90, CIRFS, para. 44.

to the prudential supervision of credit institutions and the stability of the financial system.

Central banks had their criteria to assess the viability of financial institutions under normal circumstances, i.e. before the systemic crisis.[39] They have now laid down higher norms required to cope with the systemic crisis. All aid that is designed to bring banks up to the new standard, to upgrade them, should be acceptable without the need to impose structural conditions.

4.2. Procedure

The procedures of EC State aid law are laid down in Article 108 TFEU and the procedural Regulation 659/99.[40] The assessment of state aid measures is conducted in a procedure between the Commission and the Member State concerned. The intended beneficiary, its competitors and other institutions such as the central bank can as third parties provide comments. It is important to note that the central bank cannot be considered part of the government of the Member state. It is, according to Article 130 TFEU, independent from the government of the Member state.

The procedural rules make a clear distinction between the preliminary procedure and the formal investigation procedure. Under the first procedure, the Commission has two months to take a decision. If it finds that doubts are raised, it has to open the formal investigation procedure. Article 4(3) of Regulation 659/99 does not empower the Commission to impose conditions. The Commission has developed a practice whereby it notes that conditions are accepted thus achieving its goals.[41] This practice is unsuitable for the imposition of major conditions, such as restructuring, because the preliminary procedure does allow the participation of third parties. The power to impose conditions is laid down in Article 8(4) of the Regulation. This provision does allow the Commission to attach conditions to a positive decision. Thus, any Commission decision that would require restructuring has to be taken in the context of the formal procedure. Only the formal procedure allows third parties, that is, any other company or institution, to submit comments. According to the case law of the ECJ[42], the Commission has an obligation

39 Based on discussions of the author with officials of De Nederlandsche Bank (DNB).

40 OJ 1999, L 83, 1.

41 This happened in the first ING decision.

42 Case C-367/95 P, Sytraval.

to address the arguments raised by interested parties in its decision. This is a serious obligation the non-observance of which will result in annulment of the Commission decision.

It would seem that the Commission has not always been clear which procedure it applies concerning state aid in the banking sector. It is in view of the different rights for interested parties of the greatest importance to clarify which procedure applies. It is self-evident that in every case where there is a need for a thorough analysis the formal procedure should be followed. In this context, the Commission's view expressed in paragraph 48 of the restructuring Communication does not seem correct. The Commission states that it "does not have to open formal proceedings where the restructuring plan is complete and the measures suggested are such that the Commission has no further doubts as to the compatibility in the sense of Article 4(4) of Regulation 659/99." The point is that the Commission should allow all interested parties and institutions to present their views. Not opening the formal procedure may seriously prevent this.

As we have seen, the assessment of the state aid measures under Article 107(3)(b) TFEU is virtually without precedents. As a result, there is no case law guiding the Commission which standards to apply. Normally, in state aid law such standards have been developed in the course of Commission decisions and court cases testing the Commission's standards. It is therefore of the utmost importance that the formal procedure is followed, since only this procedure allows an adequate participation of all interested parties and thus an optimal development of the relevant criteria that should be applied. Since there is not yet a developed body of case law on the question which standards should be applied for the application of Article 107(3)(b) TFEU, it is vital that relevant parties participate in the process of developing the relevant standards. As was noted above, this is even more important in the present cases involving the banking sector since in this sector Commission decisions requiring restructuring or major changes in the behavior of the financial institutions also involve the powers and duties of the central banks and the prudential supervisors. These institutions should therefore be allowed to participate in the whole state aid procedure.

An important question of procedural law is who has the burden of proof. The standard of proof is on the one hand related to the question about the burden of proof, on the other hand it is a question of substantive norms, for which see above.

4.3. The burden of proof

Under the state aid rules, the Commission has to prove that a measure by which a Member State transfers money, or grants an advantage to an undertaking, constitutes state aid. Once that is established, it is for the Member State to claim that an exemption applies under Article 107 (2) or (3) TFEU. Once the Member State, having taking into account the case-law of the Community courts and the relevant Commission decisions, has established sufficient arguments that the conditions for the exemption are satisfied, it is for the Commission to rebut those arguments. The Member State has to establish that the aid is necessary and proportionate; it does not have to prove that the aid is necessary under all theoretically possible circumstances (cf. analogy with case 157/94, *Commission v. NL* at para. 58).

Since there is no case law on the application of Article 107(3)(b) TFEU, the burden and standard of proof required by the Commission in merger control may provide guidance as to what ought to be expected of the Commission in its assessment of notified aid under Article 108 (3)(c).TFEU. The Merger Regulation (Council Regulation 139/2004) is silent on the evidentiary principles that apply in merger control proceedings. Nevertheless, it is recognised in the Merger Regulation that there is a duty to avoid potential conflicts of interest between the Community policies of Merger Control and legitimate interests of the Member States (Article 21(4)). Member States may take appropriate measures to protect these legitimate interests, which naturally must be "compatible with the general principles and other provisions of Community law" (Recital 19 and Article 21(4)). Specifically mentioned in Article 21(4) as legitimate interests are "public security, plurality of the media and prudential rules."

Further, similarities between Merger Control and State Aid rules can be seen by a comparison of Article 2 Merger Regulation and Article 107(1) TFEU. In both of these provisions, the compatibility with the common market, of a merger or state aid respectively, is to be assessed by the Commission.

Article 107(3) TFEU provides that certain state aids "may be compatible with the common market". Of current relevance is Article 107(3)(b) TFEU, where aid "to remedy a serious disturbance in the economy of a Member State" may be compatible. Such a large margin of discretion on behalf of the Commission to determine compatibility with the common market has no direct parallel in the Merger Control regime. Nevertheless, it is clear that, as with all areas of discretion in Community law, this discretion must

be exercised subject to the recognised general principles of EC law, such as proportionality. Further, as there have been no cases considering the burden and standards of proof under Article 107(3)(b) TFEU, it is appropriate to apply the rules developed by the Community courts in relation to the burden and standard of proof under the Merger Control regime.

Under the Merger Control regime, it is clear that in the case of a prohibition decision, the burden of proof is borne by the Commission[43], which must demonstrate to the requisite standard that a concentration raises antitrust concerns by significantly impeding effective competition, in particular by through the creation or strengthening of a dominant position.[44] Although the community courts have recognised that, "in the case of complex economic assessments, the burden of proof placed on the Commission is without prejudice to its wide discretion in that sphere"[45], this has not prevented the Courts from closely reviewing whether the Commission has discharged its evidentiary burden.[46]

The case of *Bertelsmann and Sony*[47] last year is particularly illustrative. The Court of Justice in *Bertelsmann and Sony* stated that there is no "general presumption that a notified concentration is compatible with, or incompatible with, the common market."[48] Nor were different standards of proof applicable whether a concentration was approved or prohibited by a decision[49] under the Merger Regulation. The Court stated in para. 47:

> *"… the prospective analysis called for in relation to the control of concentrations, which consists of an examination of how a concentration might alter the factors determining the state of competition on a given market in order to establish whether it would give*

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43 *Energias de Portugal SA v Commission* Case T-87/05 at para. 61 ("It is for the Commission to demonstrate that a concentration cannot be declared compatible with the common market.").

44 Art. 2(3) Merger Regulation.

45 See *Petrolessence SA v Commission* Case T-342/00 at para. 101; *Energias de Portugal SA v Commission* Case T-87/05 at para. 63.

46 See, e.g. *Airtours Plc v Commission*, Case T-342/99; *Schneider Electric SA v Commission,* Case T-310/01; *Tetra Laval BV v Commission,* Case T-5/02.

47 *Bertelsmann AG and Sony Corporation of America v Independent Music Publishers and Labels Association* Case C-413/06 P.

48 *Bertelsmann AG and Sony Corporation of America v Independent Music Publishers and Labels Association* Case C-413/06 P at para. 48.

49 *Ibid*. at para. 46.

> *rise to a significant impediment to effective competition, makes it necessary to envisage various chains of cause and effect with a view to ascertaining which of them is the most likely (see, to that effect, Case C-12/03 P Commission v Tetra Laval [2005] ECR I-987, paragraph 43).”*

This paragraph implies that in a prospective economic analysis, in the analogous area of Merger Control, the Commission bears the burden of proof of demonstrating which version of the future is the most likely.

The standard of evidence to create these forecasts by the Commission is crucial. It must be “a sufficiently cogent and consistent body of evidence”[50]. The importance of this is further underlined as “[t]hat case-law merely reflects the essential function of evidence, which is to establish convincingly the merits of an argument or, as in the case of the control of concentrations, to support the conclusions underpinning the Commission’s decisions (see, to that effect, *Commission* v *Tetra Laval*[51], paragraphs 41 and 44)”.[52] This illustrates the importance of the quality of the Commission’s evidence. Its strength must be, “to support the conclusions underpinning the Commission’s decisions”, equivalent to establishing “convincingly the merits of an argument”. However, by further analogy, the Commission is not obliged under the burden of proof “to go even further and prove, positively,”[53] that would be no other conceivable hypothetical outcome.

The burden of proof on the Commission can be reduced by a failure of the merging parties to provide evidence on a particular point on which they can reasonably be expected to have evidence or may potentially be construed against them. In such circumstances, the Commission may decline to accept the position being advanced, particularly where it has clear indications to the

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50 Joined Cases C-68/94 and C-30/95, *France and Others* v *Commission* [1998] ECR I-1375, *‘Kali & Salz’*, at para. 228.

51 *Commission v Tetra Laval*, Case C-12/03 P.

52 *Bertelsmann AG and Sony Corporation of America v Independent Music Publishers and Labels Association,* Case C-413/06 P at para. 51.

53 *Commission v Netherlands*, Case C-157/94 at para. 58. In this case the Netherlands was found not to be obliged by the burden of proof to demonstrate that no other measure could enable certain tasks to be performed under the same conditions in an Article 86 EC case.

contrary. Thus the burden of proof on the Commission cannot be used to evade submitting certain pieces of evidence.[54]

Advocate General Kokott recognised in *Bertelsmann and Sony* that there may be cases where "it is not possible to make any reliable prognosis… even after extensive market investigations" and recommended that in such cases a transaction "ought to be declared compatible with the Common Market".[55] This mirrored the opinion of Advocate General Tizzano in *Tetra Laval*, which concluded that where doubts persist "the most correct solution is quite certainly to authorise the notified transaction."[56] Though it is arguable that such "borderline cases" in State Aids should be permitted on the basis of the principle *in dubio pro liberate*, their rarity may make the argument purely theoretical.

In conclusion on this point, the burden of proof is, by analogy with the Merger Control regime, upon the Commission to prove whether a state aid is compatible or not with the common market. This must be proved upon evidence which is "sufficiently cogent and consistent", although the Commission is not obliged to demonstrate that its reasoned outcome is the only one possible, but simply "which is most likely to ensue."[57]

As noted above, it would appear that the Commission bears the burden of proof of demonstrating the incompatibility of the notified state aid with the common market. Once it is established that there is state aid, the burden shifts to the notifying Member State, in this instance, to demonstrate the necessity of the aid and that it is "to remedy a serious disturbance in the economy" under Article 107(3)(b) TFEU. In the banking sector, this means that the Member state will have to demonstrate that the aid will restore the viability of the institution and/or the viability of the financial sector in general (eliminate or reduce the systemic risk), after all the provision of this Article refers to a disturbance of the economy of a Member State. It is

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54 See for example Case IV.M 1383 – *Exxon/Mobil,* Commission decision of 29 September 1999, 2004 O.J. L103/1 at paras. 470-71.

55 *Bertelsmann AG and Sony Corporation of America v Independent Music Publishers and Labels Association,* Case C-413/06 P, Opinion AG Kokott at para. 223.

56 *Commission v Tetra Laval*, Case C-12/03 P, Opinion of AG Tizzano at paras. 77, 80.

57 *Bertelsmann AG and Sony Corporation of America v Independent Music Publishers and Labels Association,* Case C-413/06 P at para. 52.

important to note that the 22 of July 2009 Communication does not mention the possibility that the aid will restore the viability of the financial sector.[58]

Although phrased in the form of an "indicative table of contents for restructuring plan", the annex of the Commission's 22 July Communication does contain useful guidance. The notifying Member State will have to prepare convincing and coherent reasoning to demonstrate that the aid will restore the viability of the financial institution. It will also have to demonstrate that the aid will not distort competition. Footnote 1 of the annex to the 22 July Communication mentions that the relevant information may comprise reports prepared by or for the Member States authorities, including the regulatory authorities. This is an understatement of the role of the central banks. It is public knowledge that the Commission has received ample assistance from experts of the ECB in its dealings with the assessment of the state aid measures for the financial sector. It is highly desirable to openly acknowledge such assistance and to go beyond that. Effective management of the financial crisis requires all institutions involved to act in unison and to avoid unilateral decisions by the Commission. Article 4(3) TEU requires, according to the case law of the ECJ, the loyal co-operation of all institutions and the Member States for the achievement of the goals of the Community. In this context it is important to note that the ECB is, according to Article 13 TEU, mentioned as a Union institution. It should be remembered that in Article 7 of the EC Treaty the ECB was not listed as a Community institution.

The present financial crisis calls for active co-operation of the key players in the Community. This can be achieved in several ways.

First, the Commission should assess state aid measures whenever doubts arise and conditions are discussed in the framework of the Article 108(2) TFEU procedure, so as to allow a maximum of input from the central banks and the financial supervisors.[59]

Second, the relevant criteria for assessing the viability of the banks should be developed and applied in close co-operation with the central banks and the supervisory authorities. The criteria mentioned in the Annex to the 22 July Communication are a good starting point. In order to provide optimal

58 Point 4 of the restructuring Communication.

59 See above section 4.2 and footnote 42.

guidance to the notifying Member State and the intended beneficiary, it is also important to clearly show that the criteria are the result of a joint effort.

Third, closer co-operation between the Commission and the national central banks and the ECB should be fleshed out in a clear framework setting out the respective role and duties of the different parties involved. There are many areas in the Community where such models of co-operation have been developed, such as the network of regulators in the electricity and gas sector, the telecom sector, as well as others. Co-operation in this context is fundamentally different since there is no clear "primus inter pares", the Commission's powers do not rank higher than the powers of the central banks and in some respects of the financial supervisors.

4.4. Legal protection

The adoption of decisions in state aid cases has raised important questions about the legality of the Commission's use of imposing conditions, as we discussed in the previous paragraph. This is important for the legal protection of the beneficiaries as well as its competitors. There may also be other interested parties involved, i.e. the national central banks or regulators of financial markets. Conditions are also imposed in other areas of competition law. This is quite common in merger control and the application of prohibition decisions pursuant to Article 101 and 102. A new phenomenon is the use of conditions under Article 9 of Regulation 1/2003.

The use of commitment decisions is, of course, formally a new instrument created under Regulation 1/2003. It has some resemblance with the way the Commission previously used its power to grant individual exemptions. Under the old regime, the Commission often negotiated a limitation of restrictions of competition during the process of granting an individual exemption and subsequently granted the exemption conditionally. The instrument of commitment decisions allows the Commission to achieve results without having to go all the way by adopting a full infringement decision. It is therefore attractive for the Commission. It is also attractive for the undertakings concerned in that they may avoid being hit by ever increasingy stiff fines. It is certainly less attractive from the point of legal protection. The first commitment decisions still have to be tested in the Community courts. But the very fact that the Commission can adopt the decision without having to prove that there was an actual infringement will necessarily have an effect on the judicial protection. In the GDF case the Commission notes that

GDF might have infringed Article 102 TFEU. Moreover, the commitments imposed can, of course, have a very considerable financial and commercial effect. The Commission observes that it can impose a fine of up to 10% of the company's annual turnover if the firm were to break its commitments. If imposed, such fines will only underscore the shortcomings of this type of enforcement policy.

Commitment decisions in the state aid area are by no means a novel instrument. Suffice to recall the very extensive commitment decisions Air France and Olympic Airways.[60] Nevertheless, the recent decisions in the banking sector raise new fundamental issues. Part of the problem is the time element. Speedy financial intervention is essential. This makes an extensive consultation which is necessarily time consuming, difficult. The time pressure is mainly caused by the systemic nature of credit crisis.

5. THE INSTITUTIONAL ASPECTS

Within the Community there are several actors on economic and monetary policy. In order to assess the developments of the past two years we have to be aware of their respective powers. The institution responsible for decisions in this field is the ECOFIN Council. The Council is empowered to take decisions on the basis of Articles 120–126 TFEU. The Council has taken a decision to enhance the economic policy coordination as of 1 January 2011.

The actions to provide financial support have been taken by the Member States, individually or in coordinated manner. This took place in the framework of the Euro-group, although other Member States were actively involved. The measures were taken by the Member States and not by the ECB. The banks needed new capital and that is what only governments could provide them (the ECB can help with short-term liquidity). Such measures have to be assessed according to the State aid rules, as was discussed above.

Member States may also take measures that have a general application, e.g. a reduction of the VAT rate will not be caught by the prohibition of State aid since it is not selective. Government measures reducing the level of the VAT have to be in line with the EC rules on indirect taxes. Measures applying reduced VAT rates in selected sectors have to be decided on the basis of Article 113 TFEU by unanimous vote, lowering VAT rates across the

60 Decision 94/653/EC [1994] OJ L 254/73 and decision 94/696/EC [1994] OJ L 273/22, respectively.

board do not require unanimity.[61] Moreover, it should be observed that even if measures to stimulate the national economy are compatible with the rules of the Treaty, there is nevertheless a need for coordinated action. Without such coordination there is a risk that national measures will be less effective, because the effect of the extra expenditures will seep away to other Member States. This is what happened with the French measures to stimulate the economy in the early years of the Mitterrand Presidency.[62]

It should be remembered that, even if Member States are free to take financial measures supporting their banks, they have nevertheless to observe the Treaty rules of Article 121 TFEU. According to this provision, Member States shall regard their economic policies as a matter of common concern. Member States will have to abide by the broad guidelines of economic policy. For that purpose Article 121(3) TFEU provides for the multilateral surveillance mechanism. Even more important are the rules of Article 126 TFEU, the excessive deficit procedure and the rules of the stability pact. These rules are considerably more onerous than the broad guidelines.[63] The mechanism lays down the well-known 3% rule for the deficit of governments of the Member States.[64] It is important to note that the procedure of Article 121 TFEU applies to all Member States, i.e. also those with a derogation (the ones not participating in the Euro-zone). Article 126 TFEU applies also to all Member States, but the provisions containing sanctions, Article 126(9) and 126(11), does not apply to non-members of the Euro-zone.[65] The observance of the 3% rule has come under severe strain with the guarantees of some 400 billion and more. There will undoubtedly be pressure to apply the rules of the stability pact leniently. A precedent for such behaviour was set in the episode that led to the judgment of the ECJ in the case *Commission* v. *Council*.[66] The Court did not answer the question whether the Council is,

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61 Directive 2006/112, OJ 2006, L 347/1.

62 See e.g. Kapteyn & Themaat, 2008: 885.

63 *Idem* p. 889.

64 The additional rules of the stability pact are laid down in Reg. 1467/97, in particular in Art. 9.

65 Art. 139(2) TFEU.

66 Case C-27/04, *Commission* v. *Council*, [2004] ECR I-6649. In its judgment the ECJ held that the Council could not decide to hold the excessive deficit procedure in abeyance. The Court did not express an opinion on the question whether or not the Council is under an obligation to take a decision under Art. 104(9). In para. 90 it held: "It should be added that, in accepting that the procedure may de facto be held in abeyance simply because the Council does not succeed in adopting a decision recommended by the Commission, the

in the context of the procedure of Article 126(9) TFEU, under an obligation to take measures.

The restructuring of banks imposed by the Commission's could lead to mergers. To the extent that mergers have a Community dimension, and many will, they have to be approved by the Commission on the basis of the merger control rules. It is quite common for the Commission to lay down obligations or ask commitments from the merging companies in order to alleviate the distortions of competition. This happened for example in the case of the original Fortis-ABN AMRO merger.[67] The possibility to follow a coherent policy for the banking sector through the application of the merger control rules is, by its very nature, restricted to incidental and *ad hoc* measures. Moreover, the Commission can only act when there are mergers with a community dimension. The banking sector is still dominated by national players and mergers between banks in several Member States are not frequent. On the other hand it is not excluded that the exceptional circumstances will lead to transnational mergers.[68]

The actions of the governments are closely monitored by the ECB in order to decide whether or not its monetary policy needs to be adjusted, i.e. whether it should lower interest rates. Therefore, the ECB has been closely involved in the decision making process.

6. THE INTERNATIONAL DIMENSION

The problems discussed so far involved financial institutions in the Community. Some Community citizens were confronted with defaulting banks in third non-Member States – more in particular Iceland. After some initial individual actions, the Member States concerned undertook coordinated action to address this issue. This is just one example of the increasing globalization of international financial markets. The European Council conclusions of 11 and 12 December 2008 noted the need to work

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Court does not express a view as to whether, pursuant to Article 104(9) EC, the Council could be required to adopt a decision where the Member State persists in failing to put into practice its recommendations under Article 104(7) EC, a question which the Court is not called upon to answer in the present proceedings.´

67 According to the Commission, Fortis was to sell the activities of some parts of ABN AMRO: decision 3 Oct. 2007, case Com/M4844, Fortis/ABN - AMRO assets. Since then Fortis has been engaged in talks with the Deutsch Bank. After the weekend in September the talks have been discontinued.

68 It should be noted that Dir. 2007/44 is specifically designed to facilitate cross-border mergers in the financial sector.

together with the international partners.[69] For that purpose, the President of the European Union Council, accompanied by some colleagues, travelled to Washington for talks with the US government. In the meantime, close international cooperation has resulted in the adoption of new Basel rules for banks in early September 2010.

7. THE PRESENT STATE OF THE FINANCIAL SECTOR

Two years after the credit crisis materialized, market conditions have stabilised considerably. There are signs that the financial markets have somewhat recovered and as a result efforts are made to reduce the reliance of banks on state support. However, the phasing out of state aid has to be effected gradually, transparently and Community wide, y otherwise spill-over effects could arise. It is also clear that not all Member States are operating under similar conditions. The situation in Greece is obviously different from that in Spain and Portugal. The ECOFIN Council of 2 December 2009 agreed on the need to develop a strategy for phasing out of state aid measures. This should start with the State guarantee schemes. This would encourage sound banks to renounce on state aid and stimulate weaker banks to address their specific problems. On 18 May 2010, the ECOFIN Council welcomed the preliminary analysis of the Commission on the use of guarantee schemes. The Commission has introduced specific pre-requisites in view of the renewed provision of guarantees, in the form of higher fees and a viability review for banks still relying heavily on government guarantees. The latest Council of 7 September 2010 endorsed a new financial supervision system.

8. CONCLUSION

The Commission has displayed a remarkable agility to cope with the sudden surge in massive state aid support over the last two years. Its handling of the massive flow of national state aid measures has been impressive. Nevertheless it remains to be seen how the Commission decisions and in particular the draconian conditions that have been imposed on the beneficiaries will stand the test in the Community courts. It is to be expected that the Courts will allow the Commission a margin of discretion, especially in view of the

69 The increased globalization, and interdependence, is well illustrated by the fact that the People's Republic of China is, as of 2009, now the biggest holder of US debt with some 565 billion US dollar, the next biggest creditor is Japan with some 500 billion plus US debt and the third biggest is the UK with some 320 billion US. These enormous holdings of US government debt create delicate mutual relationships.

urgency of the subject matter and the systemic nature of it. Whether that will be enough to justify the imposition of conditions with a very serious impact on the banks remains to be seen. Similarly, it is doubtful whether the unorthodox way of taking decisions will be sanctioned by the courts. The absence of the traditional procedural safeguards in state aid matters or the "unorthodox "adherence to these principles will almost certainly raise some eyebrows of the judges in Luxemburg. It is doubtful whether the Commission's view that, in case Member States submit complete restructuring plan they can proceed according to the preliminary procedure of Article 108(3) TFEU, is correct.

The developments in the financial sector demonstrate the intricate interaction of Member State and Community actions within their respective spheres of competences. The absence of clear Community powers to grant the type of aid that is required by providing massive guarantees, makes it all the more necessary that Member States actions are closely coordinated. The decision-making process for the measures to safeguard the financial sector also demonstrates that it is very difficult to distinguish between the prerogatives of the ECOFIN council and the Euro group. Given the design of the Treaty rules, briefly outlined above, it was always going to be difficult to draw a clear line between the closely coordinated economic policy and the common monetary policy. For the former the ECOFIN is responsible for the latter it is, in the absence of an introduction of the Euro by all Member States, the Euro group. In the meantime the Council has been able to take measures designed to safeguard the stability of the Euro. It has also agreed on closer economic policy cooperation.

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