

COMMISSION DECISION

of 20 October 2004

on aid granted by Germany Landesbank Hessen-Thüringen — Girozentrale

(notified under document number C(2004) 3931)

(Only the German text is authentic)

(Text with EEA relevance)

(2006/742/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first subparagraph of Article 88(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to the provisions cited above ⁽¹⁾ and having regard to their comments,

Whereas:

I. PROCEDURE

(1) By letters dated 31 May and 21 December 1994, the *Bundesverband deutscher Banken e.V.* ('BdB'), an association representing private banks established in Germany, informed the Commission among other things that housing-promotion loans had been or would be transferred to the liable equity capital of the Landesbanks in North Rhine-Westphalia, Lower Saxony, Schleswig-Holstein, Bavaria, Hamburg and Berlin, i.e. the Westdeutsche Landesbank, the Norddeutsche Landesbank, the Landesbank Schleswig-Holstein, the Hamburger Landesbank and the Landesbank Berlin. The BdB considered the resulting increase in the equity capital of the relevant Landesbanks distorted competition in their favour, since the parties had not agreed remuneration consistent with the market-economy investor principle. In its second letter, the BdB accordingly lodged a formal complaint and called on the Commission to initiate proceedings under Article 93(2) of the EC Treaty (now Article 88(2)) against Germany. In February and March 1995 and December 1996, several banks associated themselves individually with the complaint lodged by their association.

(2) By letters dated 6 August 1997 and 30 July 1998, the BdB informed the Commission of two further transfers of assets, to Landesbank Schleswig-Holstein in Schleswig-Holstein and Landesbank Hessen-Thüringen in Hessen. As regards the latter transaction, the Commission wrote to Germany on 31 July 1998 requesting information. Germany answered by letter dated 2 October 1998 that this was currently still only at the planning stage and that the Commission had no cause for concern either now or at a later stage.

(3) The Commission first examined the transfer of assets to Westdeutsche Landesbank ('WestLB'), but announced that it would review the transfers to the other banks in the light of the findings in that case ⁽²⁾. It finally adopted a decision on the WestLB case in 1999, concluding that there was a state aid component equal to the difference between the remuneration paid and the normal market remuneration, which was incompatible with the common market and should be recovered ⁽³⁾. The decision was annulled by the Court of First Instance on 6 March 2003 for not setting out sufficient reasons as regards two of the factors used to calculate the appropriate remuneration, but it was confirmed in all other respects ⁽⁴⁾. On 20 October 2004, the Commission issued a new decision which took account of the Court's criticisms.

(4) On 1 September 1999, the Commission sent Germany a request for information on the transfers of assets to the other Landesbanks, including Helaba. By letter dated 8 December 1999, Germany submitted information on

⁽²⁾ OJ C 140, 5.5.1998, p. 9 (Decision to initiate proceedings).

⁽³⁾ OJ L 150, 23.6.2000, p. 1; actions challenging that decision were brought by Germany (before the Court of Justice, Case-C 376/99), by North Rhine-Westphalia (before the Court of First Instance, Case T-233/99) and by WestLB (before the Court of First Instance, Case T-228/99); the Commission brought proceedings for an infringement of the Treaty (before the Court of Justice, C-209/00).

⁽⁴⁾ Joined Cases T-228/99 and T-233/99 *Westdeutsche Landesbank Girozentrale and Land Nordrhein-Westfalen v Commission* [2003] ECR II-435.

⁽¹⁾ OJ C 72, 26.3.2003, p. 3.

the transfer of the special assets of the *Land* to Helaba, which it supplemented, following a further request for information from the Commission sent on 31 October 2000, by letter dated 21 January 2001.

- (5) By letter dated 13 November 2002, the Commission informed Germany that it had decided, with regard to the transfer of the special assets by the *Land* of Hessen as a silent partnership contribution to Helaba, to initiate formal proceedings under Article 88(2) of the EC Treaty. At the same time, the Commission also initiated proceedings in respect of similar transfers of assets to Norddeutsche Landesbank — Girozentrale ('NordLB'), Landesbank Schleswig-Holstein — Girozentrale ('LSH'), Hamburgische Landesbank — Girozentrale ('HLB') and Bayerische Landesbank-Girozentrale ('Bayern LB'). It had already initiated proceedings in respect of a further similar transfer of promotion-related assets by the *Land* of Berlin to Landesbank Berlin back in July 2002.
- (6) The decisions initiating proceedings were published in the Official Journal of the European Union ⁽⁵⁾. The Commission called on interested parties to submit comments.
- (7) By letter dated 9 April 2003, Germany submitted comments on the initiation of proceedings in the Helaba case.
- (8) By letter dated 29 July 2003, the BdB submitted comments on all the decisions taken on 13 November 2002 to initiate proceedings, and those comments were forwarded to Germany by letter dated 28 July 2003 for its opinion.
- (9) By letters dated 10 October and 4 December 2003, Germany submitted comments on the BdB's remarks in the Helaba case. By letter dated 30 October 2003, Germany also forwarded comments by the Government of North Rhine-Westphalia and by WestLB on the BdB's remarks.
- (10) By letter dated 7 April 2004, the Commission requested further information from Germany on all the Landesbank proceedings, and wrote specifically requesting information on the Helaba case by letters dated 19 May and 3 August 2004. Germany replied by letters dated 1 June, 23 June and 23 August 2004.
- (11) In September and October 2004, talks took place between the BdB, the *Land* of Hessen and Helaba on the question of an appropriate remuneration for the capital provided. No understanding was reached. By letter dated 28 September

2004, the BdB sent comments on the proceedings. The Commission then asked Germany for further comments, which were submitted by letters dated 1 October and 6 October 2004.

II. DETAILED DESCRIPTION OF THE MEASURES

1. HELABA

- (12) Landesbank Hessen-Thüringen Girozentrale (Helaba), with head offices in Frankfurt am Main and Erfurt, has a group balance-sheet total of EUR 140 billion (as at 31 December 2003), which makes it one of Germany's largest banks. The bank's balance-sheet total amounts to some EUR 130 billion, which is more than 90 % of the group balance-sheet total. It is a publicly owned credit institution operating in the form of a public institution (*Anstalt des öffentlichen Rechts*). The owners and guarantors of the bank have since 1 January 2001 been the *Sparkassen- und Giroverband Hessen-Thüringen* with an 85 % stake (at the time of the transfer at the end of 1998, it was the sole owner and guarantor), the *Land* of Hessen with a 10 % stake and the *Land* of Thuringia with a 5 % stake. According to its annual report for 2003, the group had equity capital of EUR 4,1 billion. As at 31 December 2003, the group's core capital ratio was 7,8 % and its equity ratio 11,3 %.
- (13) Given its ownership structure, Helaba operates as the principal banker to the *Land* of Hessen and to the *Land* of Thuringia and as the central institution of the Hessen and Thuringia savings banks. Helaba also operates as a customer-orientated and market-orientated commercial bank with a particular emphasis on wholesale banking, and as a partner for public-sector customers, supporting the *Länder* and municipalities in financing and implementing investment plans. Via its holding in the *Landesförderinstitute*, Helaba supports economic and structural-policy objectives in Hessen and Thuringia.
- (14) The Helaba group had some 3 500 employees as at 31 December 2003. It is present in major world financial centres. In addition to its two head offices in Frankfurt am Main and Erfurt, it is represented internationally in London, New York, Zurich, Dublin, Madrid, Paris and Luxembourg.

2. THE TRANSFER OF THE SPECIAL 'HOUSING AND FUTURE INVESTMENT' FUND AS A SILENT PARTNERSHIP CONTRIBUTION TO HELABA

- (15) By the Law of 17 December 1998, the *Land* of Hessen established a special 'Housing and Future Investment' fund.

⁽⁵⁾ NordLB: OJ C 81, 4.4.2003, p. 2; BayernLB: OJ C 81, 4.4.2003, p. 13; HLB: OJ C 81, 4.4.2003, p. 24; Helaba: OJ C 73, 26.3.2003, p. 3; LBKiel: OJ C 76, 28.3.2003, p. 2.

The Hessen Finance Ministry was empowered to transfer all or part of this fund to a credit institution as a silent partnership contribution or in any other form of equity holding recognised for supervisory purposes in return for a market remuneration that remained with the special fund.

- (16) The special fund comprises *Land* claims from loans granted between 1948 and 1998 for the purpose of promoting social housing construction. As at 31 December 1998, the loan portfolio amounted to DEM 7,829 billion (*Land* portion: DEM 6,026 billion). Its cash value was determined by two independent experts at DEM 2,473 billion (EUR 1,264 billion). This special fund was transferred to Helaba as a silent partnership contribution under a contract between the *Land* of Hessen and Helaba signed in December 1998 and entering into force on 31 December 1998.
- (17) A contractually agreed re-valuation by an expert on 31 December 2003 put the value of the promotion-related assets at EUR [...] (*) million. The increase in value is due to the fact that accruals had exceeded outflows from the promotion-related assets since 1999. However, pending final agreement with BAFin on the outcome of the expert valuation as at 31 December 2003, Helaba continues to have only the previous reference amount available.
- (18) No injection of liquidity or inflow of revenue for the bank is associated with the transfer of the special fund as a silent partnership contribution. Income (interest and repayments) from the house-building loans does not accrue to the bank, but to the special fund and must be ploughed back into the promotion of housing construction.
- (19) The transfer of the special fund to Helaba should be seen in the light of the *Land's* efforts to tighten up its aid and structural-policy instruments and make them more efficient.
- (20) According to information provided by Germany, the *Land* initially considered the possibility of inviting bids for the outstanding claims and selling them by auction (highest bidder) to private operators for cash and split up into tranches. Although splitting the special fund into tranches would have had the advantage of increasing the number of potential banking partners for the *Land* given that very few operators would have been interested in taking on a fund of some DEM 2,5 billion, the fund was nevertheless a revolving fund involving income from loans granted being ploughed back and thus constituted a single entity. It would, according to Germany, have been very expensive to carry out a periodic valuation of the tranches divided between individual institutions. The *Land* would, moreover, have lost the flexibility it had to shift the emphasis between the various aid objectives.
- (21) The *Land* consequently decided to keep the house-building assets undivided, to continue to use the income for promotion purposes in house building and economic promotion, to organise the administration of the assets as effectively and cheaply as possible and, by using the claims in other ways, to generate additional income.
- (22) In the light of these considerations, Helaba declared itself ready to take on and administer the entire fund of outstanding claims worth DEM 2,473 billion (EUR 1,264 billion). Another advantage of transferring it to Helaba was that the latter had, since 1953, already been administering the *Landestreuhandstellen* (LTH) as a legally independent business division and handling aid programmes in a trust capacity. Helaba is moreover required under the State Treaty and its own statutes to comply with general economic basic principles in pursuing its business policy. These three factors convinced the *Land* that Helaba would be best suited as a banking partner in realising the objectives of the Special Fund Law.
- (23) Under [...] within the meaning of Section 10(4) of the German Banking Act of 30 December 1998, the *Land* transferred the special fund to the bank as a silent partnership contribution in the form of an internal partnership. This means that the *Land* co-founded a silent partnership with Helaba under Sections 230 *et seq.* of the German Commercial Code, i.e. a partnership whereby the silent partner has a capital holding in another business involving the transfer of a contribution to the assets of the active partner.
- (24) According to the [...] the purpose of the contribution is 'to serve permanently as liable equity capital in the form of core capital within the meaning of Section 10(2), the first sentence of Section 10(2a) and Section (4) of the Banking Act, taking account of the requirements formulated by the Basle Committee on Banking Supervision (Bank for International Settlements) on 27 October 1998'.
- (25) For a silent partnership contribution to count as the liable equity capital of a credit institution under Section 10(4) of the German Banking Act, it must in particular participate fully in losses and, in the event of the institution's bankruptcy or liquidation, be repayable only after all creditors' claims have been met. The fact that, as was agreed, the silent partnership contribution cannot be

(*) Confidential information, also indicated below by [...].

withdrawn by the *Land* of Hessen means that, according to the information provided by Germany, it does not count towards the 15 % limit for innovative financial instruments laid down by the Basle Committee, but is fully recognised by BAKred, as tier 1 liable equity capital (core capital).

- (26) The alternative of transferring the housing construction fund not as a silent partnership contribution, but as share capital was, according to Germany, not pursued by the *Land* because it was not at the time willing to commit itself to being a direct shareholder and guarantor, and this was in any case not desired by the then sole shareholder, the *Sparkassen- und Giroverband Hessen-Thüringen*.
- (27) The asset transfer to Helaba by the *Land* of Hessen in 1998 occurred later than the earlier transfers of promotion-related assets to Landesbanks in Germany, which are also the subject of the complaint by the BdB and of proceedings initiated by the Commission. However, according to Germany, the earlier transfers did to some extent serve as a model to the *Land* of Hessen even though, in the asset transfer to Helaba, account was taken of the developments which had in the meantime taken place on the capital market and in banking supervisory rules in the direction of increased use and recognition of hybrid or innovative equity capital instruments, which in the first half of the 1990s were not yet available in Germany in that form or to that extent and could not yet be taken into consideration for supervisory purposes.

3. CAPITAL REQUIREMENTS UNDER THE OWN FUNDS AND SOLVENCY DIRECTIVES

- (28) The German Banking Act (*Kreditwesengesetz*) has been amended in line with Council Directive 89/647/EEC⁽⁶⁾ (the 'Solvency Directive') and Council Directive 89/299/EEC⁽⁷⁾ (the 'Own Funds Directive'), which require banks to have own funds of 8 % of their risk-adjusted assets. At least four percentage points must consist of what is termed core

capital, or 'tier 1' capital, meaning capital items which are at the credit institution's disposal without restriction and immediately in order to cover risks or losses as soon as they arise. In determining the total own funds available to a bank for supervisory purposes, the core capital is of decisive importance, because additional capital, or 'tier 2' capital, is accepted as underpinning for risk-bearing transactions only up to the amount of the available core capital.

4. EFFECTS OF THE TRANSFER ON HELABA'S EQUITY CAPITAL ENDOWMENT

- (29) The scale of a credit institution's business depends to a large extent on the amount of its equity capital. This was increased to a not inconsiderable extent by the transfer of the special fund to Helaba.
- (30) Of the silent partnership contribution of DEM 2,473 billion (EUR 1,264 billion) as valued by an independent expert, entered in Helaba's balance sheet and recognised for supervisory purposes as core capital, an annually fluctuating amount of some DEM 2,3 billion (around EUR 1,2 billion), potentially usable to underpin its competitive business, is available to Helaba. The rest is, according to Germany, required as capital coverage for the claims making up the special fund. However, the *Land* of Hessen and Helaba agreed in the contract on a phased arrangement under which, in the period from 1999 to 2002, only an annually increasing partial amount of the usable core capital was to be actually used by Helaba to cover competitive business, and only this partial amount was to be remunerated accordingly. Only as from 2003 was the amount recognised by BaFin, in so far as not required for promotion-related business, to be usable in full to underpin competitive business. The precise amounts available to Helaba as core capital and usable or actually used for competitive business are shown in the following table:

⁽⁶⁾ OJ L 386, 30.12.1989, repealed and replaced by Directive 2000/12/EC, OJ L 126, 26.5.2000.

⁽⁷⁾ OJ L 124, 5.5.1989, repealed and replaced by Directive 2000/12/EC.

Table:

Extent, recognition for supervisory purposes and use or usability of the silent partnership contribution (in EUR millions; end-of-year figures = annual average figures) ⁽⁸⁾

	1999	2000	2001	2002	2003
Nominal value in the balance sheet	1 264,4	1 264,4	1 264,4	1 264,4	1 264,4
Core capital recognised for supervisory purposes for the underpinning of risk assets	1 264,4	1 264,4	1 264,4	1 264,4	1 264,4
Core capital used as cover for promotion-related business	[...]	[...]	[...]	[...]	[...]
Core capital usable as cover for competitive business, but not to be so used under the agreed phased arrangement	[...]	[...]	[...]	[...]	[...]
Core capital usable or actually used under the phased arrangement to cover competitive business	[...]	[...]	[...]	[...]	[...]

- (31) Pending final agreement with BAFin on the outcome of the independent expert valuation of the promotion-related assets as at 31 December 2003, EUR [...] million continue to be available to Helaba as the reference amount (usable for competitive business).
- (32) As a result of the capital transfer, according to the information provided by Germany, the core capital ratio (as defined by the Basle Capital Agreement) notified to BAKred, now BAFin, increased from 5,4 % (31 December 1997) to 9,3 % (31 December 1998), while the equity ratio rose from 9,6 % (31 December 1997) to 13,1 % (31 December 1998). The notified core capital and equity ratios thus rose by some 72 % and 36 % respectively.
- (33) Through the injection of funds, Helaba's capacity to expand its business with risk-assets to be weighted at 100 %, assuming a multiplication factor of 12,5, which corresponds to the equity ratio of 8 %, was enhanced by some DEM 28 billion (EUR 14 billion). In reality, however, the permissible credit volume could have been expanded even more as a result of a DEM 2,3 billion increase in own funds, since a bank's assets are not usually deemed to bear an average risk of 100 %.
- (34) Since this increase in its core capital enabled Helaba to take up further additional capital, its actual lending capacity indirectly increased still further.

⁽⁸⁾ Letter from Germany of 23 June 2004, p. 2-7.

- (35) Set out in tabular form, the absolute and relative changes in Helaba's core capital since 1997, including the silent partnership contribution of the *Land* of Hessen and other silent partnership contributions, are as shown in the chart, with a distinction being made between the situation in accordance with recognition for banking supervisory purposes and the situation in accordance with the contractually agreed phase arrangements.

Chart: End-of-year figures		1997	1998	1999	2000	2001	2002	2003
		EUR millions	EUR millions	EUR millions	EUR millions	EUR millions	EUR millions	EUR millions
Under supervisory rules	Silent partnership contribution <i>Land</i> Hessen	—	1 023	1 264	1 264	1 264	1 264	1 264
	Other silent partnership contributions	153	153	[...]	[...]	[...]	[...]	[...]
	Core capital	1 449	2 579	[...]	[...]	[...]	[...]	[...]
	Share silent partnership contribution <i>Land</i> Hessen in %	—	40 %	[...]	[...]	[...]	[...]	[...]
	Share other silent partnership contributions in %	11 %	6 %	[...]	[...]	[...]	[...]	[...]
Under agreed phased arrangements	Silent partnership contribution <i>Land</i> Hessen	—	—	[...]	[...]	[...]	[...]	[...]
	Other silent partnership contributions	153	153	[...]	[...]	[...]	[...]	[...]
	Core capital	1 449	1 556	[...]	[...]	[...]	[...]	[...]
	Share silent partnership contribution <i>Land</i> Hessen in %	—	—	[...]	[...]	[...]	[...]	[...]
	Share other silent partnership contributions in %	11 %	10 %	[...]	[...]	[...]	[...]	[...]

5. REMUNERATION OF THE OWN FUNDS TRANSFERRED

- (36) According to the information provided by Germany, for the silent partnership contribution Helaba paid the *Land* a remuneration (the so-called liability commission) of 1,4 % a year, consisting of a remuneration for the liability function of 1,2 % a year and a premium of 0,2 % a year for the perpetuity of the contribution and the bank's unilateral right of notice, plus trade tax on the part of the special fund usable by the bank, i.e. a total of 1,66 %. It was agreed under the phased arrangement that this remuneration should not be payable in the first four years (1998 to 2002) on the full value of the fund, but on the agreed fixed tranches (reference amounts) rising in annual increments, which under the agreements reached in the transfer contract were to be used as cover for competitive business.

According to the information provided by Germany, Helaba is liable to pay this remuneration on the basis of the phased arrangements irrespective of whether the silent partnership contribution is used to underpin competitive business or the business it pursues as part of its public task or whether the transferred capital is indeed used for solvency purposes at all.

6. GROUNDS FOR INITIATING THE PROCEEDINGS

- (37) In its decision of 13 November 2002 to initiate proceedings, the Commission took the preliminary view that the transfer of the housing-promotion loans by the *Land* of Hessen to Helaba probably constituted new state aid within the meaning of Article 87(1) of the EC Treaty, which, since

the derogations provided for in Article 87(2) and (3) and in Article 86(2) of the EC Treaty were not met, appeared to be incompatible with the common market.

- (38) The starting point for its investigation was the principle of the market-economy investor. According to that principle, favourable treatment exists through the provision of public money if state funds are made available to an undertaking on terms which it would not have obtained under normal market conditions.
- (39) In view of the long-term risk-free rate (ten-year federal bonds) of around 4 % at the end of 1998, it appeared doubtful to the Commission whether the agreed remuneration could be regarded as appropriate, in particular allowing for a proper risk premium. On the other hand, the Commission conceded that, in determining the normal market remuneration, the lack of liquidity of the capital provided in this instance should not be ignored. The promotion-related loans transferred as a silent partnership contribution would have to be used for public promotion purposes in the same way as before the transfer. Consequently, Helaba could not use the transferred resources directly for its business. The broadening of the bank's equity capital base would, it is true, broaden Helaba's lending capacity (business-expansion function of equity capital). However, the bank could achieve the full potential scope of the increase in business volume only if it refinanced the additional credit volume to the full extent on the capital market. In the Commission's view, therefore, the *Land* could not expect exactly the same yield as a provider of liquid capital, and a corresponding reduction was therefore proper. However, whether this could justify the deduction of the entire gross refinancing costs from the usual market remuneration for a liquid silent partnership contribution was doubtful in view of the tax deductibility of the refinancing costs.
- (40) The Commission doubted that the basic remuneration of 1,2 % a year agreed for the silent partnership contribution lay within the market corridor for comparable transactions, particularly as the absolute volume seemed to be above what was otherwise usual on the market. It also doubted whether the addition of 0,2 % a year for the long-term nature of the contribution was usual on the market and whether the trade tax of 0,26 % a year payable by Helaba here, but not payable by it if it took on a silent partnership contribution from commercial investors, could be regarded as a further constituent part of the remuneration and as relevant for the market comparison.
- (41) The Commission further doubted whether a market-economy investor in a comparable situation would have agreed to limit the remuneration in the first few years to partial amounts. It had moreover to be examined in this context whether Helaba derived from the non-remunerated part of the silent partnership contribution further advantages that had to be remunerated, in particular an improvement in credit standing, since the silent partnership contribution was from the outset entered in full in the balance sheet and hence was available for liability purposes.

III. COMMENTS FROM GERMANY

- (42) Germany stated that the *Land* of Hessen had in 1997/1998 sought ways of achieving additional income from its housing-promotion assets, while maintaining the specific earmarking of their use, by transferring them to a credit institution. It was intended that the assets should remain undivided. Only Helaba was prepared to accept this arrangement. The shareholders of Helaba would not have agreed to a share capital investment by the *Land*. Consequently, the only core capital instrument considered was a silent partnership contribution.
- (43) According to Germany, none of the comments made by the Commission regarding the other Landesbanks applied to Helaba, particularly since it was profitable and not relatively under-endowed with liable capital and was not dependent on a transfer of promotion-related assets in order to maintain its existing business volume or to underpin its growth. Helaba was able to cover its capital requirements through its shareholder, the *Sparkassen- und Giroverband Hessen-Thüringen*, and on the capital market.
- (44) After the Basle Committee on Banking Supervision had, on 21 October 1998, in the 'Sydney Declaration', formulated new guidelines on the supervisory recognition of core capital instruments for credit institutions that operated internationally, the *Land* and the bank decided that the funds raised would be of unlimited rather than limited duration, so as to comply with the new provisions regarding recognition as core capital above the 15 % limit. However, the *Land* had required a remuneration premium of 0,20 % a year in return for the perpetuity of the contribution and the bank's unilateral right of notice.
- (45) According to Germany, in the wake of the Sydney Declaration by the Basle Committee on Banking Supervision, a fungible market for silent partnership contributions had developed which was characterised by broad diversification on the investor side, with investors ranging from private investors to large institutional investors.
- (46) A silent partnership differed here fundamentally from a holding in the share capital. The silent partner did not have a holding in the undertaking and had only rudimentary rights of control. Whereas subscribed capital had to be remunerated through dividends after tax, the remuneration for a silent partnership contribution was a tax deductible operating expense. Under German banking supervision law, silent partnership contributions had been recognised even before 1998 as core capital without any limitation as to amount, and under international banking supervision law too, perpetual silent partnership contributions had been recognised as core capital since the 'Sydney Declaration' in October 1998. In 1998/99, credit institutions had made increasing use of silent partnership contributions. The amounts involved had ranged up to USD 1 billion or DEM 1,2 billion (around EUR 0,6 billion). Whereas they had not been very widespread at the beginning of the

1990s, silent partnership contributions were certainly no longer a marginal financing instrument in 1998/99.

(47) In working out the legal arrangements and in agreeing on the remuneration, the *Land* based itself on comparable transactions involving private credit institutions. According to Germany, in 1998 SGZ Bank, for example, had agreed a liability remuneration of 1,2 % a year above the reference rate and HypoVereinsbank Luxemburg one of 1,6% a year, while in 1999 Dresdner Capital LLC had agreed a liability remuneration of 1,65 % above the relevant reference rate, HypoVereinsbank Luxemburg one of 1,25 % a year and Deutsche Bank one of 1,15 % a year for a so-called 'perpetual'. The remuneration premiums for the funds taken up by private institutions were basically in a corridor between 0,80 % above twelve-month Libor⁽⁹⁾ and 2,15 % above US federal bonds⁽¹⁰⁾. Furthermore, the savings banks in Hessen and Thuringia had granted Helaba a silent partnership contribution with effect from 5 December 1997, for which the remuneration was 1,2 % a year above the reference interest rate.

(48) Germany further stated that, in the case of variable interest rates, the reference interest rates related to money market instruments (Libor and Euribor), while in the case of fixed interest rates they related to bond market instruments (fixed-interest government bonds such as US treasuries and German federal bonds) or the interest rates on the swap market. On the euro money market, lendings were usually carried out on the inter-bank market without any further premiums on the basis of Libor or Euribor. In so far as these reference interest rates were chosen for silent partnership contributions, the premiums were identical to the liability remuneration for silent partnership contributions. On the bond market, the yields on government bonds were usually used as reference interest rates and, since the end of the 1990s, mid-swaps were increasingly used as the reference rate. Even for first-rank bank bonds, banks had, on credit standing and/or liquidity grounds, to pay a different premium, varying with the state of the market, compared with government bonds having the same term. This premium was described as the refinancing premium. In assessing the fixed-interest silent partnership contributions of credit institutions, therefore, these refinancing premiums had to be deducted from the remuneration premiums.

(49) These refinancing premiums for euro banks (senior bonds, JP Morgan-Index) compared with federal bonds had, according to Germany, ranged from just under 20 to over 40 basis points in the two-year period 1998-99. At the end of 1998, they amounted to just under 40 basis points⁽¹¹⁾. In so far as the swap rate (mid-swaps) was chosen as the reference figure, however, the interest rate premium of a silent partnership contribution corresponded largely to the

specific liability remuneration of the silent partnership contribution, since the swap rate interest premium relative to federal bonds corresponded roughly in market terms to the interest premium of 'covered' bank bonds relative to federal bonds and could therefore also be converted into interest premiums compared with Euribor.

(50) The negotiations on the contribution and remuneration were carried out between the *Land* and the bank as between two independent parties. They had based themselves, in determining the finally agreed remuneration of 1,4 % a year (1,2 % plus a 0,2 % premium for the perpetuity of the contribution and the unilateral right of notice of the bank), on the above-mentioned corridor, with a whole series of data from the market as it then stood.

(51) With regard to the premium for the perpetuity of the contribution, Germany stated that the comparable transactions referred to had terms of ten or twelve years and also 32 years or were of unlimited duration. The premium of 0,2 % a year for the perpetuity of the contribution was in conformity with the market in view of Helaba's AAA/Aaa rating at the relevant time, a rating which none of the comparable institutions achieved. The transactions on the capital market referred to for comparison purposes did not moreover reveal any dependence of the level of the remuneration on the amount of the funds taken up, either from the point of view of the institutions (total amount of the issue) or from the point of view of the investors (amount of the subscribed tranche).

(52) In addition, Helaba had to pay trade tax, to which the *Land* of Hessen was not liable, on the remuneration of 1,4 %, so that the total charge was 1,66 % (before tax). According to Germany, therefore, in comparing the remunerations, the trade tax effect of 0,26 % a year in relation to Helaba's silent partnership contribution had to be taken into account. Commercial investors in Germany pay trade tax on profit shares from silent participations. However, the *Land* of Hessen is not subject to trade tax. In its place, Helaba had to pay the trade tax applicable to the remuneration of the silent partnership contribution. A market-economy institutional investor would therefore have required a higher remuneration than the *Land* in order to offset the charge he had to pay in the form of trade tax. Conversely, Helaba would have been immediately prepared to pay a remuneration premium to such an investor, since it made no difference to it whether it paid the premium as a remuneration to the investor or as trade tax to the tax office. Inclusive of the trade tax effect of 0,26 % a year, Helaba's charge resulting from the remuneration it had to pay of 1,40 % a year for the silent partnership contribution

⁽⁹⁾ See Germany's letter of 9 April 2003, p. 25: variable-interest-rate tranche of the silent partnership contribution of USD 700 million with a term of ten years taken up by Deutsche Bank in January 1998.

⁽¹⁰⁾ See Germany's letter of 9 April 2003, p. 25: tranche of the silent partnership contribution of USD 1 000 million with a term of 32 years taken up by Dresdner Bank in May 1999.

⁽¹¹⁾ See chart in annex 15 of Germany's letter of 9 April 2003.

amounted in total to 1,66 % a year, which was clearly in the market corridor and represented the result of negotiations between Helaba and the *Land* of Hessen.

- (53) According to Germany, the remuneration paid was tax deductible by Helaba as operating expenditure. Silent partnership contributions represented equity capital only in the calculation of solvability for banking supervisory purposes, whereas in company and tax law terms they were treated as outside capital.
- (54) According to Germany, the bank needed only DEM [...] million in equity capital for its planned annual growth, whereas the value of the promotion-related assets as liable equity capital for banking supervisory purposes amounted to over DEM [...] billion. Helaba would, according to Germany, not have taken up a silent partnership contribution amounting to some DEM 2,5 billion in a single step, since this amount covered its equity capital requirements for several years; rather, it would have made repeated calls on the capital market. Despite these effects and the charges they imposed on Helaba, no deduction from the remuneration rate of 1,4 % was agreed. The *Land* and Helaba had instead agreed, as a transitional solution, on a gradual use and remuneration of the silent partnership contribution (the phased arrangement). The bank had endeavoured here to reach an arrangement under which it would remunerate the silent partnership contribution only in accordance with the growth targets agreed with its owner to the tune of its actual use to cover risk assets. However, this had been too unfavourable for the *Land* of Hessen and had therefore not been acceptable to it. Following negotiations to offset the conflicting interests, an arrangement had been agreed involving annually increasing remunerated tranches (DEM [...] million in 1999, DEM [...] billion in 2000, DEM [...] billion in 2001, DEM [...] billion in 2002, DEM [...] billion in 2003, i.e. the upper limit for usable core capital). These phased arrangements had provided for a significantly faster increase for the first few years than was necessary for the bank's planned growth. The managing board had then asked the board of directors to approve an additional special quota of DEM [...] million to cover liable equity capital, from whose yields the remuneration of the difference was to be financed so as to ensure that the contribution was used in a way that was neutral in terms of operating result. In Germany's view, this showed that the 'over-endowment' of the bank had not only not conferred any additional advantage, but that, without the special quota, it would rather have burdened the profit situation of the bank, because the remuneration for those parts of the gradually increasing assessment basis not covered by additional business would not have been matched by any income.
- (55) This would have produced annually increasing payment obligations up to an amount of some DEM 33 million as from 2003. In addition to the remuneration of the silent partnership contribution, the bank had to bear the refinancing costs of lending.
- (56) Germany also made comments on the market-economy investor principle. It followed from case law that an assessment must be made of the market nature of the transaction from the investor's point of view. It therefore had misgivings if the Commission, as made clear in the decision to initiate proceedings, set out to examine primarily from the recipient's point of view whether Helaba had received an economic concession which it would not receive under normal economic conditions.
- (57) It could not therefore be right for the Commission, irrespective of whether a market-economy investor would have accepted a gradually increasing assessment basis for the remuneration, to set out to examine whether Helaba gained further advantages (improvement in general credit rating) from the non-remunerated part of the silent partnership contribution. In accordance with paragraph 327 of the *WestLB* judgment, reference could not be made only to the single undertaking benefiting from the investment. Any additional advantage to the recipient was irrelevant if, for whatever reason, a market-economy investor would not have required additional remuneration for such advantage. No institution would have been prepared to pay immediate remuneration on the total volume if it could use only slowly increasing partial amounts for business expansion purposes and also had no use whatsoever for the surplus amounts. However, the *Land* of Hessen wanted to invest its special housing fund, despite its size, *en bloc* with a single credit institution. A private investor would in such a situation not have insisted on immediate remuneration of the entire investment, unless it had found a credit institution which needed a capital injection on such a scale either because of explosive growth in its business activity or to offset massive losses. However, this had not been the case. Helaba had derived no advantage from those parts of the silent partnership contribution which in the first few years it could not use for banking supervisory reasons and was also not supposed to use because of the wishes of its owners.
- (58) On the basis of the phased arrangements agreed with the *Land* of Hessen, Helaba made use for business expansion purposes only of tranches of some DEM [...] million a year plus the abovementioned special quota of some DEM [...] million. In economic terms, the phased arrangements corresponded to the taking up of several silent partnership contributions spread over time. The amounts taken up by private institutions were therefore at best to be compared with the amounts of individual tranches. It could therefore be said that the order of magnitude involved was in conformity with the market. The *Land* could not demand a remuneration premium for the taking up of the special fund *en bloc*, which only Helaba was prepared to do, but had rather, as a result of the negotiations, to accept that a remuneration would be paid only on gradually increasing partial amounts of the investment.

- (59) The investment had quite properly not received any remuneration for its additional liability function through payment of a guarantee commission, since it had not been used by the bank in banking supervisory terms for business expansion. It would not have made sense in economic terms for a credit institution that was already accorded the top credit rating by all the rating agencies to pay a remuneration for the liability function of additional resources it had taken up. The terms and conditions under which the institution could take up outside capital would not have improved any further, so that no monetary advantage existed. The investor in whose interest the entire capital was transferred *en bloc* to the bank could therefore not have imposed any remuneration for the liability function.
- (60) The Commission's doubts, referred to in the decision to initiate proceedings, regarding the non-liquidity of the capital were based partly on the methodology of the WestLB decision, which could not however be applied to the present case because of the major differences in the underlying facts. According to Germany, in the present case the gross and not just the net refinancing costs had to be deducted from the remuneration of otherwise comparable, but liquid silent partnership contributions. This was because, even in the case of private credit institutions, the remuneration for the liquidity function of the silent partnership contributions taken up by them was tax deductible. If, in the case of Helaba, only the net refinancing costs were deducted from the notional remuneration for a liquid silent partnership contribution, the same process would have to be applied in the case of private credit institutions as regards the remuneration actually paid by them for liquid silent partnership contributions. Otherwise the comparison would be distorted.

IV. COMMENTS FROM INTERESTED PARTIES

1. COMMENTS FROM THE COMPLAINANT BDB

- (61) The BdB submits that Helaba did not pay an appropriate remuneration for the transferred core capital and was therefore in receipt of state aid.
- (62) In its comments of 29 July 2003 on the proceedings initiated on 13 November 2002 in respect of the Landesbanks, the BdB states that the question of whether the remuneration was appropriate should be determined using the method employed by the Commission in its WestLB decision.
- (63) The first step was therefore to compare the capital provided with other equity instruments. The second step was to determine the minimum remuneration which an investor would expect for a real equity-capital investment in the Landesbank. Finally, a calculation had to be made of any

premiums and discounts applied by virtue of the peculiarities of the transfer.

1.1. COMPARISON WITH OTHER EQUITY INSTRUMENTS

- (64) Nearly all the Landesbanks are said by the BdB to have required fresh core capital from 1992 onwards in order to meet the stricter requirements arising from the new Solvency Directive. Without these increases in capital, the Landesbanks would have had to scale down their business. It could therefore be concluded, the BdB argues, that the capital injected could be compared only with equity instruments that were recognised as core capital ('tier 1 capital') and available in Germany in the year of the transfer. This immediately excluded from any comparison non-voting preference shares, profit participation rights and perpetual preferred shares. In Germany, these three equity instruments were recognised not as core capital, but as additional capital ('tier 2 capital').
- (65) At the time of the respective transfers, only share capital and silent partnership contributions were recognised as core capital in Germany. In the BdB's opinion, the only legal form properly available to Helaba for the investment was share capital. The BdB does not challenge the recognition by the relevant authorities that actually took place. It argues rather that such recognition should not have taken place, since the silent contribution by the *Land* of Hessen that was specifically agreed was economically and legally comparable not with 'normal' silent partnership contributions, but rather with share capital. Given then, that such recognition had actually taken place, the remuneration at least of the silent partnership contribution of the *Land* of Hessen had to be based on that of share capital, since a market-economy investor would have required such remuneration on the basis of its similarity to share capital and specific risk structure.

- (66) The BdB gives an analysis here, based on a list of criteria, of why in its opinion the silent partnership contribution of the *Land* of Hessen was, in economic and legal terms, comparable with share capital and not with silent partnership contributions observed on the market.

- (67) The BdB bases this view essentially on the fact that 'normal' silent partnership contributions are only of limited duration and can be withdrawn and, under the principles of the Basle Committee on Banking Supervision, cannot be used for volumes above 15 % of core capital, whereas the silent partnership contribution of the *Land* of Hessen, like share capital, was of unlimited duration and allowed the 15 % limit to be exceeded. Furthermore, it could not be deduced from an agreement on the junior-ranking nature of the assets that there was a lower risk for the investor, since the transferred capital represented an important part of the entire core capital, in some instances more than 50 %. This

meant a much higher probability that the transferred capital would be called upon in the event of a loss, for which consequently a higher risk premium should be paid. The BdB also stated that, for banking supervisory purposes, silent partnership contributions were to be recognised only as lower tier 1 capital and hence, under the 1998 'Sydney Declaration' of the Basle Committee on Banking Supervision, could make up only 15 % of the necessary core capital ratio. Large-volume silent partnership contributions above this limit could not therefore be used. Lastly, the Deutsche Bank *perpetuals* referred to by Germany could not be taken as a criterion for the appropriate remuneration, since they all lay below the 15 % limit and hence would not have been alternatives for Helaba at the end of 1998.

(68) Another factor was that the *Land* made its contribution available to Helaba without any possibility of withdrawal on its part, i.e. for unlimited duration. Although a shareholder could not 'withdraw' his share capital, he was nevertheless

free to decide to sell his shares and invest elsewhere. Regardless of the details of the legal form, there was no such transferability in this instance if only because at all events there was virtually no market for a capital investment of this size and of unlimited duration. Private investors, by contrast, usually kept open the possibility of withdrawing their capital again in the event of persistently bad results and of investing again more profitably. A private investor would — if at all — accept the permanent tying of risk capital only in return for a correspondingly high yield.

(69) The form of capital transfer opted for here was therefore a normal share capital investment, for which a market-economy investor would expect a corresponding yield. In particular, it was not sufficient to take account of the unlimited term merely through a premium on the basic yield, determined for comparison purposes, on a silent partnership contribution of limited duration.

(70) The following two tables showed the essential differences between Helaba's 'silent partnership contribution' and other forms of equity capital available at the time of the investment:

	Helaba's 'silent partnership contribution'	Share capital	Silent partnership	Preference shares	Profit participation rights	Preferred shares
Availability on the German market in 1998	Yes	Yes	Yes	Yes	Yes	Yes
Status for banking supervisory purposes	Core capital	Core capital	Core capital only under certain conditions and 15 % limit	Additional capital	Additional capital subject to special conditions	Additional capital or core capital with 15 % limit

	Share capital	Helaba's 'silent partnership contribution'	Silent partnership
Usability for large volumes	Yes	Yes	No
Unlimited duration	Yes	Yes	No
Investor has no right of withdrawal	Yes	Yes	Yes
Participation in current losses	Yes	Yes	Yes
Repayment in insolvency proceedings, by creditor	Yes	Yes No internal 'junior-ranking nature' compared with share capital	Yes Repayment before share capital

	Share capital	Helaba's 'silent partnership contribution'	Silent partnership
Profit-share remuneration	Yes	Yes	Yes
No subsequent payment in the event of absence of remuneration	Yes	Yes	No Cumulative subsequent payment possible

1.2. TAX DEDUCTIBILITY

- (71) The BdB doubts that the profit share of the *Land* of Hessen is tax deductible as operating expenditure. In its view, it was to be assumed that the *Land* of Hessen was incurring a substantial business risk with the silent partnership contribution. This was evident not only from the size of the capital investment, but also from the fact that the participation was not withdrawable. This business risk justified the existence of a partnership (so-called atypical silent partnership), the ranking of the silent partnership contribution for tax purposes as partnership equity capital and the non-deductibility of the silent partner's profit share as operating expenditure on the part of Helaba.

1.3. MINIMUM REMUNERATION FOR A SHARE-CAPITAL INVESTMENT IN A LANDESBANK

- (72) The BdB argues that all methods of determining an appropriate remuneration (return) for the provision of equity capital start from a risk-free return and add a risk premium. They can be traced back to the following basic principle:

$$\begin{aligned} &\text{Expected return on a high-risk investment} \\ &= \text{risk-free return} + \text{risk premium for the high-risk} \\ &\quad \text{investment} \end{aligned}$$

- (73) To determine the risk-free return, the BdB uses the returns on long-term government bonds, fixed-rate securities issued by state bodies being the form of investment with the least or no risk⁽¹²⁾.

- (74) To derive the risk premium, the BdB first works out the 'market risk premium', i.e. the difference between the long-term average return on shares and that on government bonds. For the German share market, the BdB assumes, on

⁽¹²⁾ To offset the effects of inflation, the rate of return on a long-term government bond should be determined for each transfer period, initially disregarding the inflation expectations. Then, to estimate the long-term risk-free base rate, the estimated figure for average long-term inflation expectations (3,60 %) is added to the 'real base rate' at the time in question.

the basis of a study by Stehle-Hartmond (1991), a uniform long-term market risk premium of 4,6 %.

- (75) The BdB then determines the beta value for the Landesbanks, i.e. the individual risk premium for the banks, on the basis of which the general market risk premium was to be adjusted. The BdB stated that it had determined the beta values statistically, which means that it had estimated them on the basis of a historical data sample. The BdB concludes that all the beta values for all the Landesbanks and periods considered are greater than one⁽¹³⁾.

- (76) The BdB therefore calculates the expected minimum remuneration for an investment in the share capital of Helaba to be 11,66 % a year at the time when the promotion-related assets were transferred on 31 December 1998.

1.4. PREMIUMS AND DISCOUNTS ON ACCOUNT OF THE PARTICULARITIES OF THE TRANSACTIONS

- (77) The BdB notes that the Commission's deduction in its decision on WestLB of 4,2 % from the minimum remuneration of 12 % to take account of the lack of liquidity of the Wfa assets was upheld by the Court of First Instance. It therefore sees no reason to depart from this method in the present case, with the result that a deduction for liquidity should also be made here. The amount of the discount for lack of liquidity would be calculated, using the WestLB method, on the basis of net refinancing costs (gross refinancing costs minus the applicable corporation tax).

- (78) The liquidity deduction would be calculated for Helaba on the basis of a gross refinancing rate of 6,57 % a year (corresponding to the long-term risk-free base rate at the time of the transfer in 1998), to which the overall tax rate should be applied to obtain the net refinancing rate.

⁽¹³⁾ For the purposes of comparison, the BdB also gives the theoretical beta values calculated using the Capital Asset Pricing Model (CAPM), which, as it indicates, differ very little from the empirically determined values.

(79) In the BdB's view, three aspects of the transfer increase its risk compared with a 'normal share capital investment': the in part exceptionally high volume of assets transferred, the failure to issue new shares in the company and the related forgoing of additional voting rights, and the lack of fungibility of the investment, i.e. the impossibility of withdrawing the invested capital from the company again at any time. The BdB considers a premium of at least 1,5 % a year justified here in line with the WestLB methodology.

1.5. CAPITAL BASE AND ELEMENTS OF REMUNERATION

(80) The BdB stresses firstly that, in calculating the appropriate remuneration in the case of Helaba, the total amount which was recognised as core capital for underpinning competitive business should be taken as the basis and not solely the actually used or usable part. It backs up this argument by stating that a market-economy investor would never agree to limit his remuneration to the portion of funds actually used. For a private investor bearing the risk of losing his investment, it is irrelevant whether the credit institution actually uses the injected capital to expand its business. What matters to the investor is that he himself can no longer invest that amount and obtain a corresponding return.

(81) The calculation of the remuneration in the period 1998 to 2002 on the basis of tranches rising in annual steps had been justified not as a discount because of the fact that the transferred capital had not been 'split up' or by the fact that transfer 'en bloc' to Helaba would have had the effect of imposing a burden on it. Even if the capital transfer was perhaps not necessary to meet solvability criteria, it had nevertheless considerably increased Helaba's equity capital base and had allowed a strong expansion in its competitive activity. A market-economy investor would therefore require a full remuneration on the entire amount on the basis of its recognition as liable equity capital.

(82) The 0,3 % a year guarantee commission (*Haftungsprovision*) applied by the Commission in its WestLB decision, which it calculated by comparing the amount of capital with a guarantee, had to be charged for the part of the transferred core capital that could not be used to underpin competitive business.

(83) Only the guarantee commission (*Haftungsprovision*) and the perpetuity premium (*Permanenzzuschlag*) could be taken into account as components of the remuneration. Trade tax, most of which went not to the *Land* at all, but to the municipality, was not a part of the remuneration. It was a charge imposed by law, stemming from tax-related circumstances that were independent of the intentions of the parties.

(84) Lastly, the return was paid not to the *Land* of Hessen, but — after deduction of capital yield tax — 'allocated as a net

amount to the special fund'. Since Helaba was the (sole) owner of the special fund, it was in reality paying itself. A private investor would not have accepted this as a return for his investment.

2. COMMENTS FROM THE LAND OF NORTH RHINE-WESTPHALIA AND WESTLB

(85) On 30 October 2003, Germany forwarded a response from the *Land* of North Rhine-Westphalia and WestLB to the Commission's decision of 13 November 2002 to initiate proceedings in which they disputed the statement that the assets transferred to the Landesbanks could be compared to share capital. They argued that silent partnership contributions and 'perpetuals' had in fact been recognised as core capital in Germany since 1991. They added that remuneration for an investment depended not on how it was classified by the banking supervisory authorities, but on its risk profile. Since the assets were junior-ranking, the risk pattern had more in common with silent partnership contributions or 'perpetuals' than with share-capital investments.

(86) WestLB had no objections to the CAPM method for calculating the minimum remuneration for a share-capital investment, but it felt that the beta values determined by the BdB — at well over one — were inappropriate. A beta factor of more than one meant that a company's shares represented a higher risk than the market as a whole. Yet the risk of investing in a Landesbank was well below the overall market risk because of the institutional liability (*Anstaltslast*) and guarantor liability (*Gewährträgerhaftung*) which it enjoyed and which were not challenged at the time.

(87) Moreover, in the specific case of the Landesbanks, it was a mistake to use as a benchmark the return expected at the time that the assets were transferred to the banks. Although this was generally a sensible approach to adopt in relation to the private-investor test, it here meant using as a basis the returns expected in 1991. But for an investor to receive in 2003 the return expected in 1991, which was much higher than the returns actually achieved, flew in the face of all economic realities. Permanently and systematically applying a rate of return of around 12 % placed the Landesbanks at an unjustifiable disadvantage compared with private competitors.

(88) As regards the discount for the lack of liquidity of the transferred assets, WestLB and the *Land* of North Rhine - Westphalia considered that the rate for risk-free government bonds should be deducted in full from the basic return. They argued that the Landesbanks had received no liquidity as a result of the asset transfers. It was not defensible in economic terms to reduce this rate by the tax savings since the pricing of capital market instruments was

independent of the tax situation. Otherwise the price of a capital market instrument would have to differ according to tax considerations.

- (89) Lastly, the fact that the assets' lack of liquidity did not pose a risk to the liquidity position should be seen as reducing the risk — and hence the remuneration. This should be taken into account by applying a corresponding deduction. Likewise, a discount should be granted on account of the 'owner effect' since an investor who already owned shares in a company took a different view of an additional investment from that of a new investor.

V. GERMANY'S RESPONSE TO THE BdB'S COMMENTS

- (90) In Germany's view, the BdB was not successful in its attempt to reinterpret the silent partnership contribution as a share capital investment, nor was it able to raise doubts as to the appropriateness of the remuneration which was agreed and paid to the *Land* of Hessen. In Germany's view, therefore, there was no aid.
- (91) In Germany's view, there was no justification, in calculating the remuneration, for taking the roundabout approach of calculating the remuneration on a fictitious share capital investment. The *Land* of Hessen had from the outset transferred its housing-promotion assets as a silent partnership contribution to the bank. What was involved was therefore a financing instrument which was defined in company, tax and banking supervision law and which differed fundamentally from a share capital investment, in which the *Land* was not interested and which the owners of the bank did not want.
- (92) The BdB ignored important differences between share capital and silent partnership contributions and tried to identify non-existent differences between 'normal' silent partnership contributions and the silent partnership contribution of the *Land* of Hessen.
- (93) The BdB essentially argued that silent partnerships were of only limited duration or could be withdrawn and consequently, in accordance with the principles of the Basle Committee on Banking Supervision, were recognised as core capital only up to 15 % of the entire core capital of a credit institution. Since the silent partnership contribution of the *Land* of Hessen had been made available to Helaba without any time limit and was not covered by the 15 % limit and therefore did not represent a 'normal' silent partnership contribution, but functionally represented share capital, the criterion in assessing the remuneration should not be other silent partnership contributions or other innovative capital instruments, but share capital investments.
- (94) This core argument on which the BdB was relying was, for a number of reasons, erroneous. For example, limited duration or withdrawability were not a necessary and indispensable feature of silent partnerships either under company law or under banking supervision law. Conversely, share capital was not necessarily of unlimited duration and unwithdrawable. Under German company law, rather, all companies irrespective of their legal form could be set up for a limited period or it could be agreed that a contribution could be withdrawn subject to notice, which did not stand in the way of its recognition as core capital under German banking supervision law.
- (95) The BdB was also wrong in arguing that the 15 % limit for recognition as core capital under international banking supervision law did not, under the 'Sydney declaration' of the Basle Committee on Banking Supervision and the practice of the Germany supervisory authority based on it, apply to permanent capital instruments, which could be withdrawn only on the initiative of the issuer (but not of the investor). Furthermore, the practice of the German supervisory authority was now based on the assumption that a contribution with a term of at least 30 years and the explicit exclusion of withdrawal was made available to the investor on a 'permanent' basis and consequently did not come under the 15 % limit. This too showed that the difference between contributions of limited and unlimited duration was by no means as great as the BdB was arguing. As far as the appropriate remuneration was concerned, there was no cause or justification on this account for reinterpreting silent partnership contributions as share capital.
- (96) Only a few months after Helaba, the Deutsche Bank had taken up a 'permanent' contribution in the form of 'perpetuals', and had done so on the capital market. Contrary to what the BdB asserted, the 15 % limit did not, according to a newspaper report submitted on the subject, apply to this contribution, since no increase in the interest rate had been agreed if the bank did not exercise a right of withdrawal that had been accorded to it (no 'step-up' clause). The Deutsche Bank perpetuals were by no means exceptional in character, since in the subsequent period numerous other credit institutions had taken up 'permanent' contributions on the market, examples of which Germany provided. No single issue, whose volumes ranged from EUR 150 million to over EUR 2 billion, provided anything like the return of share capital; the remuneration lay in the range between 110 and 290 basis points above mid-swaps. Already in 1999, the market had, as regards remuneration, not attached any major importance either to the distinction between capital instruments of limited and unlimited duration or to the question of whether the issue proceeds fell under the 15 % limit or not.
- (97) Nor did Germany accept the criteria selectively applied by the BdB, which were supposed on the one hand to demonstrate common features between share capital and the silent partnership contribution of the *Land* of Hessen

and, on the other, differences between this silent partnership contribution and a 'normal' silent partnership contribution. The BdB was overlooking on the one hand the extent to which the shaping of silent partnership contributions could be shaped by agreement between the parties and, on the other, features that were essential and indispensable to the distinction between share capital and a silent partnership.

- (98) Share capital did not yield interest, but conferred a claim to payment of a dividend, which was not only dependent on profits, but above all in proportion to profits. The remuneration on a silent partnership contribution, by contrast, was only profit-dependent. Whether or not provision was made for retrospective payments in the case of a silent partnership contribution was a matter for agreement between the parties and was not in any case one of the constitutive features of a 'normal' silent partnership. However, under [...] pursuant to Section 10(4) of the German Banking Act, specific provision had been made, in the event of losses, for the junior-ranking retrospective payment requirement typical of silent partnership contributions. The prior-ranking requirement was to replenish the contribution again to the original amount from future profits ⁽¹⁴⁾.
- (99) The assertion that for very large volumes only share capital and not 'normal' silent partnerships could be used was contradicted by the size of the silent partnership contributions which private credit institutions had taken up on the capital market in 1998/99 and were also currently taking up. These ranged up into the area of around EUR 1 billion. In relative terms, any silent partnership contribution even over the 15 % limit was recognised as core capital if it met the requirements of the Basle Committee on Banking Supervision and was in line with the practice of the German supervisory authorities which was based on them.
- (100) Current evidence of the possibility of the 15 % limit being exceeded was provided by a capital measure taken on 2 December 2003 by a BdB member institution, the Deutsche Bank. This was the taking up of silent partnership contributions from private investors totalling EUR 300 million for an unlimited term (a so-called 'perpetual') ⁽¹⁵⁾. This illustrated once again how liquid and transparent the market for silent partnership contributions in respect of German banks was, even where large volumes were involved. With an agreed liability premium of 0,99 %, moreover, the measure provided further evidence that the liability remuneration that had been agreed for the silent partnership contribution of the *Land of Hessen* to Helaba had been calculated in a way that was market-related and market-adequate.
- (101) In response to a request from the Commission, Germany submitted a table showing the trend of silent partnership contributions and other hybrid core capital instruments for selected large banks in the private sector from 1998 to 2003. Germany argued that this made it clear that the institutions listed had also taken up hybrid core capital beyond the 15 % limit set for banking supervisory purposes, and the extent to which they had done so, since the proportion of total core capital accounted by such instruments exceeded 15 % (*).

	[Bank A]			[Bank B]			[Bank C]		
	Hybrid core capital instruments (of which silent partnership contributions)	Core capital (€ millions)	Share of hybrid core capital (%)	Hybrid core capital instruments (€ millions)	Core capital (€ millions)	Share of hybrid core capital (%)	Hybrid core capital instruments (€ millions)	Core capital (€ millions)	Share of hybrid core capital (%) (*)
1998	612 (612)	15 978	4 %	—	10 623	—	614	13,0	5 %
1999	3 096 (713)	17 338	18 %	1 495	12 908	12 %	1 937	14,6	13 %
2000	3 275 (768)	21 575	15 %	1 574	12 046	13 %	2 014	21,3	9 %

⁽¹⁴⁾ [...] states: '[...]'

⁽¹⁵⁾ See *Börsenzeitung* of 7 November 2003 and *International Financial Review* of 22 November 2003.

(*) The names of the listed banks in the private sector are confidential information and are referred to as Bank A, Bank B and Bank C.

		[Bank A]			[Bank B]			[Bank C]		
	Hybrid core capital instruments (of which silent partnership contributions)	Core capital (€ millions)	Share of hybrid core capital (%)	Hybrid core capital instruments (€ millions)	Core capital (€ millions)	Share of hybrid core capital (%)	Hybrid core capital instruments (€ millions)	Core capital (€ millions)	Share of hybrid core capital (%) (*)	
2001	3 404 (811)	24 803	14 %	1 923	11 542	17 %	3 650	21,7	17 %	
2002	2 973 (686)	22 742	13 %	1 732	8 572	20 %	4 164	19,1	22 %	
2003	3 859 (**) (572)	21 618	18 %	1 561	7 339	21 %	4 076	14,4	28 %	

(*) On the basis of full appropriation to core capital.

(**) Including cumulative preference shares after deconsolidation of trust companies.

(102) Contrary to what the BdB argued, both the silent partnership contribution of the *Land* of Hessen and silent partnership contributions taken up on the capital market would be paid back in the event of insolvency before the share capital, i.e. on a prior-ranking basis compared to the share capital. Contrary to what the BdB stated, the *Land* of Hessen like the investor of any other silent partnership contribution would in the event of insolvency receive the recovery percentage, whereas the owner would receive nothing, resulting in a reduced risk compared with share capital.

(103) A silent partnership differed significantly from share capital because the silent partner did not have a stake in the assets of the undertaking and also did not have any voting rights. The BdB had mistaken this in its analysis and thought that a premium should be paid for it. The market did not follow this line of thinking.

(104) The BdB's doubts as to the tax deductibility of the remuneration were unfounded. The *Land* of Hessen had taken on neither the entrepreneurial risk nor the entrepreneurial initiative necessary for the assumption of a partnership. The *Land* of Hessen, like any typical silent partner, participated, under the contract on the setting up of the silent partnership, only in Helaba's current profit and loss, but not in its undisclosed reserves, nor in the business value and increases in value in the operating assets. Upon termination of the silent partnership, it merely got back its contribution. The *Land* of Hessen had not been given any possibility of exercising company rights that corresponded to the voting, monitoring and contradictory rights of a limited partner or the monitoring rights of a shareholder in accordance with Article 716(1) of the Civil Code.

Furthermore, the state contract between the *Länder* of Hessen and Thuringia on the formation of a joint savings bank organisation had authorised the bank to take up an atypical silent partner. In the absence of partnership, the financial authorities had accordingly also recognised the tax deductibility of the remuneration paid to the *Land* of Hessen.

(105) Balance sheet treatment was also different. Share capital was serviced from the balance sheet profit (surplus of asset items over liability items) by decision of the general meeting of shareholders. In the case of the silent partnership contribution of the *Land* of Hessen, by contrast, the remuneration reduced the bank's operating result by reducing net interest received (the remuneration was a component part of expenditure on interest) and did not constitute profit utilisation, and did not therefore require any decision by shareholders. This mandatory balance sheet treatment of the silent partnership contribution reduced the cost-income-ratio and the balance-sheet equity return.

(106) Contrary to what the BdB argued, a market-economy investor would have agreed to the assessment basis for calculating his remuneration being limited to the part actually used for business expansion and would, for the excess part, not have required a remuneration of 0,3 % in line with the Commission's WestLB decision. Because of Helaba's limited requirement, made known from the outset, any other investor would not have been able to achieve any better negotiating result than the *Land* of Hessen.

(107) As far as the level of the appropriate remuneration was concerned, the BdB's argument was mistaken in its very approach. The criterion could only be remunerations that

had been agreed during the relevant period on the market for comparable silent partnership contributions to credit institutions. Differences in the shaping of the various silent partnership contributions, but also in the quality of the credit institutions taking them up, should be taken into account in the comparison of the remunerations through deductions from or premiums on such remunerations and not on the remuneration for a hypothetical share capital investment.

- (108) Quite apart from that, the determination of the yield on share capital investments by the BdB was erroneous. In determining the beta value, the Landesbanks should not be equated with credit banks with an above-average systematic risk. Rather, the proper criterion should be the clearly defined group of banks listed on the stock exchange, the so-called CDAX banks. A large proportion of Helaba's balance sheet total related to low-risk local authority, interbank and mortgage claims. As part of an objective business appraisal, an independent expert had, on 1 January 1999, determined for seven credit institutions with a comparable risk structure in terms of business risk, business activity, customer structure and size, an average beta factor of [...], i.e. well below 1. The expert had started from the assumption of a long-term market yield of 5,0 % and a long-term risk-free interest rate of 6,0 %. This gave, on 1 January 1999, an equity capital cost of [...] %. The BdB's assertion regarding the equity yield of 11,66 % on 31 December 1998 for Helaba was based on an excessive beta factor and, moreover, on historical data that were no longer current. The level of interest rates had changed significantly in recent decades, and the BdB's comments on inflation and inflation expectations were not comprehensible in this context.
- (109) Furthermore, the agreed remuneration for the duration of the silent partnership contribution could be compared only with the changing level of the relevant share capital yield and not, for example, with the share capital yield of the undertaking at the time of the investment. No-one would have guaranteed an owner of the bank an equity yield at the level of the end of 1998 and thus afforded protection from the risk of yield fluctuations.
- (110) The BdB's comments on the level of the deduction of refinancing costs did not stand up. Reference could be made to the net refinancing costs only if, from the comparative remunerations which private credit institutions pay for comparable silent partnership contributions taken up by them on the capital market, the theoretical or actual overall tax ratio of such institutions was deducted. For the contributions taken up on the capital market, however, it was usually not the overall remuneration, but only the remuneration premium that was given, which in the case of variable interest rate instruments and in the case of illiquid contributions, was identical with the liability remuneration. The comparison between the remuneration on the silent partnership contribution of the *Land* of Hessen and the remunerations paid on the market could, therefore,

be made directly. The roundabout approach of taking a fictitious overall remuneration on a fictitious cash contribution from which the refinancing costs then had to be deducted was unnecessary and, moreover, increased the uncertainty of the quantitative assessment many times over, since estimates then had to be introduced at a number of stages.

- (111) Contrary to what the BdB argued, there was no justification for any remuneration premiums. There was no empirical evidence that a premium was paid on the market for a particularly large contribution. Comparable capital-raising operations by private credit institutions did not reveal any connection between the amount and the remuneration. Rather, the *Land* had had to accept the agreed phased arrangements because Helaba had initially no use for the special fund *en bloc*. On the market, no investor would have been able to receive not only a remuneration immediately for the entire amount, but in addition a premium as well.
- (112) Furthermore, the argument that, in the case of share capital investments, the waiving of a voting right must be compensated for by an additional remuneration could not be applied to a silent partnership. The silent partner had by law no voting right, and the market did not grant any remuneration for the silent partner's 'waiving' of the possibility of exercising influence.
- (113) It was in principle true that, on the market, an investor accepted the lack of fungibility of his investment in return for a higher yield. Indeed, the lack of fungibility of the silent partnership contribution of the *Land* as compared with profit-sharing capital had been taken into account in the discussions leading up to the transaction. The parties had taken account of the perpetuity of the contribution in the form of the remuneration premium of 0,20 % a year. However, a private investor would have taken account of the fact that in this instance an investment was sought not for cash, but for a large, non-divisible special fund earmarked for a specific purpose that could be transferred only as an illiquid capital contribution. When the BdB argued that there was virtually no market for such an investment, this applied not only to reinvestment (fungibility), but also to the initial investment. It was not plausible that a private investor would in view of this have demanded or received an even higher premium than the 0,20 % a year agreed for the perpetuity aspect. Nor had the BdB provided any further explanation or justification on this point.
- (114) In the market comparison, lastly, contrary to the view put forward by the BdB, the trade tax effect had to be taken into account. Silent partnership contributions to credit institutions were usually provided by institutional investors which had themselves to pay the trade tax on the remuneration received. The *Land*, by contrast, was not liable to trade tax and would therefore be satisfied with a correspondingly lower remuneration. The counter effect of the non-liability

of the *Land* was the liability of the bank, which accordingly had to pay the trade tax. Whether it was paid to the *Land* or the municipality was irrelevant, as was the fact that the trade tax was assessed on the taxable income (usually the taxable income of the recipient of the remuneration, but here the taxable income of the bank), so long as the bank did in fact achieve income. If, by contrast, it suffered losses, not only was there no payment of trade tax, but also no payment of the remuneration on the contribution.

- (115) Contrary to what the BdB argued, Helaba did not pay the remuneration to itself either. In accordance with the decision of the *Land* of Hessen, the yield remaining after tax from the investment of the special fund did not accrue to the general budget, but was similarly tied to the earmarked purposes of the fund and was to be used to strengthen the promotion-related business. This was a question of the use of the resources paid by Helaba to the *Land*.

VI. ASSESSMENT OF THE MEASURE

1. STATE AID WITHIN THE MEANING OF ARTICLE 87(1) OF THE EC TREATY

- (116) Article 87(1) of the EC Treaty states that, save as otherwise provided in that Treaty, any aid granted by a Member State or through state resources which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods is incompatible with the common market, insofar as it affects trade between Member States.

1.1. STATE RESOURCES

- (117) With the transfer of silent partnership assets, the *Land* of Hessen opted for a form of contribution of resources based on the concept of transferring public aid resources to Helaba in order to strengthen its equity-capital base, but also of achieving additional income for the *Land* of Hessen. In spite of the fact that the returns from these claims were still available for promotion-related assets and hence served a public-benefit purpose, the assets were recognised by the supervisory authority and could therefore be used to provide cover for the liabilities of Helaba, which was in competition with other credit institutions. State resources therefore were transferred to Helaba.

1.2. FAVOURING OF A PARTICULAR UNDERTAKING

- (118) In order to verify whether the transfer of state resources to a publicly-owned undertaking favours the latter and is therefore liable to constitute state aid within the meaning of Article 87(1) of the EC Treaty, the Commission applies the

'market-economy investor principle'. This principle was accepted and developed by the Court of Justice and the Court of First Instance in a number of cases, in particular by the *WestLB judgment*, in a context which is relevant to the present case ⁽¹⁶⁾.

a) *Market-economy investor principle*

- (119) According to this principle, no state aid is involved where funds are made available on 'terms which a private investor would find acceptable in providing funds to a comparable private undertaking when the private investor is operating under normal market-economy conditions' ⁽¹⁷⁾. In contrast, the undertaking is being favoured within the meaning of Article 87(1) of the EC Treaty if the proposed remuneration arrangement and/or the financial position of the undertaking is such that a normal return on investment cannot be expected within a reasonable period of time.
- (120) The market-economy investor principle is applicable in the same way to all public enterprises, whether profitable or loss-making. The Commission's view here was upheld by the Court of First Instance in *WestLB* ⁽¹⁸⁾.

- (121) It follows that the key question in examining this case is whether a market-economy investor would have transferred to Helaba capital that had the same characteristics as the *Land* of Hessen's promotion-related assets and under the same conditions, especially in view of the probable return on the investment.

b) *Legal and economic classification of the capital contributed*

- (122) The *Land* of Hessen contributed to Helaba up to 31 December 1998 as silent partnership reserves promotion-related assets with a nominal loan portfolio for the *Land* share of DEM 6,026 billion (EUR 3,081 billion) and a cash value assessed on the basis of an expert evaluation of DEM 2,473 billion (EUR 1,264 billion). BAKred recognised these, as stated above, in full as basic own funds for supervisory purposes. They were to only a small extent required, on the basis of an amount which varied from year to year, to underpin promotion operations. This part of the silent partnership reserves shown in the balance sheet served only a guarantee function for Helaba. Most of the remainder was available to Helaba to underpin and expand its competitive business.
- (123) As in the *WestLB* case the Commission has determined the appropriate remuneration for the transferred promotion-related assets in the light of their commercial usefulness for

⁽¹⁶⁾ Judgment in Joined Cases T-228/99 and T-233/99.

⁽¹⁷⁾ Commission communication to the Member States on the application of Articles 92 and 93 of the EEC Treaty and of Article 5 of Commission Directive 80/723/EEC to public undertakings in the manufacturing sector (OJ C 307, 13.11.1993, p. 3, point 11). While this communication deals explicitly with the manufacturing sector, the principle can undoubtedly be applied in the same way to all other sectors. As regards financial services, this has been confirmed by a number of Commission decisions, e.g. *Crédit Lyonnais* (OJ L 221, 8.8.1998, p. 28) and *GAN* (OJ L 78, 16.3.1998, p. 1).

⁽¹⁸⁾ *WestLB judgment* paragraph 206 *et seq.*

Helaba. As explained above, the starting point for determining the normal market remuneration is primarily the remuneration that would be demanded by a market-economy investor providing a bank with equity capital.

- (124) The complainant argues that the capital made available to Helaba is, as in the case of the transfer of the WfA assets to WestLB, an investment similar to share capital. Germany disputes its similarity with share capital. It argues, rather, that the capital is a silent partnership, which affects the level of the remuneration.
- (125) Germany, Helaba and the complainant agree that the promotion-related assets comprised in the silent partnership of the *Land* of Hessen constitute core capital. The special-purpose reserve was recognised by BAKred as core capital ('tier 1 capital') and could therefore only be compared with equity instruments that were recognised as core capital in Germany in the year of the transfer and that were available to Helaba at the time of contribution specifically for an investment of this order of magnitude, which made up significantly more than 15 % of the core capital.
- (126) The Commission agrees with the parties on this point. It already made clear in its WestLB decision of 1999 that a comparison between the Wfa assets, which were also recognised as core capital, and equity instruments that were recognised only as additional capital, such as profit participation certificates and non-voting preference shares, cannot serve as a basis for determining the appropriate remuneration for the transferred capital (Decision 2000/392/EC, paragraph 199). Core capital is of much greater use to an undertaking because it can be used to raise additional own funds (such as profit participation certificates) up to the same amount in order to increase the bank's own funds. For the capital provided to be recognised as basic own funds, there must be greater exposure to risk, which as a general rule is also reflected in a higher market remuneration for such instruments. Any point of comparison with 'additional funds' that offer only limited scope for use in business expansion can therefore be ruled out from the outset.
- (127) In the view of the BdB, however, the only legal form properly available to Helaba for this specific investment was that of share capital. In the view of Germany, another legal form available was that of a silent partnership contribution of unlimited duration (*perpetual*), which met the requirements of Section 10(4) of the German Banking Act (KWG) and at the same time the criteria of the 'Sydney Declaration' of the Committee on Banking Supervision of the Bank for International Settlements in Basle, which in turn guided the decisions taken by the German banking supervisory authority BAKred. The subject of the agreement between the *Land* of Hessen and Helaba was, therefore, the legal form of a silent partnership contribution of unlimited duration, which was recognised as such both by the competent banking supervisory authority BAKred and also by the competent tax authority.
- (128) In the Commission's view, Germany has demonstrated sufficiently that the BdB's argument will not stand up. The BdB argues that the silent partnership of the *Land* of Hessen represented a formal abuse of a 'normal' silent partnership. In economic terms, the silent partnership contribution had so many points in common with share capital that an investor would have insisted on the payment of interest corresponding to the remuneration of share capital.
- (129) The Commission notes firstly that the silent partnership contribution was expressly agreed as such between the *Land* of Hessen and Helaba and accepted as such by the competent German authorities. In order to be able to assume that there was an abuse of form, it would have to be beyond question that the competent German authority wrongly recognised the silent partnership of the *Land* of Hessen as such. However, there is no evidence of this. The Commission agrees here with Germany's view that the limited duration or withdrawability of a silent partnership contribution is, neither from the company law nor banking supervision points of view, a necessary characteristic feature for the recognition of a silent partnership as core capital pursuant to Section 10(4) of the German Banking Act. Furthermore, the Commission interprets the 'Sydney Declaration' of the Basel Committee on Banking Supervision of October 1998 as imposing a 15 % limit only for the recognition of certain innovative capital instruments, particularly those limited in time, as core capital. However, the converse conclusion may not be drawn that permanent innovative capital instruments may not at all be recognised as core capital or are also covered by this limit. Moreover, the usefulness of permanent innovative capital instruments as core capital above the 15 % limit is testified to by the practice of private banks as well in recent years, as was amply demonstrated by Germany.
- (130) Nor does the Commission regard the selective criteria adduced by the BdB as sufficiently convincing. From the risk analysis point of view, the silent partnership of the *Land* of Hessen is more similar in type to a 'normal' silent partnership than to share capital. The Commission agrees with Germany's comments here too.
- (131) For the Commission, it is crucial in this context that both the silent partnership of the *Land* of Hessen and other 'normal', i.e. time-limited silent partnerships taken up on the capital market must in insolvency proceedings be paid back before share capital and that the investor thus gets the recovery percentage, whereas in the case of a share capital investment he gets nothing. Germany submitted a legal opinion demonstrating that, under the contractual provisions, the silent partnership contribution of the *Land* of Hessen will, in the event of solvency or liquidation, in so far as it has not been reduced or used up by losses, be met on a prior-ranking basis before share capital from any remaining assets.
- (132) Furthermore, so long as the undertaking is not making a loss, both the *Land* of Hessen and the investor of a time-

limited silent partnership get the entire agreed remuneration, whereas the investor in share capital can claim only payment of a dividend that is in proportion to profits. In this respect too, the silent partnership contribution of the *Land* of Hessen is a typical silent partnership contribution within the meaning of Section 10(4) of the German Banking Act.

(133) Nor is the BdB's objection convincing that the silent partnership was equivalent to share capital because in the long term it had resulted in an increase of almost 50 % in Helaba's core capital. Account should be taken here firstly of the phased arrangement which the *Land* of Hessen and Helaba had agreed and under which, in the period from 1999 to 2002, in line with its actual capital requirement, Helaba could use only an annual increasing partial amount of the usable core capital to actually cover core business. Furthermore, the Commission would in this context draw explicit attention to the fact that, in the WestLB case too, the large volume of the capital injection is merely an indicator, but not on its own decisive in assuming similarity to share capital. In the WestLB decision, the Commission concluded, on the basis of an overall assessment, that the similarity of the transaction being examined to a share capital investment was predominant. An essential consideration in this respect was, for example, the fact that the WfA assets had, like share capital, been exposed to the full risk of loss in the event of solvency or liquidation. Furthermore, in the WestLB case, the Commission also took account of the fact that, at the time of the transfer of the WfA assets in 1991 — in contrast to the time of the transfer of the silent partnership contribution of the *Land* of Hessen to Helaba in 1998 — there was not yet a developed market for hybrid core capital instruments in Germany and a credit institution such as WestLB could have taken up a comparable core capital volume on the market only in the form of share capital. In the current case, Helaba could also easily have covered its estimated capital requirement in the period from 1998 to 2002 on the market by taking up, at intervals, several smaller silent partnership contributions from a number of different institutional investors.

(134) The BdB also points out that, with the silent partnership contribution of the *Land* of Hessen, Helaba's share capital buffer was only 50 %, whereas, in the case of private credit institutions, the share of hybrid instruments in core capital is below 20 % and hence the share capital buffer amounts to more than 80 %. An institutional investor would, according to the BdB, against the background of this high share in Helaba's overall core capital, not have agreed to a comparable contribution. Germany confirmed that the proportion of core capital accounted for by the silent partnership contribution in 2003, i.e. after the last stage of the phased arrangement had been reached, was [...] % and that the proportion accounted for by all the silent partnership contributions (i.e. not only the silent

partnership contribution of the *Land* of Hessen) in 2003 amounted to [...] %. Nevertheless, in the Commission's view, it cannot necessarily be deduced from this that an institutional investor would not have made a comparable silent partnership contribution because of the high proportion of total equity capital it represented. Germany pointed out that Landesbanks generally make greater use of silent partnership contributions beyond the 15 % limit as instruments of core capital procurement, and do so predominantly from amongst their guarantors, but also from third-party investors. For example, according to the information provided by Germany, the share of silent partnership contributions of in 2003 was 72 % in the case of [...] ⁽ⁱ⁾, 39 % in the case of [...] ⁽ⁱⁱ⁾, 33 % in the case of [...] ⁽ⁱⁱⁱ⁾ 39 %, in the case of [...] ^(iv) and 42 % in the case of [...] ^(v) ⁽¹⁹⁾. The reasons for this high share of hybrid instruments have to do with the fact that, because of their public-law structure, the Landesbanks are not allowed to raise capital on the stock markets. It also seems that investors in Landesbanks are more prepared to accept a smaller share capital buffer, since, because of the different business orientation and the accompanying reduced risk structure of the institutions, the capital is exposed to a generally smaller risk. At least in the case of Helaba, which, even within the group of the above-mentioned Landesbanks, must be regarded as a comparatively low-risk credit institution, the Commission cannot therefore exclude the possibility that, despite a share capital buffer of (only) some 50 %, an institutional investor would have made a comparable investment in the form of a silent partnership contribution to Helaba.

(135) The Commission also examined in detail to what extent the perpetuity of the contribution, i.e. the fact that it is of unlimited duration and not withdrawable subject to notice by the *Land* of Hessen, affects the risk analysis to be carried out here.

(136) The BdB argues here that no hybrid instruments of unlimited duration exist on the capital market. Institutional investors were in principle prepared to acquire only hybrid equity instruments of fixed duration or instruments for which repayment could be assumed, because the payout rate was higher (so-called step-up) or the instrument was transformed into another form of investment at a given point in time. Step-up clauses gave the debtor (issuer) a strong economic incentive to repay the silent partnership contribution. A step-up clause thus made a *perpetual* in actual fact into an instrument with a fixed term. Furthermore, innovative core capital instruments were typically placed only by private investors.

(137) Germany and Helaba argue in response to this that, even in the case of *perpetuals*, investors have to reckon with step-up, that, contrary to possible expectations, at the time when the step-up clauses become effective, there is no 'on-schedule'

⁽ⁱ⁾ Confidential information, designated here as bank I.

⁽ⁱⁱ⁾ Confidential information, designated here as bank II.

⁽ⁱⁱⁱ⁾ Confidential information, designated here as bank III.

^(iv) Confidential information, designated here as bank IV.

^(v) Confidential information, designated here as bank V.

⁽¹⁹⁾ Communication from the Federal Government of 1 October 2004, p. 16.

repayment and that thus the perpetuity risk exists. This was due, firstly, to the fact that the right of withdrawal lay solely with the debtor (issuer); secondly, the economic situation of the issuer at the time the step-up clause became effective was crucial for on-schedule repayment; thirdly, the supervisory authority had to approve the withdrawal, and it gave its approval only if the debtor had, at the time of the withdrawal, a comfortable equity capital base or carried out a replacement transaction on the market. Furthermore, examples showed that even institutional investors placed hybrid instruments with unlimited duration and without step-up, one instance cited by Germany being a junior-ranking Air Canada loan of unlimited duration from 1987 which, as the Commission ascertained, did indeed not have any step-up arrangement. Germany also argued that, although the existence of withdrawal rights was taken into account in the prices, the remuneration corridor was not wide.

- (138) For the Commission, the key point in the situation to be assessed here is the fact that the perpetuity of the contribution in this instance involves primarily the risk for the investor of not being able to profit from interest rate increases on the market, since, on the one hand, he has no possibility of withdrawal and, on the other, cannot rely on a step-up. The perpetuity aspect does not, however, involve the risk of loss in the event of insolvency or liquidation. Against this background and taking account of the market description provided by Germany, the Commission therefore takes the view that the unlimited duration of the contribution does not in this instance justify changing the reference to the product from 'silent partnership contribution' to 'share capital'. However, the Commission will later examine whether the perpetuity aspect justifies a premium on the usual market remuneration for the silent partnership contribution.
- (139) The conclusion must be, therefore, that in the case of Heleba the transfer was undoubtedly made in the legal form of a silent partnership that has much more in common with other silent partnerships than with share capital. There is, therefore, in the Commission's view, not sufficient evidence of an abuse of the legal form of a silent partnership for a contribution of capital that in actual economic terms constituted share capital. The basis for the remuneration of the relevant capital instrument is, therefore, 'normal', i.e. time-limited silent partnership assets typical in size of those observable on the market, on whose remuneration a premium may possibly have to be charged. The comments of the BdB on the appropriate remuneration of share capital are therefore not relevant.
- (141) The 'business-expansion function' of capital refers to the expansion of business potential by means of risk-bearing assets following the recognition for supervisory purposes of a bank's additional equity capital. In this regard the starting point for determining the normal market remuneration is the remuneration that would be demanded in the specific situation by a private investor providing a bank with equity capital. In so far as capital made available is shown in the balance sheet as equity capital but is not recognised for supervisory purposes as equity capital or is used to underpin promotion activities or for other reasons cannot be used to underpin competitive business, it is not available for business expansion. However, capital is also important for reasons other than banking supervision. Its availability to the bank's creditors at least for the purposes of covering liabilities ('liability function') means that its economic function can still be compared to that of a surety or guarantee. The amount of equity shown in the balance sheet gives the bank's lenders an indication of its soundness and may thus influence the conditions under which the bank is able to raise outside funds. The normal market remuneration of the 'liability function' of capital is calculated according to the return which a private guarantor would have demanded in this specific situation from a credit institution comparable to Heleba in size and risk strategy.
- (142) Consequently, in calculating the remuneration, the silent partnership recognised in full as core capital must be divided into two separate capital bases. The capital base which was available to underpin Heleba's competitive business must be remunerated in the same way as a market-economy investor would have reasonably required for a silent partnership with the same characteristics in this specific situation. The capital base that was not available for Heleba's competitive business must be remunerated in such a way as a market-economy investor would have reasonably required in this specific situation.

Capital base that was available to underpin Heleba's competitive business

c) Determination of the capital base to be used in determining the remuneration

Capital base standard

- (140) In determining the capital base to be remunerated, the Commission distinguishes firstly between the 'business-expansion function' and the (mere) 'guarantee function' of the promotion-related assets made available as equity capital for the business activity of the credit institution.
- (143) The Commission takes the fundamental view that the extent to which the capital provided was actually used cannot be a factor in determining the appropriate remuneration. All that matters is the possibility of using the capital to expand business. Even a private investor would not be happy with a remuneration dependent on the capital being used. In this regard, the Commission agrees in principle with the BdB's observation that, for the market-economy investor who runs the risk of losing his investment, it is irrelevant whether the credit institution actually uses the injected capital to expand its business. As the BdB rightly points out in principle, all that matters to the market-economy investor is that he himself can no longer use the amount transferred to engage in economic activity and hence achieve corresponding returns. To illustrate the point one might take the example of a rented

house: a landlord will insist on rent being paid even if, for whatever reason, the tenant no longer lives in the house, as by renting to the tenant, the landlord is forgoing the possibility of renting to someone else, and, in any event, he has no control over where the tenant resides. It is therefore the usability of the house that is the subject of the contract.

(144) The Commission notes firstly that the capital base to be remunerated as agreed which was available to Helaba to underpin competitive business is not dependent on actual use, but focuses only on usability to underpin competitive business. The arrangement accordingly is in line with the Commission's criteria outlined above.

(145) The *Land* of Hessen and Helaba agreed on the 'phased model' described above. Under that model, although the cash value of the entire promotion-related assets was entered in the balance sheet on 31 December 1998 so as not to have to divide up the promotion-related assets, most of the promotion-related assets, i.e. with the exception of the part required to underpin the promotion-related business, were de facto usable to underpin the competitive business. However, Heleba made it clear from the outset to the *Land* that, in line with its business plan, it required the assets only in stages, i.e. according to the agreed phased instalments, to underpin its competitive business. Within the stages, however, the key criterion was the usability of the capital, i.e. the remuneration was not dependent on actual use. On the basis of this clear plan of use, the capital base to be remunerated was clearly predictable for the *Land* of Hessen. The *Land* of Hessen therefore did not leave use to the business discretion of the bank, but accepted the arrangement on the basis of Heleba's clear wish.

(146) The Commission considers this approach compatible with the conduct of a market-economy investor who, in the situation of the *Land* of Hessen, would not realistically have been able to achieve any faster increase in the capital base to be remunerated, since, in view of its business plan, Heleba would not have agreed to it. Consequently, in the Commission's view, from 1999 to 2002 only the stages provided for and, only from 2003, the full amount of the silent participation usable to underpin competitive business are to be remunerated in such a way as a market-economy investor would have required for a silent participation having the same characteristics in this specific situation.

Capital base entered in the balance sheet, but not available to Helaba for competitive business

(147) As stated above, the amount of the silent participation that could not be used to underpin competitive business was

also entered in Heleba's balance sheet on 31 December 1998. It was in full a component part of the liable equity capital and was thus from the outset available as security to the bank's creditors. Potentially at least, this represents an advantage for the bank, since the level of the equity capital shown in the balance sheet gives the bank's investors an indication of its soundness and may thus influence the conditions under which the bank is able to raise outside funds.

(148) Germany argues that the fact that Helaba entered the full amount of the silent partnership contribution of EUR 1 264.4 million in the balance sheet directly after receiving it cannot be interpreted as having had any effect in improving the bank's credit standing. Since the mid-1980s Helaba has been ranked in the top category AAA/Aaa in the long-term credit standing rating which is relevant for creditors of the bank, with the key criteria being the existing liability arrangements such as 'institutional responsibility' (*Anstaltslast*) and 'guarantor liability' (*Gewährträgerhaftung*) and hence the creditworthiness of the guarantors. Showing the silent partnership contribution in the balance sheet could not have improved this outstanding top-rank credit standing any further. ⁽²⁰⁾

(149) Germany also argues in response to further enquiry from the Commission that even if the Moody's Investors Service financial strength rating for Helaba and Fitch's individual rating during the relevant period are taken into account, the silent partnership could have had no perceptible influence on the ranking of Helaba's financial strength. The two ratings mentioned were based, notwithstanding the existing state liabilities in the form of *Anstaltslast* and *Gewährträgerhaftung* and ownership structures, solely and directly on the profitability of the relevant institution, the quality of its management, the market position and also equity capital endowment. ⁽²¹⁾ The two ratings remained unchanged from 1997 to 2000, i.e. despite the contribution of the silent partnership at the end of 1998 (Moody's financial strength rating remained at C+ and the Fitch individual rating at B/C) and deteriorated as from 2001 (Moody's financial strength rating fell to C+ (neg.) and C(neg.) and the Fitch individual rating to C). In Germany's view, this showed that the silent partnership had had no influence on Helaba's credit standing even leaving aside the existing state liabilities. ⁽²²⁾

⁽²⁰⁾ Germany's reply of 23 June 2004, p. 12.

⁽²¹⁾ Germany's reply of 23 June 2004, p. 12, Annex 29/2004, Fitch Ratings: Bank Rating Methodology: May 2004, p. 12: 'Principal considerations are profitability, balance sheet integrity (including capitalisation), franchise, management, operating environment, consistency, as well as size (in terms of a bank's equity capital)'.

⁽²²⁾ Germany states that the reason for this, as already mentioned, was the fact that the minimum supervisory standards for capital ratios (core capital ratio of 4,0 %, overall ratio or equity ratio of 8,0 %) were more than met during the relevant period, which was a significant difference compared to the situation with WestLB. In 1997, for example, i.e. before the contribution, in accordance with Principle I to Section 10a of the German Banking Act, the core capital ratio was 4,8 % for the Helaba group and 5,0 % for the Helaba institution on its own. In accordance with the principles of the Bank for International Settlements, the core capital ratio (tier 1) was 5,4 % in 1997. The overall ratio and equity ratio in 1997 were 8,9 % and 9,6 % for the group and 9,2 % for the institution on its own. Even against the background of the business growth planned by Helaba for the following financial years, there was no direct need for the taking-up of core capital amounting to EUR 1 264.4 million.

- (150) The Commission cannot agree with Germany's argument. Germany's comments on the financial strength rating and individual rating show rather than a financial institution's endowment with equity capital is an important factor for the quality of a rating and hence also for financial standing. From an ex ante perspective, i.e. at the time of the agreement on the silent partnership between the *Land* of Hessen and Helaba, the two parties had to start from the assumption that the entering of core capital amounting to some EUR 1,2 billion was such as to further improve the bank's financial standing. The financial strength ratings given by Moody's and Fitch and cited by Germany show that a further improvement was entirely possible, since the ratings had by no means reached the highest level. The fact that ex post no change in the financial strength rating was discernible does not necessarily mean that there was no positive influence on the financial strength rating. The positive influence of the significant increase in the core capital base could have helped to ensure that the financial strength rating did not fall for other reasons or did not fall faster than it in fact did, i.e. only as from 2001.
- (151) In assessing the potential influence (to be assessed ex ante) of a measure on the financial standing of a bank and/or on future financing conditions, the Commission sees the financial strength rating of a Landesbank as being important in its own right alongside the long-term rating based on the existing state liabilities in the form of *Anstaltslast* and *Gewährträgerhaftung*.
- (152) As far as the (from the point of view of 1998) future borrowing of outside capital is concerned, Helaba obtained in 1998 and the following years the top rating of AAA/Aaa on the basis of *Anstaltslast* und *Gewährträgerhaftung*. As far as the Commission is aware and as Germany itself points out, the actual refinancing costs of a bank vary or fluctuate, in comparison with other similarly rated banks, within a corridor for a given rating category. In other words, specific refinancing costs cannot be deduced precisely and unchangingly for all similarly rated banks and over time from a specific long-term rating, in this instance AAA/Aaa. It follows from this empirical observation that other influences and factors play a role, such as the financial strength of Helaba in relation to other Landesbanks with the same long-term rating on the basis of *Anstaltslast* and *Gewährträgerhaftung*. The better Helaba's financial strength is, the better are its prospects, within the AAA/Aaa rating category, in specific negotiations on refinancing conditions, of finding itself at the favourable edge of the corridor of the refinancing conditions observable on the market for AAA/Aaa. Furthermore, its dependence on the rating of the guarantors is reduced, i.e. in the event of a possible deterioration in their rating, which cannot be excluded ex ante, Helaba could use its individual financial strength as an argument in defence of its favourable refinancing conditions.
- (153) As far as the (from the point of view of 1998) future borrowing of further outside funds is concerned, which in fact took place in 2001 in the form of further silent partnership assets, a large capital buffer entered in the balance sheet reduces the probability of the new capital being lost in the event of bankruptcy provided that old and new capital are liable on a *pari passu* basis. Germany stated that such *pari passu* liability is the rule with silent partnerships. From the perspective of 1998, therefore, it could not be ruled out that new investors might insist on it.
- (154) Germany also argued, in response to an enquiry by the Commission, that silent partnerships within the meaning of Section 10(4) of the German Banking Act do not fall within the protected area of *Anstaltslast* and *Gewährträgerhaftung*. This was the direct consequence of the contractually arranged participation in losses as a precondition for the recognition of the silent partnership reserves as liable own funds. Consequently, the investor was not to be regarded as a creditor of the bank and was not covered by *Gewährträgerhaftung*. Similarly, he was not covered by *Anstaltslast*, since that provided only for the obligation of providing the institution with an economic basis and of making available the contributions required for maintaining normal business operation. This in no way excluded third-party participation in losses. Losses were in principle possible up to the point where the liable own funds had been used up. Consequently, the silent partner is not protected in his asset interests by the intervention of the guarantor on the basis of *Anstaltslast*. In view of the fact that equity investors do not fall within the protective scope of '*Anstaltslast*' and '*Gewährträgerhaftung*', the individual financial strength of Helaba, which was enhanced or kept constant, had, from the viewpoint of 1998, in the Commission's view a positive influence on the future terms and conditions on which Helaba was able to take up further equity such as silent partnerships.
- (155) The Commission concludes that the substantial improvement in the core-capital ratio for supervisory purposes which was achieved through the immediate entry of the silent partnership in the balance sheet in 1998 represented, at least from an ex ante point of view, a potentially decisive factor in the assessment of the individual financial strength and future financing conditions of the bank and hence an advantage for Helaba, regardless of whether the amount was used to underpin competitive business. A market-economy investor who, as a result of the immediate entry of the entire invested capital in the balance sheet, exposed it in full to the risk of loss in the event of bankruptcy would have required an appropriate remuneration reflecting this loss risk. For its part Helaba, on the basis of the at least potential advantage to it, whose actual achievement depended on future developments which were not fully foreseeable in 1998, would have agreed to a remuneration. The Commission therefore agrees on this point in principle and on the basis of a factual analysis with the comments of the complainant BdB.

d) **Appropriate remuneration for the capital contributed and comparison with remuneration actually paid**

(1) *Assessment of whether the remuneration that was agreed for the capital to be used to underpin competitive business was the normal market remuneration*

(aa) Preliminary remark

(156) As explained, the Commission considers the capital measure agreed between the *Land* of Hessen and Helaba to be a silent partnership. Consequently, in examining whether the remuneration specifically agreed was appropriate to the market, it is important to determine whether such remuneration can be regarded as lying within the corridor of remunerations agreed on the market in economically and legally comparable transactions involving silent partnerships.

(157) According to information provided by Germany, however, in making the market comparison of the silent partnership of the *Land* of Hessen, the trade tax effect of (in relation to Helaba's silent partnership) 0,26 % a year must be taken into account. Helaba had to pay on the remuneration of 1,4 % trade tax to which the *Land* of Hessen was not subject, so that there was a total charge of 1,66 % (before tax). Commercial investors operating in Germany pay trade tax on dividends from silent partnership assets. However, the *Land* of Hessen is not subject to trade tax. Instead, Helaba had to pay the trade tax applicable to the remuneration of the silent partnership. A market-economy institutional investor would therefore have required a higher remuneration than the *Land* in order to offset the charge he had to pay in the form of trade tax. Conversely, Helaba would have been immediately prepared to pay a remuneration premium to such an investor, since it makes no difference to it whether it pays the premium as a remuneration to the investor or as trade tax to the tax office.

(158) When the BdB argues that the trade tax, most of which does not go to the *Land* at all, but to the local authority, is not a component part of the remuneration, but a charge imposed by law, stemming from tax-related circumstances that are independent of the intentions of the parties, this is in itself, in the Commission's view, correct. However, the BdB fails to recognise that in making the market comparison the question is not ultimately whether the trade tax does or does not represent a part of the remuneration. The point is rather to take account of Helaba's special situation in taking up the silent partnership of the *Land* of Hessen and, in particular, of the particular charge involved here, which would not have arisen in taking up silent partnerships from commercial investors, in the market comparison to be carried out here.

(159) The Commission therefore shares Germany's view that, in the market comparison, the trade tax of 0,26 % a year to be paid by Helaba must be added to the remuneration of

1,40 % a year, giving a total charge of 1,66 % a year. According to information provided by Germany, the trade tax may be divided proportionally between the two remuneration components, with 0,23 % a year apportioned to the agreed initial remuneration of 1,2 % a year and 0,03 % apportioned to the agreed perpetuity premium of 0,2 %. For the purposes of the market comparison, therefore, the rate of 1,43 % a year is to be applied for the initial remuneration and the rate of 0,23 % a year for the perpetuity premium.

(bb) Customary market nature of the agreed initial remuneration of 1,2 % a year (rate of 1,43 % a year for the purposes of the market comparison taking account of the trade tax)

(160) The initial remuneration of the relevant silent partnership is to be determined, using the method applied by the *Land* of Hessen and Helaba, on the basis of time-limited, but otherwise comparable, silent partnerships. The question of the appropriate remuneration for the unlimited nature of the period covered by the silent partnership of the *Land* of Hessen must be examined separately under point bb) with a view to a premium on this initial remuneration.

(161) Germany presented comprehensive data on remunerations of time-limited silent partnerships round about the time of the contribution at the end of 1998 and thereafter.

(162) According to the information provided by Germany, in comparing premiums for silent partnerships, a distinction should be drawn on the basis of the reference interest rate. If, in the case of a variable overall remuneration, the remuneration premium relates to the (variable) money market interest rate on the interbank market (Libor or Euribor), i.e. the refinancing rate for first-class banks, this corresponds to the liability remuneration for the silent partnership without any need for further adjustment. However, if, in the case of a fixed overall remuneration, the remuneration premium relates to the (fixed-interest) bond market rate (generally the yield on public bonds with a ten-year maturity), the remuneration premium consists of the (general) refinancing premium of the bank vis-à-vis the State for the procurement of liquidity and the specific liability remuneration for the silent partnership. For the purposes of comparing the liability remuneration with money-market-related liability remunerations, therefore, the refinancing premium must in this case be deducted from the remuneration premium. With illiquid capital contributions, as in the case of the silent partnership contribution of the *Land* of Hessen, the remuneration premium is, however, as with variable-interest money-market-related instruments, usually identical to the liability remuneration.

(163) It follows from this that the remuneration for the silent partnership contribution of the *Land* of Hessen, as an

illiquid capital contribution, can be compared directly with money-market-related remuneration premiums (i.e. variable-interest overall remunerations), since these correspond to the liability remunerations. In the comparison with bond-market-related overall remunerations, however, the refinancing premium (from in principle around 20 to 40

basis points, leaving aside further short-term upward or downward deviations, in the relevant periods according to the information provided by Germany⁽²³⁾ must be deducted from these in order to determine the specific liability remuneration for the silent partnership contribution.

- (164) On the basis of the information provided by Germany, the Commission has carried out the market comparison on the basis of the comparative transactions which are listed in the following table and which were known to the *Land* of Hessen and Helaba either at the time of the transaction at the end of 1998 or, where they took place some months later, through their direct chronological proximity, allow conclusions to be drawn as to the market conditions prevailing at the time of the transaction at the end of 1998:

Relevant comparative transactions ⁽²⁴⁾						
Description of the transaction	Volume	Term	Financial strength/ product ratings	Remuneration premium p.a. (in basis points)	Reference interest rate and any adjustment (²⁵) of the remuneration premium by deduction of the refinancing premium	Liability remuneration of relevance for comparison
Silent partnership contribution to Helaba made in December 1997 by the Hessen and Thuringia savings banks	DEM 300 million	10 years	FSR: Aaa/AAA (because of state liabilities) PR: ?	1,2 %	10-year federal loan (adjustment through deduction of 20-40 bp)	80-100 bp
Fixed-interest USD tranche of the silent partnership contribution to Deutsche Bank, January 1998	First tranche of USD 700 million	10 years	FSR: AAA/Aa1 PR: AA-	80 bp	12-month Libor (no adjustment)	80 bp
Variable-interest USD tranche of the silent partnership contribution to Deutsche Bank, January 1998	Second tranche of USD 700 million	10 years	FSR: AAA/Aa1 PR: AA-	140 bp	10-year US treasuries (adjustment through deduction of 65 bp ⁽²⁶⁾)	75 bp
Variable-interest silent partnership contribution to SGZ-Bank, October 1998	DEM 50 million	10 years	FSR: A1/A+ PR: ?	120 bp	12-month Libor (no adjustment)	120 bp

⁽²³⁾ See Germany's reply of 9 April 2003, Annex 15-16. The figures relate to the refinancing premium for euro banks as opposed to federal loans and the refinancing premium on bank bonds (10-year mortgage bonds) as opposed to federal loans. In the absence of figures for the corresponding refinancing premium as compared with US treasuries and on the basis of their fundamental economic comparability, the Commission is using the above-mentioned corridor for refinancing premiums for US treasuries as well, since it is not precise figures, but the order of magnitude that matters in determining the corridor for the relevant liability remuneration.

Relevant comparative transactions ⁽²⁴⁾

Description of the transaction	Volume	Term	Financial strength/ product ratings	Remuneration premium p.a. (in basis points)	Reference interest rate and any adjustment ⁽²⁵⁾ of the remuneration premium by deduction of the refinancing premium	Liability remuneration of relevance for comparison
Silent partnership contribution to HypoVereinsbank, December 1998	First tranche of DEM 1,2 billion ⁽²⁷⁾	10 years	FSR: Aa2, Aa3/ AA- PR: A2	160 bp	DEM Libor (no adjustment)	160 bp
Euro tranche of the silent partnership contribution to Dresdner Bank, May 1999	EUR 500 million	12 years	FSR: Aa1/AA PR: Aa2; A+	165 bp	10-year German federal loan (adjustment through deduction of 20-40 bp)	125-145 bp
USD tranche of the silent partnership contribution to Dresdner Bank, May 1999	USD 1 billion	32 years	FSR: Aa1/AA PR: Aa2; A+	215 bp	30-year US treasuries (adjustment through deduction of 65 bp ⁽²⁸⁾)	150 bp
Silent partnership contribution to HypoVereinsbank, May 1999	EUR 500 million	12 years	FSR: Aa2, Aa3/ AA- PR: ?	125 bp	12-month Euribor (no adjustment)	125 bp
Euro tranche of the perpetual for Deutsche Bank, July 1999	EUR 500 million	No limit	FSR: Aa3/AA PR: A1	Overall 6,6 % (corresponds to 115 bp)	Corresponds to 30-year federal loan (adjustment through deduction of 20-40 bp)	75-95 bp
USD tranche of the perpetual for Deutsche Bank, July 1999	USD 200 million	No limit	FSR: Aa3/AA PR: A1	Overall 7,75 % (corresponds to 160 bp)	Corresponds to 30-year US treasuries (adjustment through deduction of 65 bp)	95 bp

⁽²⁴⁾ See in particular Germany's reply of 9 April 2003, Annexes 2-4, 8-12, 17-18.

⁽²⁵⁾ Downward adjustment carried out by the Commission on the basis of the data provided by Germany.

⁽²⁶⁾ Refinancing premium as compared with US treasuries having the same term, see letter from Germany of 9 April 2003, p. 27.

⁽²⁷⁾ Second tranche fixed-interest, but equivalent terms.

⁽²⁸⁾ Refinancing premium as compared with US treasuries having the same term, see letter from Germany of 9 April 2003, p. 27.

- (165) The above table gives a corridor for the market comparison of relevant liability remunerations of 0,75 % to 1,6 % a year. In support of this, Germany also presented a survey from the investment bank [...] which shows the trend of liability remunerations on euro-denominated, hybrid capital instruments that can be treated as core capital from December 2001 to July 2004 ⁽²⁹⁾. This shows that, during this period, the average liability remuneration in relation to all rating classes (as a premium above Libor) moved within a corridor between 2,25 % a year (briefly around the end of 2002 and beginning of 2003) as an upper limit and around 0,8 % a year (in 2004) as a lower limit, with a rate of just under 1,5 % a year being the average for the period. The figure for credit institutions rated at A or better is, according to the survey, some 10 to 20 basis points lower and the figure for credit institutions rated BAA some 10 to, during the brief peak in the spring of 2003, around 250 basis points higher.
- (166) The Commission is aware that the market remunerations contained in the table can in methodological terms give only a very rough indication. For example, the transactions differ in many respects, in particular as regards the rating of the issuing financial institutions, the volume and the underlying reference interest rate. These factors all have a significant influence on price formation and a further market survey would have to be carried out to quantify their respective influence on price formation in methodologically correct terms.
- (167) For the purposes of the competition assessment of the market nature of the silent partnership contribution by the *Land* of Hessen, however, any such further market survey can in the Commission's view be dispensed with. It is sufficient if, on the basis of trends, the Commission checks that the agreed remuneration lies within the market corridor.
- (168) It is apparent that the comparative transactions shown are, in terms of volume, in an area of under DEM 50 million (some EUR 25 million) to some USD 1 billion (taking account of evolving exchange rates, around EUR 1 billion). The volume of the silent partnership contribution of the *Land* of Hessen, at some EUR 1,2 billion, is somewhat above this area. However, the Commission agrees with Germany that the silent partnership contribution of the *Land* of Hessen can, on the basis of the above-mentioned phased model, be compared with a series of four smaller silent partnership contributions each amounting to around EUR 150 million and EUR 300 million. Helaba was not dependent on the immediate injection of such a large amount, but would have been able, in accordance with its business plan, to take up silent partnership contributions of this size gradually on the market. The Commission notes that it was primarily in Germany's interest that the silent partnership contribution could from the outset be provided to Helaba in one whole so as not to have to divide up the promotion-related assets.
- (169) On the other hand, as a result of the silent partnership contribution of the *Land* of Hessen, even if it is understood as a series of several silent partnership contributions, the proportion of Helaba's core capital accounted for by silent partnerships rose to some [...] %. According to Germany, this is significantly higher than is usually the case with hybrid core capital instruments in the case of private banks. ⁽³⁰⁾ The Commission considers that the higher the proportion of hybrid core capital compared with share capital, the higher the remuneration would tend to be which a private investor would require, since there would then be a greater probability of silent partnership contributions being claimed rather than share capital if the bank got into difficulties. Germany disputes this, arguing that silent partnership contributions usually have equal liability ranking and that silent partnership contributions taken up later are not prior-ranking. However, regardless of the liability relationship of silent partnership contributions amongst themselves, the Commission also sees an increased risk in the fact that, with silent partnership contributions making up a larger proportion of the core capital, the bank's risk assets are necessarily based more on silent partnership contributions and hence the buffer effect of the core capital decreases, with the result that the probability of their being utilised in the event of a loss is greater and the speed with which they are replenished in the event of improved profitability is slower. Germany also points out that it cannot be deduced from market data that investors contributing silent partnerships in undertakings with an already high proportion of silent partnership contributions also require higher liability remuneration. The Commission notes this point and considers that it is not feasible to carry out a methodologically sound quantification of any such premium for the purposes of this Decision. Nevertheless, the Commission sees this as evidence that a market-economy investor would at least not have accepted a remuneration in the lower part of the market corridor.
- (170) Contrary to the view taken by Germany, the Commission does not regard Helaba's top rating of AAA/Aaa at the end of 1998 on the basis of the state liabilities in the form of *Anstaltslast* and *Gewährträgerhaftung* as significant in examining the remuneration on the silent partnership contribution. As explained above, the silent partnership investor is not protected by intervention by the guarantor on the basis of *Anstaltslast* in the interests of his assets.

⁽²⁹⁾ Germany's reply of 23 August 2004, Annex 6.

⁽³⁰⁾ Germany's reply of 23 August 2004, pp. 11-12. In the case of the [...] private banks in Germany listed there, [...], [...] and [...], the relevant proportion rose from some 5 % in 1998 to around 20-30 % in 2003. According to the information provided by Germany, the relevant proportion in the case of Helaba lies within the 33 % to 72 % range typical of Landesbanks.

- (171) The Commission concludes here too that the rating based on *Anstaltslast* and *Gewährträgerhaftung* cannot be taken as an indicator of the risk the investor is running. In the Commission's view, the long-term rating without state liabilities is more significant. Germany argues in this context that this type of rating could not be determined for the period at the end of 1998, since a corresponding rating methodology for Landesbanks as a whole was developed only after the agreements on the abolition of the state guarantees, i.e. after 2001 and 2002. For the purposes of this Decision, therefore, the Commission assumes that a market-economy investor in Helaba would have started from the assumption of a somewhat similar risk of loss as in the case of an investment in one of the large private banks included in the market comparison whose rating was consistently in the A category, and not of a reduced risk corresponding to the top rating of AAA. Consequently, a reduction in the appropriate remuneration premium as compared with the market comparison data does not appear apposite; rather, the market comparison data can be applied directly.
- (172) For the reasons set out above, the Commission would regard any remuneration of the silent partnership contribution of the *Land* of Hessen in the lower part of the market corridor as not being in line with the market. However, given the market corridor of 0,75 % to 1,6 % determined for the liability remuneration for silent partnership contributions, the relevant comparative figure for the silent partnership contribution of the *Land* of Hessen at 1,43 % (taking account of the trade tax effect) is in the middle to upper range of the corridor. In view of this, therefore, the Commission does not, in respect of the initial remuneration, see any evidence of favourable treatment of Helaba and hence of state aid.
- (cc) Market nature of the agreed perpetuity premium of 0,2 % a year (market comparison rate of 0,23 % a year taking account of trade tax)
- (173) The silent partnership contribution of the *Land* of Hessen is of unlimited duration and is what is known internationally as a *perpetual*. This distinguishes it from most of the other transactions cited by Germany for comparison purposes and typical during the 1990s, which generally have a term of ten or twelve years.
- (174) Looking at the market in abstract terms, unlimited duration means that an investor is faced with a higher risk of non-payment and a higher interest rate fluctuation risk, which a premium is supposed to offset, although in the present instance, because liquidity was not provided, the interest rate fluctuation risk is not relevant. Furthermore, the *Land* restricted its freedom in the use of the silent partnership contribution more than would normally have been the case with limited duration.⁽³¹⁾ The unlimited duration of the silent partnership contribution does, on the other hand, give Helaba the added economic benefit that it can be recognised above the 15 % limit as core capital and was in fact so recognised. This was provided for by the above-mentioned 'Sydney Declaration' of the Basle Committee for Banking Supervision in October 1998.
- (175) For these reasons, the *Land* of Hessen and Helaba agreed to a further premium on the initial remuneration, the so-called perpetuity premium, of 0,2 % a year. Taking account of the above-mentioned trade tax effect, the rate applicable for the market comparison rises to 0,23 % a year.
- (176) In assessing whether this rate of 0,23 % a year is in line with the market-economy investor principle, the Commission cannot, or can to only a very limited extent, rely on market data from the time of the transaction. According to the information provided by Germany, Helaba and the *Land* of Hessen were to some extent market pioneers in arranging the transaction in such a way that, in coordination with the relevant banking supervisory and financial authorities, recognition in full as core capital above the 15 % limit was achieved. According to Germany, the transaction was evidently the first of this kind. Comparative data on the market nature of the perpetuity premium were not available to the parties at the end of 1998, since, in the period between the 'Sydney Declaration' of 28 October 1998 and 1 December 1998, it was not possible for a transparent market for permanent silent partnerships to develop.
- (177) The Commission notes firstly that a public investor or a public bank cannot be prevented from acting as a market pioneer. On the contrary, a market pioneer must actually be allowed greater leeway in setting terms and conditions than is the case with established benchmarks that determine the relevant market corridor on the basis of which the market test is to be carried out. The Commission can therefore at most examine whether the determination of the perpetuity premium was wrong in economic terms, i.e. was based for example on false premises.
- (178) In carrying out this examination, therefore, reference must be made to market data from a later period. In the Commission's view, there is no reason to believe that a premium for the perpetuity of a silent partnership varies
- ⁽³¹⁾ This does not automatically mean that the *Land* has committed itself to Helaba 'forever' or can never again have at its disposal the funds comprised in the silent partnership. The *Land* can assign its rights from the silent partnership (at least with Helaba's agreement) to a third party against payment. The fungibility of the silent partnership is not thus necessarily reduced to zero.

much over time. However, no specific data on the level of the perpetuity premium can be deduced from the market. *Perpetuals*, including the silent partnership contribution of

unlimited duration, have established themselves on the market since the Sydney Declaration of October 1998, but more particularly since 1999.

- (179) Germany did not therefore present separate data on the level of the appropriate perpetuity premium for carrying out the market comparison, but rather presented data on overall pricing of *perpetuals* and silent partnerships of unlimited duration observable on the market since 1999 (contributions with a term of thirty years or more are also regarded as being of unlimited duration on the market). The data are summarised in the following table, with the *perpetuals* from 1999 listed in the above table being listed here once again for the sake of completeness:

Relevant comparative transactions ⁽³²⁾						
Description of the transaction	Volume	Term	Financial strength/product ratings	Remuneration premium p.a. (in bp)	Reference interest rate and any adjustment ⁽³³⁾ of the remuneration premium by deduction of the refinancing premium	Liability remuneration of relevance for comparison
USD tranche of the silent partnership contribution to Dresdner Bank, May 1999	USD 1 billion	32 years	FSR: Aa1/ AA PR: Aa2; A+	215 bp	30-year US treasuries (adjustment through deduction of 65 bp ⁽³⁴⁾)	150 bp
Euro tranche of the perpetual for Deutsche Bank, July 1999	EUR 500 million	no limit	FSR: Aa3/ AA PR: A1	Fixed 6,6 % (corresponds to 115 bp)	Corresponds to 30-year federal loan (adjustment through deduction of 20-40 bp)	75-95 bp
USD tranche of the perpetual for Deutsche Bank, July 1999	USD 200 million	no limit	FSR: Aa3/ AA PR: A1	Fixed 7,75 % (corresponds to 160 bp)	Corresponds to 30-year US treasuries (adjustment through deduction of 65 bp)	95 bp
Deutsche Bank, December 2003	EUR 300 million	no limit	PR: A2/A	Fixed 6,15 % (corresponds to 99 bp over mid-swaps)	Corresponds to mid-swaps (no adjustment)	99 bp

⁽³²⁾ See in particular Germany's reply of 9 April 2003, Annexes 2-4, 8-12, 17-18.

⁽³³⁾ Downward adjustment carried out by the Commission on the basis of the data provided by Germany.

⁽³⁴⁾ Refinancing premium as compared with US treasuries having the same term, see letter from Germany of 9 April 2003, p. 27.

- (180) The few specified comparative data for *perpetuals* do not produce any change here in the market comparison corridor as compared with silent partnership contributions of limited duration. However, economic theory dictates that a market-economy investor naturally requires a premium for perpetuity as compared with an otherwise similar silent partnership contribution of limited duration, so as to offset in particular the additional risk of non-payment resulting from the stronger and longer tie. However, it is evident from the data presented that, on the market for *perpetuals*, it is not necessarily the case that a significantly higher liability remuneration is required than for silent partnership contributions of limited duration. This finding, though it certain cannot be described as statistically robust, given the lack of a sufficient number of comparative transactions, also lends further plausibility to Germany's argument that the perpetuity aspect does not change the silent partnership contribution into a capital instrument of a different type, as argued by the BdB, for example.
- (181) Germany presented a comparative calculation of the perpetuity premium for the Deutsche Bank's euro transaction (*perpetual*) of July 1999, which was of unlimited duration, as compared with the Dresdner Bank's transaction of May 1999, which was of limited duration⁽³⁵⁾. It stated that the Deutsche Bank *perpetual* of July 1999 showed an overall remuneration of 6.6 % a year (see above table). In 1 July 1999, the current yield for ten-year federal loans was 4.66 % a year, which meant that the remuneration premium in relation to them amounted to 1.94 % a year⁽³⁶⁾. By contrast, the euro tranche of the twelve-year silent partnership contribution to Dresdner Bank of May 1999 was remunerated at 1.65 above ten-year federal loans. This gave a difference of 0.29 % a year. This, it was argued, was only slightly above the premium agreed here of 0.20 % a year (0.23 % a year with the trade tax effect). Another reason for the difference was that the Deutsche Bank *perpetuals* were rated lower by Moody's at A1 than the Dresdner Bank silent partnership contribution, rated Aa2, and consequently had a higher remuneration.
- (182) The Commission believes this comparative calculation is plausible, bearing in mind the limited data available in the period 1998/1999, which is not the fault of the *Land* of Hessen and Helaba. The figure of 0.29 % resulting from the comparative calculation is only slightly above the perpetuity premium agreed between the *Land* of Hessen and Helaba, i.e. 0.23 %. In addition, at least part of the difference is attributable to differences in product rating, which would probably be smaller if one were to compare silent partnership contributions to Helaba of limited and unlimited duration, since the issuer is identical.
- (183) Consequently, the Commission has no evidence that the comparative rate of 0.23 % a year for the perpetuity premium lies below the market corridor and that there was therefore any favouring of Helaba, i.e. state aid.
- (dd) Taking appropriate account of liquidity costs
- (184) The arguments of Germany, Helaba and the BdB regarding liquidity costs, which are in agreement in this respect, can be accepted, in so far as a 'normal' capital injection into a bank supplies it both with liquidity and with an own funds base which it requires for supervisory reasons to expand its activities. In order to use the capital in full, i.e. to expand its 100 % risk-adjusted assets by a factor of 12.5 (i.e. 100 divided by a solvency ratio of 8), the bank must refinance itself on the financial markets 11.5 times over. Put simply, the difference between 12.5 times the interest received and 11.5 times the interest paid minus other costs of the bank (e.g. administration) gives the profit on the equity.⁽³⁷⁾ Since the silent partnership contribution of the *Land* of Hessen did not provide Helaba with initial liquidity because the assets transferred and all the income from them remained earmarked by law for housing promotion, Helaba faced additional funding costs equal to the amount of the capital if it was to raise the necessary funds on the financial markets to take full advantage of the business potential opened up by the additional capital, i.e. to expand risk-adjusted assets by 12.5 times the capital amount (or to maintain existing assets at that level).⁽³⁸⁾ Because of these extra costs, which do not arise in the case of liquid equity capital, the appropriate remuneration must be reduced accordingly. A market-economy investor could not expect to be remunerated in the same way as for a cash injection.
- (185) Unlike the BdB, but like Germany and Helaba, however, the Commission takes the view that the gross refinancing interest rate is deductible. Refinancing costs are operating expenses and thus reduce taxable income. However, the same applies to the remuneration on a silent partnership

⁽³⁵⁾ Letter from Germany of 9 April 2004, p. 28.

⁽³⁶⁾ The remuneration premium of the Deutsche Bank *perpetual* (agreed fixed-interest remuneration of 6.60 %) is put here at 1.94 % a year in relation to 10-year federal loans in order to make it more comparable with the 12-year silent partnership contribution to Dresdner Bank (1.65 % above 10-year federal loans) and thus to get some idea of the level of the perpetuity premium. In the above table, the remuneration premium for the same *perpetual* is put at 1.15 % a year in relation to 30-year federal loans, since these are equivalent to the relevant period (30 years are regarded on the market as being 'quasi-permanent'). The remuneration premium in relation to 30-year federal loans is lower, since with a normal interest rate curve, as is the case here, longer-term (30-year) loans yield a higher return than shorter-term (10-year) loans and thus represent a higher deduction item from the agreed fixed-interest remuneration of 6.60 % a year.

⁽³⁷⁾ Of course, in reality the situation is much more complex because of off-balance-sheet items, different risk weightings of assets or zero-risk items, etc. However, the principal reasoning holds.

⁽³⁸⁾ The situation does not change if one takes into account the possibility of raising additional own funds up to the same amount of original own funds (a factor of 25 instead of 12.5 for original own funds).

contribution which from the outset is made in liquid form. In comparison to the latter, which, as stated above, provides the appropriate market test, no further tax advantage arises. The bank's net result is thus reduced in both cases by the amount of the interest paid for the liquidity. The entire refinancing costs are thus deductible.

(186) This situation distinguishes Helaba significantly from WestLB and the other Landesbanks, which were also the subject of proceedings, since in the case of the latter the promotion-related assets were entered in the balance sheet as reserves and the entire remuneration is to be regarded as profit utilisation, but not as operating expenses, and must be paid from taxable profit. In the case of the others, therefore, there is a tax advantage if the costs for liquidity to be procured once more are deductible from tax as operating expenses, while this would not be the case with an investment which was from the outset cash, but otherwise identical, and which represents the relevant comparative reference.

(187) In the absence of any (further) tax advantage, consequently, Helaba has to pay only the remuneration for the risk to which the *Land* of Hessen is exposing its promotion-related assets in the form of the silent partnership contribution, i.e. the liability remuneration, expressed in basis points, above the relevant reference interest rate.

(2) *Determination of a minimum remuneration for the capital required to underpin the promotion-related business and for the capital not initially used, on the basis of the phased arrangement, to underpin competitive business*

(188) In the WestLB Decision of 1999, the Commission applied a bank guarantee commission of 0,5-0,6 % before tax and 0,3 % after tax for the amount entered in the balance sheet, but not usable to underpin competitive business. This guarantee commission is in line with the rate of 0,3 % before tax which Germany had indicated as the appropriate commission on a bank guarantee for a bank like WestLB at the end of 1991. The Commission raised this rate to 0,5-0,6 % before tax (0,3 % after tax) for two reasons. Firstly, the amount of DEM 3,4 billion (EUR 1,74 billion) in the case of WestLB exceeded what was normally covered by such bank guarantees. Secondly, bank guarantees were normally associated with certain transactions and limited in time.

(189) In the present proceedings on Helaba, the Commission similarly asked Germany to specify a guarantee provision that could be regarded as corresponding to market terms for a bank such as Helaba. Germany did not do so, but argued that guarantees were always issued only for certain transactions and that there was therefore no market from which the remuneration for such guarantees could be deduced. However, if, despite these objections, the Commission insisted on a remuneration being specified, the level of such remuneration could, in Germany's view, only be calculated individually taking account of the specific risk which, on the basis of this approach, the *Land* had incurred in view of the differential amounts involved. Since the planned growth of the risk assets, at only DEM [...] million a year, represented a modest growth policy compared to WestLB, the very low probability of the differential amount, which was decreasing annually, being called on by the bank's creditors should at all events result in the application of a very low liability remuneration.

Furthermore, Helaba had only partly used the graduated amounts that had to be remunerated in full and, in contrast to WestLB, more than filled the minimum core capital ratios required for banking supervisory purposes, so that Helaba's business risks were as a result more than adequately covered. This safety margin meant that neither the basic remuneration rate of 0,3 % a year before tax nor a premium on this rate of 0,2-0,3 % a year before tax could be transferred from the WestLB Decision (a total of 0,3 % a year after tax) to the Helaba case.

(190) The Commission therefore must itself examine an appropriate guarantee commission for a bank such as Helaba. In view of the basic similarity of WestLB and Helaba and in the absence of other criteria, the Commission assumes here that, as in the case of WestLB, a basic rate of 0,3 % a year before tax can be regarded as appropriate. However, in the Commission's view, premiums on this rate are not appropriate. In the first place, the amount of the silent partnership contribution (EUR 50 to 100 million) available in the long term to underpin the promotion-related business is much smaller than the corresponding amount of some EUR 1,7 billion in the case of WestLB. Secondly, the amount which, under the phased arrangement, was not usable to underpin competitive business was, as a result of the phased arrangement, limited in time and accordingly fell to zero by 2003. These facts show clearly that the risk to the *Land* of Hessen was no higher than in the case of a market guarantee for a bank such as Helaba and does not accordingly justify any increase in the basic rate of 0,3 % a year before tax. Since the remuneration for the entire silent partnership contribution is, as operating expenses, deductible from tax and, on this point too, differs from the tax treatment of the remuneration in the WestLB Decision, the Commission establishes the guarantee commission in this Decision as a pre-tax rate which is fully eligible as operating expenditure.

e) *Aid element*

(191) As stated above, the Commission considers a remuneration of 0,3 % a year before tax to be appropriate for the part of the capital which is not usable by Helaba to underpin its competitive business, but was entered in Helaba's balance sheet with effect from 31 December 1998.

(192) Helaba pays a remuneration of 1,4 % a year only on the amount which, in accordance with the phased arrangement, is usable to cover risk assets, but not on the part of the silent partnership contribution which is entered in the balance sheet, but not used to underpin competitive business.

- (193) The aid element can therefore be determined as the product of the guarantee commission of 0,3 % a year before tax regarded by the Commission as corresponding to market terms and the part of the silent partnership contribution entered in the balance sheet but not used to underpin competitive business, in accordance with the following table:

Year-end values in EUR millions	1999	2000	2001	2002	2003
1) Nominal value in the balance sheet	1 264,4	1 264,4	1 264,4	1 264,4	1 264,4
2) Core capital actually usable for competitive business in accordance with the phased model	[...]	[...]	[...]	[...]	[...]
3) Core capital used for promotion related business	[...]	[...]	[...]	[...]	[...]
4) Core capital usable for competitive business, but whose usability is governed by the phased model	[...]	[...]	[...]	[...]	[...]
5) Difference between (1) and (2), corresponds to the sum of (3) and (4)	[...]	[...]	[...]	[...]	[...]
6) Safety margin deduction because of lower preliminary determination in the balance sheet as at 31.12.1998 (*)	[...]	[...]	[...]	[...]	[...]
7) Capital base to be remunerated with guarantee commission of 0,3 % a year (before tax)	[...]	[...]	[...]	[...]	[...]
8) Remuneration to be paid that is deductible as operating expenses, corresponds to aid element	1,92	1,95	1,34	0,73	0,15

(*) Remark on item (6) Safety margin deduction because of lower preliminary determination in the balance sheet as at 31 December 1998: according to information provided by Germany, ⁽³⁹⁾ the process of banking supervisory recognition had not yet been completed on 31.12.1998, so that initially a figure of EUR 1 023 million (DEM 2 000 million) had been entered in the balance sheet. The figure of EUR 1 264 million produced by the assessment process had been entered directly after the assessment and had accordingly featured in the annual accounts for 1999. In view of this process, the Commission considers it appropriate to make a safety margin deduction on behalf of Helaba from the capital base to be remunerated for 1999. Helaba's creditors based their assessment of its financial strength during 1999 on the figures in the 1998 annual accounts, which contained the preliminary lower amount of EUR 1 023 million for the silent partnership contribution. Consequently, in 1999 only the difference between this amount and the core capital usable, under the phased arrangement, to underpin competitive business is to be remunerated with the guarantee commission of 0,3 % a year (before tax), i.e. EUR [...] million. For the following years, the figure in the previous year's balance sheet corresponds to the figure for the silent partnership contribution specified in the annual balance sheet.

⁽³⁹⁾ See Germany's reply of 23. August 2004, p. 6-7.

f) **Preliminary result**

(194) The Commission thus concludes that Helaba was favoured only in so far as it did not pay an appropriate liability remuneration for that part of the capital made available in the form of a silent partnership contribution by the *Land* of Hessen which was required to underpin its promotion-related business and, on the basis of the phased arrangement, was initially not used to underpin its competitive business. In the Commission's view, a liability remuneration of 0,3 % a year (before tax) would have been appropriate. In so far as it was possible for the capital to be used to underpin the competitive business, however, this was remunerated appropriately through the agreed remuneration of 1,43 % a year (taking account of the trade tax) for the silent partnership contribution. In this respect, no favourable treatment exists.

1.3. DISTORTION OF COMPETITION AND EFFECT ON TRADE BETWEEN MEMBER STATES

(195) As a result of liberalisation of financial services and the integration of financial markets, banking within the Community has become increasingly sensitive to distortions of competition. This development is intensifying in the wake of economic and monetary union, which is dismantling the remaining obstacles to competition in the financial services markets.

(196) Helaba carries on regional and international banking business. It defines itself as an all-purpose commercial bank, central bank for the savings banks and the bank of the *Land* and its municipalities. Despite its name, tradition and legally stipulated tasks, Helaba is much more than a mere local or regional bank.

(197) These facts show clearly that Helaba offers its banking services in competition with other European banks outside Germany and, since banks from other European countries are active in Germany, inside Germany. It is clear, therefore, that aid given to Helaba distorts competition and affects trade between Member States.

1.4. RESULT

(198) In so far as Helaba did not pay an appropriate liability remuneration for the part of the capital made available which was required to underpin its promotion-related business and, on the basis of the phased arrangement, was not initially used to underpin its competitive business, all the preconditions for state aid within the meaning of Article 87(1) of the EC Treaty are met. With regard to the part of the capital which was used to underpin the competitive business, the remuneration of 1,43 % a year

(taking account of the trade tax) that had to be paid only on this amount is to be regarded as being in conformity with the market. In this respect, there is no favourable treatment and hence no state aid within the meaning of Article 87(1) of the EC Treaty for Helaba.

2. COMPATIBILITY WITH THE COMMON MARKET

(199) In so far as the transfer of the silent partnership contribution involves state aid within the meaning of Article 87(1) of the EC Treaty, an assessment must be made as to whether the aid can be considered compatible with the common market.

(200) None of the exemption clauses of Article 87(2) of the EC Treaty are applicable. The aid does not have a social character and is not granted to individual consumers. Nor does it make good the damage caused by natural disasters or exceptional occurrences or compensate for the economic disadvantages caused by the division of Germany.

(201) Given that the aid has no regional objective — it is designed neither to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment nor to facilitate the development of certain economic areas — neither Article 87(3)(a) nor (c) of the EC Treaty, as regards the latter's regional aspect, is applicable. Nor does the aid promote the execution of an important project of common European interest. The aid is not aimed either at promoting culture or heritage conservation.

(202) Since the economic survival of Helaba was not at stake when the measure was implemented, there is no need to consider whether the collapse of a single large credit institution like Helaba could lead to a general banking crisis in Germany, which might possibly justify aid to remedy a serious disturbance in the German economy under Article 87(3)(b) of the EC Treaty.

(203) Under Article 87(3)(c) of the EC Treaty, aid may be found compatible with the common market if it facilitates the development of certain economic activities. This might in principle also apply to restructuring aid in the banking sector. However, in the case at hand the conditions for the application of this exemption clause are not met. Helaba was not an undertaking in difficulty whose viability had to be restored with the support of state aid.

(204) Article 86(2) of the EC Treaty, which allows exemptions from the Treaty's state aid rules under certain conditions, is

in principle also applicable to the financial services sector. This has been confirmed by the Commission in its report on Services of general economic interest in the banking sector. ⁽⁴⁰⁾ However, the formal conditions are not met in this case: the tasks which Helaba carries out in providing services of general economic interest are not specified, and nor are the costs generated by such tasks. It is therefore clear that the transfer was effected without any regard to any services of general economic interest. Accordingly, this exemption clause does not apply either in the case at hand.

(205) Since no exemption from the principle of the ban on state aid pursuant to Article 87(1) of the EC Treaty applies, the aid in question cannot be found compatible with the Treaty.

3. NOT EXISTING AID

(206) Nor, contrary to what was argued by Germany in other Landesbank proceedings, can the capital injection be regarded as being covered by the existing state aid scheme for 'institutional responsibility' (*Anstaltslast*) and 'guarantor liability' (*Gewährträgerhaftung*), but must be regarded as new aid.

(207) *Gewährträgerhaftung* is a default guarantee offered to creditors in the event that the bank's assets are no longer sufficient to satisfy their claims, and this is not the case here. The capital injection is not intended to satisfy the Landesbank's creditors and the bank's assets have not been exhausted.

(208) Nor does *Anstaltslast* apply. *Anstaltslast* requires the guarantor, the *Sparkassenverband Hessen-Thüringen*, to provide Helaba with the resources it needs to function properly for as long as the *Sparkassenverband Hessen-Thüringen* decides to maintain it in existence. However, at the time of the capital injection, Helaba was far from being in a situation where it was no longer able to operate properly for lack of sufficient resources. The capital injection was therefore not needed in order to keep the Landesbank in operation. The conscious economic calculation by the *Land* as (joint) owner also enabled the Landesbank to seize future opportunities in its competitive business. The 'necessity requirement' for *Anstaltslast* does not apply to such a normal economic decision by the *Land* as (joint) owner of the bank. In the absence of another applicable existing state aid scheme pursuant to Articles 87(1) and 88(1) of the EC Treaty, the capital injection must be classed as new aid

within the meaning of Articles 87(1) and 88(3) of the EC Treaty, and examined as such.

VII. CONCLUSION

(209) The aid cannot be found compatible either under Article 87 (2) or (3) or under any other provision of the Treaty. The aid should therefore be declared incompatible with the common market and the aid element of the measure illegally put into effect should be recovered by the Germany,

HAS ADOPTED THIS DECISION:

Article 1

1. The waiver of an appropriate remuneration amounting to 0,3 % a year (before corporation tax) for the part of the capital transferred by the *Land* of Hessen to the Landesbank Hessen-Thüringen — Girozentrale which the latter has been able to use as a guarantee as from 31 December 1998 is aid which is incompatible with the common market.

2. The aid referred to in paragraph 1 amounts to EUR 6,09 million for the period from 31 December 1998 to 31 December 2003.

Article 2

1. Germany shall discontinue the aid referred to in Article 1(1) by 31 December 2004.

2. Germany shall take all necessary measures to recover the aid referred to in Article 1(1) which was unlawfully made available to the beneficiary. The amount to be recovered shall include the following:

(a) for the calculation period 31 December 1998 to 31 December 2003, the amount specified in Article 1(2);

(b) for the calculation period from 1 January 2004 to the time when the aid is discontinued, an amount determined in accordance with the calculation method specified in Article 1(1).

Article 3

Recovery shall be effected without delay and in accordance with the procedures of national law provided that they allow the immediate and effective execution of this Decision.

The amount to be recovered shall include interest from the date on which the unlawful aid was at the disposal of the beneficiary until the date of its recovery.

⁽⁴⁰⁾ This report was presented to the Ecofin Council on 23 November 1998 but has not been published. It can be obtained from the Competition Directorate-General of the Commission and can also be found on the Commission's website.

Interest shall be calculated in accordance with the provisions of Chapter V of Commission Regulation (EC) No 794/2004 ⁽⁴¹⁾

Article 5

This Decision is addressed to Germany.

Article 4

Done at Brussels, 20 October 2004.

Germany shall, using the form set out in the Annex, inform the Commission, within two months of notification of this Decision, of the measures which it has taken in order to comply with it.

For the Commission

Neelie KROES

Member of the Commission

⁽⁴¹⁾ OJ L 140, 30.4.2004, p. 1.