COMMISSION DECISION

of 20 October 2004

on State Aid implemented by Germany for Norddeutsche Landesbank — Girozentrale

(notified under document number C(2004) 3926)

(Only the German text is authentic)

(Text with EEA relevance)

(2006/738/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 the Member State and other interested parties to submit their comments pursuant to the provisions cited above [1] and having regard to their comments,

Whereas:

I. PROCEDURE

(1) The subject of these proceedings is the transfer of three *Land* trust agencies (*Landestreuhandstellen* ('LTS')) to Norddeutsche Landesbank — Girozentrale ('NordLB') by the *Land* of Lower Saxony. There are a further six cases in which proceedings have been initiated against Germany in connection with transfers of assets to Landesbanks, and in particular to Westdeutsche Landesbank — Girozentrale ('WestLB').

(2) By letter of 12 January 1993, the Commission asked Germany for information on a capital increase in WestLB resulting from the incorporation of the housing organisation *Wohnungsbauförderanstalt* ('WfA') and on similar increases in the own funds of the Landesbanks of other *Länder*. It also asked which Landesbanks had benefited from a transfer of publicly owned promotion-related assets and for information on the reasons for those transactions.

(3) Germany replied by letters dated 16 March and 17 September 1993. The Commission requested further information by letters of 10 November and 13 December 1993, to which Germany replied by letter of 8 March 1994.

(4) By letters of 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, under a law adopted on 17 December 1991, the *Land* of Lower Saxony's shares in assets used to promote housing, agriculture, trade and industry had been transferred to NordLB with effect from 31 December 1991. This increased the own funds at NordLB's disposal and, in the BdB's view, distorted competition in its 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 against Germany under Article 93(2) of the EC Treaty (now Article 88(2)). In February and March 1995 and December 1996 several banks associated themselves individually with the complaint lodged by the BdB.

(5) The Commission investigated first the transfer of assets to WestLB but announced that it would examine the transfers to the other Landesbanks, including NordLB, in the light of the findings in that case. [2] By Decision 2000/392/EC [3], it finally declared in 1999 that the aid measure (the difference between the remuneration paid and the normal market remuneration) was incompatible with the common market and ordered that the aid should be recovered. This decision was annulled by the Court of First Instance of the European Communities on 6 March 2003 as insufficient reasons had been given for two of the factors used to calculate the appropriate remuneration, but it was confirmed in all other respects. On 20 October 2004 the Commission, having become aware of an understanding between the complainant, WestLB and the Land of North-Rhine Westphalia, issued a new decision which took account of the Court's criticisms.

(6) On 1 September 1999, following Decision 2000/392/EC, the Commission sent Germany a request for information on the transfers of assets to the other Landesbanks. By letter

[1] OJ C 81, 4.4.2003, p. 2.

[2] OJ C 140, 5.5.1998, p. 9.

[3] OJ L 150, 23.6.2000, p. 1; actions challenging that decision have been brought by Germany (Case C-376/99), by North Rhine-Westphalia (Case T-233/99) and by WestLB (Case T-228/99). The Commission has also brought proceedings for infringement of the Treaty (Case C-209/00).

of 8 December 1999, Germany supplied information on the transfer of the LTS to NordLB which it supplemented in a letter dated 22 January 2001 in response to the Commission's requests for further information.

(7) On 1 March 2001 the Commission asked for more information, in particular on the transfers of capital by the *Niedersächsische Sparkassen und Giroverband* ('NSGV'). Germany replied on 15 May 2001.

(8) By letter of 13 November 2002, the Commission informed Germany of its decision to initiate the formal investigation procedure laid down in Article 88(2) of the EC Treaty in respect of the transfer to NordLB of the promotion-related assets of the *Land* of Lower Saxony. At the same time, it launched the investigation procedure in respect of similar transfers of assets to Bayerische Landesbank — Girozentrale, Landesbank Schleswig-Holstein — Girozentrale, Hamburgische Landesbank — Girozentrale and Landesbank Hessen-Thüringen. It had already opened an investigation into a further similar transfer of assets by the *Land* of Berlin to Landesbank Berlin back in July 2002.

(9) The decisions initiating the procedure were published in the *Official Journal of the European Union* ([1]). The Commission called on interested parties to submit comments.

(10) By letter of 11 April 2003, Germany submitted its comments on the initiation of the procedure in the NordLB case.

(11) By letter of 29 July 2003, the BdB submitted comments on all the decisions taken on 13 November 2002 to initiate the investigation procedure. On 30 October 2003 Germany forwarded a reply by the *Land* Government of North Rhine-Westphalia and WestLB AG to the BdB's comments on the proceedings concerning the transfer of LTS to NordLB.

(12) In response to the Commission's request for further information dated 1 September 2003, Germany supplied additional information and replied to the BdB's comments on NordLB on 28 October.

(13) On 7 April and 3 May 2004 the Commission sent Germany further requests for information, to which the latter replied by letters dated 27 May and 28 June 2004. On 16 August and 9 September 2004 Germany sent further comments supplementing its previous position.

(14) On 19 July 2004 the complainant (the BdB), the *Land* of North Rhine-Westphalia and WestLB AG submitted a provisional understanding on the appropriate remuneration for the transferred assets. In their view, this remuneration should form the basis for the Commission's decision. Likewise, the BdB, the *Land* of Lower Saxony and NordLB submitted a proposal for an understanding on appropriate remuneration for the transfer of the LTS assets. These parties and Germany subsequently addressed several letters to the Commission. The final version of the understanding on the transfer of the LTS assets to NordLB reached the Commission on 7 October 2004.

II. DETAILED DESCRIPTION OF THE MEASURES

1. *NORDDEUTSCHE LANDESBANK — GIROZENTRALE*

(15) NordLB, to which the LTS were transferred, is a publicly owned credit institution operating in the form of a public-law institution (*Anstalt des öffentlichen Rechts*) with registered offices in Hanover, Braunschweig, Magdeburg and Schwerin. With a group balance-sheet total of EUR 193 000 million (at 31 December 2003), it is one of Germany's largest banks. NordLB currently employs around 9 500 staff.

(16) NordLB was formed in 1970 by the union of four publicly owned credit institutions (Niedersächsische Landesbank, Braunschweigische Staatsbank (including Braunschweigische Landessparkasse), Hannoversche Landeskreditanstalt and Niedersächsische Wohnungskreditanstalt-Stadtschaft).

(17) When the capital transfer under investigation took effect, 60 % of NordLB by the *Land* of Lower Saxony and 40 % by NSGV, a public-law corporation.

(18) Under two State Treaties of 1991 and 1992, the *Länder* of Lower Saxony, Saxony-Anhalt and Mecklenburg-Western Pomerania agreed to operate NordLB as a joint *Land* institution. With effect from 12 January 1993, the ownership and guarantor structure was altered as follows: *Land* of Lower Saxony 40 %, NSGV 26,66 %, *Land* of Saxony-Anhalt 10 %, *Land* of Mecklenburg-Western Pomerania 10 %, Sparkassenbeteiligungsverband Sachsen-Anhalt ('SBV') 6,66 %, and Sparkassenbeteiligungszweckverband Mecklenburg-Vorpommern ('SZV') 6,66 %.

(19) Under the terms of its articles of association, NordLB is required to operate as a *Land* bank, a central savings bank and a commercial bank. It may also engage in any other business that serves the purposes of the bank, its owners and the municipal corporations in the *Länder*. In the Braunschweig area it operates as a savings bank. NordLB offers financial services to private customers, businesses, institutions and public authorities and is an important player on international capital markets, both for its own account and as manager of other issuers' debt instruments. Like many German all-purpose banks, NordLB holds a number of stakes in financial and non-financial enterprises.

([1]) OJ C 81, 4.4.2003, p. 2.

(20) NordLB has a presence in the world's major financial and trading centres. It has a stock-exchange office in Frankfurt, branches in London, New York, Singapore, Stockholm, Helsinki and Shanghai, representative offices in Oslo, Tallinn and Beijing and subsidiaries in London, Zürich, Luxembourg, Riga, Vilnius and Warsaw.

(21) In 2003 NordLB's equity ratio was 11,5 % at institutional level and 10,1 % at group level; its core-capital ratio was 7,1 % at institutional level and 6,3 % at group level. Its income-to-equity ratio stood at [...] (*) % in 2003.

2. *LAND TRUST AGENCIES ('LTS')*

(22) In 1948 the *Land* of Lower Saxony set up a trust agency with the task of promoting social housing. On the basis of a 'trustee agreement' between the *Land* and NordLB, the bank took over the administration of the promotion-related assets and the tasks carried out by the trust agency. On the basis of this and two other, similar trustee agreements, NordLB became the owner — in legal but not in financial terms — and the trustee administrator of the assets for promoting housing, agriculture and industry on the *Land*'s behalf. It granted promotional loans in its own name, but on the *Land*'s financial account.

(23) The three LTS are not legally independent but are managed within NordLB as autonomous and — in operational, personnel and organisational terms — separate business divisions. The three LTS are exempt from corporation tax, property tax and tax on business capital.

(24) The *Land* housing trust agency (*LTS-Wohnungswesen*) manages assets specifically earmarked for housing and *Land* guarantees for the promotion of housing construction. In particular, it promotes the construction and modernisation of owner-occupied homes and rented homes and the purchase and acquisition of owner-occupied homes.

(25) The *Land* agriculture trust agency (*LTS-Agrar*) administers public loans and grants to promote agriculture, in particular agricultural investment and forestry measures.

(26) The *Land* industry trust agency (*LTS-Wirtschaft*) issues and administers loans and grants for the promotion of industry, specialising in investment by small and medium-sized enterprises and in business start-ups. It looks after the EU's Interreg Initiative and is recognised as a financial intermediary under the Joint European Venture (JEV).

(*) Confidential information.

3. *CAPITAL REQUIREMENTS UNDER THE OWN FUNDS DIRECTIVE*

(27) The German Banking Act (*Kreditwesengesetz*, or KWG) was amended in line with Council Directive 89/647/EEC of 18 December 1989 on a solvency ratio for credit institutions ([1]) (the 'Solvency Directive') and Council Directive 89/299/EEC of 17 April 1989 on the own funds of credit institutions ([2]) (the 'Own Funds Directive'), which require banks to have a level of own funds equal to 8 % of their risk-adjusted assets, of which at least four percentage points must consist of what is termed core capital, or 'tier I' 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 II' capital, is accepted as underpinning for risk-bearing transactions only up to the amount of the available core capital.

(28) By 30 June 1993 German banks had to adapt their own funds to the new requirements of the Solvency Directive and the Own Funds Directive ([3]).

(29) The own-funds cushion of many Landesbanks was comparatively small even before transposal of the Solvency Directive into German law. They now had to strengthen their own-funds base as a matter of urgency in order to avoid restrictions on their business expansion or at least to maintain their current level of activities.

(30) However, because the budgetary situation was tight, the public shareholders were unable to provide any fresh capital but were not prepared to contemplate privatisation and to raise additional capital on capital markets. It was therefore decided to undertake transfers of assets and capital: for example, in WestLB's case the assets of WfA and in NordLB's case the above-mentioned promotion-related assets of the three LTS.

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

([2]) OJ L 124, 5.5.1989, repealed and replaced by Directive 2000/12/EC (OJ L 126, 26.5.2000).

([3]) Under the Solvency Directive, credit institutions must have own funds equivalent to at least 8 % of their risk-adjusted assets, whereas the old German legislation required a ratio of 5,6 %; however, this ratio was based on a narrower definition of own funds than that which has applied since the entry into force of the Own Funds Directive.

4. *TRANSFER OF THE LTS AND ITS EFFECTS*

(a) THE TRANSFER

(31) By the Act on the contribution of the promotion-related assets of the *Land* of Lower Saxony to the liable equity capital of Norddeutsche Landesbank — Girozentrale, adopted by the Lower Saxony Parliament on 17 December 1991 ([1]), the *Land*'s Finance Ministry was empowered to transfer at their market value the *Land*'s shares of the promotion-related assets of the three LTS to NordLB as equity capital. The *Land* also undertook to maintain the total market value of the transferred assets at not less than DEM 1 500 million.

(32) On the basis of this Act, the *Land* of Lower Saxony and NordLB concluded a transfer agreement on 20 December 1991 by which the *Land* transferred to NordLB as liable equity capital its entire shares of the respective promotion-related assets. The purpose of transferring the assets was to increase by DEM 1 500 million the equity capital of NordLB recognised for supervisory purposes.

(b) VALUE OF THE LTS

(33) On 21 February 1992 NordLB charged the audit firm Treuarbeit AG with the task of determining the value of the transferred assets at 31 December 1991. Treuarbeit AG concluded that the total value of the assets transferred came to DEM 1 754 million and confirmed that the special-purpose reserve of DEM 1 500 million, formed in connection with the transfer and shown on NordLB's balance sheet at 31 December 1991 as equity capital, should be regarded as containing value.

(34) The value of the assets transferred to NordLB by the *Land* of Lower Saxony is continually updated. The table below shows the values established up to the end of 2003:

Date	Value (DEM million)
31.12.1991	1 754,4
31.12.1992	[...]
31.12.1993	[...]
31.12.1994	[...]
31.12.1995	[...]
31.12.1996	[...]
31.12.1997	[...]
31.12.1998	[...]
31.12.1999	[...]
31.12.2000	[...]
31.12.2001	[...]
31.12.2002	[...]
31.12.2003	[...]

(35) On the basis of Treuarbeit AG's report, NordLB applied to the German Banking Supervisory Authority (*Bundesaufsichtsamt für das Kreditwesen* — 'BAKred') on 26 February 1992 asking for the special-purpose reserve of DEM 1 500 million to be recognised for supervisory purposes as liable equity capital within the meaning of the second sentence of Section 10(2) KWG.

(36) On 26 July 1993 BAKred provisionally recognised the DEM 1 500 million as liable equity capital. In response to a request by BAKred, the *Land* of Lower Saxony again confirmed its undertaking to maintain the value of the promotion-related assets at not less than DEM 1 500 million. On 22 November 1993 BAKred finally gave notice that it was withdrawing its initial reservations regarding the value of the special-purpose reserve. Before formally recognising the promotion-related assets of the LTS as core capital, BAKred allowed them to be used to cover liabilities, in so far as was necessary to comply with the solvency rules in force at the time.

(37) From the time of the transfer, the sum of DEM 1 500 million was shown under NordLB's equity capital as a combined special-purpose reserve, while the difference vis-à-vis the value of the assets was booked as a provision for commitments arising from the transfer agreement.

(38) Germany has stated that each year around DEM 100 million of the assets transferred was required to underpin promotion-related business. All the remaining assets were available to NordLB to underpin its competitive business from the time when BAKred granted its recognition. Until BAKred granted its final recognition, only the portion of the assets that was actually necessary to comply with solvency rules was available for competitive business.

(39) In detail, the following amounts were available for competitive business:

1992	Value of assets available for competitive business, according to Germany (DEM million)
January	120
February	101
March	145
April	109
Mai	71
June	0
July	0
August	0
September	0
October	19
November	63
December	162

([1]) Lower Saxony Official Gazette [*Niedersächsisches Gesetz- und Verordnungsblatt*], No 47/1991, p. 358.

1993	Value of assets available for competitive business, according to Germany (DEM million)
January	133
February	133
March	207
April	147
May	174
June	1 143
July	1 222
August	1 071
September	1 176
October	1 204
November	1 149
December	1 197

Irrespective of the use to which the assets may be put for the purposes of banking supervision, NordLB is committed by agreement to inform the *Land* before the beginning of each business year how much of the LTS promotion-related assets it plans to use ('earmarking of capital'). For 1992 NordLB notified the use of DEM 180 million. For 1993 the figure was DEM 1 400 million. Since 1994 the amount of capital notified to the *Land* has coincided with the maximum value available for competitive business (the different amounts totalling DEM 1 500 million were needed for promotion-related activities).

Date	Earmarked capital (DEM million)
31.12.1991	—
31.12.1992	180
31.12.1993	1 400
31.12.1994	1 400
31.12.1995	1 390
31.12.1996	1 390
31.12.1997	1 390
31.12.1998	1 390
31.12.1999	[...]
31.12.2000	[...]
31.12.2001	[...]
31.12.2002	[...]
31.12.2003	[...]

(c) EFFECTS OF THE TRANSFER OF THE LTS ASSETS ON NORDLB

(40) Germany states that, as at 31 December 1991, NordLB had core capital of DEM 2 043 million and additional capital of DEM 543 million. The promotion-related assets of DEM 1 500 million therefore increased the total equity capital base of DEM 2 586 million by 58 %.

(41) The scope for business expansion using 100 % risk-adjusted assets was increased by a factor of 12,5, i.e. by around DEM 17 500 million. In reality, however, an increase in own funds of around DEM 1 400 million can expand the permissible credit volume by much more, as a bank's assets are normally not 100 % risk-adjusted. Since the increase in core capital allowed NordLB to raise further additional capital, there was an even greater indirect increase in its actual lending capacity.

(d) REMUNERATION FOR THE TRANSFER OF THE LTS

(42) Under Section 7(1) of the transfer agreement of 20 December 1991, a remuneration of 0,5 % per annum after tax was agreed for the transfer of the promotion-related assets of all three LTS. The remuneration is payable each subsequent year. In this context NordLB must determine the amount of remuneration for the following business year by 31 January. According to the terms of the agreement, the rate of remuneration is based on the notified use of the reserves formed pursuant to the transfer agreement, i.e. only on the capital actually earmarked. Accordingly, the following amounts have been paid:

Date	Earmarked capital (DEM million)	Interest rate	Remuneration paid (DEM million)
31.12.1992	180	0,5 %	0,9
31.12.1993	1 400	0,5 %	7
31.12.1994	1 400	0,5 %	7
31.12.1995	1 390	0,5 %	6,95
31.12.1996	1 390	0,5 %	6,95
31.12.1997	1 390	0,5 %	6,95
31.12.1998	1 390	0,5 %	6,95
31.12.1999	[...] (*)	0,5 %	[...]
31.12.2000	[...]	0,5 %	[...]
31.12.2001	[...]	0,5 %	[...]
31.12.2002	[...]	0,5 %	[...]
31.12.2003	[...]	0,5 %	[...]

(43) Under the transfer agreement, the *Land* of Lower Saxony also has the right to withdraw interest payments and amortisations that flow back to the promotion-related assets, in so far as the market value of the assets exceeds DEM 1 500 million. Germany stated that, up to March 2003, a total of DEM 473,88 million (EUR 242,29 million) was withdrawn, which, it argues, corresponds to an interest

(*) Confidential information.

premium of around 2,79 %-2,85 % per annum on top of the agreed 0,5 % per annum.

e) CAPITAL CONTRIBUTIONS BY THE OTHER SHAREHOLDER (NSGV)

(44) In preliminary discussions on the transfer of the LTS promotion-related assets to NordLB, the *Land* of Lower Saxony made it clear to the only other guarantor at that time, namely NSGV, that, in its view, both guarantors bore joint financial responsibility and that NSGV would have to make its own contribution in accordance with its 40 % share of capital. If this were to pose problems, a change in ownership structure would have to be discussed.

(45) A draft agreement to be concluded between the two guarantors was annexed to the draft law of 15 October 1991. According to Germany, the only obstacle to this 'guarantor agreement' being signed immediately was the fact that it had to be co-signed by the *Land* of Saxony-Anhalt and SBV, and the latter had not yet been set up at that time. On concluding the transfer agreement on 20 December 1991, the assembled guarantors, consisting at that time of the *Land* of Lower Saxony and NSGV, decided to reach such a guarantor agreement which was then duly concluded on 5 March 1992 — after the entry into force of the State Treaty — with the participation of the *Land* of Saxony-Anhalt and SBV.

(46) According to Germany, NSGV subsequently honoured its undertakings under the guarantor agreement of 5 March 1992 and in July and October 1994 increased NordLB's own funds recognised for supervisory purposes by a total of DEM 1 000 million (in line with its 40 % share of NordLB's capital at that time) by means of two measures described in more detail below.

(i) ***LBS special-purpose reserve of DEM 450 million***

(47) Following negotiations between the *Land*, NSGV and NordLB at the end of 1993, the Landesbausparkasse (LBS), previously incorporated in NordLB, was hived off by an Act adopted on 6 June 1994 and turned into an independent public-law institution (*Anstalt des öffentlichen Rechts*) with legal capacity, with effect from 1 July 1994.

(48) Up to then, LBS had been 60 %-owned by the *Land* of Lower Saxony and 40 %-owned by NSGV. Their value was estimated at DEM 900 million. It was agreed that NordLB would withdraw DEM 450 million from LBS before it was hived off and that NSGV would inject the same amount into LBS. This last measure was effected by deducting DEM 450 million from NGSV's commitment under the guarantor agreement to inject DEM 1 000 million into NordLB, on condition that NSGV would make a further capital contribution of DEM 550 million.

(49) NordLB booked the sum of DEM 450 million it had withdrawn to a revenue reserve in the form of a special reserve as additional liable equity capital within the meaning of the banking supervisory rules. The special reserve yielded cumulative interest before tax of 7,5 % per annum and was owned jointly by the guarantors in accordance with their internal relationship, i.e. 60 % by the *Land* and 40 % by NGSV.

(ii) ***Silent partnership contribution of DEM 550 million***

(50) Germany states that on 10 October 1994 NSGV and NordLB concluded an agreement concerning a capital contribution under Section 10(4) KWG. Under that agreement, NSGV undertook to make a capital contribution to NordLB in the form of a silent partnership amounting to DEM 550 million, with effect from 10 October 1994, in return for payment of a profit-linked remuneration the amount of which would be derived from the interest rate (specified in more detail) on 10-year bearer bonds amounting to 7,91 % plus a margin of 1,2 % per annum. This produces a total interest rate of 9,11 %, which, according to the German authorities, corresponds to the normal market remuneration for silent partnerships and at the same time to the remuneration payable to the *Land* of Lower Saxony for contributing the promotion-related assets as liable equity capital. The German authorities state that the contribution was made in accordance with the agreement and was recognised for supervisory purposes as liable equity capital of NordLB.

III. COMMENTS FROM INTERESTED PARTIES

1. *COMPLAINT AND OBSERVATIONS BY THE COMPLAINANT (THE BDB)*

(51) In BdB's view, the transfer of the LTS promotion-related assets and the associated increase in NordLB's capital distorted competition in favour of NordLB since the latter did not pay remuneration consistent with the market-economy investor principle.

(52) The BdB submits that the application of the market-economy investor principle is not limited to enterprises which are loss-making or in need of financial restructuring. An investor is not guided by the question of whether the enterprise in question is profitable at all but rather by whether the profitability corresponds to the market rate. If capital injections by the public authorities were examined only in the case of loss-making enterprises, this would discriminate against private enterprises and thus infringe Article 86(1) of the EC Treaty.

(53) It also submits that Article 295 of the EC Treaty cannot be used to exempt the transfer of the LTS from the competition rules, arguing that the Article in question may well protect the freedom of the State to create such a special asset but, as soon as it is transferred to a commercial enterprise, the competition rules must be applied.

(54) The BdB states that the question of what remuneration was appropriate for the transfer of the promotion-related assets, particularly in the case of NordLB, should be determined

using the method employed by the Commission in its WestLB decision of 8 July 1999. The first step is therefore to compare the capital provided with other equity instruments. The second step is to determine the minimum remuneration which an investor would expect for a real equity-capital investment in the Landesbank. Finally, a calculation must be made of any premiums and discounts applied by virtue of the particularities of the transfer.

Comparison with other equity instruments

(55) The BdB comes to the conclusion that the transfer of the LTS promotion-related assets to NordLB — and the transfer of capital in all the other Landesbank cases — can be compared to an injection of share capital.

(56) It argues that the promotion-related assets transferred cannot be compared with capital in the form of profit participation certificates, as profit participation rights constitute only additional capital. At the time of the respective transfers, in particular at the end of 1991, only share capital (and reserves within the meaning of Section 10(2) KWG) and silent partnership contributions were recognised as core capital in Germany. Any comparison with silent partnership contributions could be ruled out across the board. First, such contributions were made available by an investor for a limited period only. An investor could not therefore expect to receive the same return on a silent partnership contribution as for equity instruments recognised for supervisory purposes for an unlimited period, in particular a injection of share capital.

(57) Second, although it was asserted that the transferred capital was subordinate in liability to share capital pursuant to agreements between the Landesbanks' owners, this did not necessarily mean a lower risk for the investor. The injected capital made up a significant proportion of the total core capital, making it extremely likely that it would be drawn on — at least in part — in the event of losses ([1]).

(58) Third, the BdB submits that the difference in quality between silent partnership contributions and the capital transferred to the Landesbanks as promotion-related assets is confirmed by the definition of core capital for supervisory purposes adopted by the Basle Committee for Banking Supervision. According to this definition, silent partnership contributions must be recognised for supervisory purposes as no more than lower tier I capital, which may account for no more than 15 % of the requisite core-capital ratio. In other words, where the core-capital ratio is 4 %, 3,4 % must be made up of nominal capital and open reserves (e.g. the special-purpose reserves transferred to the Landesbanks). Furthermore, banks only ever took up subordinate equity instruments such as preference shares or profit participation rights in small volumes. Under pressure from the rating agencies, such instruments hardly ever accounted for more than 10 % of a bank's total core capital — a very different situation from that in the cases under examination. Against this background, silent partnership contributions could not be used for large volumes invested by a single investor.

([1]) Moreover, a risk or liability premium was paid primarily because of the risk of loss in the event of insolvency. If this were to happen, the capital would be irretrievably lost. In the event of ongoing (partial) losses, i.e. outside insolvency, there was always a chance that the equity capital might be replenished through profits.

Minimum remuneration for a share-capital investment in a Landesbank

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

Expected return on a risky investment

=

risk-free return + risk premium for the risky investment

(60) 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. 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 basic rate, the estimated figure for average long-term inflation expectations (3,6 %) is added to the 'real basic rate' at the time in question.

(61) According to the BdB, the first step in working out the *market-risk premium* is to determine the difference between the long-term average return on shares and that on government bonds.

(62) As a second step, the BdB determines the beta value for the Landesbanks, i.e. the individual risk premium for the banks by which the general market-risk premium was to be adjusted.

Premiums and discounts on account of the particularities of the transactions

(63) The BdB notes that the Commission's deduction, in Decision 2002/392/EC, from the minimum remuneration to allow for the *lack of liquidity* of Wfa's 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 this discount would be calculated using the WestLB method, on the basis of net refinancing costs (gross

refinancing costs minus the applicable corporation taxes).

(64) The Court of First Instance also upheld the premium applied by the Commission in Decision 2000/392/EC. If the circumstances leading to an increase in risk compared with a 'normal share-capital investment' are also present in the other Landesbank cases (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 that a premium is also justified here.

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

(65) On 30 October 2003 Germany forwarded a response from the *Land* of North Rhine-Westphalia and WestLB to the Commission's decision to initiate the investigation procedure in which they disputed the statement that the assets transferred to the Landesbanks, including NordLB, 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, adding 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.

(66) WestLB had no objections to the Capital Asset Pricing Model (CAPM) method for calculating the minimum remuneration for a share-capital investment but felt that the beta values determined by the BdB — at well over 1 — were inappropriate. A beta factor of more than 1 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.

(67) Moreover, they argued that, 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 placed the Landesbanks at an unjustifiable disadvantage compared with private competitors.

(68) 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 remuneration for 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.

(69) Finally, 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 — and 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.

3. *COMMENTS BY NORDLB AND THE LAND OF LOWER SAXONY*

(70) Since the observations made by NordLB and by the *Land* of Lower Saxony were also presented by the Federal Government, they are included here together with the comments by Germany.

4. *COMMENTS BY GERMANY*

(71) Germany argues that, even after the decision by the Court of First Instance, there are still fundamental doubts as to whether investments in profitable undertakings by public authorities can be assessed using the private investor test. It is also convinced that the transfer of promotion-related assets to NordLB by the *Land* of Lower Saxony does not constitute aid according to the principles applied by the Commission in Decision 2000/392/EC.

(72) In NordLB's case, the only other partner besides the *Land* at the time the assets were transferred, i.e. NSGV, undertook to make a contribution corresponding in volume to that of the *Land* — proportionate to its own shareholding — and under similar conditions. It duly made such a contribution. In this respect, the *Land* already acted like a private investor in its transfer of the promotion-related assets to NordLB.

(73) Moreover, Germany argued, NordLB also paid an appropriate remuneration. It pointed out here that the remuneration paid (0,5 % after tax or 1,2 % before tax) corresponded to an indicative interest rate of around 9,5 % before tax (1,2 % + 8,3 %), taking into account the refinancing costs of around 8,3 % which the *Land* as investor had saved. Furthermore, in addition to the remuneration of 0,5 % after tax, the *Land* of Lower Saxony had also obtained continuous revenue flows from the promotion-related assets amounting to EUR 242,29 million (DEM 473,88 million).

(74) Germany argues that the BdB and the Commission were mistaken in the way they calculated the minimum remuneration in the Decision 2000/392/EC. The CAPM method is said to be unsuitable for determining the market return for a number of reasons. First, the assets transferred to NordLB were not freely available. This meant that the investment alternatives assumed under the CAPM method were practically non-existent. The risk assumed in the CAPM to account for market fluctuations did not exist either, as the Landesbanks were not quoted on the stock exchange, the investment was remunerated at a fixed rate and at that time the Landesbanks still benefited from *Anstaltslast* (institutional liability) and *Gewährträgerhaftung* (guarantor liability). There were therefore no historical data series for beta factors.

(75) Among the special circumstances of the asset transfer, consideration should be given to the fact that the liability of the promotion-related assets is limited in accordance with the proportion of NordLB's share capital held by the *Land* of Lower Saxony and that the *Land* is entitled to compensation from NordLB's other guarantors. In deciding to invest, an investor would pay particular attention to the fact that, although externally the promotion-related assets were exposed to loss without limitation, internally their liability was restricted to an amount corresponding to the share of NordLB's capital held by the *Land* of Lower Saxony. The *Land* was therefore entitled to compensation from NordLB's other guarantors — all of them public-law corporations — which ran no risk of insolvency.

(76) With regard to a premium on account of the exceptionally high volume of the transaction, Germany cannot understand how such a volume is to be defined or why such a premium is justified. In 1992 the assets transferred represented only 34,89 % of the total equity of the NordLB group recognised for supervisory purposes. This proportion had fallen to a mere 9,62 % by 2001. The figures for NordLB's equity capital used as a basis for these calculations are DEM 4 298 million in 1992 and DEM 15 596 million in 2001. They already include the LTS assets.

(77) Germany also argues that no premium is justified on account of the failure to issue new shares to the *Land* of Lower Saxony. At the time of the transfer, NSGV gave an undertaking to inject capital in line with its share of NordLB, which it subsequently did. There was therefore no reason to increase the shares held by the *Land*.

(78) Finally, in Germany's view, no premium is justified either for the lack of fungibility of the promotion-related assets. For the purposes of calculating the minimum return, the BdB and the Commission compared the asset transfer to a share-capital investment. But the fungibility of share-capital investments was just as low as that of the LTS promotion-related assets.

(79) If NordLB were indeed favoured by the transfer of the promotion-related assets, the favourable treatment consisted only in compensation for NordLB for the costs it incurred for carrying out its public mandate. NordLB was not only the *Land* bank but also a savings bank in the Braunschweig area. It therefore performed not only the traditional public tasks of a *Land* bank, with the attendant costs, but also the function of a savings bank.

(80) If, nevertheless, there were aid in this case, it was in any event existing aid since the promotion-related assets had been transferred on the basis of *Anstaltslast*, on which a final settlement was reached by the Brussels compromise of 17 July 2001.

5. *UNDERSTANDING BETWEEN BDB, THE LAND OF LOWER SAXONY AND NORDLB*

(81) On 7 October 2004 the Commission was informed of the outcome of an understanding reached between the complainant BdB, the *Land* of Lower Saxony and NordLB. Irrespective of their basic interpretations of the legal situation, which remained unchanged, the parties to the understanding agreed on what they themselves would regard as suitable parameters for determining an appropriate remuneration and as an appropriate remuneration. The parties asked the Commission to take account of the outcome of the understanding in its decision.

(82) Applying the CAPM, the parties first determined a minimum remuneration for a hypothetical share-capital investment in NordLB. They arrived at an appropriate minimum remuneration of 10,03 % for the LTS promotion-related assets. They took as their basis the risk-free interest rates of the REX1O Performance Index of Deutsche Börse AG and, for the beta factors, a KPMG report of 26 May 2004 drawn up on behalf of the Landesbanks (and now in the Commission's possession). In practical terms, a risk-free basic interest rate of 7,15 % was calculated for NordLB as at 31 December 1991 and a beta value of 0,72 was applied on the basis of the KPMG study. The market-risk premium was set at 4 % (for all Landesbanks).

(83) A deduction was then determined for the capital's lack of liquidity on the basis of the risk-free interest rate of 7,15 % as gross refinancing costs. To determine the net refinancing costs, the standard tax burden of NordLB at the transfer date was fixed at a flat rate of 50 %, giving a liquidity discount of 3,75 %.

(84) Lastly, a premium of 0,3 % was added to allow for the failure to issue voting rights.

(85) This resulted overall in an appropriate remuneration of 6,76 % per annum after tax for that portion of the LTS proportion-related assets that could be used for the

competitive activities of NordLB. This remuneration was payable as of the end of the month when the assets were recognised as core capital (30 November 1993).

(86) The understanding makes no mention of any remuneration for that portion of the LTS promotion-related assets that could not be used for the competitive activities of NordLB (bank guarantee — *Avalprovision*).

IV. ASSESSMENT OF THE MEASURE

(87) The first step in appraising the measure under the state aid rules of the EC Treaty is to assess whether it constitutes state aid within the meaning of Article 87(1) of the EC Treaty.

1. *STATE RESOURCES AND FAVOURING OF A PARTICULAR UNDERTAKING*

(88) As described above, the *Land* of Lower Saxony's shares in the promotion-related assets of the three LTS were transferred to NordLB as equity capital. If state assets of this kind, which have a commercial value, are transferred to an undertaking, then state resources within the meaning of Article 87(1) of the EC Treaty are involved.

(89) 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 has been accepted (and developed) by the Court in a number of cases. The assessment under that principle will be made in paragraph 93 *et seq*. below.

2. *DISTORTION OF COMPETITION AND EFFECT ON TRADE BETWEEN MEMBER STATES*

(90) As a result of the liberalisation of financial services and the integration of financial markets, banking within the Community has become increasingly sensitive to distortions of competition, especially since remaining obstacles to competition in the financial services markets are being gradually dismantled.

(91) NordLB is an all-purpose bank and an important player on the international capital markets. It offers banking services in competition with other European banks inside and outside Germany. Aid given to NordLB therefore distorts competition and affects trade between the Member States.

(92) It should also be recalled that there is a close link between the equity of a credit institution and its banking activities. Only on the basis of sufficient accepted equity capital can a bank operate and expand its commercial operations. As the state measure provided NordLB with such equity capital for solvency purposes, it directly influenced the bank's business possibilities.

3. *MARKET-ECONOMY INVESTOR PRINCIPLE*

(93) In deciding whether a financial measure taken by a public owner of an enterprise constitutes aid within the meaning of Article 87(1) of the EC Treaty, the Commission applies the market-economy investor principle. This principle has been applied by the Commission in many cases and has been accepted and developed by the Court of Justice of the European Communities in several decisions. [1] It allows the Commission to bear in mind the specific circumstances of each case, e.g. to take into account certain strategies of a holding company or group of companies or to distinguish between the short- and long-term interests of an investor. The market-economy investor principle will also be applied to the case at hand.

(94) According to the principle, no state aid is involved if 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'. [2] In particular, a financial measure must be considered unacceptable to a market-economy investor if the proposed remuneration arrangements are less attractive than the market-rate remuneration paid for comparable investments.

(95) In the light of the market-economy investor principle, the key question is therefore whether such an investor would have supplied NordLB with capital that had the specific characteristics of the LTS assets and under the same conditions, especially in view of the probable return on the investment. This question will be examined below.

(a) ARTICLE 295 OF THE EC TREATY

(96) Article 295 of the EC Treaty lays down that the system of property ownership in the various Member States must not be affected. This does not, however, justify any infringement of the competition rules of the Treaty.

(97) Germany claims that, because of the constraints imposed by the special purpose assigned to the LTS assets, the only possible profitable use of these resources was to transfer them to a similar public-law institution. Consequently, the transfer represented the commercially most sensible use of

[1] See, for example, Cases C-303/88 Italy v Commission [1991] ECR I-1433 and C-305/89 Italy v Commission [1991] ECR I-1603.

[2] 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).

those assets. So any remuneration for the transfer, i.e. any additional return on the LTS capital, would be sufficient to justify the transfer in the light of the market-economy investor principle.

(98) This line of argument cannot be accepted. It may be that the transfer of the three LTS to NordLB, which subsequently allowed NordLB to use part of the LTS capital to underpin its competitive business, was the commercially most sensible use. However, simply taking the view of a public investor would leave out of account the fundamental question of whether the recipient benefited from preferential treatment. The presence of such treatment can be ascertained only by checking whether the price paid by the recipient corresponds to the market price. As soon as public monies and other assets are used for commercial, competition-oriented activities, the normal market rules must be applied.

(b) NO CHANGE IN OWNERSHIP STRUCTURE

(99) One way of ensuring an adequate return on the capital provided would have been to increase the *Land*'s participation in NordLB accordingly, provided that the bank's overall profitability corresponds to the normal rate of return that a market-economy investor would expect from his investment. However, this course was not taken by the *Land* of Lower Saxony.

(100) Germany also attributes the failure to increase the *Land*'s shares in NordLB to the fact that, at the time of the asset transfer, NSGV undertook to inject capital in proportion to its share in NordLB, which it then did by creating the LBS special-purpose reserve of DEM 450 million and making the silent partnership contribution of DEM 550 million. Moreover, Germany argues that, in *Alitalia*, the Court held that a capital injection from public funds would always satisfy the private investor principle if another shareholder made an investment and that in such a case no state aid was involved. ([1])

(101) It should be pointed out that the Court of Justice's ruling in *Alitalia* referred to investments by private parties. But, in the case of NSGV, we are dealing not with a private party but with a public-law entity. The contributions by NSEV were, moreover, not comparable to the transfer of the LTS assets either in timing or in content.

(102) Whereas the LTS assets were transferred to NordLB with effect from 31 December 1991, it was only with effect from 1 July 1994 that LBS was hived off from NordLB and the LBS special-purpose reserve of DEM 450 million was formed. The silent partnership contribution of DEM 550 million took effect only from 10 October 1994. In the Commission's view, this difference in timing between the transactions already shows that they did not take place under similar conditions.

(103) Moreover, the investments in question took a different form, at least in the case of the silent partnership. At that time, all silent partnership contributions constituted 'lower tier I capital', i.e. additional capital which could not be drawn on to the same extent as share capital in order to comply with solvency regulations. Also, in contrast to share-capital investors, silent partners do not share in a company's increases in value, but are remunerated entirely by means of direct payments, which are normally lower than those for share-capital investments.

(104) Even if one assumes that a higher remuneration should have been paid for the (liquid) silent partnership contribution of DEM 550 million than for the (non-liquid) promotion-related assets of the LTS, the transfers of assets by the *Land* and by NSGV are not comparable given the differences in remuneration. Each year a payment of 7,5 % (before tax) is made for the LBS special-purpose reserve, while, according to the Federal Government, the silent partnership contribution yields interest of around 9,11 % (before tax). By contrast, the LTS assets yield interest of 0,5 % after tax (around 1,2 % before tax). So the remuneration for the LTS assets is much lower than that for the measures taken by the NSGV.

(105) Given such marked differences between the transactions carried out by the *Land* and by NSGV, the question can ultimately be left open as to whether, at the time when the LTS assets were transferred to NordLB, NSGV was in fact bound by an obligation to inject into NordLB an amount of capital corresponding to its shareholding or whether this obligation was laid down only later.

(106) It can therefore be concluded that there was no proportional, comparable capital injection by a private investor, so that the conditions underlying the *Alitalia* case are not met here. The investment was made by another public shareholder, NSGV, and the conditions of the capital injection are not comparable since the two contributions took place at different times and the terms also differed.

(c) OWNER EFFECT

(107) Germany believes that, in calculating the remuneration, a market-economy investor would have taken into account the increase in value in its own holding in NordLB. At the time when the LTS assets were transferred, the *Land* of Lower Saxony had a 60 % share in NordLB, the value of which increased as a result of the transfer. Moreover, according to Germany, the *Land* ensured that NSGV also injected capital commensurate with its own holding in order to prevent NSGV from sharing in an increase in value brought about solely by the *Land*.

([1]) Judgment given by the Court of Justice on 12 December 2000 in Case T-296/97.

(108) For the reasons set out in paragraph 102 *et seq*., no importance can be attached to the fact that the *Land* had shares in NordLB and NSGV's capital injection cannot be regarded as a comparable investment. By means of that injection NSGV shared in the increase in value without having made a corresponding contribution. No market-economy investor would agree, as a joint owner, to bear the entire cost of an investment if it were then to realise only part of the gains from it. The Court of First Instance has specifically confirmed this view in its judgment in *WestLB* ([1]).

(d) CAPITAL BASIS FOR CALCULATING THE REMUNERATION

(109) Germany submits that only the part of the accepted original own funds which can be used by NordLB to underpin its commercial business has an economic value for the bank, so that a remuneration can be demanded by the *Land* in respect of this part only. BdB claims that the whole amount of DEM 1 754.4 million is at risk and therefore a remuneration must be paid on that amount.

(110) As determined in Decision 2000/392/EC and confirmed by the Court of First Instance, remuneration is, in principle, payable on the entire value of the transferred assets. This approach was applied in the WestLB case and upheld by the Court. However, the remuneration may differ for the different parts of the transferred assets.

(111) For the purpose of determining an appropriate remuneration, a distinction should be made between the different parts of the LTS assets according to their use to NordLB.

(112) The value of the assets is determined every year. At the end of 1991 it stood at DEM 1 754.4 million. However, only DEM 1 500 million was entered as equity on NordLB's balance sheet. The difference between this amount and the value of the LTS assets was booked as a provision for commitments arising from the transfer agreement. Such provisions are built up against imminent liabilities and do not constitute equity capital. As a consequence, they generally do not improve a firm's credit standing. The *Land* of Lower Saxony is also entitled to withdraw interest payments and amortisations which flow back to the promotion-related assets, in so far as the market value of the assets exceeds DEM 1 500 million. Since NordLB is therefore unable to use the capital that exceeds the value of DEM 1 500 million either to expand its business or to cover liabilities, the Commission assumes that an investor could not demand a remuneration for this portion of the promotion-related assets.

([1]) OJ L 150, 23.6.2000, p. 1, paragraph 316.

(113) Since the time of the transfer, a value of DEM 1 500 million has been booked as equity capital in NordLB's balance sheet. However, the LTS assets could not be used in full as equity capital until recognised by BAKred. Until the amount was provisionally recognised on 26 July 1993, the use of the promotion-related assets was tolerated by BAKred only in so far as was necessary in order to comply the solvency rules in force at the time. The full amount of DEM 1 500 million could be used only after it was provisionally recognised on 26 July 1993. However, of this DEM 1 500 million, only around DEM 1 400 million — the exact amount fluctuates from year to year — can be used by NordLB to expand its competitive business activities since the remainder is needed for its promotion-related business. The main basis for determining the remuneration payable to the *Land* should therefore be, for 1992 and up to August 1993, only the capital actually used and, from August 1993, the capital earmarked for use, i.e. around DEM 1 400 million each year.

(114) Although the remaining original own funds (around DEM 100 million a year from August 1993, previously a higher amount) cannot be used to expand competitive business, they are of use to NordLB since the amount of own funds shown in the balance sheet is an indication to the bank's lenders of its soundness and thus influences the conditions under which the bank is able to raise outside funds. Creditors and ratings agencies look at the bank's overall economic and financial standing. Since the amount of around DEM 100 million each year cannot be used to expand business but improves the bank's appearance in the eyes of creditors, its economic function may be compared in that respect to at least that of a guarantee.

(115) Since the amount of around DEM 100 million each year is also of economic use to WestLB, a market-economy investor would have asked for a remuneration to be paid on it. The level of this remuneration will certainly be lower than that for the DEM 1 400 million, which is of greater use to NordLB, since it can also be used under the solvency rules as own funds to expand its commercial business.

(116) A final point to be made here is that the text of the understanding between the *Land* of Lower Saxony, NordLB and BdB states that remuneration is payable for the transferred assets only as of the end of the month in which they were finally recognised as core capital by BAKred, i.e. 30 November 1993. On this point, however, the Commission cannot agree with the understanding. The transferred LTS assets were available for use by NordLB following the transfer on 31 December 1991 at least to the extent that their use was tolerated by BAKred, and NordLB did indeed use a considerable portion of the assets before they were finally recognised by BAKred.

(e) APPROPRIATE REMUNERATION FOR THE CAPITAL

(117) Investments of differing economic quality require differing returns. In analysing an investment's acceptability to an investor acting under normal market conditions, it is important therefore to bear in mind the special economic nature of the financial measure in question and the value to NordLB of the capital provided.

(i) ***Comparison with other equity instruments***

(118) Germany believes that the remuneration for share capital is not the correct benchmark for calculating an appropriate remuneration for the LTS assets. While acknowledging that, for supervisory purposes, share capital counts as core capital, it points out that not all of a bank's capital that qualifies as core capital is at the same time share capital. In particular, share capital which is fully at the bank's disposal for it to invest is entirely different in quality from the transferred LTS assets, which continue to be available to the *Land* for specific promotion-related purposes and are therefore not profitable for NordLB itself.

(119) At the time of their transfer, the LTS assets were most comparable to capital in the form of profit participation certificates. At that time, NordLB and the *Land* of Lower Saxony compared the remuneration for the promotion-related assets with remuneration for profit participation certificates. Profit participation capital is additional capital which may, in principle, be taken into account only up to the extent of the core capital. At 31 December 1991, NordLB is said to have had core capital of DEM 2 043 million and additional capital of DEM 543 million. The need for equity capital could therefore have been covered by issuing profit participation certificates amounting to DEM 1 500 million, instead of the promotion-related assets recognised as core capital.

(120) In their comments, the *Land* of North Rhine-Westphalia and WestLB also dispute the assertion that the various transfers of assets to the Landesbanks, i.e. also in the case of NordLB, could be compared to share capital. They argue instead that the transfers are comparable to silent partnership contributions or so-called 'perpetuals'. Silent partnership contributions and 'perpetuals' had been recognised as core capital in Germany since 1991. Moreover, remuneration for an investment depended not on how it was classified by the banking supervisory authorities, but on its risk profile. Since the LTS assets were junior-ranking, the risk pattern had more in common with silent partnership contributions or 'perpetuals' than with share-capital investments.

(121) The Commission shares the BdB's view that the transfer of the LTS assets, which were recognised by BAKred as core capital, is most comparable to a share-capital investment.

(122) In this connection, it should first be stressed that the relatively wide range of innovative equity instruments now available to credit institutions in several countries did not exist in Germany back in 1991, when a decision was taken on transferring the LTS to NordLB or, in 1993, when NordLB had to comply with new, stricter capital requirements. Some of these instruments were developed in the meantime, while others already existed but were not accepted in Germany. In practice, the main instruments which were available and used at that time were profit participation certificates and subordinated loans (both of which are merely additional own funds, the latter being accepted only since 1993).

(123) It is therefore inappropriate to compare the LTS capital to such innovative instruments, most of which have developed in the meantime and some of which are available only in other countries. Germany itself (indirectly) rejects such a comparison, claiming that the Commission must examine the case on the basis of the facts available at the time of the decision at the end of 1991.

(124) As regards perpetual preferred shares and profit participation certificates, a number of specific points should be stressed. Perpetual preferred shares count as core capital in some countries but are still not accepted in Germany. Profit participation certificates constitute only additional own funds, whereas the LTS capital qualifies as core capital. The latter is therefore of much greater use to NordLB 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 base. Moreover, if profitable years followed loss-making ones, profit participation certificates would be replenished before the LTS capital. In addition, the LTS capital is available to NordLB without any time limitation, while profit participation certificates are usually issued for a period of ten years. Furthermore, the enormous size of the capital injection would be atypical for profit participation certificates, and the ranking in the event of losses must be seen in this context. Since the share of the LTS capital is rather large, it will be used relatively quickly when major losses occur.

(125) The Commission considers that a comparison with silent partnership contributions is not suitable either for determining the appropriate remuneration for the special-purpose reserve recognised as core capital. In its view, an important factor here is that the LTS assets were transferred precisely not in the form of a silent partnership contribution but as a special-purpose reserve. BAKred too recognised the transfer as a reserve and not as a silent partnership contribution under Section 10 KWG. The fact that the German supervisory authority treated the transfer as a reserve suggests that the capital made available is more akin to share capital than to a silent partnership contribution.

(126) In addition, there is no less risk that at least part of the transferred capital might be lost in the event of insolvency or liquidation than would be the case for a share-capital investment, as the LTS assets make up a considerable proportion of NordLB's equity capital and NordLB has used a substantial amount of those assets to cover risk-bearing assets over many years.

(127) For all these reasons, the Commission believes that, because of the peculiarities of the LTS capital, a comparison with perpetuals, profit participation certificates and silent partnership contributions is not a suitable way to determine the appropriate remuneration to be paid for the LTS capital. Instead, the transfer of the LTS assets has most in common with a share-capital investment.

(ii) ***Right to compensation and low liability risk***

(128) The liability in respect of the promotion-related assets is limited internally to the share of the *Land* of Lower Saxony in NordLB's capital, and the *Land* is entitled to seek compensation from all of NordLB's other guarantors. Germany argues that an investor would have given this due consideration in his investment decision and his demand for remuneration.

(129) However, the internal restriction on liability cannot justify any reduction in remuneration since, from NordLB's point of view, it remains the case that the advantage obtained by means of the capital transfer must be adequately remunerated in order to avoid distortions of competition. The *Land*'s right to compensation from the other guarantors constitutes an agreement between guarantors and not a concession by NordLB that might justify a lower remuneration. If, for example, the other guarantors had agreed to assume full liability for the promotion-related assets internally, this could not have led to a situation where NordLB had to pay no remuneration at all.

(130) Moreover, from the Commission's point of view, it is irrelevant whether the LTS assets were used continuously and fully in order to meet solvency requirements. Even if this were not the case, a market-economy investor would have insisted on remuneration in full since the bank was free to employ all the capital in its competitive business according to its economic discretion.

(iii) ***Appropriate remuneration for the amount of DEM 1 400 million***

(131) There are no doubt different ways of calculating the appropriate remuneration for the amount of DEM 1 400 million which was available to NordLB each year for its competitive business. However, as will be shown, all the methods for calculating the remuneration for capital made available follow the same basic principles. Taking these basic principles, the Commission here does the calculation in two steps: first, it determines the minimum remuneration that an investor would expect for a (hypothetical) investment in the share capital of NordLB. It then examines whether, in view of the particularities of the transaction at issue, the market would have agreed on a premium or a discount and, if so, whether it can produce a methodically robust quantification of that amount.

Determination of a likely minimum remuneration for an investment in the share capital of NordLB

(132) The expected return on an investment and the investment risk are key determinants in the decision of a market-economy investor to invest. In order to determine their level, the investor incorporates all available firm-related and market-related information into his calculation. He bases himself on historical average rates, which, generally speaking, are also a point of reference for a firm's future efficiency, and *inter alia* on an analysis of the company's business model for the investment period in question, the strategy and quality of management or the relative prospects for the sector in question.

(133) A market-economy investor will undertake an investment only if it produces a higher return or a lower risk than the next-best alternative use of his capital. Similarly, he will not invest in a company whose expected return is lower than the average return expected for other companies with a similar risk profile. It can be assumed in the present case that there are sufficient alternatives to the assumed investment project that promise a higher expected return with the same risk.

(134) Various methods exist for determining the minimum appropriate remuneration. They range from differing variants of the financing approach to the CAPM method. In describing the various approaches, it makes sense to distinguish between two components, viz. a risk-free return and a project-specific risk premium:

Minimum appropriate return on a risky investment

=

risk-free base rate + risk premium for the risky investment.

Consequently, the minimum appropriate remuneration for a risky investment can be described as the sum of the risk-free rate of return and the additional risk premium for assuming the investment-specific risk.

(135) The basis for any determination of return is thus the existence of a default-risk-free form of investment with an assumed risk-free return. The expected return on fixed-interest government securities is normally used in determining the risk-free basic rate (or, as the case may be, an index based on such securities), but these represent forms of investment with a comparably low risk. The various methods differ, however, when it comes to determining the risk premium:

— *Financing approach*: An investor's expected return on capital represents, from the point of view of the bank using the capital, future financing costs. Under this approach, the historical capital costs incurred by comparable banks are first of all determined. The arithmetic average of the historical capital costs is then compared with the future expected equity capital costs and hence with the investor's expected-return requirement.

— *Financing approach with compound annual growth rate*: At the heart of this approach stands the use of the geometric rather than the arithmetic mean (compound annual growth rate).

— *Capital Asset Pricing Model (CAPM)*: The CAPM is the best-known and most frequently tested model of modern finance, by which the return expected by an investor can be determined using the following equation:

Minimum return
=
risk-free base rate + (market-risk premium × beta)

The risk premium for the equity investment is obtained by multiplying the risk premium on the market by the beta factor (market-risk premium × beta). The beta factor is used to quantify the risk of a company relative to the overall risk of all companies.

(136) The CAPM is the predominant method of calculating investment returns in the case of large listed companies. However, since NordLB is not a listed company, it is not possible directly to infer its beta value. The CAPM can be used only on the basis of an estimate of the beta factor.

(137) In its comments of 29 July 2003, the BdB, using the CAPM, concluded that the minimum remuneration to be expected for an investment in the share capital of NordLB at 31 December 1991, when the LTS assets were transferred, was 13,34 % per annum. Germany raised objections in principle to the use of the CAPM. It also argued that the BdB started from a high beta value and was incorrect in its calculation of the risk-free base rate, and that the market-risk premium of 4,6 % was too high. Had the BdB applied the CAPM correctly, it would have arrived at a much lower minimum remuneration for a hypothetical investment in the share capital of NordLB.

(138) In their understanding on the normal market remuneration, the *Land* of Lower Saxony, NordLB and the BdB concluded that a minimum remuneration of 10,03 % was appropriate.

(139) In their calculations, the parties based themselves on the CAPM and applied a risk-free basic interest rate of 7,15 % for NordLB. Determination of this interest rate was based on the assumption that the LTS special-purpose assets were to be made available on a permanent basis. The parties thus decided not to use a risk-free rate obtaining on the market at the time of the capital injection for a fixed investment period (e.g. 10-year return on government bonds) since such an approach would disregard the reinvestment risk, i. e. the risk that it would not be possible to invest again at the level of the risk-free interest rate once the investment period had expired. In the view of the parties, a total return index was the best way of taking the investment risk into account. They opted, therefore, for the REX10 Performance Index of Deutsche Börse AG, which tracks the performance of an investment in Federal loans over a period of ten years. The index series used in the present case contains the relevant end-of-year results of the REX10 Performance Index after 1970. The parties then determined the rate per annum, which reflects the trend tracked by the REXIO Performance Index in the period 1970-91 and, in this way, arrived at the risk-free basic interest rate of 7,15 % referred to above.

(140) Since NordLB's capital injection was made available on a permanent basis, the method of determining the risk-free basic interest rate appears appropriate in this specific case. Moreover, the REX10 Performance Index is a generally recognised source of data. The risk-free basic interest rate calculated thus appears appropriate here.

(141) The beta factor of 0,72 was estimated on the basis of a KPMG report on adjusted beta factors for all listed credit institutions in Germany that is available to the Commission. In the light of the report and of HLB's business profile, this beta factor is to be regarded as appropriate.

(142) The Commission also regards the market-risk premium of 4,0 % as acceptable. Previously, in Decision 2000/392/EC, the so-called general long-term market-risk premium, i.e. the difference between the long-term average return on a normal share portfolio and that on government bonds, was applied on several occasions. In the corresponding report on the procedure, a range of some 3 % to 5 % was applied,

depending on the method, the period under examination and the basic relevant data. A report prepared for BdB calculated figures of 3,16 % and 5 %. Another report on WestLB drawn up in the first procedure produced figures of 4,5 % and 5 %, while Lehman Brothers, also for WestLB, calculated a figure of 4 %. Against this background, the Commission has here no reason to depart from the market-risk premium used in the understanding. On the basis of the CAPM, the Commission considers there to be no doubt that the minimum remuneration determined by the parties can be regarded as appropriate.

(143) The Commission therefore has no reason to believe that the minimum remuneration determined by the parties for a hypothetical share-capital investment cannot stand up to a market test. Accordingly, it sets the minimum remuneration for the special-purpose reserve at 10,03 % per annum (after corporation tax and before investor tax).

(iv) ***Return discount for lack of liquidity***

(144) Germany believes that NordLB paid an appropriate remuneration, as a private investor would have deducted from the remuneration the refinancing costs he had saved. Since the investor saved the cost of refinancing the capital, Germany concludes that the LTS promotion-related assets yielded around 9,5 %.

(145) However, the Commission considers that the key question here is not how much the *Land* saved as an investor. The *Land* transferred the LTS assets to NordLB as non-liquid capital. The *Land* made no savings as it was not obliged to ensure the assets' liquidity.

(146) 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 ([1]).

(147) Since the LTS capital does not provide NordLB with initial liquidity, NordLB faces additional financing costs equal to the amount of the capital if it is to raise the necessary funds on the financial markets to take full advantage of the business 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) ([2]). Because of these extra costs, which do not arise in the case of equity capital in other forms, 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.

(148) The Commission does not believe that the entire refinancing interest rate has to be taken into account. Refinancing costs constitute operating expenses and therefore reduce taxable income. This means that the bank's net result is not reduced by the amount of additional interest expenses incurred. These expenses are offset in part by reduced corporation tax. Only the net costs should be taken into account as an additional burden on NordLB because of the special nature of the capital transferred. Overall, the Commission accepts that NordLB incurs additional 'liquidity costs' to the extent of 'refinancing costs minus corporation tax'.

(149) On the basis of the REX10 Performance Index of Deutsche Börse AG, the risk-free interest rate stood at 7,15 % at the end of 1991. Two 30-year German Government bonds issued in 1986 had secondary-market yields of 7,8 % and 7,6 % at the time. Germany stated that NordLB's individual refinancing rate at 31 December 1991 was [...] %. In the understanding the parties used a long-term risk-free rate of 7,15 %. They also agreed to assume a flat 50 % tax rate ([3]). On this basis, they arrive at a net refinancing rate of 3,57 % and hence a corresponding deduction for liquidity.

(150) In view of that understanding and the fact that the amounts in question still fall below the range previously cited by Germany, the Commission sees no reason to regard 3,57 % as inappropriate and consequently uses this rate as a basis for determining the aid element.

(v) ***Return premium on account of the particularities of the transfer***

(151) In practice, when remuneration is determined, atypical circumstances which depart from a normal investment in the share capital of the company concerned generally give rise to discounts or premiums. It must therefore be examined whether the particularities, and especially the specific risk profile of the transfer of the LTS capital, constitute grounds for adjusting the determined minimum remuneration of 10,03 %, which a private investor would

([1]) 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.

([2]) 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).

([3]) According to documents provided by Germany, the corporation tax rate was 46 % in 1992, plus a solidarity surcharge of 3,75 %, i.e. 49,75 % in total. The overall tax rate fell to 46 % in 1993 and stood at 49,5 % from 1994 to 2000. From 2001 the overall tax rate was 30 %.

expect for a (hypothetical) investment in the capital of NordLB, and whether a methodically robust quantification of that adjustment can be produced. In this connection, three aspects should be considered: first, the non-issuance of new shares in the company with the associated voting rights; second, the exceptional volume of the asset transfer; and, third, the non-marketability of the assets.

(152) The transfer did not provide the *Land* with any additional voting rights. Nor was this disadvantage offset by a comparable investment by the other shareholder. By forgoing voting rights, an investor renounces a say in decisions taken by the bank's board. To compensate for this acceptance of a higher risk of loss without a corresponding increase in influence over the company, a market-economy investor would demand a higher remuneration (even if the potential risk were cushioned by internal agreements with the other shareholders). On the basis of the higher remuneration for preference shares compared with ordinary shares, the Commission considers a premium of at least 0,3 % p.a. (after corporation tax) to be appropriate. The parties to the understanding also regard a premium of 0,3 % as appropriate to take account of the failure to issue new voting rights.

(153) The size of the amount transferred and its effect on NordLB from the point of view of the Solvency Directive have already been mentioned (paragraph 40 *et seq*.). Through the transfer of the LTS, NordLB's core capital was increased substantially without any acquisition or administration costs. A market-economy investor would probably have demanded a premium for an injection of capital as large in relative and absolute terms as the LTS assets. On the other hand, in the light of the exceptional capital requirements of credit institutions in the EU laid down by the Solvency Directive, a capital injection of some DEM 1 500 million in one of the largest German all-purpose banks must not be regarded as completely alien to any normal business decision. Moreover, where an investment involves a large volume of assets, this suggests a similarity with share capital. When the transfer took place at the end of 1991, large silent partnership contributions were atypical on the market. So if the volume of assets transferred is used to justify a further premium in the case of an investment that is similar to share capital, this means that the volume is being unduly taken into account twice over. Consequently, the Commission is not imposing a premium linked to the volume of the asset transfer, something which works in NordLB's favour. The understanding between the parties also assumes that no premium should be applied on account of the high volume of assets transferred.

(154) Lastly, attention must be drawn to the lack of fungibility of the assets, i.e. the impossibility of withdrawing the invested capital at any time from the company. Normally, an investor can sell an equity instrument on the market to third parties, thereby terminating his investment. A normal transfer of capital takes place as follows: the investor brings in assets (either in cash or in kind), which are entered on the assets side of the balance sheet. As a rule, these are matched on the liabilities side by a tradable interest registered in the name of the investor, taking the form, in the case of a limited company for example, of shares. The investor can sell these shares to a third party. He cannot withdraw the assets he originally brought in since these now form part of the company's liable equity capital and are no longer at his disposal. But by selling the shares — at the prevailing exchange price — he can realise their economic countervalue. His assets have thereby become fungible. Because of the special circumstances surrounding the transfer of LTS assets, this option was not available to the *Land*. However, the Commission sees no reason for a further premium. Although the *Land* was unable to realise the economic countervalue by trading freely in the investment, it was and is able at any time to withdraw the special-purpose assets from NordLB by law and achieve possibly higher returns by reinvesting them in other institutions. Here too the understanding between the BdB, the *Land* and NordLB assumes that no premium should be applied on account of the lack of fungibility

(155) Overall, the Commission therefore considers a premium of 0,3 % per annum (after corporation tax) to be appropriate for forgoing additional voting rights.

(vi) ***No reduction in remuneration for agreement on a fixed amount***

(156) In the case of shares, the remuneration depends directly on the performance of the company and is expressed mainly in the form of dividends and a share in the increased value of the company (expressed, for example, in share price increases). The *Land* receives a fixed remuneration which should reflect these two aspects of remuneration for 'normal' capital injections. It could be argued that the fact that the *Land* receives a fixed remuneration instead of one directly linked to NordLB's performance constitutes an advantage which justifies a reduction in the rate of the remuneration. Whether such a fixed rate actually constitutes an advantage as compared with a variable, profit-linked rate depends on the company's performance in the future. If the performance declines, a fixed rate benefits the investor but, if it improves, it places him at a disadvantage. However, the actual trend cannot be taken into account subsequently when it comes to assessing the investment decision. Taking all these factors into consideration, the Commission believes that the rate of remuneration need not be reduced.

(vii) ***Total remuneration***

(157) On the basis of all these considerations, the Commission concludes that an appropriate remuneration for the investment in question would be 6,76 % per annum (after corporation tax), namely, a 10,03 % normal return on

equity plus a premium of 0,3 % for the particularities of the transaction minus 3,57 % on account of the financing costs resulting from the transferred assets' lack of liquidity for NordLB.

(viii) ***Appropriate remuneration for the amount of DEM 1 400 million***

(158) As already mentioned, the equity share of around DEM 100 million each year is also of material value to NordLB and its economic function may be compared to that of a guarantee. A market-economy investor would demand an appropriate remuneration in return for exposing himself to a risk of this sort. This question is not addressed in the understanding between the BdB, the *Land* and NordLB.

(159) In its decision to initiate the procedure laid down in Article 88(2) of the EC Treaty, the Commission quoted a rate of 0,3 % per annum (after tax) as having been indicated by Germany as the appropriate commission on a bank guarantee (*Avalprovision*) for a bank like NordLB. It seems inappropriate to increase this remuneration on account of a particularly large 'guarantee', given that the amount involved is around DEM 100 million. Even for the two years in which a much higher amount was available (1992 and 1993), the Commission feels there is no justification for a premium. For the same reasons that no premium was applied on the remuneration of the capital available for competitive business, it is also doubtful whether this rate can be increased on the grounds that the LTS promotion-related assets were, in principle, available to NordLB without restriction.

(160) The guarantee premium counts as operating expenses for NordLB and hence reduces the taxable profit. The remuneration payable to the *Land* of Lower Saxony for the LTS assets comes out of after-tax profits. The rate of 0,3 % must therefore be adjusted for the tax rate. As with the refinancing costs, the Commission assumes a single overall tax rate of 50 %, in this case in NordLB's favour. Consequently, it sets a rate of 0,15 % per annum after tax.

(f) AID ELEMENT

(161) As calculated above, the Commission considers the following remuneration to be in line with market conditions: 6,76 % per annum after tax for the part of the capital which could be used by NordLB to underpin its commercial business, i.e. around DEM 1 400 million, and 0,15 % per annum after tax for the difference between this part and the DEM 1 500 million shown as equity in NordLB's balance sheet, i.e. around DEM 100 million.

(162) Currently, NordLB pays a remuneration of 0,5 % per annum after tax on the amount which it can actually use for underpinning its competitive business. This remuneration was first paid for 1992.

(163) In addition to the remuneration of 0,5 % per annum after tax, Germany argues that there is a further remuneration component, namely the *Land*'s right to withdraw interest payments and amortisations that flow back to the LTS promotion-related assets, in so far as the market value of the assets exceeds DEM 1 500 million.

(164) The Commission believes that a market-economy investor would not have consented to receive remuneration from income that depended on the behaviour of the bank administering the promotion-related assets. Furthermore, NordLB derived no economic advantage from the part of the assets exceeding DEM 1 500 million (consequently, no remuneration is payable for that part). Nor can amounts withdrawn from that portion of the LTS assets be viewed as additional remuneration since, as in economic terms, they belong not to NordLB but *a priori* to the *Land*.

(165) Germany also claims that one reason for the transfer was to achieve potential synergies rather than to increase NordLB's equity. Yet, at least part of the purpose of transferring the promotion-related assets was to satisfy the requirements of the Solvency Directive. If the LTS benefit from such synergies and cost savings, this will help them by reducing costs but cannot be regarded as a consideration paid by NordLB for the provision of the original own funds. Since these synergies neither reduce the usability of the transferred capital for NordLB nor increase the costs to NordLB arising from the transfer, they should also not influence the level of remuneration which a market-economy investor can demand from the bank for the equity provided. Even if there were an actual benefit accruing to the *Land* as a result of synergies, any competitor would have been forced by competition to pay to the *Land* for the financial instrument (the LTS) not only the appropriate consideration for the equity provided but also a 'remuneration' in the form of such benefits. Moreover, following a merger operation, synergy effects normally arise in both merged entities. It is difficult to understand why NordLB should not profit at all from such advantages. The Commission therefore takes the view that any synergy effects do not constitute remuneration paid by NordLB for the transfer of the LTS.

(166) Lastly, the 'owner effect' is not a reason to assume a remuneration of more than 0,5 % per annum. As pointed out above, a market-economy investor who already holds shares in a company will not forgo full direct remuneration if one or more shareholders profit from the capital injection without themselves having made a corresponding contribution. Since NSGV has not made a corresponding

capital contribution, the *Land* should therefore have insisted on comprehensive direct remuneration.

(167) The aid element can be calculated as the difference between the actual payments and the payments which would correspond to market conditions.

(168) Calculation of the aid element (DEM million)

1992

1992	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1. Amount available for competitive business	120	101	145	109	71	0	0	0	0	19	63	162
2. Remainder (difference vis-à-vis DEM 1 500 million)	1 380	1 399	1 355	1 391	1 429	1 500	1 500	1 500	1 500	1 481	1 437	1 338
Remuneration of 6,76 % per annum (after tax) on point 1	0,67	0,56	0,81	0,61	0,39	0	0	0	0	0,1	0,35	0,91
Remuneration of 0,15 % per annum (after tax) on point 2	0,17	0,17	0,16	0,17	0,17	0,18	0,18	0,18	0,18	0,18	0,17	0,16
Total remuneration in line with market conditions	0,84	0,73	0,97	0,78	0,56	0,18	0,18	0,18	0,18	0,28	0,52	1,07
												Σ 6,47
Actual remuneration (after tax) (0,5 %) for the whole of 1992												0,9
Aid element												5,57

1993

1993	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1. Amount available for competitive business	133	133	207	147	174	1,143	1,222	1 400	1 400	1 400	1 400	1 400
2. Remainder (difference vis-à-vis DEM 1 500 million)	1,367	1,367	1,293	1,353	1,326	357	278	100	100	100	100	100
Remuneration of 6,76 % per annum (after tax) on point 1	0,74	0,74	1,16	0,82	0,98	6,43	6,88	7,88	7,88	7,88	7,88	7,88
Remuneration of 0,15 % per annum (after tax) on point 2	0,17	0,17	0,16	0,16	0,16	0,04	0,03	0,01	0,01	0,01	0,01	0,01
Total remuneration in line with market conditions	0,91	0,91	1,32	0,98	1,14	6,47	6,91	7,89	7,89	7,89	7,89	7,89
												Σ 58,09
Actual remuneration (after tax) (0,5 %) for the whole of 1993												7
Aid element												51,09

Year	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
1. Amount available for competitive business	1,400	1,390	1,390	1,390	1,390	[...]	[...]	[...]	[...]	[...]
2. Remainder (difference vis-à-vis DEM 1 500 mil- 1 500 million)	100	110	110	110	110	[...]	[...]	[...]	[...]	[...]
Remuneration of 6,76 % per annum (after tax) on point 1	94,64	93,96	93,96	93,96	93,96	[...]	[...]	[...]	[...]	[...]
Remuneration of 0,15 % per annum (after tax) on point 2	0,15	0,16	0,16	0,16	0,16	[...]	[...]	[...]	[...]	[...]
Total remuneration in line with market conditions	94,79	94,12	94,12	94,12	94,12	[...]	[...]	[...]	[...]	[...]
Actual remuneration (after tax) (0,5 %)	7	6,95	6,95	6,95	6,95	[...]	[...]	[...]	[...]	[...]
Aid element	87,79	87,17	87,17	87,17	87,17	87,17	85,88	85,88	85,88	85,88

Since 1 January 1999, marks have been converted into euros at a rate of EUR1 = DEM 1,95583. The figures in DEM must be converted accordingly.

(169) Thus, the difference between the agreed remuneration of 0,5 % per annum and the appropriate remuneration of 6,76 % per annum (for the portion of the LTS promotion-related assets which NordLB can use for its competitive business) and 0,15 % per annum (for the portion of the assets that can be likened to a bank guarantee) constitutes state aid within the meaning of Article 87(1) of the EC Treaty.

(170) The aid element for the period from the granting of the aid up to the end of 2003 amounts to DEM 923,82 million. Converted into euros this comes to EUR 472,34 million. As the LTS assets are still at NordLB's disposal, the amount of the aid element is continually increasing.

4. *COMPATIBILITY OF THE MEASURE WITH THE EC TREATY*

(171) It can therefore be stated that the transfer of the LTS promotion-related assets is caught by all the criteria laid down in Article 87(1) of the EC Treaty and thus involves state aid within the meaning of that Article. On this basis, an assessment must be made as to whether the aid can be considered compatible with the common market. However, it must be noted that Germany invoked only the exemption laid down in Article 86(2) of the EC Treaty in relation to any aid elements present in the transfer of the promotion-related assets.

(172) 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.

(173) 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 aspects, 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.

(174) Since the economic survival of NordLB was not at stake when the measure took place, there is no need to consider whether the collapse of a single large credit institution like NordLB 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.

(175) 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. NordLB is not described as an undertaking in difficulty whose viability must be restored with the support of state aid.

(176) Article 86(2) of the EC Treaty, which allows exemptions from the Treaty's state aid rules under certain conditions, is also applicable, in principle, to the financial services sector. This was confirmed by the Commission in its report on services of general economic interest in the banking sector [1].

[1] 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.

(177) Germany submits that, if the transfer of the LTS promotion-related assets did constitute favourable treatment for NordLB, it was no more than compensation for NordLB for the costs it incurred for carrying out its public mandate. It argues that NordLB is not only the *Land* bank but also a savings bank in the Braunschweig area. So it performs not only the traditional public role of a *Land* bank, with the attendant costs, but also the function of a savings bank.

(178) However, Germany has not quantified the costs to NordLB of the public tasks in question. On those grounds alone the Commission cannot allow an exemption from the application of Article 87(1) of the EC Treaty on the basis of Article 86(2). Moreover, it is clear that the transfer was made in order to enable NordLB to comply with the new own funds requirements, not as compensation for a public mandate carried out by NordLB.

(179) 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 common market.

5. *NO EXISTING AID*

(180) Contrary to the arguments put forward by Germany, the transfer of the LTS promotion-related assets cannot be regarded as being covered by the existing state aid scheme for *Anstaltslast* and *Gewährträgerhaftung*.

(181) *Gewährträgerhaftung* is a default guarantee offered to creditors in the event that the bank's assets are not sufficient to satisfy their claims, and this is not the case here. The capital injection is not intended to satisfy NordLB's creditors and the bank's assets have not been exhausted.

(182) Nor does *Anstaltslast* apply. *Anstaltslast* requires the guarantors (the *Land* of Schleswig-Holstein and NSGV) to provide NordLB with the resources it needs to function properly for as long as the *Land* decides to maintain it in existence. However, at the time of the capital injection, NordLB was far from being in a situation where it was no longer able to operate properly. The capital injection was not needed in order to keep NordLB in operation. Rather, it was made in order to enable the Landesbank to increase its capital in the light of the new capital requirements under the Solvency Directive so as to avoid an otherwise necessary reduction in its business volume and to enable it to expand in future. This conscious economic calculation by the *Land* as joint owner also enabled NordLB 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*. In the absence of another existing applicable 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.

VI. **CONCLUSION**

(183) The Commission finds that Germany has unlawfully implemented the new aid in question in breach of Article 88(3) of the EC Treaty.

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

HAS ADOPTED THIS DECISION:

Article 1

1. The difference between the appropriate remuneration of 6,76 % per annum (after corporation tax and before investor tax) and the remuneration of 0,5 % per annum (after corporation tax and before investor tax) agreed by Norddeutsche Landesbank — Girozentrale and the *Land* of Lower Saxony for the part of the transferred capital which Norddeutsche Landesbank — Girozentrale was able to use to underpin its competitive business as of 1 January 1992 constitutes aid which is incompatible with the common market.

2. The waiver of an appropriate remuneration amounting to 0,15 % per annum (after corporation tax and before investor tax) for the part of the capital transferred to Norddeutsche Landesbank — Girozentrale which could be used as a guarantee as from 1 January 1992 constitutes aid which is incompatible with the common market.

3. The amounts of aid referred to in paragraphs 1 and 2 total EUR 472,34 million for the period from 1 January 1992 to 31 December 2003 taken for the calculation.

Article 2

1. Germany shall discontinue the aid referred to in Article 1(1) and (2) by not later than 31 December 2004.

2. Germany shall take all necessary measures to recover from the beneficiary the aid referred to in Article 1(1) and (2) and unlawfully made available.

The aid to be recovered and specified in Article 1(1) and (2) comprises:

(a) the amount specified in Article 1(3) for the period from 1 January 1992 to 31 December 2003;

(b) an amount determined in accordance with the methods of calculation referred to in Article 1(1) and (2) for the period from 1 January 2004 to the time at which the aid is discontinued.

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 the Decision.

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

Interest shall be calculated in accordance with the provisions of Chapter V of Commission Regulation (EC) No 794/2004 [1].

Article 4

Germany shall, by means of the questionnaire annexed hereto, inform the Commission, within two months of notification of this Decision, of the measures taken to implement the Decision.

Article 5

This Decision is addressed to the Federal Republic of Germany.

Brussels, 20 October 2004.

For the Commission

Mario MONTI

Member of the Commission

[1] OJ L 140, 30.4.2004, p. 1.

ANNEX

INFORMATION REGARDING THE IMPLEMENTATION OF THE COMMISSION DECISION ON STATE AID MEASURE

1. **Calculation of the amount to be recovered**

1.1. Please provide the following details regarding the amount of unlawful state aid that has been put at the disposal of the recipient:

Date(s) of payment (°)	Amount of aid (*)	Currency	Identity of recipient

(°) Date or dates on which the aid or individual instalments of aid were put at the disposal of the recipient; if the measure consists of several instalments and reimbursements, use separate rows.
(*) Amount of aid put at the disposal of the recipient, in gross grant equivalent.

Comments:

1.2. Please explain in detail how the interest payable on the amount to be recovered will be calculated.

2. **Recovery measures planned or already taken**

2.1. Please describe in detail what measures have been taken and what measures are planned to bring about the immediate and effective recovery of the aid. Please also explain what alternative measures are available in national legislation to bring about the recovery of the aid. Where relevant, please indicate the legal basis for the measures taken or planned.

2.2. By what date will the recovery of the aid be completed?

3. **Recovery already effected**

3.1. Please provide the following details of aid that has been recovered from the recipient:

Date(s) (°)	Amount of aid repaid	Currency	Identity of recipient

(°) Date or dates on which the aid was repaid.

3.2. Please attach supporting documents for the repayments shown in the table at point 3.1.