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EU & UK Antitrust/Competition Legal Alert

EU State aid in the current financial crisis: repayment may be necessary

For financial institutions and corporations, particularly those active in acquiring businesses that have received State aid, great care must be taken to ensure that the full cost implications of the State aid are taken into account, because repayment of the aid -once the current crisis subsides- is a real possibility.

Amid the recent global financial turmoil, national governments intervened in several instances as private financial institutions found themselves in difficulty. Northern Rock, Bradford and Bingley (UK), Roskilde (Denmark), Fortis and Dexia (Belgium, the Netherlands and Luxembourg) IKB Deutsche Industriebank, SachsenLB, West LB and most recently Hypo Real Estate Holding (Germany) are some of the banks in the EU that benefited from State intervention that took the form of capital injections, loan guarantees and guarantees for retail deposits, or risk shields.

State intervention of this type is subject to review under EU State aid rules. In all the instances mentioned above, the respective Member States communicated to the Commission their intention to provide rescuing and, subsequently, restructuring aid to the failing companies in order to protect financial stability in their jurisdictions. The Commission, in turn, had to determine that these measures would not distort competition by granting an unfair advantage to the beneficiaries of the measures, at the expense of the remaining competitors in the market and that they would in the long-term restore the viability of the aid beneficiary.

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The situation in the banking sector has worsened rapidly in the last few weeks and because of the imperative need for Member States to act quickly and to be reassured that the measures they are considering would not infringe EU State aid rules, the Commission swiftly implemented an expedited process for rescue aid approvals. This temporary arrangement has considerably reduced the time required for the approval of a rescue aid package to a few days (or even to less than 24 hours in some instances) instead of the usual duration of a few weeks or months.

However, these decisions are not the end of the process. Under EU State aid rules, the granting of a rescue aid must be followed by a restructuring or a liquidation plan, which needs to be submitted at the latest within six months from the Commission's authorisation of the rescue aid. The restructuring plan needs to ensure that the beneficiary's long-term viability will be restored. The Commission will also examine whether or not aid measures lead to market inefficiencies in the longer term. The decision of the Commission on the restructuring plan may take several months.

If the Member State and the beneficiary of the State aid do not ensure that this process is followed, then the aid will be deemed unlawful automatically and the Commission can require the State to recover the State aid. The implications of such a decision are clearly significant.

Considering that the impact of the global crisis could also lead to other banks in need to resort to State help, and that several of the rescued banks will most likely merge or be acquired by other players in the market, it is of pivotal importance to ensure that EU State aid rules are respected in the process. Moreover, a bank, financial institution or corporation that has not benefited from State aid, but is finding trading conditions difficult because of the market behaviour of the beneficiary of State aid, could be the first to step forward to complain to the Commission that its ability to compete has been prejudiced because of the aid package. The Commission can open an investigation, and may order the termination or the recovery of the aid, the reduction of the size of the aid or other measures that would restore competition to the market. Such a decision can occur many months or even years after the State aid was granted.

The Commission announced on Tuesday 7 October 2008 that it intends to complement the existing guidelines in relation to aid for rescuing and restructuring firms in difficulty, with specific guidance in relation to bank recapitalisation and guarantee schemes. This initiative is intended to provide clarity and legal certainty in relation to aid in the financial sector, and ensure that aid granted meets the criteria for lawfulness.

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