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Subject: State aid SA.38562 (2014/N) - Ireland Transfer of the last tranches (from tranches 3 to 9) of assets to NAMA

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**Subject: State aid SA.38562 (2014/N) - Ireland
Transfer of the last tranches (from tranches 3 to 9) of assets to NAMA**

Sir,

I. PROCEDURE

- (1) On 26 February 2010, the Commission took a no objection decision on the Irish asset relief scheme for banks in Ireland ("the NAMA decision"¹).
- (2) On 3 August 2010, the Commission took a no objection decision on the transfer of a first tranche of impaired assets from the participating institutions to the National Asset Management Agency ("NAMA")².
- (3) On 29 November 2010, the Commission took a no objection decision on the transfer of the second tranche of assets from the participating institutions to NAMA³.

¹ Commission Decision in case N725/2009, *Establishment of a National Asset Management Agency (NAMA): Asset relief scheme for banks in Ireland*, OJ C 94, 14.04.2010, p. 10.

² Commission Decision in case N331/2010, *Transfer of the first tranche of assets to NAMA*, OJ C 37, 5.02.2011, p. 3.

³ Commission Decision in case N529/2010, *Transfer of the second tranche of assets to NAMA*, OJ C 40, 9.02.2011, p. 6.

Mr. Charles FLANAGAN, T.D.
Minister for Foreign Affairs,
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80, St. Stephen's Green,
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- (4) The transfer of the last tranches (i.e. tranches 3 to 9) of assets to NAMA was completed in March 2012.
- (5) On 4 April 2014, the Irish authorities notified to the Commission the transfer of those last tranches of assets to NAMA.
- (6) Between April and July 2014, several discussions and exchanges of information took place between the Commission and the Irish authorities.

II. DESCRIPTION OF THE MEASURE

1. Introduction

- (7) NAMA was established on 22 December 2009 to arrange and supervise the purchase of land, development property and associated commercial loans from five financial institutions in Ireland. The purchase price is paid through the issuance by NAMA of State-guaranteed senior debt securities for 95% of the purchase price and the issuance of (non State-guaranteed) subordinated debt securities for 5%. The issued securities are held by the participating credit institutions pro rata to their share in the real economic value ("REV") of assets transferred to NAMA. The State-guaranteed debt securities may then be used by the participating credit institutions as collateral to receive financing from the financial markets, and if necessary, from the European Central Bank, helping to improve the liquidity position of those banks.
- (8) Assets are transferred by "impaired borrower" exposures across all participating institutions, i.e. (i) Anglo Irish Bank ("Anglo"), (ii) Allied Irish Banks ("AIB"), (iii) Bank of Ireland ("BOI"), (iv) Irish National Building Society ("INBS") and (v) Educational Building Society ("EBS").
- (9) The Irish authorities committed to notify to the Commission each transfer of a tranche of assets to NAMA.
- (10) As mentioned in the NAMA decision⁴, the Commission was given a commitment from the Irish authorities to claw back any payment in excess of the REV of the assets that becomes apparent after the review by the Commission of the individual notifications related to the transfer of each tranche of assets.

2. Portfolio description of the last tranches of assets transferred to NAMA⁵

- (11) Two kinds of assets were transferred to NAMA, (i) loans and (ii) a portfolio of associated derivatives.
- (12) The total balance of loans transferred in the last tranches amounts to EUR 46 958 million⁶. The split by participating institution is the following: (i) Anglo: EUR 18 263 million (38,9% of total); (ii) AIB: EUR 14 367 million (30,6% of total); (iii) BOI:

⁴ See recital (122) of the NAMA decision.

⁵ More details are available in the Annex.

⁶ That amount corresponds to the loan balance as of the date of the transfer, using for foreign currency balances exchange rates two business days prior to the transfer date.

EUR 6 126 million (13% of total); (iv) INBS: EUR 7 479 million (15,9% of total); (v) EBS: EUR 723 million (1,5% of total).

- (13) The aggregate market value of the loans amounts to EUR 15 681 million, which corresponds to 33,4% of the total balance⁷ of the loans. The REV of the loans amounts to EUR 18 919 million, which corresponds to 40,3% of the total balance⁸ of the loans.
- (14) The market value of the underlying properties amounts to EUR 19 556 million, while the REV of the properties amounts to EUR 20 884 million, suggesting an average uplift of 6,8% above the market value.
- (15) In terms of asset class, the split of properties⁹ is the following: (i) investment property (44,64%); (ii) hotels (8,10%); (iii) land (including development property less than 30% completed) (25,26%); (iv) residential property for resale (16,15%); and (v) development property (at least 30% completed) (5,85%).
- (16) In terms of geography, the split of properties¹⁰ is the following: (i) Ireland (50,74%); (ii) Britain and Channel Islands (31,94%); (iii) Northern Ireland (5,71%); (iv) US and Canada (1,64%); (v) Rest of Europe (9,97%).
- (17) As well as the loans, a portfolio of derivatives associated with the loans was also transferred to NAMA at a market value¹¹ of EUR 76 million.
- (18) In total, the transfer price of assets (including both loans and derivatives) amounts to EUR 18 995 million. The difference between the transfer price and the market value, i.e. the aid amount, represents EUR 3 239 million, which can be broken-down between participating institutions as follows: (i) Anglo: EUR 1 132 million; (ii) AIB: EUR 872 million; (iii) BOI: EUR 544 million; (iv) INBS: EUR 638 million; (v) EBS: EUR 52 million. The total market value of the assets transferred amounts to EUR 15 757 millions.

3. Payment by NAMA for the last tranches

- (19) As payment for the assets received by NAMA under the last tranches, NAMA has issued debt instruments (bonds) to the participating institutions.
- (20) Total bonds issued by NAMA amounted to EUR 18 995 million, of which EUR 18 045 million (95%) consisted of State-guaranteed bonds and EUR 950 million (5%) consisted of (non State-guaranteed) subordinated bonds.

4. Losses incurred by each participating institution

- (21) Total losses¹² that each of the participating institutions made following the transfer of loans to NAMA are as follows: (i) Anglo: EUR 11 448 million; (ii) AIB: EUR 8 707

⁷ Or outstanding nominal amount.

⁸ Or outstanding nominal amount.

⁹ Expressed in % of the market value of the properties.

¹⁰ Expressed in % of the market value of the properties.

¹¹ See the Annex for more details.

¹² Losses are calculated as the difference between the loan balances and the transfer price paid by NAMA.

million; (iii) BOI: EUR 2 949 million; (iv) INBS: EUR 4 491 million; (v) EBS: EUR 444 million. In total, losses amount to EUR 28 039 million.

5. Certification of the valuation

- (22) The valuation process for the loans has been certified by independent experts (Ernst & Young for the Financial Regulator and KPMG for NAMA), and validated by the relevant supervisory authority, the Financial Regulator.
- (23) The loan valuers have also certified the valuation of the underlying properties.
- (24) Regarding the transfer of some assets of tranche 9 to NAMA, the report of the external Audit Co-Ordinator to the NAMA, KPMG, includes a mention of an exception to the usual procedures. In order to expedite the transfer of certain loans by a participating institution special arrangement were agreed and put in place. The total nominal value of those loans amounted to EUR 758 million and the total consideration paid was EUR 264 million, which implied a final discount of 65,17%.

III. THE POSITION OF IRELAND

- (25) The Irish authorities acknowledge that the notified transfer of assets under the Irish asset relief scheme may contain elements of State aid.
- (26) However, the Irish authorities consider the conditions and criteria of the transfer are in line with the scheme.

IV. ASSESSMENT

1. State aid character of the measure

- (27) As set out in Article 107(1) of the Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.
- (28) As described in the NAMA decision, the asset relief scheme (and, *de facto*, any measure falling under that scheme) constitutes aid to the participating institutions pursuant to Article 107(1) of the Treaty.

2. Compatibility

Applicability of Article 107(3)(b) of the Treaty

- (29) Article 107 (3)(b) of the Treaty enables the Commission to declare aid compatible with the internal market if it has the effect "to remedy a serious disturbance in the economy of a Member State".
- (30) Despite a slow economic recovery which was observed since 2013, the Commission still considers that the requirements for State aid to be approved pursuant to Article 107(3)(b) of the Treaty continue to be fulfilled in view of the persisting stress in financial markets. In July 2013 the Commission confirmed that view by adopting the Communication on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis (the "2013 Banking Communication")¹³.
- (31) As described in the NAMA decision, the Commission finds that the asset relief scheme and, *de facto*, any measure falling under this scheme are apt to remedy a serious disturbance in the Irish economy.

Framework for evaluating compatibility

- (32) As explained in the 2013 Banking Communication, in order for an aid or aid scheme to be compatible under Article 107(3)(b) of the Treaty, it must comply with the general criteria for compatibility under Article 107(3) of the Treaty. That requirement implies that the measure has to be appropriate, necessary and proportionate.
- (33) More specifically, asset relief measures, irrespective of their exact nature, need to be assessed under the Impaired Assets Communication¹⁴ (IAC) which provides guidance for the methodologies concerning the valuation of the impaired assets, the necessary remuneration of the State for the asset relief provided and the procedural steps that are to be followed, as well as the criteria that will be used to evaluate the State aid given to the banks as a result.

3. Assessment

- (34) The IAC sets out criteria for the compatibility of such measures with the internal market. These criteria comprise (i) the appropriate identification of the problem and disclosure, (ii) the appropriateness of the remuneration and burden-sharing, (iii) the alignment of banks' incentives with public policy objectives, (iv) the eligibility of assets, (v) the valuation of eligible assets, (vi) the management of assets subject to relief measures and (vii) the requirement of the assessment of a restructuring plan by the Commission.

¹³ OJ C 216, 30.7.2013, p. 1 (see in particular point 6).

¹⁴ Commission Communication on the Treatment of Impaired Assets in the Community Banking Sector, OJ C 72, 26.3.2009, p. 1.

Transparency and ex-ante disclosure

- (35) The IAC requires that any bank participating in an asset relief scheme should (i) provide full ex-ante transparency and disclosure of impairments on the assets to be covered by the scheme (including the additional impairment and/or losses to be taken as a result of the participation to the scheme) and (ii) follow-up on any application to the scheme by a full review of that bank's activities and balance sheet with a view to assessing the bank's capital adequacy and its prospect for a return to future viability.
- (36) The Commission views positively that the incurred losses for the participating institutions from the asset transfer were identified in advance of the asset transfer (see recital (21)) and that the valuation process for the eligible bank assets was certified by recognised independent experts and validated by the relevant supervisory authority, the Financial Regulator (see recital (22)). The property valuation outcome per se was certified by each independent loan valuer who provided a certificate to the audit coordinator (see recital (23)).
- (37) As for the full review of the banks' activities and balance sheet, the Commission notes that the Irish authorities have complied with their commitment to submit a restructuring plan for each participating institution.

Burden-sharing and remuneration

- (38) The principle of burden-sharing as set out in the IAC requires that banks ought to bear the losses associated with impaired assets to the maximum extent. Therefore, the assets should be transferred at a price that matches or stays below the real economic value. In this respect, the Commission notes that the assets were transferred at a price equal to the REV for loans and at a price equal to the market value for derivatives, i.e. a total transfer price of EUR 18 995 million, leading to total losses of EUR 28 039 million for the participating banks, which represents a significant burden-sharing.
- (39) The IAC also explains that burden-sharing is achieved through an adequate remuneration of the scheme. In that respect, the Commission recalls that, in compliance with the NAMA decision, the remuneration of the State is embedded in the purchase price as a 170 basis point margin is added to the Irish government bond yield for the relevant maturity used to discount the assets' expected long-term cash flows. The Commission concluded in the NAMA decision that the margin added to the risk-free rate is a reasonable estimate for the remuneration of the unexpected losses that a market operator would have required for similar assets under normalised market circumstances¹⁵.
- (40) Consequently, the Commission considers that the measure provides an appropriate framework for adequate burden-sharing of the costs of the measure between the State and participating institutions.

¹⁵ See recitals (102) and (118) of the NAMA decision.

Alignment of banks' incentives with public policy objectives

- (41) The Commission already concluded in the NAMA decision that the scheme included adequate provisions to align participating banks' incentives with public policy interests.

Eligibility of assets

- (42) The Commission already concluded in the NAMA decision that the scope of assets included in the NAMA scheme was in line with the eligibility requirements of the IAC.

Valuation of eligible assets

- (43) The Commission already concluded in the NAMA decision that the valuation methodology used to value the assets was in compliance with the requirements of the IAC. The Commission notes that the valuation process for the loans has been certified by independent experts on behalf of the Financial Regulator and on behalf of NAMA, and validated by the relevant supervisory authority, the Financial Regulator (see recital (22)). The property valuation outcome per se was certified by each independent loan valuer who provided a certificate to the audit coordinator (see recital (23)).
- (44) With the exception of those assets mentioned in recital (24), the Commission recognizes that the methodology used to value and transfer the assets of tranches 3 to 9 to NAMA, is that agreed in the NAMA decision¹⁶ and that has also been implemented for the previous transfers of assets to NAMA. The final total discount for the assets transferred amounts to 60%.
- (45) As for those assets transferred to NAMA mentioned in recital (24) the average discount amounts to 65,17%. Although the procedures applied to the transfer of the latter group of loans was not exactly the same as the ones applied to all the other transfers of assets to NAMA, that fact does not substantially modify the Commission's assessment since it only affects 1,6% of the nominal value of all the loans transferred and 1,4% of the total remuneration for all assets of tranches 3 to 9, and since the average discount applied to those loans is in line with the one applied to the rest of the loans transferred from that participating credit institution.

Management of assets

- (46) The Commission already concluded in the NAMA decision that the management of assets was in compliance with the requirements of the IAC.

Follow-up (restructuring plan)

- (47) The Commission notes that the Irish authorities have complied with their commitment to submit a restructuring plan for all participating institutions.

¹⁶ Recitals (113) to (121) of the NAMA decision.

V. DECISION

The Commission concludes that, in line with the Commission Decision in State aid case N725/2009, the application of the Irish asset relief scheme in the transfer of the last tranches (i.e. tranches 3 to 9) of assets from certain financial institutions in Ireland to NAMA constitutes State aid within the meaning of Article 107(1) of the Treaty.

Since the transfer fulfils the requirements of Article 107(3)(b) of the Treaty in general and the conditions and criteria set forth in that Commission decision in particular, it is compatible with the internal market and the Commission raises no objections.

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State Aid Greffe
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Fax No: +32-2-296 12 42

Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President

ANNEX

1. Tranches 3-9 portfolio statistics

<i>In EUR million</i>	AIB	Anglo	BOI	EBS	INBS	Total
Loans						
Loan balance retranslated* (a)	14.367	18.263	6.126	723	7.479	46.958
Loan CMV** (Market value) (b)	4.788	5.683	2.633	227	2.350	15.681
Loan LEV*** (Real economic value; total payment) (c)	5.660	6.815	3.177	279,3	2.988	18.919
Average discount (d)/(a)-1	-61%	-63%	-48%	-61%	-60%	-60%
Aid amount (c) - (b)	872	1.132	544	52	638	3.239
CMV** of property	5.972	6.862	3.199	291	3.233	19.556
LEV*** of property	6.354	7.310	3.437	311	3.472	20.884
Property average uplift	6,40%	6,53%	7,44%	6,87%	7,39%	6,79%
Derivatives						
Market and transfer value of derivatives (e)	4	51	21	0	0	76
Transfer price of derivatives (f)	4	51	21	0	0	76
Aid amount (f) - (e)	0	0	0	0	0	0
Total						
Total transfer price (d) + (f)	5.664	6.866	3.198	279	2.988	18.995
Total aid amount	872	1.132	544	52,3	638	3.239

*The loan balance retranslated is the foreign currency balances translated at exchange rates 2 business days prior to transfer.

** CMV - Current Market Value

*** LEV - Long term Economic Value

2. Split by type of property of the market value of the properties

<i>In EUR millions</i>	Amount (€m)	% of Total
Land (including development property <30% complete)	4.940	25,26%
Residential property for resale	3.159	16,15%
Investment property	8.731	44,64%
Hotels	1.583	8,10%
Development property (>30 %complete)	1.144	5,85%
Total	19.557	100,00%

3. Split by geography of the market value of the properties

<i>In EUR millions</i>	Amount (€m)	% of Total
Ireland	9.923	50,74%
Northern Ireland	1.117	5,71%
Britain and Channel Islands	6.246	31,94%
USA/Canada	321	1,64%
Rest of Europe	1.949	9,97%
Total	19.557	100,0%