Commission Decision of 20 September 2011 on State aid granted by Germany to HSH Nordbank AG SA.29338 (C 29/09 (ex N 264/09)) (notified under document C(2011) 6483) (Only the German text is authentic) (Text with EEA relevance) (2012/477/EU)

COMMISSION DECISION

of 20 September 2011

on State aid granted by Germany to HSH Nordbank AG SA.29338 (C 29/09 (ex N 264/09))

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(Text with EEA relevance)

(2012/477/EU)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union, and in particular the first subparagraph of Article 108(2) thereof,

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

Having called on Member States and other interested parties to submit their comments pursuant to those provisions[(1)],

Whereas:

1. PROCEDURE

(1) On 30 April 2009 Germany notified the Commission of state aid measures for HSH Nordbank AG (hereinafter 'HSH') in the form of a guarantee comprising a EUR 10 billion second-loss tranche (hereinafter 'the risk shield') and a EUR 3 billion capital injection (hereinafter 'the recapitalisation'). The measures had been provided indirectly by the public-sector owners of HSH, namely the Free and Hanseatic City of Hamburg and the *Land* of Schleswig-Holstein (hereinafter referred to separately as 'Hamburg' and 'Schleswig-Holstein' respectively, or together as 'the public-sector owners').

(2) By Decision of 29 May 2009 in case N 264/09[(2)] (hereinafter 'the Rescue Decision'), the Commission authorised the recapitalisation and the risk shield for HSH for a period of six months, as rescue measures compatible with the internal market on the basis of Article 107(3)(b) of the Treaty on the Functioning of the European Union (TFEU)[(3)]. In the Decision the

Commission required the German authorities to submit a restructuring plan within three months.

(3) On 1 September 2009 Germany notified a restructuring plan to the Commission.

(4) On 22 October 2009 the Commission adopted a Decision initiating the procedure under Article 108(2) TFEU with regard to the risk shield and the valuation of HSH in the context of the recapitalisation (hereinafter the 'Decision initiating the procedure')[(4)].

(5) On 21 November 2009 the Decision initiating the procedure was published in the *Official Journal of the European Union*[(5)] and interested parties were requested to submit their comments within two weeks from the publication date.

(6) On 30 November and 11 December 2009 the Commission received comments from Sparkassen- und Giroverband für Schleswig-Holstein and from Schleswig-Holsteinische Sparkassen-Vermögensverwaltungs- und Beteiligungs GmbH & Co. KG (hereinafter referred to separately as 'SGVSH' and 'SVB' respectively, or together as 'the savings bank associations').

(7) On 3 December 2009 a group of investors advised by J.C. Flowers & Co. LLC (hereinafter 'Flowers') requested an extension of the deadline to submit comments, which was granted by the Commission on 7 December 2009. The Commission received their comments on 17 December 2009.

(8) On 1 December 2009 Germany requested an extension of the deadline to submit comments, which was granted by the Commission on 7 December 2009. On 7 December 2009, HSH also requested an extension of the deadline to submit comments, which was granted by the Commission on 17 December 2009. On 17 December 2009, Germany forwarded joint comments from the public-sector owners and HSH on the Decision initiating the procedure.

(9) On 2 December 2009 a meeting took place between Flowers, the savings bank associations, the German authorities and the Commission.

(10) On 21 December 2009 the Commission sent Germany the non-confidential versions of the comments submitted by interested parties and requested Germany to comment within one month.

(11) On 18 January 2010 Germany forwarded the response made by the public-sector owners to the comments by Flowers and the savings bank associations.

(12) As regards the risk shield, and in particular the valuation of the portfolio of assets whose risk was covered by the risk shield ('the shielded portfolio'), several meetings, teleconferences and other information exchanges between the German authorities and the Commission took place between September 2009 and February 2010. The German authorities submitted additional

information, inter alia, on 6, 20, 21, 22, 23 and 29 October, 11, 12, 16 and 27 November and 17 December 2009, 26 and 27 January and 19 February 2010.

(13) The restructuring plan, risk shield and recapitalisation, and the valuation of the shielded portfolio were discussed by the German authorities and the Commission departments in a series of meetings, teleconferences and other information exchanges in the period between October 2009 and June 2011, including on 5, 21 and 27 October, 4, 12, 13, 18, 27 and 30 November, 7, 9, 14 and 15 December 2009, 14 and 19 January, 21 April, 5, 12, 20, 26, 28 and 31 May, 15 June, 13, 16, 22 and 23 July, 30 September, 22 November, 9 and 22 December 2010, 23 and 28 February, 18 March, 1 and 8 April, 25 May and 7, 16 and 29 June 2011. The final version of the restructuring plan was submitted on 11 July 2011.

(14) On 5 September 2011 Germany submitted the list of commitments that is attached in Annex I to this Decision.

2. DESCRIPTION OF THE BENEFICIARY

HSH Nordbank AG

(15) The HSH group is the fifth-largest German Landesbank, with head offices in Hamburg and Kiel. It is a public limited company (*Aktiengesellschaft*), established on 2 June 2003 as the result of the merger between Hamburgische Landesbank and Landesbank Schleswig-Holstein. In October 2006, Flowers[(6)] acquired 24,1 % of HSH shares (26,6 % of voting rights) from WestLB, with a view to an initial public offering (IPO) of HSH in 2008.

(16) On 31 December 2008 HSH had a balance sheet total of EUR 208 billion and risk-weighted assets (‘RWA’) of EUR 112 billion.

(17) After the implementation of the measures approved by the Commission in the Rescue Decision on 29 May 2009, the ownership structure of HSH was as follows: Hamburg 10,89 %; Schleswig-Holstein 10,42 %; HSH Finanzfonds AöR, a public-law institution established and controlled in equal shares by Hamburg and Schleswig-Holstein, 64,18 %; SGVSH 4,73 %; SVB 0,58 %; and Flowers 9,19 %[(7)].

(18) HSH is a commercial bank, its core region is northern Germany and its main focus is on merchant and private banking. The merchant banking activities are concentrated on shipping, corporate banking, transportation, real estate and renewable energy projects. HSH is the world’s largest provider of ship finance and has a significant market share in aviation financing (part of its transportation business unit). As at December 2008 HSH was present in 21 major financial centres in Europe, Asia and America.

(19) HSH is one of the German public banks which until 18 July 2005 benefited from the unlimited State guarantees *Anstaltslast* and *Gewährträgerhaftung*[(8)].

(20) In the beginning of the 1990s asset and capital transfers of EUR 523 million took place that favoured HSH's predecessor institutes, Hamburgische Landesbank and Landesbank Schleswig-Holstein. On 20 October 2004 the Commission decided that those transfers were incompatible state aid and had to be recovered[(9)]. HSH had to repay its public-sector owners a total amount of EUR 756 million, including interest. It did so in two instalments, on 31 December 2004 and 3 January 2005.

(21) In order to compensate for the capital outflow, the shareholders increased HSH's capital by EUR 556 million on 20 July 2005[(10)]. The capital increase was provided from own funds in combination with so-called partial payments. As a result of this mechanism the ownership structure changed only slightly. On 6 September 2005 the Commission decided that the capital increase was in line with the market investor principle, and thus did not constitute state aid[(11)].

(22) In mid-July 2008, HSH's shareholders decided to increase its capital base with a view to financing its growth. The capital measures had a volume of nearly EUR 2 billion, and around EUR 1,26 billion of that figure was fresh funds.

(23) The first part of the capital measures consisted of a conversion into ordinary shares of all silent participations (*stille Beteiligungen*) totalling EUR 685 million[(12)], and preference shares, totalling EUR 57 million, held by the public-sector owners. At the time of the conversion, Flowers signed a cash equity issue in order to avoid a dilution of their shareholdings[(13)]. As a result, HSH received an additional EUR 300 million or thereabouts.

(24) As a second part of the capital measures the owners made a new convertible silent capital contribution, totalling EUR 962 million. The public and private shareholders participated in the silent partnership in line with the ratio of their shareholdings (public EUR 660 million, private EUR 240 million). An additional EUR 62 million was taken over by the private shareholders. With effect from 31 December 2010, these silent partnerships were converted into ordinary shares.

(25) Germany informed the Commission about the capital measures described in recitals 21 to 23. The Commission considered the investments by the public-sector shareholders to be in conformity with the market economy investor principle, because a private investor participated significantly in the transaction on the same conditions as the public-sector shareholders. On 1 August 2008 the Commission informed Germany that it would not pursue the issue.

(26) In the period 1999-2009, HSH registered cumulated losses of EUR 1,85 billion and paid cumulated dividends of EUR 354 million to its public-sector owners. In the same period the public-sector owners recapitalised HSH with EUR [4-5][(14)] billion of new capital and guaranteed liabilities of up to EUR 166 billion.

TABLE 1

HSH financial track record for public-sector owners 1999–2009[a]

Business year	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Profit and Loss (EUR million)[b]	111	110	204	239	261	127	400	460	270	-3 195	-838
Cumulated Profit and loss (EUR million)	111	221	425	664	925	1 052	1 452	1 912	2 182	-1 013	-1 851
Dividend payments to public-sector owners (EUR million)					36	44	72	96	105	0	0
Cumulated dividend payments to public-sector owners (EUR million)					36	80	153	248	354	354	354
New capital injection by owners (EUR							[300-600]	0	0	[700-1 400]	3 000

a Before 2 June 2003 (date of merger), cumulated data for Hamburgische Landesbank and Landesbank Schleswig-Holstein.

b 1999-2006 figures local GAAP, 2007-2009 IFRS.

million) according to local GAAP											
Cumulated capital injection by public-sector owners (EUR million)							[300-600]	[300-600]	[300-600]	[1 000-2 000]	[4 000-5 000]
Risk shield — guarantee (EUR billion)											10
Guaranteed liabilities (EUR billion), of which			162	166	152	144	161	88	78	75	73
Gewährträgerhaftung (EUR billion)			*162*	*166*	*152*	*144*	*161*	*88*	*78*	*65*	*56*
SoFFin guarantees (EUR billion)			*0*	*0*	*0*	*0*	*0*	*0*	*0*	*10*	*17*

a Before 2 June 2003 (date of merger), cumulated data for Hamburgische Landesbank and Landesbank Schleswig-Holstein.

b 1999-2006 figures local GAAP, 2007-2009 IFRS.

(27) Historically HSH has been rated in the AA range by all three major rating agencies[(15)]. The long-term rating has reflected the unlimited state guarantees provided by HSH's public-sector owners. The assumption of future support from the public-sector owners remains a significant factor in HSH's credit rating, which includes a rating uplift[(16)] of 7 notches by Fitch. Moody's assigns

in total 7 notches support uplift, of which one notch is for the support provided by the public-sector owners (regional support).

(28) The C stand-alone rating (for Moody's 'Bank Financial Strength Rating', or 'BFSR')[17] reflected the rating agencies' view that HSH possessed adequate financial strength with a limited but valuable business franchise. According to Moody's BFSR methodology, banks rated at C display either acceptable financial fundamentals within a predictable and stable environment or good financial fundamentals within a less predictable and stable operating environment.

(29) In July 2004 Fitch started to provide a rating for HSH's non-guaranteed obligations in an A range, keeping its stand-alone rating at C. Moody's and S&P followed with ratings for non-guaranteed obligations in July 2005. Until the beginning of the crisis in 2008, the ratings of HSH remained stable.

(30) Since October 2008, two trends can be observed in the ratings of HSH. The first trend started in October 2008 when HSH's stand-alone ratings were successively downgraded to the lower D and higher E range by Fitch and Moody's (E being the lowest possible BFSR rating by Moody's)[18]. As reasons for the downgrading the agencies referred to (a) the significant risk stemming from HSH's cyclical asset base and in particular the shipping assets; (b) HSH's limited access to capital while running a highly capital-intensive lending business; and (c) HSH's weak and low profitability compared to pre-crisis levels due to lower asset yields, relatively higher risk-provisioning levels in asset-based finance and significantly increased funding costs compared to the pre-crisis environment. Furthermore, the agencies raised fundamental concerns about HSH's business profile. Because HSH does not have access to retail customers to any significant extent, the bank will continue to rely on the wholesale markets where it will have difficulties securing funding. Compliance with more stringent regulatory requirements on capitalisation, liquidity buffers, and funding mismatches would be a particular challenge for pure wholesale banks like HSH.

(31) The second trend started in May 2009, when S&P downgraded HSH's credit rating to BBB+, followed by Moody's and Fitch downgrading HSH to A3/A- in May and July 2010. As justification for the downgrading the rating agencies pointed to the limit on further support by the public-sector owners due to (a) the EU state aid rules and (b) their budgetary restrictions. The extent of the past support measures represented a high burden on the public-sector owners' financial strength so that they would be less inclined to offer further support. An important aspect in assessing the public-sector owners' further availability to offer support measures was the large amount of grandfathered debt[19] that then remained on HSH's balance sheet.

The events leading up to the rescue measures

(32) Already in 2007 the impact of the financial crisis led to EUR 1,3 billion of loss-provisioning in HSH's USD 30 billion structured credit portfolio (CIP)[20]. The contagion effect on the real economy adversely affected the traditional loan portfolio and had a severe impact on the quality of HSH's claims related to its shipping, transportation, real estate and renewable energy project financing. Additional loss-provisioning of EUR 1,6 billion on the CIP and loan loss provisions of EUR 1,9 billion on the loan portfolio significantly contributed to the negative result of EUR 3,2 billion in 2008.

(33) The bankruptcy of Lehman Brothers in September 2008 also intensified the refinancing difficulties of HSH, so that it applied for EUR 30 billion liquidity guarantees with the Sonderfonds Finanzmarktstabilisierung (German Fund for Stabilising the Financial Markets, hereinafter 'SoFFin').

(34) On 29 April 2009, the Bundesanstalt für Finanzdienstleistungsaufsicht (German Banking Regulator, hereinafter 'BaFin') informed HSH that, in light of its prudential situation, BaFin considered that HSH had difficulties meeting the regulatory capital requirements. BaFin announced that it would order a moratorium pursuant to paragraph 47 of the German Banking Act if the owners of HSH did not reinforce its capital basis.

(35) On 6 May 2009, S&P downgraded HSH's credit rating by two notches from A to BBB + with a negative outlook.

3. THE AID MEASURES

(36) In May and June 2009 HSH obtained aid of two kinds from Schleswig-Holstein and Hamburg: the EUR 3 billion recapitalisation and a EUR 10 billion second-loss guarantee measure (the 'risk shield'). In addition HSH received aid from SoFFin in the form of liquidity guarantees which in the end amounted to EUR 17 billion (hereinafter 'liquidity guarantees').

3.1. *THE RECAPITALISATION*

(37) The recapitalisation consisted of a cash injection of EUR 3 billion in total of core Tier 1 capital in exchange for ordinary shares with voting rights. The shares were issued by HSH and fully subscribed by HSH Finanzfonds AöR. The latter is an institution under public law established, owned and controlled by Hamburg and Schleswig-Holstein in equal shares.

(38) HSH Finanzfonds AöR obtained the financial means needed for the recapitalisation by issuing bonds on the capital markets. Its liabilities resulting from the bond issues are guaranteed equally by Hamburg and Schleswig-Holstein as partial debtors and by means of guarantees to the bond holders. The bonds issued by HSH Finanzfonds AöR serve solely to finance the HSH recapitalisation. HSH Finanzfonds AöR operates exclusively as a vehicle for Hamburg and Schleswig-Holstein and does not pursue any other purpose besides providing the recapitalisation and the risk shield.

(39) The issue price of the new shares was based on a valuation of HSH by PricewaterhouseCoopers (‘PwC’), which arrived at a value in a range between EUR [> 2] billion and EUR [< 3] billion (EUR [> 19] to EUR [< 28] per share). The average value of HSH based on the valuation is EUR [2-3] billion (EUR [19-28] per share). The valuation was established before the rating downgrade of HSH of 6 May 2009. The impact of the downgrading on the value of HSH was not taken into account in the valuation, but was considered during the pricing discussion. The valuation was based on the assumption that an upgrade to the previous A rating would be achieved in 2013.

(40) For the EUR 3 billion in newly injected capital Hamburg and Schleswig-Holstein intended to achieve a yearly remuneration of 10 % (EUR 300 million per year). Given that HSH’s business plan did not project sufficient profits for the period 2009-2012 to pay a 10 % dividend on all ordinary shares, the issue price of the new ordinary shares was reduced by a discounted 10 % dividend payment for the period 2009-2012. The present value of the 10 % dividend payment for the period 2009-2012 amounts to EUR [650-800] million (EUR [3-6] per share). The price for the new shares was fixed at EUR 19 per share (EUR [19-28] minus EUR [3-6]). HSH Finanzfonds AöR acquired 157 894 737 new ordinary shares.

(41) The savings bank associations and Flowers did not participate in the recapitalisation. Consequently, following the recapitalisation, their shareholdings were diluted from 13,20 %, 1,62 % and 25,67 % to 4,73 %, 0,58 % and 9,19 % respectively, and the joint direct and indirect shareholdings of Hamburg and Schleswig-Holstein (including the shares held via HSH Finanzfonds AöR) increased from 59,51 % to 85,49 %.

3.2. *THE RISK SHIELD*

(42) The risk shield was put in place at the same time as the recapitalisation in June 2009. It was also provided directly by HSH Finanzfonds AöR. Neither the savings bank associations nor Flowers participated. The risk shield consists of a second-loss guarantee in the amount of EUR 10 billion, which shelters HSH from losses stemming from total assets of about EUR 172 billion (EUR 187 billion exposure at default) as of a cut-off date in March 2009. The first-loss tranche of EUR 3,2 billion is to be covered by HSH. The second-loss tranche of up to EUR 10 billion is to be covered by HSH Finanzfonds AöR. Losses beyond EUR 13,2 billion (first- and second-loss tranches together) are to be covered by HSH. The transfer value of the shielded portfolio is [around EUR 168] billion ([around EUR 172] billion total assets value minus EUR 3,2 billion).

(43) In principle, HSH can cancel the guarantee at any time, but until 31 December 2013 the cancellation is limited to EUR [2-5] billion in total and at most to EUR [1-4] billion per year. HSH cancelled EUR 1 billion of the guarantee as of 9 March 2011. On 18 June and again on 6 September 2011, HSH cancelled

another EUR 1 billion of the guarantee, thus reducing the remaining guarantee to EUR 7 billion. BaFin was informed of the cancellations. BaFin indicated that it would not object to the termination.

Composition of the shielded portfolio

(44) Impaired assets such as assets-backed securities ('ABS') represent around [3-6] % of the approximately EUR [172] billion portfolio covered by the risk shield. The majority of the shielded assets consist of customer loans, HSH's core activity. The shielded portfolio is denominated in various currencies including EUR, USD and GBP.

TABLE 2

Breakdown of the shielded EUR [172] billion approximately of assets

Category of assets	**Assets on balance sheet(in EUR billion)**	**% of the portfolio**
Customer loans	[115 approx]	[…]
Fixed income securities	[30 approx]	[…]
Secured tradable loans[a]	[15 approx]	[…]
Assets-backed securities	[10 approx]	[…]
Guarantees on payments	[5 approx]	[…]
Total	[172 approx]	100,0

a Specific German financial products (*Schuldscheindarlehen*).

Valuation of the shielded assets

(45) HSH did not have a valuation of the whole portfolio conducted by external experts before the implementation of the risk shield, except for the ABS portfolio and part of the CIP portfolio, which were valued by Blackrock and by Cambridge Place. At the Commission's request, HSH conducted a valuation of the shielded portfolio in the period November 2009 to January 2010 based on the Commission's severe stress assumptions. The valuation was conducted in cooperation with the Commission's experts. The valuation assumptions were in line with the severe stress scenarios applied by the Commission in other cases. The valuation was based on the in-depth analysis of a sample of 40 deals representing a notional amount of EUR 1 billion, i.e. 0,6 % of the total exposure, and a tranche valuation on a large representative part of the portfolio using Moody's CDOROM[(21)] tool. The underlying assumptions were discussed with the Commission's experts. HSH was assisted by its external expert Morgan Stanley, who confirmed the technical accuracy of the calculations. The capital relief effect of the risk shield at the time of its implementation was determined to be [around EUR 3,5] billion. The accuracy

of the method and the underlying calculations used to determine the capital relief effect was confirmed by BaFin in February 2010.

Remuneration of the risk shield

(46) According to the contract on the provision of a guarantee concluded between HSH Finanzfonds AöR and HSH on 2 June 2009, HSH Finanzfonds AöR receives a premium for providing the second-loss guarantee in the amount of 400 bps p.a. on the nominal amount of the guarantee (EUR 10 billion) (hereinafter the 'basic premium'). Drawings and cancellations reduce the amount on which the remuneration of 400 bps is paid. Table 3 below represents the total amount of the cumulative payment in three scenarios: (a) Scenario 1: HSH's base case, which assumes that the guarantee will not be drawn and will be fully cancelled by HSH by the end of 2015; (b) Scenario 2: an intermediate scenario, which assumes a drawing of the guarantee to the tune of EUR 5 billion; and (c) Scenario 3: the underlying case of the assets' valuation, which assumes that the guarantee will be fully drawn by [2015-2020] (no cancellations).

TABLE 3

Remuneration of risk shield as proposed by Germany in different scenarios

(In EUR million)

	Scenario 1(EUR 0 drawing of guarantee)	**Scenario 2(EUR 5 billion drawing of guarantee)**	**Scenario 3(EUR 10 billion drawing of guarantee)**
Basic premium (400 bps on outstanding nominal amount of the guarantee)	[> 1,5]	[> 2,5]	[> 4]

(47) Over the restructuring period the payments of the basic premium would represent between EUR [100-150] million and EUR 405 million per year depending on the drawing of the guarantee as described in Table 4 below.

TABLE 4

Projected basic premium (400 bps) payment of HSH to HSH Finanzfonds AöR in EUR million over the restructuring period

(In EUR million)

	2009 actual	**2010 actual**	**2011**	**2012**	**2013**	**2014**

Scenario 1 (EUR 0 drawing)	-300	-405	– [300-350]	– [200-250]	– [150-200]	– [100-150]
Scenario 2 (EUR 5 billion drawing)	-300	-405	– [300-350]	– [200-250]	– [180-230]	– [150-200]
Scenario 3 (EUR 10 billion drawing)	-300	-405	– [300-400]	– [300-400]	– [300-400]	– [300-400]

3.3. *LIQUIDITY GUARANTEES*

(48) Additionally, HSH had applied for SoFFin guarantees covering new issuances of debt up to an amount of EUR 30 billion. SoFFin approved the issuance of a first tranche of EUR 10 billion at the beginning of December 2008. The guarantees were approved within the framework of the German rescue scheme[22]. The remaining EUR 20 billion were to be activated after the submission of a restructuring plan. The second tranche of EUR 20 billion was activated after submission of the restructuring plan by HSH to SoFFin on 7 March 2009. As of 30 September 2009, a total of EUR 17 billion had been drawn. As of 1 January 2010, SoFFin reduced the guarantee limit from EUR 30 to EUR 17 million. The limit was not extended again.

4. THE RESTRUCTURING PLAN

4.1. *INITIAL RESTRUCTURING PLAN AND SUBSEQUENT REVISION OF THE FINANCIAL PROJECTIONS*

(49) The initial restructuring plan submitted on 1 September 2009 (hereinafter ‘the initial restructuring plan’) was described in the Decision initiating the procedure (recitals 23 to 28). Additional information on the restructuring model contained in the initial restructuring plan was provided in subsequent submissions during the period from October 2009 to June 2011. The modified version of the restructuring plan was submitted on 11 July 2011 (hereinafter ‘modified restructuring plan’). The financial projections contained in the initial restructuring plan with the related updates are briefly described below.

(50) The initial restructuring plan projected a decrease of [around 20 %] in the net interest income for the period 2009 to 2014, from EUR [1,4] billion approximately to EUR [1,1] billion approximately. In respect of the components of the financial results, HSH projected an increase in net income before restructuring (and after loan loss provisions) for the core bank[23]

of more than 200 % between 2009 and 2014, from approximately EUR [350] million to approximately EUR [1,1] billion. The projected net income before restructuring of approximately EUR [1,1] billion in 2014 included a positive effect of approximately EUR [100] million from reversing loan loss provisions. The net fee income and the trading result each represented [some 20 %] of the net income before restructuring costs of the core bank in 2014. In the modified restructuring plan the projected net income before restructuring for 2014 was revised to EUR [350-450] million, with net fee income and trading result representing [10-15] %.

(51) The initial restructuring plan projected a total asset reduction for HSH from approximately EUR [175] billion in 2009 to approximately EUR [150] billion in 2014. The initial restructuring plan projected an increase in the assets of the core bank from approximately EUR [100] billion in 2009 to approximately EUR [110] billion in 2014. The 2014 projected total assets for HSH and for the core bank were revised to EUR 120 billion and EUR 82 billion respectively in the modified restructuring plan.

(52) According to the initial restructuring plan the segment assets of the sector bank comprising shipping, energy and transport were projected to increase from around EUR [30] billion in 2009 to around EUR [35] billion in 2014, of which some EUR [20] billion would be mainly US dollar-financed shipping assets. In the modified restructuring plan the projected segment assets of the sector bank and the shipping assets in 2014 were revised to EUR [20-25] billion and EUR 15 billion respectively. As compared with the initial restructuring plan the aviation business line was discontinued in the modified restructuring plan.

(53) The projected Tier 1 capital ratio in the initial restructuring plan was [around 10] % in 2014 and was revised to a projected level of [10-15] % in the modified restructuring plan.

(54) In the initial restructuring plan the bank provided a breakdown per projected source of funding for some EUR [100] billion in 2014 of funded balance sheet (of which [around EUR 25 billion] of unsecured wholesale funding), leaving a gap of some EUR [50] billion as against the projected total assets of EUR around [150] billion. In the modified restructuring plan, the gap between the projected total assets and the projected total liabilities was reduced and HSH provided information on sources of funding to be used to cover the funding needs resulting from the gap.

(55) The growth assumptions in the main segments of activity of HSH as presented in the initial restructuring plan and the assumptions adjusted in the modified restructuring plan are presented in the table below.

TABLE 5

Comparison growth rates shipping and corporate

Segment	Initial restructuring plan(1 September 2009)	Modified restructuring plan(11 July 2011)	Comment on growth assumption in modified restructuring plan
Shipping	Growth rate of new business around [250] % from 2010 IST - 2014 (some [40] % CAGR)	Growth rate of new business [90-130] % from 2010 IST - 2014 ([…] % CAGR)	The growth rate is based on an annual absolute volume of new business of EUR […] billion on average from 2011 to 2014. It compares to a total market volume of around EUR [25] billion of new business on average over the period
Corporate	Growth in loan volume [around 100] % (2010 IST – 2014)	Growth in loan volume […] % (2010 IST – 2014)	That growth corresponds to an absolute volume amount of new business of EUR […] billion over four years and compares to total assets in that segment of EUR 25,7 billion as of 31 December 2008

4.2. *GENERAL DESCRIPTION OF THE MODIFIED RESTRUCTURING PLAN*

(56) The modified restructuring plan was submitted on 11 July 2011. It comprises substantial changes to HSH's business model. The new business model is characterised by reduced risk, a stronger focus on regional business, and sustainability on the funding and lending sides. The planned and already initiated restructuring measures include, besides the focus on core business activities and consequently the divestment or cessation of various activities and major holdings, the adaptation of the branch network and optimisation of the cost structure. The modified restructuring plan includes the establishment of an internal restructuring unit in which activities that will not be continued

will be concentrated for accounting and organisational purposes. The key points of the new business model are:

(a) a reorientation towards a viable core bank by way of a substantial assets reduction, a strengthening of regional business (corporates in Germany, real estate business in Germany and private banking) and the retention of core competencies in selected international business activities with a strong regional connection (shipping and renewable energies, with a focus on Europe);

(b) the exclusive focusing of the capital market business on treasury activities and customer-related business, especially in the role of a supplier of products to other business units (cross-selling); proprietary trading has been discontinued;

(c) the cessation of activities that are not in line with the strategic refocusing of HSH, i.e. the international Leverage Buy Out (LBO) business, foreign real estate business, asset-based aircraft financing and other credit business without a clear connection to the core competency;

(d) the divestment of all subsidiaries that are not in line with the strategic refocusing of HSH; the modified restructuring plan entails the divestment of [100-120] holdings in total; HSH has already reduced the number of holdings by 25; all sales are expected to happen by […] at the latest;

(e) a clear separation of the discontinued businesses to be reduced or sold in the internal restructuring unit; the restructuring unit will not engage in any new business;

(f) a significant adaptation of the national and international branches. The run-off of non-strategic activities will result in the closure of 15 out of 21 international branches. The branches or representation offices in Helsinki, Shanghai, Mumbai, Stockholm, Naples, Oslo, Riga, Tallinn, Warsaw, San Francisco and Hanoi have already been closed. The branches or representations in Copenhagen, Paris, Amsterdam and Moscow are to be closed by 2012. After the restructuring period HSH will keep six branches or representations in London, Hong Kong, New York, Singapore, Luxembourg and Athens. However, the branches in London, Luxembourg and New York will be reduced and the branch in Hong Kong transformed into a representative office.

(57) The regional focus comprises in particular the northern German corporate business and private banking, the real estate business and the savings bank business. In addition, HSH will concentrate on selected areas of international ship financing as well as on project financing in renewable energy with a focus on Europe as well as certain investments in infrastructure. HSH will close the office in Lübeck by the end of 2011.

(58) Overall, the balance sheet total of the new core bank will be reduced substantially, in particular through transfer of assets from the core bank to the internal RU. At the end of the restructuring period on 31 December 2014 HSH

(core bank) will have a balance sheet total of EUR 82 billion. Compared to the balance sheet total of EUR 208 billion in 2008, this amounts to a reduction of EUR 126 billion, i.e. almost 61 %.

(59) The modified restructuring plan is based on general assumptions about the evolution of the German, euro area, US and global GDP, short-term and long-term interest rates changes, euro area and US inflation, oil prices and the EUR/USD exchange rate. The projections of the individual business units are based on assumptions about the growth rates of the relevant market, volumes and margins on new production per segment and cross-selling capacity. Given the importance of the shipping unit in the overall financial results of HSH, HSH has provided sector-specific assumptions on the evolution of the shipping market. The projections on the evolution of the size of the market in terms of global new business (aggregated for the bulk, container and tanker segments), the size of the new business of HSH and the market share of HSH are presented in the table below.

TABLE 6

Assumptions on ship financing 2011–2014

	Average 2005–2008	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
Total global new business shipping (in EUR billion)	109,4	25,9	48,3	[10-15]	[15-25]	[25-35]	[40-50]
New business HSH (in EUR billion)	6,7	0,2	1	[0,5-1,5]	[0,5-1,5]	[1-2]	[2-3]
Market share HSH (%)	6,1	0,8	2,1	About [4]	About [5]	About [5]	About [5]

(60) HSH is assuming an average EUR/USD exchange rate of [1,30-1,50]. It has provided sensitivity data on the impact of changes in the assumptions on profit and loss and its net liquidity position, and in particular a sensitivity analysis for

changes in the interest rates and for changes in the EUR/USD exchange rate. The outcome of the sensitivity analysis is that HSH would not suffer losses beyond what it can absorb in the event of significant differences in interest rates and EUR/USD exchange rate assumptions. Moreover, HSH's liquidity position would not be negative if the EUR/USD exchange rate were to vary considerably compared to the base case assumption.

(61) HSH furthermore provided an adverse and worst case scenario for the group based on less favourable market assumptions. The financial projections in the adverse and worst case scenario show that the impact of stress on the solvency of HSH is buffered through the structure of the risk shield. In an adverse scenario HSH would delay the partial cancellations of the guarantee and thus limit the RWA increase due to the negative economic environment. In both scenarios, the resulting Tier 1 capital ratio of HSH would remain at around 10 % during the restructuring period.

4.3. *DESCRIPTION OF THE RESTRUCTURING OF THE INDIVIDUAL BUSINESS UNITS OF HSH*

Corporates

(62) The balance sheet total of the core bank's corporates business unit will be reduced from EUR 26,3 billion in 2008 to EUR [10-20] billion in 2014. In total, the unit will be reduced by about [45-55] % during that period.

(63) In the corporates business unit HSH will offer financing to larger medium-sized undertakings, most notably in the core region of northern Germany.

(64) HSH has ceased its activities in the refinancing of leasing companies and the international LBO business and will discontinue its relationship-driven business with corporate customers in Asia and Scandinavia. The corporates business unit will not provide asset-based financing of aircraft or ships. However, the ability of HSH to support regional business in the core region will not be curtailed.

(65) HSH will focus primarily on larger medium-sized businesses in the region of northern Germany as well as German companies within defined core industries. It will have a clear focus on profitable business as well as on customers with a good credit standing and a demand for multiple products. HSH will strive to achieve 'first' bank status with those customers.

(66) To support the funding situation the business unit will increasingly aim to acquire deposits and to use financing structures that enable syndications, are eligible as ECB collateral or can be passed on to investors.

Real estate

(67) The balance sheet of the core bank's real estate business unit will be reduced from EUR 30,5 billion in 2008 to EUR [9-18] billion in 2014. This amounts to a reduction of [50-70] %.

(68) HSH will offer all types of loan products and any other bank products that are relevant for real estate companies. The bank will focus on business in northern Germany and in German metropolitan regions. The main emphasis will be put on financing solutions for […] and project financing with a manageable degree of risk. In the real-estate line of business, HSH will concentrate on the financing of […]. Special property classes will be financed only selectively.

(69) Activities in other countries – including the international real-estate business, which consists of supporting German clients in European metropolitan regions – will be discontinued. In these areas, HSH will not carry out any new business and the existing business will expire.

(70) HSH will focus mainly on professional real estate investors with a focus on existing clients and on selected real estate developers and customers with a sustainable real-estate track record and a high potential for cross-selling, as well as customers connected to northern Germany with a need for complex financing structures. HSH will continue to use structures and products that reduce the funding need, e.g. business eligible for covered bonds, ECB-eligible loans, or funding and sureties provided by the Kreditanstalt für Wiederaufbau (KfW).

Savings banks

(71) The balance sheet of the core bank's savings banks business unit will be reduced from EUR 8,7 billion in 2008 to EUR [< 3] billion in 2014, in particular by reducing refinancing activities for savings banks.

(72) This business unit's customer base is composed primarily of savings banks and public-sector customers in northern Germany and secondarily of savings banks and public-sector customers outside northern Germany (secondary bank relationship).

(73) HSH provides a large range of products which focus on the core business areas of savings banks. This includes in particular the private and corporate customers business, treasury business, own securities management and credit portfolio management.

Private banking

(74) In the private banking business unit the core bank's balance sheet total will be reduced from EUR 1,7 billion (in 2008) to EUR [0,5-1,5] billion (in 2014).

(75) HSH will focus on providing services to wealthy private customers in the core region of northern Germany. In addition, it will offer private banking services at supra-regional distribution branches belonging to the other market segments. The range of services is to include […].

(76) HSH will concentrate on the acquisition and support of wealthy and very wealthy private customers as well as foundations. As part of cross-selling,

private banking services will also be provided to customers/natural persons of the other business units of the core bank.

Shipping

(77) In the shipping business unit the balance sheet will be reduced from a balance sheet total in 2008 of EUR 28,3 billion to about EUR 15 billion in the core bank in 2014, i.e. a reduction of 46 %.

(78) Until 31 December 2014 the market share of HSH in relation to new business in global ship financing will not exceed [< 8] % on an annual basis. In addition, HSH will ensure that up to 31 December 2014 it will not be among the top three ship-financing providers with the highest annual volume of new business worldwide, according to the market rankings determined on an annual basis.

(79) HSH's portfolio will be diversified both in relation to ship types and countries. In relation to asset classes an emphasis will remain on […] as well as several […]. Conventional long-term mortgage loans for new constructions and financing of second-hand ships will be important products. Furthermore, HSH will selectively operate as a supplier of structured financial services.

(80) HSH will reduce its business activities by ceasing to finance roll-on/roll-off and cruise ships as well as […].

(81) HSH will focus on medium-sized and larger worldwide shipping companies, small profitable customers and customers selected by reference to their overall revenue potential and aspects of risk. Furthermore, the readiness of the customer regarding syndications will be considered, as well as the fulfilment of syndication (e.g. transparency) and refinancing requirements.

(82) The shipping business unit will mainly offer plain vanilla[(24)] and, to a limited extent, structural financing and will act as a mandated lead arranger and bookrunner.

Transport/Aviation

(83) The transport/aviation business unit of the core bank will cease to exist. The EUR 11,7 billion balance sheet (in 2008) will expire within the restructuring unit or be assigned to other business units. In the future, HSH will not carry out any new asset-based financing of aircraft. The corresponding existing business will expire, be sold or be transferred to the restructuring unit for the purpose of reduction. As a part of the restructuring, HSH has already partially redesigned the business unit and assigned the divisions of rail and infrastructure, which are still strategically relevant, to the energy and infrastructure business unit.

Energy and infrastructure

(84) Due to the realignment of the energy and infrastructure business unit in the course of the restructuring process, the balance sheet total of the energy and infrastructure unit in the core bank in 2014 will be increased from EUR 4,6 billion in 2008 (which refers to the former energy business unit) to EUR

[5-10] billion. The energy and infrastructure business unit includes both the renewable energy segment and the infrastructure and rail segments, which had previously been assigned to the transport business unit.

(85) In the energy segment, HSH will act as a provider of project financing in the areas of wind and solar energy projects. They include the asset categories of wind (on- and offshore), solar (photovoltaic and thermal) and, as a supplementary business, networks in conjunction with wind and solar projects. The target region for those activities is mainly Europe. HSH's business relating to conventional energy sources and the entire North American energy business will be discontinued.

Miscellaneous

(86) The adjustments in the business units, in particular the cessation of the aviation business unit and the reduction in the international real estate and the shipping segments, will automatically lead to a reduction of the 'miscellaneous segment'.

(87) The 'miscellaneous segment' includes – besides the corporate centre – the capital markets business, in which HSH manages its treasury and which serves as a supplier of products for the business units.

(88) HSH will continuously improve the stability and quality of its funding. Starting from the end of 2012, it will ensure that its net stable funding ratio (NSFR) and its liquidity coverage ratio (LCR)[(25)] […]. The share of the core bank's USD business that is refinanced by means of USD-denominated funding (and not through swaps) will increase to at least […] % by the end of 2012 and to at least […] % by the end of 2014.

(89) HSH will consistently reduce capital market business with a high risk potential and has already reduced its product catalogue significantly. Proprietary trading has already been discontinued.

4.4. *DESCRIPTION OF THE FINANCIAL PLANNING IN THE MODIFIED RESTRUCTURING PLAN*

(90) HSH presented a detailed business plan for the period 2011 to 2014 including profit and loss calculations and balance sheet, profitability and production indicators broken down per business unit and consolidated for the group. HSH furthermore provided a sensitivity analysis in the form of an adverse and worst case scenario for the group. According to the profit and loss projections the HSH group will suffer an additional loss of around EUR [100-200] million in 2011 and continuously increase its profits to around EUR [400-500] million after tax in 2014. The return on equity will be negative in 2011 and increase to around [7-8] % in 2014. The Tier 1 ratio will reach around [13-16] % in the period 2012 to 2014. At the request of the Commission, the financial projections contained in the modified restructuring plan include a one-off payment of EUR 500 million in 2011 which has been deducted from net

income before tax. The total assets are projected to decrease from EUR 208 billion (in 2008) to EUR 120 billion (in 2014).

(91) The most important figures of the modified restructuring plan for HSH and the core bank are shown in the following tables.

TABLE 7

Financial planning HSH 2011–2014

	2008 actual	**2009 actual**	**2010 actual**	**2011 plan**	**2012 plan**	**2013 plan**	**2014 plan**
Total income (in EUR million)	157	2 876	1 603	[1 300-1 800]	[1 300-1 800]	[1 300-1 800]	[1 300-1 800]
Net income before restructuring expenses (in EUR million)	(2 796)	(718)	545	[500-1 000]	[500-1 000]	[500-1 000]	[500-1 000]
Net income before tax (in EUR million)	(2 968)	(1 325)	17	[– 200-300]	[0-500]	[100-600]	[200-700]
Net income (in EUR million)	(3 195)	(902)	48	[– 400-100]	[0-500]	[0-500]	[0-500]
Cost income ratio (CIR) (%)	573	29	54	[45-55]	[45-55]	[45-55]	[40-50]
Return on equity after tax	< 0	< 0	< 0	[– 5-+ 5]	[5-10]	[5-10]	[5-10]

(RoE) (%)							
Total assets (in EUR billion)	208	175	151	[130-150]	[125-145]	[120-140]	[115-135]

TABLE 8

Financial planning core bank 2011–2014

	2008 actual	**2009 actual**	**2010 actual**	**2011 plan**	**2012 plan**	**2013 plan**	**2014 plan**
Total income (in EUR million)	1 582	1 756	1 103	[750-1 250]	[750-1 250]	[750-1 250]	[750-1 250]
Net income before restructuring (in EUR million)	418	354	574	[300-600]	[300-600]	[300-600]	[300-600]
Net income before tax (in EUR million)	295	18	318	[200-500]	[200-500]	[200-500]	[200-500]
Cost income ratio (CIR) (%)	39	32	52	[40-60]	[40-60]	[40-60]	[40-60]
Segment assets (EUR billion)	113	97	88	[60-90]	[60-90]	[60-90]	82

(92) HSH’s funding plan in respect of the overall funding strategy and in respect of the USD funding strategy are shown in the following tables.

TABLE 9

HSH funding plan 2010–2014

(in EUR billion)

Volumes per funding channel	**2010 actual**	**2011**	**2012**	**2013**	**2014**
Covered bonds	[…]	[…]	[…]	[…]	[…]
State guaranteed long-term bonds	[…]	[…]	[…]	[…]	[…]
Senior unsecured long-term	[…]	[…]	[…]	[…]	[…]
Short-term wholesale funding	[…]	[…]	[…]	[…]	[…]
Wholesale funding other	[…]	[…]	[…]	[…]	[…]
Commercial and retail deposits (until 2010)/ Residual deposits (permanent average balances from 2011)	[…]	[…]	[…]	[…]	[…]
Development banks and commercial lending	[…]	[…]	[…]	[…]	[…]
Hybrids (Tier 1 and Tier 2)	[…]	[…]	[…]	[…]	[…]

Total	[…]	[…]	[…]	[…]	[…]
Derivatives	[…]	[…]	[…]	[…]	[…]
Total assets	[…]	[…]	[…]	[…]	[…]
Total assets – (total liabilities + derivatives) to be financed by short-term secured funding, excess deposits and equity		[…]	[…]	[…]	[…]

(93) The state-guaranteed long-term bonds will decrease from EUR 44 billion at the end of 2010 to EUR [13-18] billion at the end of 2014. At the same time HSH's total assets will decrease by EUR [25-35] billion. The difference between total assets and total liabilities (adjusted for the effect of derivatives) represents a gap in the funding plan which has to be covered by short-term unsecured and secured funding as well as an excess of deposits and equity. HSH's planning in respect of deposits factors in only a proportion of total deposits considered as stable (residual deposits (permanent average balances — *Bodensatz*) although the actual volume of deposits is expected to be higher and to cover a proportion of the funding gap. Although a proportion of the funding gap between funded assets and liabilities could be covered by short-term wholesale funding, HSH's reliance on short-term wholesale funding decreases in absolute terms over the restructuring period. In respect of the funding strategy in EUR, HSH will in relative terms rely more on covered bonds.

TABLE 10

Funding strategy in USD 2010–2014

(in USD billion)					
Volumes	**2010 actual**	**2011**	**2012**	**2013**	**2014**
USD denominated funding	[…]	[…]	[…]	[…]	[…]

USD funding through swaps	[…]	[…]	[…]	[…]	[…]
Total assets USD	[…]	[…]	[…]	[…]	[…]
Total assets USD shipping	[…]	[…]	[…]	[…]	[…]

(94) Whereas in 2010 HSH funded 75 % of its US dollar assets through cross currency swaps, the reliance on swaps will decrease to […] % of total US assets (including assets in the restructuring unit). The decreased reliance in relative terms on financing through swaps will be achieved through a decrease of US dollar denominated assets and therefore a decrease in the absolute amounts of US dollar funding.

(95) Over the year 2010, the saving banks provided EUR [2,5-3,5] billion of long-term unsecured funding for HSH and EUR [200-500] million of long-term secured funding. That total amount of EUR [2,7-4] billion compares to EUR [150-250] million of total funding provided by other Landesbanks and EUR [1-2] billion provided by other financial institutions (private and public other than saving banks and Landesbanks).

(96) The modified restructuring plan shows an increase in the capital positions and ratios of HSH over the restructuring period with a projected common equity ratio of [10-13] % at the end of 2014. At the request of the Commission HSH included in its financial projections an increase in share capital of EUR 500 million in 2013.

TABLE 11

HSH capital position 2009–2015

	2009 actual	**2010 actual**	**2011**	**2012**	**2013**	**2014**	**2015**
Risk-weighted assets after guarantee (EUR billion)	71	41	[40-60]	[40-60]	[45-65]	[50-70]	[50-70]
Guarantee outstanding	10	10	7,0	[< 7,0]	[< 7,0]	[< 5,0]	[< 5,0]

(EUR billion)							
Capital evolution (EUR billion)							
Common equity Tier I capital (EUR billion)	5,08	4,433	[4 000-6 000]	[4 500-6 500]	[5 000-7 000]	[5 500-7 500]	[6 000-8 000]
Tier I capital (EUR billion)	7,491	6,274	[5 000-7 000]	[5 500-7 500]	[6 000-8 000]	[6 500-8 500]	[7 000-9 000]
Total capital (EUR billion)	11,523	9,4	[8 000-12 000]	[8 000-12 000]	[8 000-12 000]	[8 000-12 000]	[8 000-12 000]
Capital ratios							
Common equity/ RWA (%)	7,1	10,7	[> 7,0]	[> 8,0]	[> 9,0]	[> 10,0]	[> 10,0]
Tier 1 capital/ RWA (%)	10,5	15,2	[> 10,0]	[> 10,0]	[> 10,0]	[> 10,0]	[> 10,0]

4.5. *COMMITMENTS MADE BY GERMANY*

(97) Germany has given an undertaking that HSH will implement the modified restructuring plan and has submitted the commitments set out in Annex I and III to this Decision.

4.6. *MONITORING*

(98) Germany has given an undertaking that a monitoring trustee will provide the Commission with detailed quarterly reports. The reports will in particular contain information on the remuneration of the impaired asset measure (in line with Annex V to the Communication from the Commission on the treatment of impaired assets in the Community banking sector, hereinafter the 'Impaired Assets Communication'[26]), and on the implementation of the

modified restructuring plan (in line with paragraph 46 of the Commission communication on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis, hereinafter the 'Restructuring Communication'[(27)]).

5. GROUNDS FOR INITIATING THE FORMAL INVESTIGATION PROCEDURE IN RESPECT OF THE AID MEASURES FOR HSH

(99) On 30 October 2009 the Commission opened the formal investigation procedure in order to verify whether the risk shield complied with the conditions of the Impaired Assets Communication regarding the definition of the eligible assets, the valuation (including the valuation methodology), the remuneration and the management of the impaired assets. Furthermore the Commission wanted to investigate the conditions of the recapitalisation measure, the burden sharing, and the measures to limit distortions of competition.

(100) Regarding the eligibility of the assets covered by the risk shield, the Commission expressed doubts (recital 40 of the Decision initiating the procedure) as to whether they met the eligibility criteria laid down in the Impaired Assets Communication, since only a small fraction of the shielded portfolio fell directly into the definition of impaired assets provided for in the Communication.

(101) Regarding transparency and disclosure, the Commission stated in recital 42 of the Decision initiating the procedure that HSH had provided valuation reports by independent experts which covered only a residual fraction of the shielded portfolio, namely a large proportion of the structured credit securities. Furthermore at that time Germany had not provided a validation of the valuation process and outcome by BaFin.

(102) Regarding asset management, the Commission expressed doubts in recital 44 of the Decision initiating the procedure as to whether HSH's planned arrangements fulfilled the requirements laid down in the Impaired Assets Communication, since all assets would remain on HSH's balance sheet.

(103) Regarding the valuation, the Commission stated in recital 46 of the Decision initiating the procedure that only the valuation of the structured credit portfolio had been carried out by independent experts, and that at the time the Commission did not have sufficient information for the assessment of the real economic value of the whole shielded portfolio. The Commission sought to verify the correlation assumptions used for the shielded assets.

(104) Regarding remuneration, in recital 49 of the Decision initiating the procedure the Commission expressed doubts about the adequacy of the burden sharing, as the Impaired Assets Communication would require HSH to contribute to the loss or risk coverage in the form of first-loss clauses (typically with a minimum of 10 %). In addition, in recital 51 et seq. of the Decision initiating

the procedure, the Commission expressed doubts that the fee of 400 bps adequately remunerated the risk taken by the public-sector owners.

(105) Regarding a return to viability, in recital 59 of the Decision initiating the procedure the Commission expressed doubts as to whether HSH would be able to restore its long-term viability. In particular, in view of HSH's strong reliance on wholesale funding, the Commission questioned whether the funding strategy presented would be sustainable on a stand-alone basis in the medium and longer term once public guarantees were phased out.

(106) In recitals 60 and 61 of the Decision initiating the procedure the Commission queried the underlying assumptions of the initial restructuring plan in regard to growth rates and asset margins. The Commission questioned in particular the increased margins in the private banking segment and the growth assumptions in the shipping and transport segments, where HSH already had proportionally high market shares.

(107) In recital 62 of the Decision initiating the procedure the Commission questioned HSH's plan to continue its international capital market activities at a significant level while declaring at the same time that it intended to refocus its business model towards regional activities. In recital 63 of the Decision initiating the procedure the Commission expressed scepticism as to whether it was realistic to assume that an upgrade to the previous A rating would be achieved in 2013.

(108) Regarding the recipient's own contribution, the Commission stated that no far-reaching proposals had been made in the initial restructuring plan. The scope of the own contribution in the form of divestments remained vague. As to the burden sharing of the minority shareholders, the Commission expressed doubts about the valuation of HSH and consequently the price of the newly issued shares. In recitals 10 and 32 of the Decision initiating the procedure, the Commission questioned whether the savings bank associations and Flowers, who had not participated in the recapitalisation, might not have benefited from the capital injection by maintaining excessively high shareholdings in HSH.

6. COMMENTS FROM GERMANY

(109) On 17 December 2009 Germany submitted joint comments by the public-sector owners and HSH on the Decision initiating the procedure.

6.1. *COMMENTS ON THE RISK SHIELD*

Impaired Assets Communication not applicable

(110) Germany took the view that the Commission's legal assessment of the risk shield was erroneous, because it was based on the application of the Impaired Assets Communication, which, according to Germany, was not applicable in the present case.

(111) Germany disagreed with the Commission's assessment that the Impaired Assets Communication had to be applied and that the Commission was obliged to apply laws and guidelines in force at the time of the adoption of the Decision, irrespective of the time at which the aid measures were designed or notified[28]. According to Germany, that view would be correct only if the assessed measure fell within the scope of application of the relevant legal provision or Communication, which was not the case here. Germany further argued that the Impaired Assets Communication could not be read as covering all kinds of support measures targeting impaired assets. The Impaired Assets Communication should be regarded as an administrative instruction only, designed solely to ensure consistent administrative practice and binding on the Commission alone. The compatibility of the risk shield with the internal market should be assessed directly under the TFEU. According to Germany, the fact that the objective of the second-loss guarantee and the composition of the shielded portfolio were outside the terms of the Impaired Assets Communication was evidence that the Communication was not applicable in the HSH case.

Aid element

(112) Germany stated that applying the Impaired Assets Communication led to an erroneous assessment framework, which was unfavourable to HSH as regards the aid element, the value of the portfolio, the remuneration of the measure and the scope of restructuring.

(113) Germany referred to recital 38 of the Decision initiating the procedure, where the Commission mentioned the difficulties in assessing the market value of the portfolio, which consisted mainly of loans to corporate customers. Germany regarded those difficulties as evidence that the second-loss guarantee should not be assessed under the Impaired Assets Communication. It pointed out that the Commission had by extrapolation arrived at an aid amount equal to the nominal value of the guarantee. Germany further argued that such an outcome was evidence that the chosen method must be wrong, since the Commission estimated the aid element of a guarantee as being the same as the aid element of a recapitalisation, although the two measures were different in nature. Whereas the recapitalisation was a permanent capital injection, the guarantee was only a regulatory stability measure limited to the maturity of the covered assets.

(114) Germany pointed out that the estimation of the aid element on the basis of the market value showed that the Commission had misunderstood the nature of the risk shield, which did not cover market fluctuations. Germany considered that the Commission should determine the aid element of the second-loss guarantee according to the general state aid rules and in particular the Commission Notice on the application of Article 87 and 88 of the EC Treaty to state aid in the form of guarantees[29] (hereinafter the 'Guarantees Notice'). According to Germany, in so far as it was recognised that the

remuneration for the risk shield was market-oriented, applying the Guarantees Notice would lead to a marginal aid element.

Application of the Impaired Assets Communication

(115) Even assuming it was correct to apply the Impaired Assets Communication, Germany took the view that the Commission had applied it erroneously as regards the quantification of the aid element and the remuneration, burden sharing and the management of assets by the restructuring unit. The aid element involved in the second-loss guarantee was incorrect because incorrect assumptions had been made in regard to the transfer and market value of the portfolio. As regards the remuneration of the capital relief effect, Germany pointed out that the estimation of the capital relief effect in the Decision initiating the procedure was based on old data. According to more recently submitted data, the capital relief effect would be significantly lower. The Commission's preliminary assessment of the burden sharing was incorrect and too limited, since the Commission referred only to the first-loss tranche of the guarantee, which was considerably below the 10 % of the shielded portfolio required by the Impaired Assets Communication. There was no link between the burden sharing and the first-loss tranche measured in absolute numbers. Furthermore HSH was to bear all losses going beyond the second-loss tranche. As regards the management of assets, the principles of the Impaired Assets Communication did not apply to the risk shield and it would be unreasonable to manage all shielded assets separately. HSH might create a restructuring unit and ensure a clear accounting and organisational division between the core bank and the restructuring unit up to management board level.

Portfolio valuation

(116) Germany disagreed with the asset valuation referred to in recital 47 of the Decision initiating the procedure. The shielded portfolio contained mostly customer loans, which were difficult to value in a cash flow-based valuation. Valuation methods which used flat-rate haircuts to simulate market uncertainties and which were designed for the valuation of 'complex' assets were inappropriate for the valuation of the shielded portfolio in the current case. Whereas the CIP portfolio had been valued by external experts on a cash-flow-based valuation method, the assets in the much larger credit portfolio had been valued by applying a standard credit analysis in line with the regulatory rules. The key point of such analysis was the creditworthiness of the borrower.

Remuneration of the guarantee

(117) Germany argued that it was inappropriate to apply to the second-loss guarantee the calculation methods laid down in the Impaired Assets Communication (as described in the Decision initiating the procedure) and concluded that the Guarantees Notice should be applied in order to determine the remuneration. In several meetings, teleconferences and other information exchanges between January and August 2010 Germany provided information

demonstrating that a full claw-back of the […] would impede HSH's capacity to restore viability.

6.2. *COMMENTS ON THE RECAPITALISATION*

(118) Germany took the view that the Commission's assessment of the recapitalisation measure was incorrect as regards the valuation of HSH and the legal assessment of the possible benefits to the minority shareholders who did not participate in the recapitalisation.

(119) The Commission's doubts about the valuation of HSH were based on incorrect facts. It was unimportant that the downgrading of HSH by S&P was not taken into account in the valuation conducted by PwC, and there were good reasons to believe that HSH would return to an A rating in 2013.

(120) As regards the issue price of the new shares, discounts in a range of 30 % to 60 % were usual for listed banks. The valuation of HSH was an appropriate basis for the setting of the price of the newly issued shares and the 'old' shareholders of HSH did not benefit from the aid measures by maintaining too high a share in HSH.

6.3. *COMMENTS ON THE RISK SHIELD AND THE RECAPITALISATION IN THE LIGHT OF THE UNLIMITED STATE GUARANTEE PROVIDED BY THE PUBLIC-SECTOR OWNERS (GEWÄHRTRÄGERHAFTUNG)*

(121) Germany argued that without the rescue measures HSH would have gone bankrupt and the public-sector owners would have been liable for much higher losses under the unlimited state guarantee *(Gewährträgerhaftung)*. The possible claims under *Gewährträgerhaftung* were estimated at around EUR 30 billion or higher. Germany pointed out that a private investor in the situation of the public-sector owners would have taken the same rescue measures to avoid higher losses.

(122) Germany took the view that the rescue measures met the private investor test and therefore did not constitute state aid. The private investor test was fulfilled if it could be reasonably argued that the company would return to viability and if the liquidation costs of the company were higher than the capital measures[30]. According to Germany, the initial restructuring plan submitted on 1 September 2009 was sufficient proof of the capacity of HSH to return to viability. As for the estimation of the liquidation costs, Germany stated that a distinction should be made between the obligations of the public-sector owners as HSH's owners and as public bodies. Their obligations as public bodies (unemployment benefit, social insurance contributions) could not be taken into account when estimating the liquidation costs. Only their obligations as HSH's owners were to be counted towards the liquidation costs. Germany cited the *Linde* judgment[31] to argue that liabilities originating from state aid that had already been properly granted had to be taken into account when conducting the private investor test. *Gewährträgerhaftung* was

approved by the Commission and was therefore compatible state aid. In addition, the liabilities covered by *Gewährträgerhaftung* pertained to the obligations of the *Länder* in their capacity as HSH's owners, not as public bodies. *Gewährträgerhaftung* was in its nature comparable to a 'letter of responsibility'*(Patronatserklärung)*. Therefore the liabilities of the public-sector owners under *Gewährträgerhaftung* amounting to at least EUR 30 billion, should be taken into account when estimating the liquidation costs. Finally, Germany concluded that the liquidation costs would be much higher than the capital measures provided to HSH by the public-sector owners. Therefore the conditions of the private investor test were fulfilled and the rescue measures did not constitute state aid.

6.4. *COMMENTS ON HSH'S VIABILITY*

(123) Although Germany initially viewed the Commission's preliminary assessment of HSH's business model as expressed in recital 62 of the Decision initiating the procedure as too negative, it subsequently updated HSH's initial restructuring plan in order to alleviate the Commission's concerns.

6.5. *COMMENTS ON OWN CONTRIBUTION AND COMPENSATORY MEASURES*

(124) Germany argued that the own contribution measures included in the initial restructuring plan, which consisted of the remuneration of the measures, the release of capital reserves, the sale of subsidiaries and cost reductions, added up to EUR 5,9 billion and should be sufficient.

(125) Moreover, while Germany initially considered the proposed compensatory measures, consisting of the balance sheet reduction, the cessation of profitable business portfolios, the closure of 12[32] out of 21 international locations and the sale of sizeable subsidiaries (REAG and DAL[33]), to be sufficient, it later reconsidered them in the modified restructuring plan.

7. COMMENTS FROM THIRD PARTIES

(126) The Commission also received comments from interested third parties. Comments were submitted on 30 November and 11 December 2009 by the savings bank associations and on 17 December 2009 by Flowers.

7.1. *COMMENTS FROM SGVSH AND SVB*

(127) The savings bank associations disagreed with the Commission's preliminary view that they had disproportionately benefited from the recapitalisation granted to HSH by the public-sector shareholders as they considered that the share price of the newly issued shares was rather low.

(128) Splitting the proceedings in the HSH case, with the aid measures being authorised in one set of proceedings and the issue of indirect aid to the minority shareholders being dealt with in another, would breach Article 7 of Regulation (EC) No 659/1999[34] ('the Procedural Regulation'). The aid

measure could not at the same time be compatible with the internal market in respect of HSH, and incompatible in respect of HSH's owners. A negative decision on the recapitalisation in respect of the savings bank associations and Flowers would render the recapitalisation incompatible aid. According to the savings bank associations, the Commission should address the issue of burden sharing by the minority shareholders in the general context of the burden sharing assessment of the recapitalisation.

(129) As regards the Commission's consideration that there was insufficient dilution of the minority shareholdings, the savings bank associations did not see how this could constitute state aid. They considered a dilution to be a secondary effect of a recapitalisation. Moreover, the conditions of Article 107(1) TFEU were not fulfilled, in so far as the savings bank associations were not an undertaking within the meaning of the state aid rules. SGVSH and SVB were not active on any market; they only held shareholdings on behalf of their members (the public savings banks in Hamburg and Schleswig-Holstein). The advantage to the savings banks could be seen only in the increase of the value of the HSH shares, which was inherent in all capital injections. Furthermore, the alleged advantage was not granted from state resources. The level of dilution depended on the number of the shares and the share price. The price was decided not by the State, but by the shareholders' meeting. That decision was not imputable to the State and, in line with the *Stardust Marine* judgment[(35)], could not be considered aid. In any event, the alleged advantage had no impact on the competitive position of the savings banks in the markets in which they operated. Therefore the alleged advantage did not distort competition or affect trade between Member States.

(130) The savings bank associations also pointed out that the Commission had not investigated secondary effects in other recapitalisation cases. Nor had the Union courts endorsed such an approach in the *WestLB* judgment[(36)]. Furthermore, the savings bank associations observed that the Commission had not investigated secondary effects in other cases where the issue price of the new shares appeared extremely high[(37)] and concluded that an investigation of the issue only in cases such as those of HSH and BayernLB would infringe the principle of equal treatment.

(131) The savings bank associations further explained that the shareholders in a public limited company *Aktiengesellschaft* had an option on new stock. It was, however, an option and not a purchase obligation. The savings bank associations considered the share price of the new shares appropriate but they were not able to participate in the recapitalisation for financial reasons.

(132) Furthermore, the savings bank associations argued that in 2008 they contributed significantly to capital measures in favour of HSH. In July 2008, the savings bank associations converted a silent participation in the amount of EUR 685 million into EUR 125 million equity and EUR 560 million capital reserves. In July 2008 the savings bank associations together with

Flowers subscribed to a mandatory convertible silent capital contribution (hybrid instrument) of EUR 962 million (of which the savings banks took EUR 660,5 million). At the end of 2008, HSH released capital reserves of EUR 3,1 billion in order to compensate the balance sheet loss and avoid the loss absorption of the hybrid instruments. In that context the savings bank associations lost their EUR 560 million of the capital reserves. The mandatory convertible silent capital contribution was loss-absorbing. A coupon on that instrument had not been paid. The savings bank associations had not received dividends since 2008.

(133) In May 2009, the savings bank associations had been willing to sell their shares. A sale had, however, not been possible owing to a 'holding agreement' which had been concluded with the public-sector owners on 25 March 2003. The parties to that holding agreement had undertaken to exercise their voting rights in a manner allowing the public-sector owners and the savings bank associations to maintain the majority voting rights and not to sell certain percentages of their shares. The holding agreement could not be terminated before 31 December 2013.

(134) The savings bank associations pointed out that in the course of the recapitalisation their shareholdings had been considerably diluted, from 13,2 % and 1,62 % to 4,7 % and 0,6 % respectively. With 85,5 % of direct and indirect shareholdings, the public-sector owners had joint control over all strategic decisions in HSH. From the point of view of a private investor that joint control meant an additional decrease of the value of the shares held by the minority shareholders.

(135) The savings bank associations noted that the valuation of HSH by PwC was commissioned by HSH and not by the minority shareholders. PwC conducted the valuation in line with recognised valuation principles. The savings bank associations argued that specific values and a modified risk premium should have been taken into account, which would have given a share price of EUR 30 per share. The savings bank associations concluded that their holdings had been excessively diluted and estimated the loss at around EUR 200 million.

7.2. *COMMENTS FROM FLOWERS*

(136) Flowers put forward similar arguments to those of the savings bank associations. In addition, they argued that they had already made a considerable contribution of their own to the restructuring of HSH. They noted in particular that the capital measures taken in favour of HSH in July 2008 were closely connected to the capital injection in May 2009. In July 2008 Flowers had brought in EUR 300 million in cash. As regards the mandatory convertible silent capital contribution in the amount of EUR 962 million, Flowers had subscribed EUR 301,5 million. The mandatory convertible silent capital contribution had participated in losses; a coupon had not been paid. The

investors provided 48 % of those capital measures, which went considerably beyond their shareholding of 25,67 % at the time.

(137) Flowers disagreed with the Commission's preliminary assessment, in recitals 65 and 73 of the Decision initiating the procedure, regarding an insufficient own contribution and lack of genuine burden sharing measures. In 2009, they had taken a participation of EUR 794 million in the capital reserves of EUR 3,1 billion released by HSH. They referred to the *Commerzbank*[(38)] decision, arguing that there the Commission had considered the sale of subsidiaries and other assets as sufficient own contribution, and a ban on coupons and dividend payment as burden sharing. The investors considered that the capital measures provided in 2008 should be taken into account.

(138) The investors contended that their loss of the blocking minority due to the dilution should also be considered as own contribution. Despite their dilution to 9,19 % they would still be liable under *Gewährträgerhaftung* in line with their shareholding before the recapitalisation, i.e. 26,85 %. The investors also disputed the Commission's doubts regarding the valuation of HSH and an excessive share price. They argued that a number of aspects that would increase the share value had not been sufficiently considered.

(139) Finally, the investors pointed out that German law did not provide for a transfer of shares, which would make a recovery of the indirect aid to the minority shareholders impossible. The investors considered that a split of the ongoing proceedings would not be possible, as there was only one aid measure granted in favour of HSH.

8. COMMENTS FROM GERMANY ON THIRD PARTIES' COMMENTS

(140) Germany submitted comments on the arguments by the savings bank associations and Flowers. Germany maintained its opinion that the valuation of HSH was appropriate and that the minority shareholders had not benefited from any indirect state aid. Moreover, Germany favoured a split of proceedings if it would accelerate the conclusion of the case, which was expected by HSH and the markets. Germany questioned whether a recapitalisation was a homogeneous legal act and had to be assessed in one decision. Germany referred to the case law of the Union courts and argued that a split of the proceedings would be legally possible and that differing legal assessments of one aid measure in relation to different beneficiaries, i.e. HSH and the minority shareholders, would not put at risk the compatibility of the aid measure in favour of HSH. The proportionality of the aid measure in relation to HSH could be ensured through a set of measures in the restructuring plan, whereas any advantage granted to the minority shareholders via an excessively high issue price would have to be treated and corrected differently. Germany disagreed with Flowers that German law did not provide for a transfer of shares and thus rendered recovery of the indirect aid to the minority shareholders impossible. Germany argued that such transfer was possible

under German law, and that even if it were not possible, Germany would not be able to cite a lack of means of enforcement to justify the non-implementation of a Commission recovery decision.

9. ASSESSMENT

9.1. *EXISTENCE OF STATE AID*

(141) According to Article 107(1) TFEU, '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'.

(142) The classification of a measure as state aid requires that the following conditions be met: (a) it must be financed by a Member State or through state resources; (b) it must grant an advantage liable to favour certain undertakings or the production of certain goods; (c) that advantage must be selective; and (d) the measure must distort or threaten to distort competition and have the potential to affect trade between Member States. Those conditions being cumulative, they must all be present before a measure is characterised as state aid. The Commission maintains its view that the conditions are met.

(143) First, the measures were granted by HSH Finanzfonds AöR. This is an institution governed by German public law that was established by the public-sector owners and is owned and controlled by them in equal shares. It was created on the basis of the State Agreement between the*Länder* of Hamburg and Schleswig-Holstein[39] signed on 3 April 2009 in Kiel and on 5 April 2009 in Hamburg. The object of HSH Finanzfonds AöR is the support of HSH on behalf of the public-sector owners. In order to fulfil its task, HSH Finanzfonds AöR is empowered to issue guarantees of up to EUR 10 billion, to acquire the shares of HSH and to obtain loans for such acquisitions. According to paragraph 3 of the State Agreement, the public-sector owners are responsible for the liabilities of HSH Finanzfonds AöR. The measures are thus clearly financed by the State.

(144) Second, the risk shield and the recapitalisation were put in place to avoid insolvency on the part of HSH[40] and consequently helped it to remain in business. Therefore, they constitute economic advantages within the meaning of Article 107(1) TFEU.

(145) Third, the measures are individually targeted at HSH, so they are selective.

(146) Lastly, to qualify as aid, the measures in question must distort or threaten to distort competition and have the potential to affect trade between Member States. Those effects can be assessed on the basis of the aid amount, the features of the aid measure and the aid beneficiary[41]. The aid measures allowed HSH to avoid insolvency and remain active in a number of markets. HSH is an internationally active bank, competing with other banks in

Germany and other countries. Furthermore, HSH is a bank of systemic importance for the banking system in Germany[(42)] and a major competitor in ship and aviation financing (HSH is the world's largest provider of ship finance and has a significant market share in aviation financing). Finally it has received a relatively high amount of aid (see below): in particular, the risk shield covers around 75 % of its balance sheet. Taking into account the effect of the measure, the position of HSH in the banking sector and in shipping financing in particular, and the aid amount, the advantage granted to HSH was liable to affect trade between Member States.

(147) That assessment is not altered by the comments from Germany and third parties. The comments by Germany on the aid nature of the measures in favour of HSH are contradictory. On the one hand, Germany argues that the Commission should assess the risk shield under the Guarantees Notice instead of the Impaired Assets Communication, which seems to assume that the risk shield constitutes state aid. On the other hand, as summarised in section 6.3 of this Decision, Germany argues that, in the light of the unlimited state guarantee *(Gewährträgerhaftung)* covering estimated claims of at least EUR 30 billion, a private investor in the position of the public-sector owners would also have taken the measures in question to rescue HSH in order to avoid higher losses. Germany contends on that basis that the private investor test is fulfilled, and that the measures in question are therefore not state aid.

(148) Germany has misinterpreted the case-law cited by it. In the case at hand Germany argues that one state aid measure (an unlimited state guarantee, *Gewährträgerhaftung*) should be treated as a liquidation cost in order to declare other state aid measures (the recapitalisation and risk shield) to be in line with the private investor principle. In *Linde* the parties concluded, on market terms, a transaction involving a subsidy in order to cancel a supply contract which had previously been concluded, and which was also on market terms, because the performance of that supply contract had subsequently given rise to significant annual losses. The General Court stated that '[t]he comprehensive arrangement represents a normal commercial transaction in the course of which the [*Treuhandanstalt*] and LWG behaved as rational operators in a market economy. It is evident that they were motivated primarily by commercial considerations and did not have regard to any economic or social policy objectives'[(43)]. That situation is not comparable with the case in hand, as in *Linde* both transactions were concluded on market terms, while here neither of the transactions was concluded on market terms.

(149) *Gewährträgerhaftung* is defined as a direct liability, based on statute or by-laws, on the part of a regional authority or an association under public law with respect to the creditors of a public-law credit institution for all of its obligations. *Gewährträgerhaftung* therefore obliges the guarantor ('*Gewährträger*') to intervene in the case of insolvency or liquidation of the credit institution. It creates direct claims by the creditors of the credit

institution against the guarantor, which can, however, only be called in if the assets of the credit institution are not sufficient to satisfy the creditors. *Gewährträgerhaftung* is unlimited in time and in amount. In addition, the credit institution pays no remuneration for the guarantee[(44)]. In summary, *Gewährträgerhaftung* constitutes an unremunerated unlimited subsidiary liability of a public corporate body (municipality or *Land*) for creditor claims against a public institution (public bank) where that institution is insolvent. A private investor in the situation of the public-sector owners would not have granted a bank an unlimited unremunerated guarantee covering the entire balance sheet of that bank as the public-sector owners did with *Gewährträgerhaftung*.

(150) The Commission has in fact considered *Gewährträgerhaftung* to be state aid. It has called for the abolition of *Gewährträgerhaftung* by Germany.

(151) *Gewährträgerhaftung* is anchored in public law. The public-sector owners are liable under that guarantee as public bodies and not as private owners. In line with the Commission's decision-making practice[(45)] and the case law[(46)], liquidation costs cover only liabilities that could have been paid by a private investor. As mentioned in recital 149, a private investor would not have granted a bank unlimited unremunerated guarantees covering its entire balance sheet. Therefore, the *Linde* judgment is of limited relevance for the assessment of the current case as the liabilities under *Gewährträgerhaftung* cannot be counted as liquidation costs.

Quantification of the aid amount

(152) The aid element of the recapitalisation should be the nominal value of that recapitalisation, as no private investor would have provided such funds to a firm in difficulty. As established in recitals 27 and 28 of the Rescue Decision, the non-participation of the minority shareholders in the recapitalisation and the disproportionate share of the burden of the rescue measures borne by the public-sector owners indicate that the recapitalisation was motivated by public policy objectives, and not by private investor considerations. In line with its case practice[(47)] the Commission confirms its view that the aid element in the recapitalisation amounts to EUR 3 billion.

(153) Moreover, the aid element of the risk shield is confirmed to be EUR 10 billion. Despite Germany's arguments, the Commission remains convinced that the measure must be assessed on the basis of the Impaired Assets Communication. In the Impaired Assets Communication, the Commission has provided guidance on the treatment under Article 107(3)(b) TFEU of asset relief measures adopted by Member States. Impaired assets correspond to categories of assets on which banks are likely to incur losses. The Commission considers that the Impaired Assets Communication must cover any kind of support measure targeting impaired assets and providing effective asset relief to the recipient institution because the Impaired Assets Communication defines asset relief as any measure whereby a bank is dispensed from the need

for severe downward value adjustments of certain asset classes[(48)]. The risk shield to HSH falls into that category of measure.

(154) The Commission does not agree with Germany that the Impaired Assets Communication is inapplicable and that the aid amount involved in the second-loss guarantee should be determined according to the general state aid rules and the Guarantees Notice in particular. The Guarantees Notice applies to aid measures that are designed to provide liquidity to a bank[(49)]. The risk shield serves another purpose. It is designed to be implemented on the asset side in order to free up as much capital as possible, so that the bank can improve its capital ratio.

(155) As regards the *ratione temporis* objection of Germany, the Commission would point out that it has to apply the law and guidelines in force at the time of the adoption of a decision, irrespective of the time at which the aid measures were designed or notified[(50)]. This is a general rule, and any departure from it has to be clearly mentioned in the legal act that would otherwise be applicable. The Union courts have confirmed that a notified measure should be assessed under the rules applicable at the date of the decision[(51)]. Consequently, in the context of the current financial crisis, the Commission has previously applied the Impaired Assets Communication to measures notified before its publication[(52)].

(156) According to the Impaired Assets Communication, the amount of aid in an asset relief measure corresponds to the difference between the transfer value of the assets and their market price. The transfer value of the shielded portfolio amounts to [approximately EUR 168] billion, which corresponds to the nominal value of the portfolio of approximately EUR [172] billion minus the first loss of EUR 3,2 billion (first-loss tranche).

(157) Given the significant size and the composition of the shielded portfolio ([60-80] % of the assets covered are loans to customers), the quantification of its market value is difficult. In the absence of a market, the market value may effectively be as low as zero for some assets[(53)]. In any case the market value of the shielded portfolio lies significantly below its real economic value (REV)[(54)], which reflects the underlying long-term economic value of the assets. Given that the aid amount involved in the guarantee cannot exceed its nominal value (EUR 10 billion) it is not necessary to determine the exact value. Therefore the Commission considers that the aid element involved in the risk shield is EUR 10 billion.

(158) Finally, the Commission would point out that the liquidity guarantees provided by Soffin for an amount of EUR 17 billion constitute aid granted under the German scheme.

(159) The Commission has come to the conclusion that the aid element in the risk shield and the recapitalisation amounts to EUR 13 billion. The Commission

further considers that the aid element in the liquidity guarantees is up to EUR 17 billion.

9.2. *COMPATIBILITY OF THE AID MEASURES*

9.2.1. APPLICATION OF ARTICLE 107(3)(B) TFEU

(160) In accordance with Article 107(3)(b) TFEU, aid can be found compatible with the internal market if it serves to 'remedy a serious disturbance in the economy of a Member State'. The Commission acknowledged in its approval of the German bank rescue scheme[(55)] that there is a threat of serious disturbance in the German economy and that state support of banks is a suitable way to remedy that disturbance. Despite a slow economic recovery having taken hold since the beginning of 2010, the Commission still considers that the requirements for state aid to be approved pursuant to Article 107(3)(b) TFEU are fulfilled, in view of the reappearance of stress in financial markets. The Commission has confirmed that view by adopting in December 2010 a Communication that prolongs until 31 December 2011 the application of state aid rules to support measures in favour of banks in the context of the financial crisis[(56)].

(161) The collapse of a bank such as HSH could directly affect the financial markets and thus the entire economy of a Member State. Given the current fragility of the financial markets, the Commission continues to base its assessment of state aid measures in the banking sector on Article 107(3)(b) TFEU.

9.2.2. COMPATIBILITY OF THE RISK SHIELD WITH THE IMPAIRED ASSETS COMMUNICATION

(162) The Commission should examine the compatibility of asset relief measures in the light of Article 107(3)(b) TFEU and on the basis of the Impaired Assets Communication. Contrary to what is argued by Germany, the Impaired Assets Communication does not serve merely to ensure consistent administrative practice[(57)]. Rather, it sets out the state aid rules to be applied to asset relief measures. Taking account of their specific features, it translates the state aid rules into compatibility criteria to be applied to such measures. Applying the Impaired Assets Communication should ensure consistency between asset relief measures introduced by the Member States and compliance with state aid monitoring requirements. Paragraph 18 of the Impaired Assets Communication states that the Communication aims to establish coordinated principles and conditions to ensure the effectiveness of asset relief measures in the internal market as far as possible, taking account of the long-term objective of a return to normal market conditions. Thus the objectives of the Communication are broader than what is argued by Germany, and are not confined to administrative practice. To fulfil the above objectives the Commission has to apply the Impaired Assets Communication to all asset relief measures.

(163) The Commission therefore does not see any grounds to assess the measure directly under Article 107(3)(b) TFEU, as suggested by Germany.

(164) The Impaired Assets Communication lays down a set of conditions with which asset relief measures have to comply in order to be compatible with Article 107(3)(b) TFEU. The examination of their compatibility is carried out using a number of criteria including the eligibility of the assets, the management of the assets, the valuation of the shielded portfolio, the appropriate identification of the problem and full ex ante transparency and disclosure, the alignment of the measure with public policy objectives, the appropriateness of the remuneration and burden sharing, and the requirement of the assessment of a restructuring plan by the Commission.

9.2.2.1. **Eligible assets**

(165) Paragraphs 33 et seq. of the Impaired Assets Communication require identification of eligible assets and their organisation into categories of assets (baskets). Detailed guidance on the definitions of those categories is provided in Annex III to the Impaired Assets Communication. The variety of assets covered by the risk shield goes beyond the basket system covered by the Impaired Assets Communication. However, paragraph 35 of the Communication allows for additional flexibility in the identification of eligible assets. It allows banks to be relieved of impaired assets that are not covered by paragraph 33 without a specific justification, but only for a maximum of 10-20 % of the overall assets of a given bank. However, since [around 75] % of HSH's balance sheet is covered by the risk shield, paragraph 35 of the Impaired Assets Communication does not provide a satisfactory solution here.

(166) Nevertheless, under paragraph 32 of the Impaired Assets Communication, which lays down the guiding principles on the eligibility of assets, a pragmatic approach should be adopted when assessing the nature of the assets involved in an impaired assets measure. The Commission notes that the range of asset classes affected by the financial crisis has become broader over time due to spill-over effects. In particular, securities related to shipping, aircraft and real estate in general face illiquid markets or are subject to severe downward adjustments. Asset relief for such assets can help to achieve the objectives of the Impaired Assets Communication, namely to increase transparency and to contribute to financial stability, even if they are not in the asset classes that initially triggered the financial crisis. Therefore the Commission has in previous cases accepted asset relief measures for these assets[(58)]. The Commission considers it appropriate to do so again in the present case.

(167) Lastly, paragraph 36 of the Impaired Assets Communication allows for wider eligibility criteria if the measure is compensated by in-depth restructuring. The greater the proportion that guaranteed assets represent in the portfolio of a bank, the more thorough the restructuring that the bank will have to

undergo. In the Decision initiating the procedure the Commission expressed its doubts regarding the eligibility of assets because the initial restructuring plan submitted to it at that time was not sufficiently far-reaching to adequately compensate for the flexible application of the eligibility criteria. HSH submitted the modified restructuring plan on 11 July 2011. The modified restructuring measures comprise a balance sheet reduction of around 61 %, divestment of […] shareholdings and closure of 15 out of 21 international locations. They allow the Commission to conclude that the depth of the restructuring compensates for the flexible application of the Impaired Assets Communication as regards the eligibility of assets. Consequently, the Commission's doubts regarding the eligibility of assets have been allayed.

9.2.2.2. **Management of assets**

(168) In recital 45 of the Decision initiating the procedure, the Commission expressed doubts about the compatibility of the guarantee in relation to the management of assets on the basis that there was no evidence of a clear functional and organisational separation between HSH and the shielded assets as all assets would remain on HSH's balance sheet; this applied in particular to management, staff and customers.

(169) Germany provided additional information, explaining that HSH had set up a restructuring unit which was an internal winding-down bank with separate management. HSH had introduced segment-based reporting, including separate management for the restructuring unit, so that no conflict of interest between the core bank and the restructuring unit could arise. The Commission agrees with the comments from Germany on management of assets as summarised in recital 115 of this Decision, and accepts the changes introduced by HSH in the management of assets. Consequently, the risk shield is in line with the requirements of the Impaired Assets Communication with regard to the management of assets.

9.2.2.3. **Valuation of the shielded portfolio**

(170) In recital 45 of the Decision initiating the procedure the Commission also raised doubts about the valuation of the shielded portfolio, because only a small portion of the portfolio had been valued by independent experts, and HSH had not provided enough information for the assessment of the REV of the entire portfolio. Prior to the implementation of the measure HSH had appointed two independent experts, Blackrock and Cambridge Place. They had valued only a small fraction of the shielded portfolio, namely the assets-backed securities (ABS) and parts of the CIP portfolio.

(171) The Commission does not share Germany's view, set out in recital 116 above that customer loans are difficult to value given the number of assumptions involved in cash flow projections (such as those on future delinquencies, probabilities of default, the timing of default and recovery, and interest rates both in respect of the risk-free rate and the risk premium). Although the

valuation is more complex in the case of loans with extendable maturities, which is typically the case of the shipping loans and commercial real estate loans that make up a large proportion of the shielded portfolio, the Commission's decision-making practice demonstrates that cash-flow-based valuations of portfolios including similar assets have already been performed[59]. In addition, Germany has failed to demonstrate that a valuation based on cash flow projections would result in a materially different outcome.

(172) Valuation should follow a general methodology established at Union level. At the Commission's request, HSH and its external expert Morgan Stanley conducted a full valuation of the portfolio in close cooperation with the Commission's experts. The underlying assumptions applied by HSH in the valuation were in line with the severe stress scenarios applied by the Commission in other cases. A consistent methodology has therefore been applied.

(173) The result of the valuation was that the expected losses would considerably exceed the EUR 3,2 billion first-loss tranche and exhaust the EUR 10 billion second-loss tranche […]. The valuation of the portfolio showed that the REV lies […], at around EUR [155-170] billion (around EUR [172] billion minus EUR 3,2 billion minus EUR [2,5-10] billion).

(174) The valuation was conducted in line with the conditions set out in the Impaired Assets Communication and the Commission therefore takes the view that its doubts as expressed in recital 45 of the Decision initiating the procedure have been allayed.

9.2.2.4. **Full ex ante transparency and disclosure**

(175) In recital 42 of the Decision initiating the procedure the Commission raised doubts about the compatibility of the measure with regard to transparency and disclosure, in so far as Germany had not provided a full valuation of the assets of the shielded portfolio carried out by a recognised independent expert.

(176) In accordance with paragraph 20 of the Impaired Assets Communication, applications for aid should be subject to full transparency and disclosure of impairments by eligible banks on the assets which will be covered by the relief measures, based on adequate valuation, certified by recognised independent experts and validated by the relevant supervisory authority. The information on the impaired assets should be provided with the degree of detail suggested in point II and Table 2 of Annex III to the Impaired Assets Communication.

(177) Since the adoption of the Decision initiating the procedure, detailed information about the shielded portfolio and the assets has been provided to the Commission. The valuation determines the REV of the portfolio at around EUR [155-170] billion. The capital relief effect of the risk shield was calculated to be [around EUR 3,5] billion. Morgan Stanley has officially signed and validated the valuation, including the underlying assumptions

and the applied methodology. The capital relief effect of the measure was confirmed by BaFin in February 2010. The capital relief effect calculated on the basis of the asset valuation differs from the Commission's preliminary assessment in recitals 51 et seq. of the Decision initiating the procedure. The Commission accepts the result of the valuation and the calculated capital relief effect submitted by Germany. In view of the outcome of the investigation, the comments that Germany made on the capital relief effect no longer need to be addressed.

(178) The Commission's doubts regarding adequate transparency and ex ante disclosure have been allayed.

9.2.2.5. **Alignment with public policy objectives**

(179) Section 5.3 of the Impaired Assets Communication requires incentives for banks to participate in an impaired asset relief measure to be aligned with public policy objectives, through (a) a six-month maximum enrolment window, (b) mechanisms to ensure participation by banks most in need of asset relief and (c) appropriate behavioural constraints to, among other things, limit the impact on competition.

(180) The guarantee was specifically designed for HSH and tailored to its particular situation in the light of its systemic importance to the economy of the public-sector owners. In the context of the modified restructuring plan, HSH will be subject to a number of behavioural commitments, in particular related to the payment of coupons and dividends, corporate governance, remuneration and market presence in specific sectors such as shipping.

(181) Based on the above, the risk shield for HSH is compatible with the requirements of the Impaired Assets Communication with regard to alignment with public policy objectives.

9.2.2.6. **Remuneration and burden sharing**

(182) In recital 49 of the Decision initiating the procedure the Commission expressed doubts about the adequacy of the burden sharing. Under paragraph 24 of the Impaired Assets Communication, HSH should be requested to contribute to the loss or risk coverage in the form of first-loss clauses (typically with a minimum of 10 %). Adequate burden sharing can also be ensured by higher remuneration or *ex post* compensation. In addition, in recitals 51 et seq. of the Decision initiating the procedure, the Commission expressed doubts that the fee of 400 bps adequately remunerated the risk taken by the public-sector owners.

(183) Paragraph 41 of the Impaired Assets Communication states that for any impaired asset measure an adequate remuneration must be secured for the State. An adequate remuneration for an impaired asset measure is one that would remunerate the regulatory capital impact of the measure. Thus the capital relief effect should be adequately remunerated.

(184) As regards the remuneration of the capital relief effect, in its Decision on the state aid granted by Germany for the restructuring of Landesbank Baden-Württemberg[(60)], the Commission established that an adequate remuneration of the capital relief effect would be 6,25 % of the amount of the capital relief obtained through the measure[(61)]. The capital relief effect for the risk shield has been determined to be around EUR [3,5] billion, hence there should be an annual remuneration of approximately EUR 220 million (which corresponds to [about 220] bps of the nominal value of the guarantee) where HSH benefits from the full amount of the guarantee. Upon (partial) cancellation of the guarantee, the minimum remuneration of the capital relief should decrease proportionally to about 220 bps of the outstanding nominal value of the guarantee.

(185) As explained in recital 46, HSH has proposed to pay a guarantee fee of 400 bps for the risk shield. Thus, depending on the scenario, HSH will pay EUR [> 1,5] billion (no drawing of the guarantee), EUR [> 2,5] billion (EUR 5 billion drawing) or EUR [> 4] billion (EUR 10 billion drawing).

(186) Regarding the adequacy of the minimum capital relief remuneration of [about 220] bps per annum on EUR 10 billion (or — in the event of partial cancellations — on the outstanding nominal amount of the guarantee[(62)]), the absolute amount of capital relief remuneration is reduced if the guarantee is partially cancelled. Although it is likely that the capital relief effect will not decrease in direct proportion to the amount of the risk shield, the Commission considers that, over the life of the risk shield, it is a reasonable approximation to make for the purpose of calculating the minimum required capital relief remuneration. Consequently, the Commission would view as adequate a remuneration of [around 220] bps per annum on the outstanding nominal amount of the guarantee.

(187) As [around 220] bps on the outstanding guarantee amount is an acceptable approximation for 6,25 % on the capital relief amount, the Commission is satisfied that 6,25 % per annum on the capital relief effect will always be paid to HSH Finanzfonds AöR. The capital relief remuneration can accordingly be considered to be in line with the Impaired Assets Communication.

(188) In addition, paragraph 41 of the Impaired Assets Communication requires the transfer value for asset purchase or asset guarantee to be based on the REV of the assets.

(189) According to the Commission's valuation of the risk shield, the guaranteed value of around EUR [168] billion was set too high (above the REV) and the first-loss tranche too low when designing the guarantee measure. The difference between the guaranteed value and the REV is EUR [2,5-10] billion. The consequence should be a 'correction' of the guaranteed value and an increase in the first-loss tranche. Germany has provided evidence that it is not possible for HSH to pay back EUR [2,5-10] billion, and does not accept

such a claw-back. However, even though HSH is unable to increase the first-loss tranche by EUR [2,5-10] billion in order to cover the expected losses, the difference could, pursuant to paragraph 41 of the Impaired Assets Communication, also be recovered at a later stage, for example through some combination of a claw-back mechanism and far-reaching restructuring measures.

(190) A claw-back mechanism can be put in place through the 400 bps basic premium paid to the State. It can take the form of that part of the payment which is in excess of the remuneration of the capital relief effect of [about 220] bps. In addition, that amount would also depend on the drawing of the guarantee, given that the basic premium can change, as illustrated in the table below.

TABLE 12

Claw-back payment through the basic premium and additional claw-back requirement

(In EUR million)

	Scenario 1(EUR 0 drawing of guarantee)	**Scenario 2(EUR 5 billion drawing of guarantee)**	**Scenario 3(EUR 10 billion drawing of guarantee)**
Basic premium (400 bps on outstanding nominal amount of the guarantee)	[> 1,5]	[> 2,5]	[> 4]
Of which, capital relief remuneration ([about 220] bps on outstanding nominal amount of the guarantee)	[700-900]	[1 200-1 600]	[1 800-2 500]
Claw-back in basic premium	[500-800]	[1 000-1 400]	[1 500-2 000]
Further claw-back needed	[…]	[…]	[…]

(191) The remuneration would result in an insufficient claw-back through the basic premium. Therefore, to achieve a full claw-back, the difference between the REV and the transfer price not covered by the basic premium of 400 bps

remains to be paid to the State by HSH. Depending on the scenario, that difference ranges from EUR […] billion to EUR […] billion.

(192) As Germany and HSH refuse to increase the payment in that respect the aid measure cannot be approved as compatible under Article 7(3) of Regulation (EC) No 659/1999.

(193) The Commission observes that the modified restructuring plan does demonstrate that it is impossible to ask for an additional claw-back payment of between EUR […] billion and EUR […] billion without threatening HSH's viability, because a full claw-back would consume its profits over the entire restructuring period and beyond, based on the projections in recital 91 above.

(194) Nevertheless the Commission considers that the compatibility of the aid measure might be ensured if a remuneration system were put in place that allowed for a correction in line with the rules established by the Impaired Assets Communication and the Commission's decision-making practice regarding claw-backs and remuneration. Paragraph 41 of the Impaired Assets Communication in fact specifies that it can be acceptable for the transfer value (guaranteed value) of the assets to exceed their REV if there is far-reaching restructuring and if conditions are introduced that allow for the recovery of the additional aid at a later stage. In sum, paragraph 41 of the Impaired Assets Communication leaves some room for accepting partial claw-backs if adequately compensated through restructuring.

(195) In the case in hand the Commission considers that a partial additional claw-back could be obtained if a combination of measures were implemented.

(196) First of all, the Commission considers that, to the greatest possible extent (and without undermining HSH's return to long-term viability), the payment of any additional claw-back should be made immediately and not deferred any longer than necessary. It has therefore investigated the possibility of an upfront payment. As explained in recital 90, the Commission requested HSH to include in the financial projections a one-off lump sum payment of EUR 500 million in 2011. The financial projections in recital 91 above demonstrate that HSH is able to pay such a lump sum amount of EUR 500 million to the State. Such a payment would consume all of HSH's expected profits and is expected to lead to a EUR [150-200] million net loss for 2011. However, that loss can be absorbed in subsequent years and will not prevent HSH from establishing a track record of consistent profits (representative of its business profitability) for all the remaining years of the restructuring period. Such a track record will be necessary to demonstrate HSH's return to long-term viability and ultimately to improve its ability to attract investors. On that basis, the Commission considers that EUR 500 million is the largest possible upfront contribution towards an additional partial claw-back that HSH could afford.

(197) However, in any event, the Commission does not consider that the amount clawed back up front needs to be paid back to the State in cash. Given HSH's capital situation, which to date has been insufficient to cover losses from its investing activities or to contribute to the strengthening of its capital basis, the Commission considers that the lump sum payment of EUR 500 million could be made in shares rather than in cash. HSH's capital position needs to be reinforced, in particular in view of the fact that it will continue to operate and focus on business lines which exhibit a strong pro-cyclicality and volatility, such as ship financing, as explained in detail below (see recitals 223 to 226).

(198) In addition to the one-off up-front payment described above, the Commission considers that HSH is also able to pay additional claw-back amounts on an ongoing basis. A further correction of the transfer price can be achieved through an additional premium paid over the restructuring period on top of the basic premium. Based on the financial projections in recital 91, the Commission considers that such an additional premium could be set as high as 385 bps without endangering the capacity of HSH to return to viability. An additional premium of 385 bps would not exceed the payments of the basic premium of 400 bps set out in Table 4 above over the restructuring period[63]. The payments of the additional premium would only exceed HSH's expected net profit for the period 2012-2014 only in the scenario involving a EUR 10 billion drawing (see recital 90 above). The Commission further notes that HSH has already cancelled EUR 3 billion of the guarantee, which implies that the third scenario set out in Table 4 above (drawing of the entire EUR 10 billion of the guarantee) can be ruled out.

(199) If more than this additional premium had to be paid it would endanger HSH's ability to achieve a common equity ratio of 10 %. For the reasons set out in recitals 223 to 226 and further explained in recitals 229 to 232 below, the Commission considers that achieving a level of capitalisation sufficient to buffer variations in the financial performance of HSH resulting from swings in the economic cycle is crucial in order not to compromise its return to viability. Such a sufficient buffer is considered to be a common equity ratio of 10 %. Thus if the additional premium were to compromise that ratio, its payment should be deferred to the extent necessary to avoid compromising HSH's viability.

(200) On that basis, the Commission considers that it would be possible for HSH to make further payments during future years without impeding its ability to return to viability.

(201) Based on the above considerations, and in order to ensure the compatibility of the risk shield with the Impaired Assets Communication, the Commission requires an alternative remuneration mechanism which alters the guarantee provision agreement concluded on 2 June 2009 as follows. It should be based on the existing basic premium in the guarantee provision agreement

in the amount of 400 bps p.a. on the nominal amount of the outstanding guarantee. That basic premium should remain unchanged, except that any drawings under the guarantee would no longer reduce the nominal amount of the guarantee for the purposes of calculating the premium. This avoids providing incentives to draw the guarantee. In addition, the basic premium should be supplemented by an additional premium amounting to 385 bps and a lump sum payment of EUR 500 million in ordinary shares ('lump sum payment' or 'lump sum payment in shares'). In order to implement these conditions the initial guarantee contract needs to be amended as set out in recitals 201 to 208.

(202) First, the additional premium needs to be added. The basis for the calculation of the additional premium should be similar to the basis for the calculation the basic premium, namely the nominal amount of the guarantee reduced by partial cancellations but not by drawings. However, the basis for the additional premium should depend on the extent to which HSH ultimately cancels the guarantee regardless of the timing of such cancellations. Thus, HSH's profitability would be affected only to the extent that it makes actual use of the guarantee. Therefore, upon partial cancellation, the portion of all the paid additional premiums corresponding to the amount of guarantee cancelled should be reimbursed to HSH. In order to achieve that effect, whilst both premiums are to be calculated on the contractually agreed guarantee amount reduced by cancellations but not by drawings, the basic premium should be paid on an annual basis on the outstanding guarantee amount but the additional premium should be set aside into a reserve account. The additional premium would be paid to HSH Finanzfonds AöR only if the guarantee is drawn. On the other hand, upon partial cancellation of the guarantee, the additional premium set aside in the reserve account corresponding to the cancelled amount should be repaid to HSH.

(203) In order to ensure that cancellations are not performed at the expense of viability, partial cancellations of the guarantee should be carried out only as long as they do not result in the ratio of HSH's common equity falling below [8,5-9,5] % as at 31 December 2011, [9-10] % as at 31 December 2012, [9,5-10,5] % as at 31 December 2013 or [10-11] % as at 31 December 2014. Further, a partial cancellation may not take place if, despite the ratios being met at the time of the partial cancellation, this would no longer be the case in the light of conservative estimates for the following years.

(204) The additional premium should be calculated retroactively from 31 March 2009 and on a pro rata basis for parts of financial years. The additional premium should be payable together with the basic premium as long as HSH's common equity ratio is at least 10 % (the 'minimum common equity ratio').

(205) In order to ensure that HSH's viability will not be endangered by the payments of the additional premium, the claw-back mechanism should contain a debtor warrant *(Besserungsschein)*. The debtor warrant should have a maturity of

up to 31 December [2030-2040]. If HSH's common equity ratio were to fall below the minimum common equity ratio because of the additional premium, the payment would be delayed and transformed into a debtor warrant. If the common equity ratio increased above the target, the debtor warrant would be repaid up to the limit of that target. That mechanism gives HSH the necessary flexibility but at the same time ensures that the claw-back will be paid at a later point in time once it is again in a situation to pay.

(206) The deferred additional premium entitlement should be completely restored for the duration of the debtor warrant. The additional premium will be payable until 31 December [2015-2025] at the latest. In any case, the basic premium and the additional premium should be payable at the latest until the sum of partial cancellations and drawings on the guarantee reaches EUR 10 billion.

(207) Second, HSH Finanzfonds AöR and HSH should be required to amend the initial guarantee provision agreement by adding a claim by HSH Finanzfonds AöR against HSH to a lump sum payment amounting to EUR 500 million. In order to prevent further reductions of HSH's own capital ratio, that claim should be payable by HSH in ordinary shares by means of a capital increase. The issue price is to be calculated on the basis of the value of HSH as of the day of the resolution of the general meeting of shareholders on that capital increase, and the net value of the lump-sum payment claim. HSH should issue shares corresponding to the net amount of the claim directly to HSH Finanzfonds AöR (and thus indirectly to the public-sector owners).

(208) The capital increase can take place either through an ordinary contribution in kind, with no right of option for minority shareholders, or through a mixed capital increase by way of contribution in kind and cash, with a right of option for all shareholders other than HSH Finanzfonds AöR regarding the cash portion. It is up to HSH Finanzfonds AöR and HSH to choose the form of the capital increase which will ensure speedier implementation and entry in the commercial register.

(209) If the guarantee provision agreement is amended, the absolute amount of the additional premium should vary based on the amount of losses actually covered by HSH Finanzfonds AöR (i.e. the greater the amount of losses absorbed by HSH Finanzfonds AöR, the greater the amount of the claw-back). To summarise, the cumulative claw-back payments resulting from the two conditions imposed by the Commission and described above are represented in the table below for the three scenarios presented in recital 46.

TABLE 13

Claw-back payment through the basic premium, lump-sum payment and additional premium

(In EUR million)

	Scenario 1(EUR 0 drawing of guarantee)	**Scenario 2(EUR 5 billion drawing of guarantee)**	**Scenario 3(EUR 10 billion drawing of guarantee)**
Basic premium (400 bps on outstanding nominal amount of the guarantee)	[> 1,5]	[> 2,5]	[> 4]
Of which capital relief remuneration ([around 220] bps on outstanding nominal amount of the guarantee)	[700-900]	[1 200-1 600]	[1 800-2 500]
Claw-back in basic premium	[500-800]	[1 000-1 400]	[1 500-2 000]
Additional premium (385 bps on the ultimately drawn amount of the guarantee)	0	[1 500-2 500]	[3 500-4 500]
Lump sum payment shares	500	500	500
Total claw-back paid	[1 000-1 300]	[3 000-4 400]	[5 500-7 000]
Further claw-back needed	[…]	[…]	[…]

(210) The Commission acknowledges that, in spite of the additional conditions imposed, in all the scenarios set out in Table 13 the remuneration mechanism will still result in only a partial claw-back of the EUR [2,5-10] billion gap between the REV and the guaranteed value (EUR […] billion in scenario 1, EUR […] billion in scenario 2 and EUR […] billion in scenario 3).

(211) However, the Commission has compared the risk shield measure (including the additional conditions on remuneration) with impaired asset measures approved in respect of other banks. The Commission also notes that paragraph 41 of the Impaired Assets Communication provides some flexibility for the assessment of impaired asset measures in which adequate remuneration cannot be paid, if the measure is accompanied by in-depth restructuring

and/or claw-back mechanisms. The Commission observes as well that its decision-making practice ranges from measures for which a full claw-back was provided (such as ING[(64)] or LBBW[(65)]) to others for which no claw-back was paid but for which a very far-reaching restructuring was undertaken (such as Parex[(66)]).

(212) The risk shield allows for a partial claw-back and is combined with far-reaching restructuring. It consequently meets the requirements of paragraph 41 of the Impaired Assets Communication and falls within the outer limits of the range observed in the Commission's decision-making practice. Furthermore, the HSH guarantee remuneration mechanism provides a partial claw-back in all possible scenarios. In particular, if the full amount of the guarantee were to be drawn (as in scenario 3), that partial claw-back would amount to […] % of the claw-back required. At the same time, as illustrated below at recitals 266 to 270, the restructuring of HSH will lead to a 61 % downsizing of its balance sheet. Considered in combination with the present extent of the restructuring, that partial claw-back is in line with the Commission's decision-making practice. Therefore the Commission is of the view that the impaired asset measures can be considered compatible with the Impaired Assets Communication if the conditions described above and further detailed in Annex II are met.

9.2.2.7. **Conclusion**

(213) On the basis of the foregoing, the Commission concludes that the comments provided by the Member State and third parties have not allayed its doubts regarding the risk shield. In the Commission's view, the risk shield is not in line with the Impaired Assets Communication as regards the points examined in section 9.2.2 of this Decision. However, compatibility can be achieved under the conditions laid down in Annex II to the present Decision.

9.2.3. COMPATIBILITY OF THE MODIFIED RESTRUCTURING PLAN WITH THE INTERNAL MARKET

9.2.3.1. **The degree of restructuring required**

(214) The Restructuring Communication sets out the state aid rules applicable to the restructuring of financial institutions where the measures are notified to the Commission on or before 31 December 2010. Therefore the modified HSH restructuring plan will be assessed on that basis. According to the Restructuring Communication, in order to be compatible with Article 107(3)(b) TFEU in the context of the current financial crisis the restructuring of a financial institution has to:

(i) lead to a restoration of the long-term viability of the institution;

(ii) include a sufficient contribution of the beneficiary's own (burden sharing);

(iii) contain sufficient measures limiting the distortion of competition.

(215) In line with its practice during the financial crisis, when assessing the restructuring requirements the Commission will not add the amount of liquidity guarantees to the amount of aid.

9.2.3.2. **Restoration of long-term viability**

(216) The Decision initiating the procedure raised doubts on the ability of HSH to restore its long-term viability. Those doubts were confirmed by an in-depth viability analysis performed after the adoption of the Decision initiating the procedure.

(217) In the Decision initiating the procedure, three main areas were identified as major weaknesses likely to jeopardise HSH's long-term viability which had not been properly addressed in the initial restructuring plan: (a) HSH's dependency on wholesale funding, (b) its reliance on volatile and cyclical activities and (c) the large size of its capital market activities relative to its banking activities. Furthermore, doubts were raised as to the sustainability of the growth rates and other assumptions used in the restructuring plan.

Funding

(218) Concerning the funding position of HSH, the analysis performed highlighted the following issues: (a) a weak funding structure with limited sources of long-term stable funding, in particular as grandfathered state-guaranteed bonds gradually come to maturity and have to be refinanced, (b) a heavy reliance on savings banks as a privileged source of funding, and (c) a lack of USD-denominated funding.

(219) The Decision initiating the procedure[67] highlighted the need for HSH to refinance EUR [60-110] billion of wholesale funding coming to maturity by 2014, and questioned its ability to do so. The Commission had identified a gap of around EUR [15-30] billion for which HSH had not planned and allocated specific sources of funding. As described in recital 53 above, HSH's funding plan showed a gap of EUR 48 billion, which can be adjusted based on assumptions on equity and derivatives in line with historical levels to around EUR [15-30] billion of uncovered funding needs. However, the additional group balance sheet reduction of EUR 34 billion to a balance sheet amount of EUR 120 billion as of the end of 2014 (as opposed to EUR 150 billion in the initial restructuring plan) will reduce the wholesale funding needs, and alleviate the pressure on the funding situation of HSH. It will bridge the funding gap for which no specific sources had been identified by HSH. Further, HSH has demonstrated that its assumptions on the projected level of deposits (permanent average balances, *Bodensatz*) are conservative compared to current and historical levels of the funding from that source. The Commission therefore considers that EUR [15-25] billion of funding needs not covered by the funding sources allocated can be covered through equity, excess deposits and short-term funding (secured or unsecured funding) without a negative impact on HSH's funding costs. Thus HSH will not have

to find new funding sources, and will be able to rely on identified and existing sources for its entire funding needs through to 2014.

(220) Concerning the reliance on savings banks as a privileged source of funding (as described in recital 95 above), the Commission notes that the reduction of HSH's risk profile will also reduce their importance in comparison with other sources. The additional balance sheet reduction contained in the modified restructuring plan (EUR 30 billion additional reduction compared to the initial restructuring plan, see recital 50 above) will considerably reduce the new funding needs and the funding gap. The projected funding mix at the end of the restructuring period (as described in Table 7 and recital 93) reduces HSH's reliance on short-term unsecured funding and therefore its exposure to a liquidity crisis. HSH will also rely more for its funding in relative terms on covered bonds, which in Germany comply with strict issuance requirements and can be considered as a stable and relatively cheap source of funding.

(221) The lack of USD-denominated funding of HSH constitutes another main weakness in HSH's business profile. At the end of 2010 around [20-30] % of HSH's total assets were dollar-denominated, amounting to USD [50-70] billion, of which only USD [15-20] billion (or [20-25] %) were directly funded in USD. That gap is covered by foreign exchange swap transactions, which are rolled over on a continuous basis. Due to the permanent widening of the EUR/USD foreign exchange swap basis since the outbreak of the financial crisis, that funding strategy costs an additional [20-30] bps approximately when compared to a funding strategy based on USD-denominated funding. Furthermore, the strategy brings a number of risks. They include (a) potential additional costs resulting from likely mismatches between actual and expected USD assets cash flows, (b) increased volatility of the short-term liquidity position due to margin call obligations related to the swap positions[(68)], and (c) increased exposure to counterparty risk due to the fact that swaps are concluded over the counter and HSH bears the full counterparty credit risk for those transactions. However, as the reduction of HSH's risk profile is to take place mainly in segments which generate USD-denominated assets (i.e. aircraft, shipping and international real estate financing), it also constitutes a material step forward towards reducing the USD funding need. Further, HSH has committed to increase the share of the core bank's USD business that is refinanced by means of USD-denominated funding to at least […] % by 2014.

(222) In conclusion, the proposed measures address the concerns identified by the Commission. They should ensure that HSH is on the right path for developing a more sustainable and stable funding mix with regards to volumes, maturities, seniority, security and currency. The commitment to reach a net stable funding ratio and a liquidity coverage ratio […] by 2012, ahead of the deadline imposed for implementation of those two ratios by the Basel Committee on Banking Regulation, will enable monitoring of HSH's progress in that area

and should contribute to ensuring that it will keep improving the quality and stability of its funding and retain sufficient excess liquidity in case of stress.

Cyclical nature and volatility of main business segments

(223) The Decision initiating the procedure[69] questioned the ability of HSH to ensure long-term viability by concentrating on an expansion of business segments which are cyclical and volatile in nature[70]. The in-depth viability analysis reinforced those doubts, as it revealed a growing proportion of HSH's net interest income to be generated by volatile and cyclical activities[71]. The relative importance of shipping and aircraft financing was viewed as being particularly problematic. However, the modified restructuring plan takes proper account of assets' cyclical nature while preserving the HSH franchise in the shipping business.

(224) The EUR [30-35] billion additional asset reduction will come entirely from the core bank (to a EUR 82 billion target in 2014) and in particular from the cyclical and volatile activities. HSH will end its aircraft financing activities. The existing aircraft financing assets, amounting to EUR [3-8] billion, will be transferred to the restructuring unit as of the end of [2011-2012] and run down. HSH undertakes not to generate new business in that area. HSH has also committed to reducing its shipping division to total assets of EUR 15 billion in the core bank by the end of 2014. The reduction will be achieved by transferring an additional EUR [0,5-2] billion into the restructuring unit by the end of [2011-2012] and by limiting new business volumes. That total amount of EUR 15 billion of shipping and air transport financing assets compares to EUR [25-30] billion as of 2008.

(225) The total assets of the real estate division will also be reduced, to EUR 13 billion as of end 2014, as new international real estate business of German corporate clients will be stopped and other new business reduced. The activities of the corporate division will be significantly decreased by 2014 through lower new business volumes.

(226) That absolute reduction will be accompanied by an improvement in HSH's risk management processes. In particular, HSH is engaging in a process of reducing individual risks, in particular in the shipping segment. It has also undertaken to reduce existing large single exposures to EUR […] million and to limit new single exposures to a maximum of EUR […] million.

The volume of capital market activities

(227) In recital 62 of the Decision initiating the procedure, the Commission raised concerns in regard to the volume of HSH's capital market operations, which were viewed as remaining disproportionately large despite the refocusing on regional activities. In particular, proprietary trading contributed to HSH's difficulties.

(228) The downsizing of HSH's balance sheet will lead to a very substantial diminution of capital market operations. Capital market operations will be

reduced to reach EUR [25-35] billion in assets in the core bank by 2014. That figure compares to EUR 98,8 billion in 2008. Further, Germany has given a commitment that HSH will not engage in proprietary trading. HSH will engage in trading activities only to the extent that they are necessary to execute customers' orders, to hedge customer business, or for treasury liquidity and balance sheet management purposes (in each case, up to a ceiling expresses as a maximum value at risk). Consequently, those measures address the concerns raised in the Decision initiating the procedure.

Weak capitalisation

(229) HSH's weak capital structure constitutes another potential obstacle to its long-term viability. The adequacy of the low capitalisation which in the initial restructuring plan was expected at the end of the restructuring period (Tier 1 ratio of [around 9] %) was questionable in particular in light of (a) the cyclical and volatile nature of HSH's business profile, which called for an additional capital buffer to absorb recurring increased correlated losses, (b) the impact on HSH's capital of the financial crisis[(72)] and (c) the introduction of the new Basel III rules, which will very substantially raise the new minimum capital levels[(73)] required by the regulators. It can also be assumed that market operators, and in particular institutions likely to provide unsecured wholesale funding, will expect higher capital ratios.

(230) The further reduction of HSH's risk profile, profit retention and the EUR 500 million capital increase in 2013 will materially improve HSH's capitalisation. At the end of 2014 HSH's common equity ratio is expected to be above 10 % and the Tier 1 ratio above 12 %. Those figures compare to [around 7] % and [around 9] % levels in the initial plan for the same ratios. They are more in line with the newly emerging capital standards for banks. Although part of that improvement is also linked to the still significant reduction in risk weighted assets created by the risk shield, the capital position would improve in any event. The improvement has to be put in the context of the reduction of the risk profile of HSH's balance sheet, and in particular the reduction in the proportion of highly cyclical assets.

(231) Furthermore, one of the requirements to be imposed by the Commission as a condition for finding that the risk shield's remuneration and claw-back are compatible is that HSH cannot cancel the risk shield if that cancellation would lead to a decrease in the common equity ratio below set levels through the restructuring period, and in particular below 10 % as of 31 December 2014 (see recital 203). That safeguard ensures that HSH is able to maintain adequate levels of capitalisation throughout the restructuring period even in the event of the economic situation deteriorating. The mechanism should help HSH regain the confidence of market counterparties. HSH's plan provides that it will fully exit the guarantee by [2014-2016], at which point the common equity ratio is expected to be [> 10] %.

(232) To conclude, the capital position of HSH is improved by the proposed measures so that it is aligned with newly emerging international standards. The improved capital ratios and the higher resistance to stress will have a positive impact on HSH's funding costs in the mid-term.

Planning assumptions

(233) The Decision initiating the procedure (recitals 60 and 63) raised doubts over the sustainability of certain assumptions used in HSH's planning. Those doubts related in particular to assumptions for (a) the growth of the main business segments; (b) the growth of non-interest income; (c) margins on the key business segments; and (d) the evolution of loan loss provisions.

(234) The Commission considered the growth assumptions, especially in the shipping, transportation and corporate segments, too optimistic. The ability of HSH to achieve the planned total income was therefore questioned. The revised restructuring plan is, however, based on more reasonable growth assumptions for the shipping and the corporate segments (see Table 5 above). Furthermore, since HSH is now exiting the aircraft financing business, the issue of growth in that segment has also been addressed. As shown in Tables 5 and 6, the growth rates used for the planning of the shipping and corporate segments are materially lower than those used in the original restructuring plan of 1 September 2009. Further, they correspond to absolute volumes which are considered more reasonably achievable for HSH in those sectors in light of its market share and of the overall market volume.

(235) HSH has also revised its assumptions for the growth of its non-interest income. On average over the period 2010 to 2014, non-interest income is expected to represent about [7-12] % of net interest income for the core bank. That target should be achievable in light of HSH's plan to improve the cross-selling of products between its financial markets division and other business units.

(236) The Decision initiating the procedure questioned the margins assumptions used in the original planning. However new business margins as of end 2010 were in fact higher than initially expected and planning assumptions were adequately adjusted to reflect that fact.

Overall conclusion on HSH's long-term viability

(237) The Decision initiating the procedure questioned HSH's ability to withstand the next economic downturn without having recourse once again to State aid, and therefore its long-term viability. That scepticism was based on the following weaknesses: (a) a fragile funding structure, and in particular a large upcoming funding gap and a chronic shortage of USD-denominated funding, (b) a focus on cyclical and volatile activities likely to create recurring large combined losses, and (c) too low a capitalisation to be able to absorb such losses. However, the proposed additional measures included in the modified restructuring plan address the Commission's doubts. The new plan

has been built using more realistic and credible assumptions and therefore gives a more reliable view of HSH's viability. The resulting picture is that of a bank which by the end of the restructuring period will be adequately capitalised, with a lower proportion of its operations focused on highly cyclical segments and a stabilised, albeit still challenging, funding position, but with monitoring tools (the net stable funding ratio and USD funding proportion) that should help maintain the focus on continual improvement in the medium term. On that basis, HSH should now have the capital base and the funding position necessary to be able to withstand an economic downturn without recourse to state aid. Regarding the overall profitability of HSH, the modified restructuring plan shows that HSH's return on equity during the restructuring period reaches [5-10] % in 2014[(74)]. That figure is low in absolute terms, but should be more stable as a result of HSH's significantly lower risk profile. It should therefore be viewed as much improved compared to the levels observed in the 10 years preceding the crisis.

9.2.3.3. Own contribution and burden sharing by minority shareholders

(238) The Restructuring Communication indicates that, in order to limit the distortions of competition and to prevent moral hazard, (a) restructuring costs and (b) the aid amount should be limited, and there should be a significant own contribution. The Restructuring Communication states further that, in order to keep the aid limited to a minimum banks should first use their own resources to finance the restructuring. The costs associated with the restructuring should not be borne only by the State but also by those who invested in the institution. These include shareholders and subordinated bondholders.

9.2.3.3.1. *Own contribution, burden sharing and aid limited to the minimum*

(239) In recital 65 of the Decision initiating the procedure, the Commission noted that the volume of the divestments that were to serve as the institution's own contribution was vague. Germany has given a commitment that HSH will sell [100-120] subsidiaries by the end of the restructuring period. Besides, HSH has already sold [30-40] of those [100-120] subsidiaries and expects to have completed all sales by […] at the latest. The revenues and profits generated will be used to cover restructuring costs. The financial participations to be sold are listed in Annex III and include, among others, HSH Real Estate AG, […], DekaBank and […], which are HSH's largest subsidiaries.

(240) Further, Germany has given a commitment that HSH will not engage in any acquisition until 31 December 2014.

(241) The Commission considers that the own contribution measures set out in recitals 239 and 240 do not ensure that in HSH's current financial circumstances it is providing the maximum contribution of its own to the costs of the restructuring. In particular, the Commission considers that, in line with point 26 of the Restructuring Communication, in a restructuring context the discretionary offset of losses by beneficiary banks (for example

by releasing reserves or reducing equity) in order to guarantee the payment of dividends and coupons on outstanding subordinated debt, is in principle not compatible with the objective of limiting the aid amount to the minimum. In particular financial instruments with equity components should participate in losses incurred.

(242) As Germany refuses to propose additional own contribution measures, the aid measure cannot be approved as compatible under Article 7(3) of Regulation (EC) No 659/1999. Such measures can, however, be imposed by attaching conditions to the Decision.

(243) Thus, during the restructuring phase, the Commission should impose the condition that HSH must not make any payments in respect of profit-related equity instruments (such as hybrid financial instruments and profit participation certificates), in so far as those payments are not owed on the basis of a contract or the law. As part of such a dividend ban the Commission also considers that if HSH's balance sheet, without the adjustment of reserves and retained earnings, shows a loss, those instruments must participate in the loss. There should be no participation in losses brought forward from previous years.

(244) In order to ensure that the owners of HSH participate to the maximum extent in the reconstitution of an adequate capital basis over the restructuring period (see recitals 229 to 231 above), the Commission would also consider any dividend payment over the restructuring period to be against the principles of keeping state aid to the minimum necessary. Therefore the Commission takes the view that HSH should not pay dividends in the period up to and including the 2014 financial year.

9.2.3.3.2. *Burden sharing by minority shareholders*

(245) In the Decision initiating the procedure (recitals 66 to 72), the Commission took the preliminary view that the minority shareholders who had not participated in the recapitalisation of HSH in May 2009 had not seen their stakes sufficiently diluted. The original restructuring plan did not include burden sharing sufficient to allow the aid to HSH to be considered compatible. Further, the Commission questioned whether the minority shareholders themselves might have benefited from the state aid by maintaining excessively high shareholdings in HSH. The Commission concluded that the measure might include potential indirect aid to the minority shareholders, which might be unlawful if mechanisms to achieve adequate burden sharing were not put in place (recital 73).

The Commission responses to comments by Germany and third parties

(246) The savings banks associations have asserted that the Commission has not investigated secondary indirect aid effects in any previous recapitalisation case (see recital 129); the Commission points out that it has in fact investigated indirect aid in a great variety of aid measures in a number of decisions[(75)].

(247) The Commission recalls that according to settled case-law, Article 107(1) TFEU does not distinguish between measures of state intervention by reference to their causes or aims but defines them in relation to their effects[76]. The origin of the advantage indirectly conferred on the minority shareholders was the renunciation by the public-sector owners of that additional shareholding in HSH which they would have received if the price of the new shares had been determined correctly. There is a causal link between the aid granted through state resources to HSH and the advantage to the minority shareholders.

(248) The Commission also disagrees with the statement that the advantage to the minority shareholders is not imputable to the State because the decision about the recapitalisation, including the number of shares and the share price, was taken by the shareholders' meeting (see recital 128). At that meeting the public-sector owners were present as shareholders, and acted in their function as public bodies[77]. There was a political discussion on the future of HSH at that time.

(249) The main comments from Germany and the minority shareholders revolve around the arguments that a lesser dilution is not aid and that in any case dilution is simply the result of the parameters chosen for the capital increase, namely the number of shares and the price of those shares. Further, regarding such parameters, Germany and the minority shareholders have pointed to the fact that the valuation was conducted by PwC, a respected company, in line with recognised valuation standards. The valuation was based on the assumption that HSH would return to A rating in 2013, which it was claimed was a reasonable premise. The savings bank associations and Flowers agree with Germany as to that assessment. They claim that the issue price of the new shares was in fact too low.

(250) The Commission does not question that PwC is a respected company and that it conducted the valuation of HSH in line with recognised valuation standards. However, it maintains that the valuation of HSH did not take into account several aspects which, had they been considered, would have led to a lower value of HSH.

(251) The PwC valuation report ('the Valuation Report') was delivered on 15 May 2009[78]. On 30 April 2009 Germany notified the State aid measures for HSH to the Commission because HSH was at risk of not being able to meet regulatory capital requirements. At that point in time it was apparent that HSH would have to undergo substantial restructuring and that it would have to offer compensatory measures for competition distortions that the aid measures might cause. The PwC valuation was conducted on the basis of a business plan that did not take all those aspects into account. In the summary[79] of the Valuation Report PwC clearly stated that the valuation was based on HSH's

planning, which assumed a normalisation of the markets as of 2011. That assumption cannot be considered conservative.

(252) Furthermore, the valuation was conducted under the assumption that HSH would return to an A rating in 2013. PwC explicitly mentioned in the Valuation Report that on 6 May 2009 S&P downgraded HSH from A to BBB + with negative outlook[(80)], and that the downgrade was not reflected in the funding planning on which the valuation was based and consequently was not taken into account in the calculation of the indicative value of HSH. In addition, PwC observed that, in view of the upcoming state aid investigation, it could be expected that in order to ensure the compatibility of the aid measures, requirements would be imposed which would have a considerable impact on HSH's business plan. PwC also noted that the general economic conditions in the sectors relevant for HSH (shipping, aviation) and restrictions on the capital market (funding) made it difficult to predict future developments.

(253) Finally, it should be mentioned that the valuation was conducted under the assumption that the risk shield would be implemented. Without the risk shield the RWA relief would not have taken place, and the scale of the necessary recapitalisation would have had to have been increased and the rating assumptions reviewed. PwC also calculated the value of HSH for the scenario in which the risk shield was not implemented[(81)], and arrived at an indicative value for HSH of EUR [0,8-1,2] billion to EUR [1,5-2] billion, which corresponds to a share price between [> 9] and [< 22] EUR. In view of those facts the Commission continues to consider that the price of the newly issued shares was considerably too high.

(254) The minority shareholders also argued that in its Decision on HRE the Commission accepted a price for new shares that was above the stock exchange price without questioning its adequacy for burden sharing purposes. They claim that the issue of the share price in HSH should therefore not be investigated either. The Commission is of the opinion that those two cases are not comparable. In HRE a series of measures was taken leading to a full nationalisation of HSH. The main difference between the two cases is that HRE was taken into public ownership and that the State acquired the shares at a price based on the value of the company without state support[(82)]. That is not the case for HSH. The valuation of HSH for determining the price of the newly issued shares was conducted under the assumption that the risk shield of EUR 10 billion would be implemented. That assumption must have significantly influenced the result of the valuation.

(255) The minority shareholders further explained that in 2008 they supported HSH with significant financial contributions and would not have been able to participate in the recapitalisation in April 2009. They contend that they were also not obliged to do so since an option on new shares does not imply a purchase obligation.

(256) The Commission understands that the savings bank associations had an option on the new stock and were not obliged to exercise that right. However, the Commission cannot treat the financial support granted to HSH by the minority shareholders in 2008 as a contribution to burden sharing in the context of the aid measures provided to HSH in May and June 2009. The support granted to HSH in 2008 was a consequence of an investment decision taken by the minority shareholders at that time. The Commission does not see a connection between the capital measures in 2008 and the aid measures in 2009.

(257) The Commission does not agree with the savings bank associations' comments stating that they do not conduct any economic activities and therefore cannot be regarded as undertakings for the purposes of the state aid rules (see recital 128). The savings banks in Schleswig-Holstein carry on an economic activity[(83)]. They have grouped their economic interests in the savings bank associations. The savings bank associations provide services to the savings banks in Schleswig-Holstein and hold participations/shareholdings for the savings banks, as is the case with the savings bank's shares in HSH Nordbank. If the participations of the savings banks in the associations increase in value, the value of the savings banks also increases. The savings bank associations and their member savings banks form an economic unit. Any advantage to the associations is by the same token an advantage to the savings banks in Schleswig-Holstein. Therefore the savings bank associations, which economically speaking can be wholly identified with the Schleswig-Holstein savings banks, can be considered recipients of state aid in the meaning of Article 107(1) TFEU.

(258) The comments received from Germany and third parties have not allayed the Commission's doubts on the insufficiency of the burden sharing by minority shareholders. The Commission still believes that the minority shareholders who did not participate in the recapitalisation of HSH in 2009, did not see their stakes sufficiently diluted because the number of shares allocated to the public owners in the recapitalisation was not based on a correct valuation of HSH at the relevant time. However the Commission observes that the modified restructuring plan contains additional measures which considerably improve burden sharing by the minority shareholders.

(259) In particular, the additional measures on remuneration of the risk shield imposed by the Commission (recitals 202 to 208) will increase the degree of burden sharing. The additional remuneration for the risk shield consisting of the additional premium and the EUR 500 million lump sum payment in shares will have two major effects. First, the increase of the absolute amount of the remuneration payments to the public-sector owners will decrease the distributable profits of HSH and therefore the value of HSH to its shareholders. Second, the EUR 500 million lump sum payment in shares will dilute the stakes held by the minority shareholders, whose shareholding will

decrease from 16,8 % currently to about 14-15 % (depending on the share price valuation).

(260) In addition to the effect resulting from the conditions imposed in respect of the remuneration of the risk shield, burden sharing by minority shareholders will be further improved by the restriction on remuneration of capital instruments set out in recitals 241 to 244. The value of HSH to its shareholders depends on future cash flows, and those cash flows, in the form of dividends, will not be paid until 2014. Therefore the constraints on the timing of the future cash flows imposed by the Commission will further enhance burden sharing by the minority shareholders.

(261) The Commission considers that even though burden sharing by the minority shareholders has been significantly improved in the modified restructuring plan and through the conditions imposed by the Commission, the measures do not ensure that the burdens are shared to the maximum extent by the minority shareholders. As Germany refuses to propose additional burden sharing measures, the aid measure cannot be approved as compatible under Article 7(3) of Regulation (EC) No 659/1999. On that basis, the indirect aid to the minority shareholders would have to be deemed incompatible, unless some other conditional measures can be found which improve burden sharing by the minority shareholders.

(262) In light of the potential benefit received by the minority shareholders and the need for adequate burden sharing, the Commission considers that an extension of the dividend ban beyond 2014 is required. However, in order to be proportional, the dividend ban should be limited. To that end, the Commission should impose the condition that in the period from 1 January 2015 until 31 December 2016, dividend payments may not exceed 50 % of the annual surplus for the previous financial year. Furthermore, dividend payments should be permissible during that period only in so far as they would not jeopardise compliance with the Basel III provisions on the capital of credit institutions in the medium-term.

9.2.3.3.3. *Conclusion on own contribution and burden sharing by minority shareholders*

(263) The Commission concludes that adequate own contribution and burden sharing of the minority shareholders can be achieved, and consequently that the aid can be viewed as compatible subject to the conditions described in recitals 262, 202 to 208 and 241 to 244.

9.2.3.4. **Measures limiting distortion of competition**

(264) The Restructuring Communication requires that the restructuring plan contains measures limiting distortions of competition and ensuring a competitive banking sector. The Restructuring Communication indicates, in point 30, that the measures to limit the distortion of competition created by the aid should be tailor-made to address the distortions identified on the markets

where the beneficiary bank operates following its return to viability after restructuring. The Commission in its assessment should take as a starting point the size, scale and scope of the activities of HSH.

(265) In the Decision initiating the procedure, the Commission viewed the proposed measures to address distortion of competition as insufficient. However, the modified restructuring plan provides more measures to address distortion of competition.

(266) In the modified restructuring plan the projected balance sheet reduction has been considerably increased by comparison with the initial restructuring plan. HSH will reduce its balance sheet by 61 % by the end of 2014 compared to 2008[84]. The reduction of HSH by more than half is appropriate, given the distortions of competition stemming from the large amount of aid received. The reduction is in line with Commission decision-making practice for comparable aid amounts in relative terms. However, in the case of HSH the need to restructure and to reduce the balance sheet is especially great, owing to the insufficient burden sharing stemming from the incomplete claw-back. The reduction complements HSH's commitment to divest the majority of its participations.

(267) Further, HSH has given a commitment to reduce the number of its international branches or representation offices from 21 to 6 and the number of national branches from 9 to 7. The remaining branches or representations in London and New York will also be substantially downsized and the branch in Luxembourg will remain solely as a branch of the restructuring unit.

(268) HSH has given a further commitment to observe an acquisition ban during the restructuring period (until 31 December 2014). HSH will not expand business activities through the acquisition of other firms. Landesbank mergers remain possible, subject to the Commission's approval. Debt-to-equity-swaps and other usual asset management measures are allowed as long as they do not lead to a circumvention of the acquisition ban. If the public-sector owners relinquish control over HSH, then the acquisition ban will apply for three years only. The Commission considers that the privatisation of HSH would have a positive effect on HSH's viability and ensure effective competition. The continuation of the acquisition ban significantly beyond the date of sale could hinder a possible privatisation process.

(269) More specifically, HSH has given a commitment to take additional measures which will directly address distortion of competition in the markets in which HSH had acquired strong market positions and in which it had planned to expand. HSH will discontinue its business activities in financial services in relation to aviation[85]. EUR [3-8] billion of aviation assets will be transferred to the restructuring unit or sold as of the end of [2011-2012]. HSH will also significantly reduce its shipping, real estate and corporate activities. In particular, in the shipping segment, where HSH has established itself as a

leading provider of ship financing and in which HSH had planned to further expand, HSH undertakes that its global market share in new shipping business will not exceed [< 8] % during the entire restructuring period and HSH will not be one of the top three shipping financing providers in terms of new business.

(270) In conclusion, the proposed measures to limit distortion of competition constitute a material improvement to the steps taken by HSH in the initial restructuring plan, and are viewed as appropriate and sufficient.

9.2.3.5. **Conclusion regarding the restructuring**

(271) The Commission comes to the conclusion that the restructuring measures, including Germany's commitments in Annexes I and III, are such as to restore the long-term viability of HSH, for an adequate contribution on HSH's own part, and make up for the distortion of competition due to the aid measures in question. Under the conditions in regard to remuneration and burden sharing which are to be imposed by the Commission, and which are specified in Annex II, the modified restructuring plan also provides for adequate and sufficient burden sharing, and therefore may be deemed to be compatible with the internal market in accordance with Article 107(3)(b) TFEU.

(272) Finally, the Commission considers that the aid contained in the EUR 17 billion of liquidity guarantees provided by Soffin constitutes compatible restructuring aid in so far as it was necessary to address a market failure, in the form of the collapse of the interbank market.

10. POTENTIAL BENEFIT TO OTHER SHAREHOLDERS

(273) The minority shareholders have argued that Article 7 of the Procedural Regulation would be breached by dividing the procedure into an authorisation of the direct aid measures for HSH in one set of proceedings while dealing with the issue of the indirect aid to the minority shareholders in another. A negative decision on the recapitalisation in respect of the savings bank associations and Flowers would render the recapitalisation incompatible. According to the savings bank associations, the Commission should address the issue of burden sharing by the minority shareholders in the context of the burden sharing assessment of the recapitalisation.

(274) The Commission does not agree with the minority shareholders as to the interpretation of the Procedural Regulation. A split of the procedure is legally possible and has been carried out by the Commission in several cases[86]. If a single state aid measure has several beneficiaries whose status requires different legal assessments and might result in different paces of investigation, the formal investigation procedure can be split for the purpose of the effectiveness of the proceedings.

(275) The Commission does not agree either that a different legal assessment on the aid measure in relation to the minority shareholders as indirect beneficiaries would affect the legal assessment (and the compatibility) of the same aid

measure in relation to HSH as direct beneficiary of the aid. The Commission refers to the ruling in Case C-382/99 *Netherlands* v *Commission*[(87)], where the Court upheld the Commission's assessment that an aid measure granted to a recipient could be compatible aid (because in line with *de minimis* rules), while the same aid measure was not compatible in relation to indirect beneficiaries, and should be recovered. The Commission notes that the proportionality of the recapitalisation in relation to HSH can be ensured through adequate measures in the restructuring plan, whereas any advantage granted to the minority shareholders by means of an excessively high issue price can be treated and corrected differently, for instance by burden sharing.

(276) Nevertheless, the Commission does not see any grounds to split the case, and can deal with the different aspects of the aid measure in one decision. If there were not sufficient burden sharing any potential benefit to the minority shareholders could also be assessed, as indicated in the operational part of the Decision initiating the procedure. However, in light of the modification of the remuneration of the risk shield and the additional burden sharing measures, a substantial dilution of the minority shareholders' stakes and additional burden sharing will be achieved which mitigates substantially the flaws stemming from the valuation by PwC and thus re-establishes adequate burden sharing. In view of that adequate burden sharing established on the basis of the conditions imposed by the present Decision, the Commission considers that the sharing of burdens is sufficient and will therefore not pursue that issue further.

11. CONCLUSIONS

(277) In view of the commitments entered into by Germany regarding the restructuring and the conditions imposed by the Commission on that Member State in regard to the remuneration and burden sharing, the Commission comes to the conclusion that the risk shield is in line with Section 5 of the Impaired Assets Communication. In view of the modified restructuring plan submitted, the commitments given by Germany and the conditions imposed on that Member State by the Commission, the restructuring aid composed of the risk shield, the recapitalisation and the liquidity guarantees is in accordance with Article 107(3)(b) TFEU and can be found compatible with the internal market. The objections set out by the Commission in the Decision initiating the procedure have been dispelled,

HAS ADOPTED THIS DECISION:

Article 1

1 The EUR 3 billion recapitalisation, the EUR 10 billion guarantee granted by Germany to HSH in the form of a risk shield and the liquidity guarantees granted by Germany constitute state aid caught by Article 107(1) of the Treaty on the Functioning of the European Union.

2 The aid in the form of a EUR 3 billion recapitalisation, a EUR 10 billion guarantee granted by Germany to HSH in the form of a risk shield and the liquidity guarantees granted

by Germany are compatible with the internal market, in light of the commitments set out in Annexes I and III and subject to compliance with the conditions set out in in Annex II.

Article 2

Germany shall ensure that the original restructuring plan submitted on 1 September 2009, as last modified by Germany's communication of 11 July 2011, is implemented in full, including the commitments set out in Annexes I and III and the conditions set out in in Annex II, and in accordance with the timetable laid down therein.

Article 3

Germany shall inform the Commission within two months of notification of this Decision of the measures taken to comply with it.

Article 4

This Decision is addressed to the Federal Republic of Germany.

Germany is requested to forward a copy of this Decision to the beneficiary of the aid without delay.

Done at Brussels, 20 September 2011.

For the Commission

Joaquín ALMUNIA

Vice-President

ANNEX I

LIST OF COMMITMENTS REFERRED TO IN ARTICLE 1(2) AND ARTICLE 2

1.1. **[Restructuring phase/monitoring trustee]** The restructuring phase ends on 31 December 2014. The commitments apply in the restructuring phase, provided the individual conditions do not state otherwise.

1.2. Full and proper implementation of all commitments and conditions listed in Annexes I, II and III will be continuously and thoroughly monitored and checked in detail by a suitably qualified monitoring trustee that is independent of HSH.

2. **[Core bank and internal restructuring unit]** HSH has set up an internal restructuring unit which is responsible for winding up certain assets. In functional and organisational terms, the internal restructuring unit is separate from the ongoing business areas (the core bank), and is managed as a segment in its own right with independent governance.

3. **[Sale of parts of the business]** The hiving off or sale of parts or subparts of the business with the approval of the public-sector owners is compatible with Article 2 of this Decision.

4.1. **[Reduction of balance sheet total – group]** On the basis of the HSH group's audited balance sheet total at 31 December 2008 (EUR 208 billion), its balance sheet assets are to be reduced to around EUR [100-150] billion by 31 December 2012 and around EUR 120 billion by 31 December 2014. Of that amount, EUR […] billion will come from derivatives[(88)].

4.2. **[Reduction of balance sheet total – core bank]** The total balance sheet assets of the core bank are to be reduced to around EUR [60-90] billion by 31 December 2012 and around EUR 82 billion by 31 December 2014. Of that amount, EUR […] billion will come from derivatives[(89)].

4.3. **[Reduction of balance sheet total – restructuring unit]** The total balance sheet assets of the restructuring unit are to be reduced to around EUR [50 – 70] billion by 31 December 2012 and around EUR 38 billion by 31 December 2014. Of that amount EUR […] billion will come from derivatives[(90)].

4.4. **[Correlation]** Should the total balance sheet assets of the core bank at 31 December 2014 be less than EUR 82 billion, the maximum amount permitted for the restructuring unit will be increased by the difference. The maximum amount for the group under point 4.1 will remain unchanged.

4.5. **[Withdrawal from object-related aircraft financing]** HSH will withdraw completely from object-related aircraft financing, in accordance with the amended restructuring plan.

4.6. **[Definition of the aircraft financing business area]** HSH's aviation division offers aircraft financing solutions worldwide. HSH acts as an arranger and lead bank, particularly in priority asset and project financing. The corporate business division will not provide object-related aircraft financing either in the future.

4.7. **[Withdrawal from the international real estate business]** HSH will give up international real estate financing in accordance with the amended restructuring plan.

4.8. **[Downsizing of the ship financing business area]** HSH will cut back its ship financing business, in accordance with the amended restructuring plan. The total balance sheet assets of the ship financing division in the core bank are to be reduced to around EUR 15 billion by 31 December 2014. The reduction will be achieved in particular by relinquishing the financing of roll-on/roll-off vessels and cruise ships, […]

4.9. **[Restrictions in the ship financing business]** Until 31 December 2014, HSH's annual market share of new business in worldwide ship financing will not exceed [< 8 %] on a yearly basis. Until 31 December 2014 HSH will undertake not to be among the top three ship-financing providers with the highest annual volume of new business, according to the market rankings determined on a yearly basis.

4.10. **[Definition of the ship financing business area]** HSH's shipping division acts as a strategic partner for clients, including shipowners in the global shipping and shipbuilding industry. In contrast to the shipping division, the corporate business division will not be active in object-related ship financing.

4.11. **[New business in the ship financing business area]** The following activities constitute new business over a specific period: (a) payments made in that period pursuant to newly concluded contracts; (b) undertakings to make future payments on the basis of contracts newly concluded during that period; renewals of commitments already entered into in the past, and payments made on account of the expiry of conditions or capital tie-ups, are regarded as extensions.

5. **[Restriction of external growth]** Until 31 December 2014 there may be no further expansion of business activities through the acquisition of other firms (no external growth). Subject to the European Commission's approval, an exception may be made for acquisitions/mergers as part of the possible consolidation of *Landesbanken*, for the purposes of vertical integration or for other substantial reasons (e.g. to prepare the entry of strategic investors or to broaden the funding basis). Debt-to-equity swaps and other routine credit management measures are not considered to be expansion of business activities unless carried out with the intention of circumventing the restriction of growth referred to in the first sentence.

6.1. **[Locations]** The following HSH offices will close by no later than 31 December 2011:

(a) Within the European Union:

— Copenhagen
— Helsinki
— Paris
— Riga
— Naples
— Lübeck
— Warsaw
— Stockholm
— Amsterdam
— Tallinn

(b) Outside the European Union:

— Oslo
— Moscow
— San Francisco
— Hanoi
— Shanghai

— Mumbai

6.2. The existing business that has not been wound up by the time the offices mentioned under paragraph 6.1 close is to be transferred or allowed to expire after that time upon the maturity of the underlying business. No new business is to be accepted.

6.3. In so far as the existing business in Copenhagen has not been wound up and or cannot be transferred by 31 December 2011, and its winding up requires active management, Copenhagen may continue as a temporary location until the remaining business has finally been wound up or has expired. In that case the office being phased out will (1) have the bare minimum of staff and equipment required for actively winding up the business, (2) acquire no new business, (3) serve no core bank clients and (4) be closed down immediately once its portfolios have been dismantled. The office in question is to be assigned immediately to the restructuring unit.

6.4. HSH may retain the following offices:

— Hamburg
— Düsseldorf
— Munich
— Hannover
— London
— Hong Kong
— New York
— Kiel
— Berlin
— Stuttgart
— Singapore
— Luxembourg
— Athens

6.5. The London and New York operations will be downsized by 31 December 2012 at the latest, and by the same date the Hong Kong branch will be transformed into a representative office. From 31 December 2012, the Luxembourg branch will remain solely as a branch of the Restructuring Unit.

7.1. **[Holdings]** HSH is to sell the holdings mentioned in Annex III on the dates specified there in greater detail.

7.2. HSH may postpone a sale of the holdings referred to in Annex III for no longer than […] until […] at the latest if it should transpire after obtaining binding offers that the proceeds obtained by the transaction would be lower than the book value of the holding in the individual accounts drawn up by HSH in accordance with the German Commercial Code (HGB).

7.3. The holdings marked with an asterisk '*' in Annex III (particularly in the leasing and energy sectors) include outside financing by HSH whose duration in each case may extend beyond the date of sale stated in Annex III. If HSH cannot redeem those holdings together with the underlying loans, the sale of the holdings can be postponed for no longer than […] until […] at the latest.

7.4. The proceeds of the sale of HSH's holdings are to be used entirely to finance the company's restructuring plan.

7.5. The existing business from holdings that have not been sold within the deadlines laid down in points 7.1 to 7.3 is to be transferred or allowed to expire after the relevant deadline upon the maturity of the underlying business. No new business is to be accepted.

8. **[Trading for own account]** HSH is to end dedicated proprietary trading. This means that HSH is to carry on only trading activities indicated in its trading book that are necessary either (a) for accepting, transferring and executing its customers sales and purchase orders (i.e. trading with financial instruments as a service, up to a value measured in value at risk of EUR […]/1 day/99 % confidence) or (b) for hedging customer business or interest and liquidity management in the treasury sector (so-called trading for own account, up to a value measured with value at risk of EUR […]/1 day/99 % confidence) or (c) so that the economic transfer of balance sheet items to the restructuring unit or to third parties can be carried out (up to a value measured in value at risk of EUR […]/1 day/99 % confidence). As those positions can be taken on only within the limits defined above, they cannot jeopardise the sustainability or liquidity situation of HSH. Under no circumstances will HSH carry on business activities that serve purely to make a profit apart from the purposes mentioned in (a), (b) or (c).

9.1. **[Liquidity/funding]** Starting from 31 December 2012 and until 31 December 2014, HSH will fulfil the following liquidity indexes at the end of each year:

9.2. Net stable funding ratio (NSFR) of […] and liquidity coverage ratio (LCR) of […]. Once the corresponding liquidity indexes under Basel III have to be fulfilled by all the affected institutions, an additional premium of […] will be taken into account.

9.3. The share of the core bank's USD business that is refinanced by means of USD-denominated funding (and not through swaps) will develop as follows from 2012 to 2014: at least […] by the end of 2012, at least […] by the end of 2013 and at least […] by the end of 2014.

10. **[Advertising]** HSH must not use the granting of the aid measures or any advantages over competitors arising therefrom for advertising purposes.

11.1. **[Assurances regarding corporate governance]** All members of the supervisory board are to have the competences stated in the first sentence of Section 36(3) of the German Banking Act. They are competent if they are reliable and have the required expertise to perform regulatory functions, and to assess and monitor HSH's business transactions.

11.2. There must be no more than twenty supervisory board members. HSH and the public-sector owners must aim to reduce that number to sixteen at the end of the present board's term of office.

11.3. At least half the seats allocated to the *Länder* of Hamburg and Schleswig-Holstein are to be occupied by external experts.

12.1. **[Remuneration of bodies, employees and essential agents]** HSH must verify the incentive effect and appropriateness of its remuneration systems and ensure, using the possibilities under civil law, that they do not result in exposure to undue risks, are oriented towards sustainable, long-term company objectives, and are transparent. That obligation will be satisfied if HSH's remuneration systems meet the requirements in point 13.2 of the Annex 'Obligations of HSH' to the contract on the provision of a guarantee framework' of 2 June 2009.

12.2. In the context of the possibilities under civil law, HSH is to remunerate its bodies, employees and essential agents in line with the following principles:

(a) Its employees and essential agents must not receive any inappropriate salaries, salary components, bonuses, or any other inappropriate benefits.

(b) The salary paid to HSH's representatives and to its leading employees must be restricted to an appropriate level, whereby particular account should be taken of

— the relevant person's contribution to HSH's economic state, especially in the context of previous business policies and risk management; and

— the necessity of a market-oriented salary so as to be able to employ particularly suitable persons who can achieve sustainable economic growth.

(c) Salaries, salary components and bonuses are considered to be inappropriate if they do not meet the principles laid down in the Annex 'Obligations of HSH' to the contract on the provision of a guarantee framework of 2 June 2009. In particular, the payment of a cash remuneration to its bodies, employees and essential agents in the case of HSH's inability to pay a dividend (*Dividendenfähigkeit*) will be considered inappropriate if it exceeds EUR 500 000 a year.

13.1. **[Discontinuation of obligations]** If the public-sector owners relinquish control within the meaning of Article 3 of Regulation (EC) No 139/2004 (joint and sole control) over HSH after 31 December 2013, then the commitments in points 4, 5, 8, 9, 10, 12, 13 and 15 of this Annex, and the conditions in points 2, 3 and 4 of Annex II, no longer apply. The commitment in point 5 will nonetheless apply for at least 3 years.

13.2. **[Independence of the buyer]** The buyer of HSH must be independent of the public-sector owners. A buyer is independent of the public-sector owners if they are not able to exercise control within the meaning of Article 3 of Regulation (EC) No 139/2004 over the buyer at the time of sale. A buyer is independent of HSH if, at the time of sale, HSH has neither any direct or indirect shares in the buyer, nor any other connections under corporate law with the buyer. The Commission must confirm the buyer's independence. The public-sector owners confirm that the term 'the public-sector owners' covers all their constituent levels (*Länder*, municipalities), public institutions and publicly controlled companies. It does not exclude a sale involving, for example, one or more Landesbanks following the Commission's prior approval.

14. **[Other rules of conduct]** In the context of its lending and investing, HSH will take into account the borrowing requirements of the economy, in particular the requirements of medium-sized businesses, through conditions that are in line with market practice and appropriate from a supervisory/banking point of view. HSH must continue to expand its risk-monitoring operations. HSH's commercial policy must be prudent, sound and oriented towards sustainability.

15. **[Transparency]** During the implementation of the Decision, the Commission is to have unlimited access to all information necessary for monitoring its implementation. The Commission may ask HSH to provide explanations and clarifications. Germany and HSH are to cooperate fully with the Commission in response to any request in connection with monitoring and implementation of this Decision.

ANNEX II

LIST OF CONDITIONS REFERRED TO IN ARTICLE 2

The restructuring phase is to end on 31 December 2014. The following conditions apply during the restructuring phase, provided the commitment in question does not state otherwise.

1.1. **[Remuneration of the guarantee]** The contract concluded between HSH Finanzfonds AöR and HSH on 2 June 2009 on the provision of a guarantee framework (the 'guarantee provision contract') will be amended as follows or supplemented with further documentation in order to bring the remuneration into line with the requirements of the Commission Communication on the treatment of impaired assets in the Community banking sector[91].

1.2. The premium of 400 bps p.a. on a second-loss tranche of EUR 10 billion (the 'basic premium') will be supplemented by an additional premium amounting to 385 bps. The guarantee provision contract will lay down that the basis for the calculation of the amount of the basic premium and the additional premium (EUR 10 billion) will be reduced by (partial) cancellation of the guarantee but not by drawing on the guarantee. In so far as HSH Finanzfonds AöR also remains liable for reference undertakings following a (partial) cancellation to zero (i.e. up to no more than the amount of the last nominal value of the guarantee before the partial cancellation to zero), the (partial) cancellation to zero will not have the effect of reducing the basis of assessment.

1.3. In addition to an *ex nunc* reduction of the basis for assessment of the basic premium and the additional premium in accordance with point 1.2 of this Annex, partial cancellations will also result in a repayment of the additional premium paid on the partially cancelled amount in the past. The repayment of the additional premium in the event of partial cancellations will be made regardless of the actual settlement dates with effect from the partial cancellation in question. Repayments will be effected firstly by reducing the debtor warrant (*Besserungsschein*) in line with point 1.7 of this Annex and then through the repayment from the account in line with paragraph 1.6 of this Annex.

1.4. (Partial) cancellations of the guarantee may be carried out only in so far as it is not to be expected, according to HSH's planning at the time of notification of the (partial) cancellation in question, that as a result the share of HSH's common equity capital will fall below [8,5–9,5] % as at 31 December 2011, [9–10] % as at 31 December 2012, [9,5–10,5] % as at 31 December 2013, and [10–11] % as at 31 December 2014 (calculated in each case in accordance with the binding regulatory requirements regarding credit institutions' capital adequacy which are in force at the above-mentioned points in time). A partial cancellation may not take place if, although the above ratios are met at the time of the partial cancellation, they would no longer be so in the light of conservative estimates in the following years. The various stages of the decision-making process defined within HSH for a partial cancellation will incorporate that conservative approach, taking account of risk-bearing capacity as an important deciding factor, and will also include in the case of each partial cancellation the approval of BaFin.

1.5. The additional premium will be calculated retroactively from 1 April 2009 and on a pro rata basis for parts of financial years. It will be payable annually together with the basic premium. For the years 2009 and 2010, it will be payable four weeks after the amendment to the guarantee provision contract described in point 1.1 of this Annex comes into force.

1.6. The additional premium will be paid into an account to be set up by HSH Finanzfonds AöR with HSH. It will not affect HSH Finanzfonds AöR's control over the additional premium.

1.7. In so far as the obligation to pay the additional premium would result in HSH's ratio of common equity, calculated in accordance with the regulatory requirements in force at the time and including market price risks (common equity ratio), falling below 10 % (minimum common equity ratio) at the time the additional premium entitlement arises, or if an already existing shortfall increases further, HSH Finanzfonds AöR will waive that part of the entitlement which would lead to the common equity ratio falling below the minimum common equity ratio (deferred additional premium entitlement), with effect from the time the entitlement arises in return for the provision of a debtor warrant pursuant to the provisions of this point of this Annex:

(a) The debtor warrant will take the following form: In so far as the common equity ratio at the end of one of HSH's financial years following the provision of the debtor warrant and according to all expense and profit-related accounts, but without taking account of the entitlements under the debtor warrant, exceeds the minimum common equity ratio, the deferred additional premium entitlement will be restored in an amount ensuring that the minimum common equity ratio is met.

(b) The deferred additional premium entitlement will be restored for the duration of the debtor warrant in each financial year in which the requirements pursuant to (a) are met, but only up to the amount of the completely restored additional premium entitlement.

(c) The debtor warrant will mature on 31 December [2030–2050].

(d) In so far as HSH applies for entitlement to the additional premium to be waived against provision of a debtor warrant due to the common equity ratio falling below the minimum common equity ratio, it will submit corresponding calculations, which will be subject to review by the statutory auditor of HSH.

1.8. The additional premium will be payable until [2015–2025] at the latest. Notwithstanding that requirement, the basic premium and the additional premium will be payable at the latest up to the time when the total from partial cancellations and claims on the guarantee amounts to EUR 10 billion.

1.9. HSH will in the framework of what is legally permissible make every reasonable effort to effect complete payment of the additional premium as quickly as possible. In particular, HSH and also the public-sector owners and HSH Finanzfonds AöR will, by exercising the voting rights to which they are entitled from shares in HSH, endeavour as far as legally possible to ensure that no reserves and retained earnings are liquidated which are intended to permit payments to profit-dependent equity capital instruments (such as hybrid financial instruments or profit participation certificates). Point 2 below is unaffected.

1.10. In the case of legal separation of the restructuring unit and the core bank, both banks will pay the basic premium of 400 bps in proportion to the distribution of the portfolio covered by the guarantee. The core bank moreover will continue to be jointly and severally liable for the remuneration of the guarantee on the portfolio of the restructuring unit. That liability of the core bank may be cancelled at the initiative of the public-sector owners. In the event of legal separation, only the core bank will be liable for payment of the additional premium.

1.11. **[Lump-sum payment and capital increase]** HSH Finanzfonds AöR and HSH will amend the contract concluded on 2 June 2009 on the provision of a guarantee framework, or supplement it with further documentation, so as to ensure that HSH Finanzfonds AöR has a claim against HSH to a lump-sum payment with a nominal value of EUR 500 million. HSH Finanzfonds AöR will further contribute the claim for such lump-sum payment to HSH by way of a contribution in kind. The amendment of the guarantee provision contract will be initiated without delay after the date of this Decision and no later two months after the date of its notification.

1.12. HSH and HSH Finanzfonds AöR will make every reasonable effort to bring about, within four months from the date of this Decision, a resolution of the general meeting of shareholders on a capital increase amounting to the net value of the lump sum payment claim (issue price and premium) and, within one month of the general meeting, the contribution to HSH's capital of the claim for a lump-sum payment. The issue price will be calculated on the basis of the value of HSH as of the day of the resolution of the general meeting of shareholders on such capital increase and the value of the lump-sum payment claim.

1.13. The capital increase will take place either through ordinary contribution in kind, with no right of option for minority shareholders, or through a mixed capital increase by way of contribution in kind and cash, with a right of option regarding the cash portion for all shareholders other than HSH Finanzfonds AöR regarding the cash portion. HSH and HSH Finanzfonds AöR will make every reasonable effort to bring about the coming into effect of the capital increase within 18 months following the resolution of the general meeting of shareholders. HSH Finanzfonds AöR and HSH may choose the form of the capital increase which will guarantee speedier implementation and entry in the commercial register.

1.14. The claim to the lump-sum payment may not be converted into a debtor warrant if the minimum common equity ratio of 10 % is not met.

1.15. If there is a sale of shares by the public-sector owners, the amount of the additional premium can be reduced at their initiative in proportion to their direct and indirect share.

2. **[Hybrids]** Until 31 December 2014, HSH may not make any payments in respect of profit-related equity instruments (such as hybrid financial instruments and profit participation certificates (*Genussscheine*)), in so far as those payments are not owed on the basis of a contract or the law. If HSH's balance sheet, before adjustment of reserves and retained earnings, shows a loss, those instruments will also participate in the loss. There will be no participation in losses brought forward from previous years.

3. **[Dividend ban]** HSH will not pay dividends in the period up to and including the financial year ending 31 December 2014.

4. **[Protection of reserves]** In the period from 1 January 2015 until 31 December 2016, dividend payments may not exceed 50 % of the annual surplus for the previous financial year. Furthermore, dividend payments may be made during that period only in so far as they do not jeopardise compliance with the Basel III provisions on the capital of credit institutions in the medium-term.

ANNEX III

TIME OF SALES OF HOLDINGS (DATE OF SIGNING OF SALES CONTRACT) IN ACCORDANCE WITH POINT 7.1 OF ANNEX I

The holdings marked with an asterisk '*' in the Table below include outside financing by HSH (especially in the leasing and energy sectors) with terms that may extend beyond the intended date of sale of the holding in question (see point 7.3 of Annex I).

Name	Date of sale
[…]	[…]
Aegean Baltic Bank SA	sold
[…]	[…]
[…]	[…]
[…]	[…]
Albes Verwaltungsgesellschaft mbH (formerly Albes Grundstücksverwaltungsgesellschaft mbH)	wound up
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
BEG Baugrundentwicklungsgesellschaft mbH i. L.	liquidated
BIKO Grundstücks-Verwaltungsgesellschaft mbH & Co. KG i. L.	liquidated
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
CRE Financial Group LLC	inactive
Credaris Portfolio Management GmbH	inactive

[…]	[…]
DOLANA Grundstücksverwaltungsgesellschaft mbH & Co. Objekt Sehnde KG	inactive
[…]	[…]
[…]	[…]
Embley Investment Funds	sold
[…]	[…]
[…]	[…]
[…]	[…]
Freebay Holdings LLC	inactive
[…]	[…]
[…]	[…]
[…]	[…]
Gesellschaft bürgerlichen Rechts der Altgesellschafter der Deutschen Leasing AG (GbR)	inactive
GLB GmbH & Co. OHG (DekaBank holding)	inactive
GLB-Verwaltungs-GmbH	inactive
[…]	[…]
[…]	[…]
GR Holding 2009 A/S (formerly Gudme Raaschou Bank A/S)	sold
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
HSH N Real II GmbH	wound up
[…]	[…]
HSH Nordbank Private Banking SA – silent participation	settled
[…]	[…]

[…]	[…]
[…]	[…]
HSH Structured Finance Services GmbH	Wound up
[…]	[…]
[…]	[…]
[…]	[…]
Lamatos GmbH	wound up
Leashold Verwaltungs-GmbH & Co. KG	2013
[…]	[…]
[…]	[…]
Mietdienst Gesellschaft für Investitionsgüterleasing mbH & Co. Leasinggesellschaft	inactive
Minerva GmbH	wound up
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
Nordic Blue Container Ltd	inactive
[…]	[…]
NORDIC BLUE CONTAINER VI Ltd	inactive
NORDIC BLUE CONTAINER VII Ltd	inactive
Norship Italia Srl	liquidated
[…]	[…]
Nubes GmbH	inactive
Pellecea GmbH	wound up
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
Rumina GmbH	wound up

[…]	[…]
[…]	[…]
[…]	[…]
Solent Holding II GmbH	Sold
[…]	[…]
Spielbank SH GmbH	Sold
Spielbank SH GmbH & Co. Casino Flensburg KG	Sold
Spielbank SH GmbH & Co. Casino Kiel KG	Sold
Spielbank SH GmbH & Co. Casino Lübeck-Travemünde KG	Sold
Spielbank SH GmbH & Co. Casino Stadtzentrum Schenefeld KG	Sold
Spielbank SH GmbH & Co. Casino Westerland auf Sylt KG	Sold
Sun Edison LLC	Sold
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
TERRANUM Gewerbebau GmbH & Cie	wound up
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
[…]	[…]
White Sails Limited	liquidated
Yara Sourcing Oy	liquidated

(**1**) Commission Decision in case C 10/09 (ex N 138/09) *ING* (OJ C 158, 11.7.2009, p. 13).

(**2**) Commission Decision of 29 May 2009 in case N 264/09 *HSH Nordbank AG* (OJ C 179, 1.8.2009, p. 1).

(**3**) With effect from 1 December 2009, Articles 87 and 88 of the EC Treaty have become Articles 107 and 108, respectively, of the Treaty on the Functioning of the European Union; the two sets of provisions are in substance identical. For the purposes of this Decision references to Articles 107 and 108 of the TFEU should be understood as references to Articles 87 and 88 of the EC Treaty when appropriate.

(**4**) Commission Decision of 22 October 2009 in case N 503/09 *HSH Nordbank AG* (OJ C 281, 21.11.2009, p. 42).

(**5**) OJ C 281, 21.11.2009, p. 42.

(**6**) The investors advised by Flowers are: HSH Alberta I LP, HSH Alberta II LP, HSH Luxembourg Sàrl., HSH Delaware LP, HSH Alberta V LP, HSH Coinvest (Alberta) LP, and HSH Luxembourg Coinvest Sàrl.

(**7**) Before the implementation of the rescue measures the respective shareholdings had been as follows: Hamburg 30,41 %, Schleswig-Holstein 29,10 %, SGVSH 13,20 %, SVB 1,62 % and Flowers 25,67 %.

(**8**) *Anstaltslast* conferred rights on a financial institution vis-à-vis its owners, whereas *Gewährträgerhaftung* provided for rights of the creditors of the financial institution *vis-à-vis* the owners. Those guarantees have been abolished pursuant to the Commission Decision in case E 10/2000 (OJ C 146, 19.6.2002, p. 6 and OJ C 150, 22.6.2002, p. 7). According to that Decision all liabilities that arise in a transitional period from 2001 to 2005 which mature before 2015 are still covered by the guarantees. As at 31 December 2009 liabilities covered by those guarantees amounted to EUR 56 billion.

(**9**) Commission Decisions C(2004) 3928 final and C(2004) 3930 final of 20 October 2004 on Hamburgische Landesbank – Girozentrale (case C 71/02) and Landesbank Schleswig-Holstein – Girozentrale (case C 72/02).

(**10**) EUR 488 million in ordinary share capital and EUR 68 million in the form of preference shares.

(**11**) Commission Decision of 6 September 2005 in case NN 71/05 – Capital increase HSH Nordbank AG.

(**12**) Hamburg EUR 108,2 million, Schleswig-Holstein EUR 498,1 million, the SGVSH EUR 78,3 million.

(**13**) At the end of 2007, the public-sector shareholders of HSH had already converted silent participations of EUR 578 million into ordinary shares and, in that connection, Flowers bought a portion of the new shares for EUR 166 million in order to avoid a dilution of their shareholdings. That transaction, conducted on equal terms, had already been agreed between the public and private shareholders in 2006, when the trusts entered into the capital of HSH.

(**14**) Confidential information […]

(**15**) Fitch, Moody’s and Standard & Poor’s (‘S&P’).

(**16**) The rating uplift corresponds to the number of notches the credit rating of an institution exceeds its stand-alone rating (or Bank Financial Strength Rating (‘BFSR’)) due to external credit support elements (i.e. the probability that the bank will receive external support from third parties such as its owners, its industry group, or official institutions).

(**17**) According to Moody’s definition of stand-alone ratings, BSFRs represent the rating agency’s opinion of a bank’s intrinsic safety and soundness and, as such, exclude certain external credit support elements (i.e. public ownership). BFSRs do not take into account the probability that the bank will receive such external support, nor do they address risks arising from sovereign actions that may interfere with a bank’s ability to honour its obligations. BFSRs are a measure of the likelihood that a bank will require assistance from third parties such as its owners, its industry group, or official institutions.

(**18**) The rating category E contains banks with very modest intrinsic financial strength, with a higher likelihood of periodic outside support or an eventual need for outside assistance.

(**19**) In the context of the so-called 'grandfathering' which was agreed as an interim solution, liabilities which were incurred from 18 July 2001 to 18 July 2005 and which mature no later than 31 December 2015 will continue to be covered by '*Gewährträgerhaftung*'.

(**20**) As per 31 December 2007, the CIP contained amongst other assets US subprime and synthetic Collateralised debt obligations.

(**21**) Moody's Analytics CDOROM is a Monte Carlo simulation model used to calculate the expected loss on tranches of a given static portfolio of assets. It is used by rating analysts at Moody's Investors Services to assign ratings on static synthetic CDOs. Similar models and methodologies were used to assess expected losses in other impaired assets measures.

(**22**) Commission Decision of 27 October 2008 in case N 512/08 *German bank rescue scheme* (OJ C 293, 15.11.2008, p. 2), as amended by Commission Decision of 12 December 2008 in case N 625/08 *German bank rescue scheme*, extended by Commission Decision of 22 June 2009 in case N 330/09 (OJ C 160, 14.7.2009, p. 4).

(**23**) Following the creation of the restructuring unit, the bank was split into two divisions, the restructuring unit and the core bank. The core bank is the unit actively engaged in business operations as the restructuring unit is in wind-down. Eventually the bank will be reduced to its core bank.

(**24**) The most basic or standard version.

(**25**) […]. Once the corresponding liquidity indexes under Basel III have to be fulfilled by all the affected institutions, an additional premium of […] % will be taken into account.

(**26**) OJ C 72, 26.3.2009, p. 1.

(**27**) OJ C 195, 19.8.2009, p. 9.

(**28**) Recital 37 of the Decision initiating the procedure.

(**29**) OJ C 155, 20.6.2008, p. 10.

(**30**) Submission by Germany of 17 December 2009 referring to the judgment of the General Court in Joined Cases T-129/95, T-2/96 and T-97/96 *Neue Maxhütte Stahlwerke GmbH und Lech-Stahlwerke GmbH* v *Commission* [1999] ECR II-17, paragraph 119.

(**31**) Case T-98/00 *Linde AG* v *Commission* [2000] ECR II-3961.

(**32**) In the modified restructuring plan the number of closures of international locations has been revised from 12 to 15.

(**33**) Submission by Germany, p. 35, HSH initial restructuring plan of 1 September, Chapter 7.1.1.

(**34**) Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty (OJ L 83, 27.3.1999, p. 1).

(**35**) Case C-482/99 *France* v *Commission* (*Stardust Marine*) [2002] ECR I-4397.

(**36**) Joined Cases T-228/99 and 233/99 *WestLB v Commission* [2003] ECR II-435, paragraph 316.

(**37**) Commission Decision of 24 July 2009 in case C 15/09 *HypoRealEstate*, point 47 (the opening decision in *HypoRealEstate* where the issue price was about three times as high as the stock-market price); Commission Decision of 14 January 2009 in case N 9/09 *Anglo-Irish Bank* (OJ C 177, 30.7.2009, p. 1).

(**38**) Commission decision of 7 May 2009 in case N 244/09, recital 104.

(**39**) Hamburg Gesetz zum Staatsvertrag zwischen der Freien- und Hansestadt Hamburg und dem Land Schleswig-Holstein über die Errichtung der 'HSH Finanzfonds AöR' als rechtsfähige Anstalt des öffentlichen Rechts, HmbGVBl. 2009, p. 95; Schleswig-Holstein Gesetz zum Staatsvertrag zwischen der Freien- und Hansestadt Hamburg und dem Land Schleswig-Holstein über die Errichtung der 'HSH Finanzfonds AöR' als rechtsfähige Anstalt des öffentlichen Rechts, GVOBl. 2009, p. 172.

(**40**) Recital 44 of the Rescue Decision.

(**41**) See Case C-494/06 P *Commission* v *Italy* [2009] ECR I-3639, paragraph 50; Case 248/84 *Germany* v *Commission* [1987] ECR 4013, paragraph 18; and Case T-357/02 *Freistaat Sachsen* v *Commission* [2007] ECR II-1261, paragraph 31.

(**42**) Recitals 33 and 34 of the Rescue Decision.

(**43**) Case T-98/00 *Linde AG* v *Commission* [2000] ECR II-3961, paragraph 49.

(**44**) Commission Decision in case E 10/2000 *State guarantee for public banks in Germany* (OJ C 146, 19.6.2002, p. 6, point 2).

(**45**) Commission Decision in case C 9/08 *SachsenLB* (OJ C 71, 18.3.2008, recital 82).

(**46**) Case C-334/99 *Gröditzer Stahlwerke* [2003] ECR I-1139, paragraph 133; Joined Cases C-278/92, C-279/92 and C-280/92 *Spain* v *Commission (Hytasa)* [1994] ECR I-4103, paragraph 22.

(**47**) See recital 77 of the *IKB* Decision of 21 October 2008 (OJ L 278, 23.10.2009, p. 32); recital 122 of the *Lloyds* Decision of 18 November 2009 (OJ C 46, 24.2.2010, p. 2); recital 95 of the *Ethias* Decision of 20 May 2010 (OJ C 252, 18.6.2010, p. 5); recital 47 of the *Sparkasse KölnBonn* Decision of 4 November 2009 (OJ C 2, 6.1.2010, p. 1).

(**48**) Paragraph 15 of the Impaired Assets Communication.

(**49**) Guarantees Notice, point 1.3; Commission Decision of 16 December 2003 in case N 512/03 *Guarantee scheme on ship financing* (OJ C 62, 11.3.2004.)

(**50**) See Case C-334/07 P *Commission* v *Freistaat Sachsen* [2008] ECR I-9465.

(**51**) Case C-334/07 P *Commission* v *Freistaat Sachsen* [2008] ECR I-9465, paragraph 59.

(**52**) See Commission Decision in case C 9/09 on aid to Dexia SA in the form of a guarantee on bonds and certain assets, liquidity assistance and a capital increase (OJ L 274, 19.10.2010, p. 54).

(**53**) See point 39 of the Impaired Assets Communication.

(**54**) That conclusion is in line with the Commission's preliminary analysis of the market value of the shielded portfolio, which concluded that the market value was between EUR [150 – 180] billion (see recital 38 of the Decision initiating the procedure).

(**55**) Commission Decision of 27 October 2008 in case N 512/08 *German bank rescue scheme* (OJ C 293, 15.11.2008, p. 2), amended by Commission Decision of 12 December 2008 in case N 625/08 *German bank rescue scheme*, prolonged by Commission Decision of 22 June 2009 in case N 330/09 (OJ C 160, 14.7.2009, p. 4), and by Commission Decision of 23 June 2010 in case N 222/10 (OJ C 178, 3.7.2010, p. 1).

(**56**) Communication from the Commission on the application, from 1 January 2011, of State aid rules to support measures in favour of banks in the context of the financial crisis (OJ C 329, 7.12.2010, p. 7).

(**57**) See paragraph 105.

(**58**) See Commission Decision of 22 December 2009 in case N 555/09 *Additional aid for WestLB AG related to spin-off of assets* (OJ C 66, 17.3.2010, p. 15, recital 56). See also Commission Decision of 30 June 2009 in case C 17/09 *Recapitalisation and asset relief for LBBW* (OJ C 248, 16.10.2009, p. 7, recital 18), and Commission Decision of 15 December 2009 in case C 17/09 *Restructuring of LBBW* (OJ L 188, 21.7.2010, p. 1, recitals 49-55).

(**59**) For example, cash flow-based valuations of land and development loans were performed to assess the REV of assets transferred in the context of the Irish National Asset Management Agency (see Commission Decision *Establishment of a National Asset Management Agency (NAMA)*: OJ C 94, 14.4.2010). Additionally, the expected credit losses of shipping loans were also valued in the context of the impaired asset measure put in place for Royal Bank of Scotland (Commission Decision *Restructuring of Royal Bank of Scotland and participation in the Asset Protection Scheme* (OJ C 119, 22.4.2010)).

(**60**) OJ L 188, 21.7.2010, recitals 64 and 65.

(**61**) See recital 65 of the Commission Decision of 27 October 2008 in case N 512/08 *German bank rescue scheme* (OJ C 293, 15.11.2008, p. 2). According to the current legal provisions the Tier 2 capital must not exceed 100 % of the Tier 1 capital. Equity capital can accordingly consist of 50 % of Tier 1 capital and 50 % of Tier 2 capital in order to meet the regulatory requirements. As there is a difference of 1,5 % for the pricing of Tier 1 and Tier 2 capital, according to the European Central Bank's recommendation on recapitalisations of 20 November 2008, a reduction of 150 basis points is appropriate. Assuming that 7 % is an appropriate remuneration for unfunded Tier 1 capital according to the Recapitalisation Communication (Communication from the Commission - The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition (OJ C 10, 15.1.2009)), Tier 2 capital is to be remunerated at 5,5 %. The average of the two rates is 6,25 %.

(**62**) Original amount of the guarantee minus cancellations but not reduced by drawings.

(**63**) The additional premium cannot exceed the basic premium, because the amount ultimately drawn cannot exceed the outstanding nominal amount of the guarantee, and because the level of the premium in basis points is lower than the basic premium

(**64**) Commission Decision in State aid C 10/09 for ING's illiquid assets back-facility and restructuring plan (OJ L 274, 19.10.2010, p. 139).

(**65**) Commission Decision in case C 17/09 *LBBW* (OJ L 188, 21.7.2010, p. 1).

(**66**) Commission Decision in case C 26/09 *Parex* (OJ L 163, 23.6.2011, p. 28).

(**67**) Recital 59.

(**68**) As a result of margin calls on its cross-currency swap positions, HSH experienced severe liquidity problems during the crisis.

(**69**) Recital 61.

(**70**) The Commission in its analysis differentiates between volatile and cyclical activities. Cyclical activities are activities whose performance is closely linked to the economic cycle. Volatile activities are activities which show large differences in performance from one period to another. The volatility typically results from the fact that the business activity is prone to unpredictable events beyond the fluctuations attributable to the economic cycle (for example natural disasters or geopolitical events such as terrorism etc.). The Commission views HSH's air transport and shipping activities as being both volatile and cyclical.

(**71**) They include shipping, transport financing (both viewed as volatile and cyclical), real estate, financial market activities and corporate (cyclical).

(**72**) The in-depth viability analysis showed that without the recapitalisation and impaired assets measures, HSH's Tier 1 capital would have dropped to […] % in 2010, i.e. a […] % fall from its peak in 2008.

(**73**) Under Basel III, the minimum common equity ratio must be 7,00 % (including the conservation buffer). The new Tier 1 capital ratio must be 8,00 % (including conservation buffer).

(**74**) See Table 7.

(**75**) See Commission Decision 1999/99/EC of 3 March 1998*Sicilian Regional Law* (OJ L 32, 5.2.1999, p. 18, recital 30); Commission Decision 98/476/EC of 21 January 1998*Tax concession* (OJ L 212, 30.7.1998, p. 50); Commission Decision 1999/705/EC of 20 July 1999*Dutch service stations* (OJ L 280, 30.10.1999, p. 87); Commission Decision 97/303/EEC of 14 January 1997*Industrial Modernisation Fund* (OJ L 152, 12.6.1987); judgment of the Court of Justice in Case 102/87 *French Republic* v *Commission (Codevi)* [1988] ECR 4067; and Commission Decision in Case C 52/05 *Digital Decoders* (OJ L 147, 8.6.2007, p. 1, recital 116), upheld by the Court of Justice in Case C-403/10 P *Mediaset* v *Commission*, not yet published.

(**76**) Case 173/73 *Italy* v *Commission* [1974] ECR 709, paragraph 27, and Case C-241/94 *France* v *Commission* [1996] ECR I-4551, paragraph 20.

(**77**) Commission Decision of 4 June 2008 in case C 9/08 *SachsenLB* (OJ L 104, 24.4.2009, p. 34).

(**78**) PricewaterhouseCoopers, *Indikative Unternehmensbewertung der HSH Nordbank AG, Hamburg und Kiel, zum 31. März 2009, Stand: 15. Mai 2009.*

(**79**) Valuation Report, p. 150-152.

(**80**) Valuation Report, p. 98, 101 (Funding planning and planning of liquidity costs), p. 150 (summary).

(**81**) Valuation Report, p. 152 (summary), second bullet point.

(**82**) Commission Decision of 18 July 2011 in Case C 15/09 *Hypo Real Estate*, recital 121, not yet published.

(**83**) See Commission Decision of 4 November 2009 in case C 32/09 *Sparkasse KölnBonn* (OJ C 2, 6.1.2010, p. 1).

(**84**) That reduction figure is based on the assumption of an accounting value of derivatives on the asset side of EUR[…] billion in 2014 (see Table 9); if the value of derivatives on the asset side is higher, the total balance sheet could exceed the target reduction. If the balance-sheet total is exceeded because of a higher share of derivatives or a fall in the EUR/USD exchange rate, this will not have any detrimental effects.

(**85**) HSH had initially planned to increase its new business volume in the aviation segment by 25 % from 2010 to 2014 and to quadruple its market share.

(**86**) See, e.g., Commission Decision in case C 36/A/06 *ThyssenKrupp, Cementir and Nuova Terni Industrie Chimiche*, recital 8 (explanation of the splitting of the case) (OJ L 144, 4.6.2008, p. 37); Commission Decision in case C 38/A/04 *Alcoa Transformazioni*, recital 9 (explanation of the split of the case) (OJ L 227, 28.8.2010, p. 62).

(**87**) Case C-382/99 *Netherlands* v *Commission* [2002] ECR I-5163.

(**88**) EUR […] billion is the projected value of derivatives in both 2012 and 2014.

(**89**) EUR […] billion is the projected value of derivatives in both 2012 and 2014.

(**90**) EUR […] billion is the projected value of derivatives in both 2012 and 2014.

(**91**) OJ C 72, 26.3.2009, p. 1.