


EFTA SURVEILLANCE AUTHORITY

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EFTA SURVEILLANCE AUTHORITY DECISION

OF 30 DECEMBER 1994

**TO PROPOSE APPROPRIATE MEASURES TO FINLAND
WITH REGARD TO AID TO BANKS**

THE EFTA SURVEILLANCE AUTHORITY,

Having regards to the Agreement on the European Economic Area¹, in particular to Protocol 26 and Articles 61 to 63,

Having regard to the Agreement between the EFTA States on the establishment of a Surveillance Authority and a Court of Justice², in particular to Article 24 and Article 1(1) of Protocol 3 thereof,

WHEREAS,

I. FACTS

1. Introduction - procedural situation

Article 1(1) of Protocol 3 to the Surveillance and Court Agreement provides that "The EFTA Surveillance Authority shall, in cooperation with the EFTA States, keep under constant review all systems of aid existing in those States. It shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the EEA Agreement".

By letter of 4 January (1994/467D) the EFTA Surveillance Authority requested the submission of information on existing State aid in Finland, i.a. by reference to the above provision of Protocol 3 to the Surveillance and Court Agreement. Finland submitted this information on 3 March (1994/470A).

¹Hereinafter referred to as the EEA Agreement

²Hereinafter referred to as the Surveillance and Court Agreement

On 31 January 1994 an informal meeting on banks support was held by the Surveillance Authority. At this meeting representatives from the EFTA Surveillance Authority, the Swedish, Norwegian, Finnish and Austrian authorities participated.

At a meeting in Finland on 2 May 1994 the subject of state aid to banks was discussed at the Ministry of Finance. Following that meeting additional information on state aid to banks was submitted on June 28 1994 by the Finnish authorities (94-9597A).

After having carried out a preliminary assessment of the bank aid, further information and clarifications, in particular on existing aid was needed. At a meeting at the Ministry of Finance in Helsinki 19 September 1994, such clarifications were given by the Finnish authorities.

In the course of the autumn 1994 additional information has informally been submitted to the EFTA Surveillance Authority by the Finnish authorities.

2. Relevant provisions of the aid

The most important legal basis for granting the aid is the Act on the Government Guarantee Fund (379/92) and amendments to the Act (933/92), (246/93) and (857/93). The purpose of the Government Guarantee Fund is to safeguard the stability of the financial markets and of the activities of deposit banks and the claims of their depositors.

In Finland there exist three private deposit guarantee schemes for banks, one for the savings banks, one for the commercial banks and one for the co-operative banks. The objectives of these funds is to protect depositors. A bank that encounters problems of such a magnitude that its existence is threatened can seek support from such a fund.

The Government Guarantee Fund (hereafter referred to as the Fund), shall, under special conditions, grant **loans** to the three private guarantee funds of the banks and to Postipankki Ltd. These funds can then, in their turn, grant loans to the private banks. The Fund may also **guarantee** loans extended by the private funds. The Fund may also **subscribe shares and holdings** in a bank belonging to the Fund, provide **guarantees for loans taken by such a bank** and grant **other financial support** if this proves necessary to safeguard the stability of a bank's activities and that of the financial markets. Guarantees that are granted may concern both interest and principal. Guarantees will remain in force for a maximum of 10 years.

Eligible for support under the Act on the Government Guarantee Fund are banks with a Finnish charter including their subsidiaries and branches in Finland and abroad. A bank subsidiary of a foreign credit institution has to have a Finnish charter before starting its activities in Finland. Branches in Finland of foreign banks do not need a special Finnish charter under the EEA agreement.

The Fund is authorized to make decisions on aid up to a total maximum of FIM 20 billion of which the Fund has used about 17 billion. Decisions on guarantees are proposed by the Fund but taken by the Council of State.

The administration and operations of the Fund is supervised by a Supervisory Board comprising all the trustees appointed by Parliament at the time. The responsibilities of the Supervisory Board is inter alia to approve the Fund's rules, to confirm the Fund's annual budget, profit and loss account and balance sheet etc. The Supervisory Board has set up a number of criteria for granting support. One of these criteria is that the terms of support should be set in such a way that the support will promote efficiency and necessary structural changes in the banking system. Other criteria are;

- 1) Bank support is to be open and public
- 2) It should be endeavoured to minimize the attractiveness of bank support and the commitment of public funds to such support. Similarly, the owners of a bank receiving support are to be made financially responsible to the greatest possible extent.
- 3) The terms and conditions of support are to be set so as to promote efficiency and necessary structural change in the banking system.
- 4) It should be endeavoured to minimize the distortive effects of support measures on competition.
- 5) Distortive interest rate competition is not allowed.
- 6) The public authorities must be assured the possibility to supervise the re-organization of a bank receiving support. In particular, it should be endeavoured to assure that the support is not used to grant credit or to waive the collection of loans that have fallen due at terms differing from those normally applied.
- 7) The terms and conditions of employment of the management of a bank receiving support must be reasonable and any injustices should be eliminated.

It is also the responsibility of the Fund's Supervisory Board, to supervise the use of support granted to the banks.

Banks adhering to the Fund, pay a member ship fee to the Fund regardless of whether they have received support or not. It is the Board of Management that shall confirm the total sum of the annual payment to be collected from the banks and the grounds on which each bank's share is determined. The annual payment cannot exceed one ten thousandth of the combined total on the most recently approved balance sheets of the banks in the Fund. The annual payment for a branch office of foreign credit institution shall be determined according to the combined total sum of deposits by the public in the branch office. The annual payment shall be based on the risks taken by the bank in

its operations and the grounds for calculating it must be the same of all banks belonging to the Fund.

The act on the Fund was amended in October 1993 (857/93) in such a way that the Fund may own or administer shares of an asset management company whose purpose is to sell or otherwise transfer assets or liabilities of a bank subject to support measures taken by the State or the Fund. In November 1993 the Fund together with the State of Finland founded a special asset management company, Arsenal Ltd, whose responsibility is to administer and eventually liquidate the bad assets transferred to it.

The aid schemes in Finland were introduced before the entry into force of the EEA Agreement. They were introduced at a time when several Finnish banks were making substantial losses, when their share of non-performing loans were increasing and several banks encountered problems with fulfilling capital adequacy requirements. The aid measures were introduced at a time when Finland was affected by a deep recession. The situation for the banks have improved markedly. The aid schemes are, however, still legally in force. The Finnish authorities have informed the Authority that they plan to abolish the schemes as soon as possible but no formal time limits exist for the Government Guarantee Fund nor for the asset management company Arsenal.

II. APPRECIATION

The Act on the Government Guarantee Fund provides a framework for a wide range of measures to support banks directly or via the private insurance funds existing in Finland. Such measures include granting support loans, different forms of equity capital instruments as well as guarantees.

Support under the Act can be given under conditions which may constitute state aid within the meaning of Article 61(1) of the EEA Agreement. The provisions of the Act as well as the criteria set up by the Supervisory Board of the Fund are general and broad in scope and do not lay down exact criteria or limit the aid to certain maximum aid intensities. Therefore, by examining the legal provisions governing the aid, it is not possible for the EFTA Surveillance Authority to assess whether individual awards of aid disbursed under the Act would be compatible with Article 61 of the EEA Agreement.

In view of the general principles of state aid control, the EFTA Surveillance Authority considers basically three ways of adjusting the provisions at hand to the requirements of the EEA Agreement. The required adjustment could be effected by

- (a) abolishing the Act in question,
- (b) introducing criteria for the aid in accordance with the principles reflected in the relevant parts, e.g Chapter 15 on Aid for Rescue and Restructuring, of the Procedural and Substantive Rules in the Field of State Aid, or
- (c) notifying all individual awards of aid, including conditions which may be attached to such aid, based on the Act prior to implementation pursuant to Article 1 (3) of Protocol 3 to the Surveillance and Court Agreement.

Decisions to grant new aid under the act are to be done in circumstances where major difficulties in the banking sector have occurred. According to the information submitted by the Finnish authorities the situation in the banking sector has improved considerably and new aid would be granted rarely, if at all. Therefore, the EFTA Surveillance Authority considers option (c) to be the most appropriate means of adjusting aid under the Act on Government Bank Insurance Fund to the principles of State aid control under the EEA-Agreement.

Aid which may be granted to banks outside the existing schemes falls under the normal state aid control by virtue of Article 1(3) of Protocol 3 to the Surveillance and Court Agreement which obliges the Finnish authorities to notify individually such awards, if any, prior to their implementation. Such aid may include the selling of assets by the asset management company Arsenal to banks below market price.

In order to enable the EFTA Surveillance Authority to fulfil its review obligation under Article 1(1) of Protocol 3 to the Surveillance and Court Agreement, it is proposed that a detailed annual report on the aid under the Act on the Government Guarantee Fund shall be submitted.

HAS ADOPTED THIS DECISION:

1. The EFTA Surveillance Authority proposes to Finland, on the basis of Article 1(1) of Protocol 3 to the Surveillance and Court Agreement, the following appropriate measures with regard to the support measures based on the Act on the Government Guarantee Fund (valtion vakuusrahostosta annettu laki 379/92).

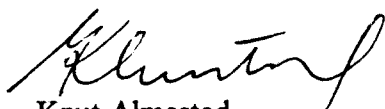
- (i) The Finnish authorities are obliged to notify all individual awards of aid under the Act prior to implementation pursuant to Article 1(3) of Protocol 3 to the Surveillance and Court Agreement.
- (ii) The Finnish authorities are obliged to submit a detailed annual report in accordance with chapter 30 of and Annex III to the Procedural and Substantive Rules in the Field of State Aid on the application of aid awarded under the Act.

2. Finland shall signify its agreement to the above proposal or otherwise submit its observations by 31 January 1995.

3. The Finnish Government is reminded of its obligation to notify all individual awards of aid to banks outside existing aid schemes prior to implementation pursuant to Article 1(3) of Protocol 3 to the Surveillance and Court Agreement.

Done in Brussels, 30 December 1994

For the EFTA Surveillance Authority



Knut Almestad
President



Heinz Zourek
College Member