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ROUNDTABLE ON EXIT STRATEGIES

-- Note by the Delegation of Spain --

This note is submitted by the delegation of Spain to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 16 - 17 June 2010.

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ROUNDTABLE ON EXIT STRATEGIES

-- Note by Spain[1] --

1. Since the outburst of the financial crisis in 2007, the Spanish government has implemented several measures so as to limit its impact. Those measures have focused on economic policy and public aid aimed at easing the crisis, but also on regulatory reforms put in place in order to strengthen the capacity of the Spanish economy to react in the event of future crises.

1. Public intervention in the context of the crisis: State aids

2. Public financial support has been granted both in the financial and in the real sectors. In the financial sector, the goal was to restore credit. In the real sector, the aid has focused on the construction and the automotive sector.

3. The European Commission (EC) exercises supervisory powers over State aids -above certain thresholds- granted by member States. Following the deepening of the financial crisis in the autumn of 2008, the EC has provided guidance in the form of Communications on the design and implementation of State aids in the crisis context, in order to minimise competition distortions[2].

1.1. Financial sector

4. The following support schemes were notified to the EC and have been approved:

- *State aid NN 54/A/2008 Fund for the Acquisition of Financial Assets*[3]. The objective is to provide liquidity to credit institutions and to encourage them to grant more credit to businesses and households. The Fund is financed by the State Treasury with €30 billion[4] and was meant to purchase high quality assets from volunteer credit institutions at market prices. The purchases had to take into consideration the principles of objectivity, security, transparency, efficiency, profitability and diversification.

  Between November 2008 and January 2009 four auctions were organised, in which 54 credit institutions acquired €19.34 billion (64% of total funds available) for three years. A large share of the funds (74%) went to savings banks. No more auctions have taken place as a result of other aid schemes put in place and of liquidity injected by the European Central Bank. The scheme will however be active until banks have paid back the funds.

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1 Contribution submitted by the Comisión Nacional de la Competencia (Spain).

2 See contribution by the EU to the roundtable on State Aid of the GFC of February 2010 (DAF/COMP/GF/WD(2010)3. DGCOMP has recently issued a Staff Working Paper on the application of state aid rules to government guarantee schemes covering bank debt to be issued after 30 June 2010. http://ec.europa.eu/competition/state_aid/studies_reports/phase_out_bank_guarantees.pdf.

3 Royal Decree-Law 6/2008 of October 10, on the creation of the Financial Assets Acquisition Fund (FAAF).

4 1 billion=1.000 millions.

- *State Aid NN 54/B/2008 Spanish Guarantee scheme*[5]. The State guarantee covers, against remuneration, the issuance of new notes, bonds and obligations admitted to the official secondary market. The maturity of the financial instruments covered is between three months and three years (up to five years in exceptional circumstances). The scheme's overall budget was set at €100 billion for 2008 and 65 billion for 2009, of which only 51 billion have been used. Only solvent banks have access to the guarantee scheme; 59 of them have made 160 bond issues in two years. The scheme contains elements of State aids but safeguards have been introduced so that it is ensured that the State intervention is proportionate and limited to what is necessary, and that it takes place through the adequate instruments.

  On May 18th 2010 the ECOFIN decided to extend the global EU guarantee framework, with some changes. Member States are required to apply for an extension of their own national scheme. Spain has not applied yet, but in any case issuances would only be allowed until the end of the year.

- *Enlargement of the Deposit Coverage Fund*. Following EC's advice, the Spanish Deposit Coverage Fund has been increased from €20.000 to €100.000 for every depositor and account.

- *N 28/2010 Fondo de Reestructuración Ordenada Bancaria* (FROB)[6]. The purpose of the Fund is threefold: to finance restructuring processes of institutions with insolvency problems, to increase the resources of institutions experiencing short term difficulties but with good prospects of long-term viability, and to maintain confidence in the system by increasing the strength and solvency of surviving institutions. This mechanism will be in place at least until June 30th 2010. Up to now, the FROB has issued €3 billion in 5-year bonds. In addition, the FROB's aid to financial institutions in merger processes is estimated at €2.155 billion, although the CNC has only received four merger notifications so far (even in the context of the FROB, mergers need to be notified to the CNC for approval).

1.2. Real Economy

5. The following horizontal aid schemes have been approved by the EC:

- *State aid N 307/2009 Temporary aid scheme for granting limited amounts of compatible aid*. Temporary grants are provided to undertakings having to face sudden shortages or unavailability of credit as a result of the global financial and economic crisis. The scheme allows for the provision of limited amounts of aid until the end of 2010. Firms that were in difficulty before July 1st 2008 in the meaning of the EU guidelines, are excluded. The total amount of aid available is estimated at €1.4 billion.

- *State aid N 68/2010 Guarantee regime according to the EU general temporary framework*. Guarantees are provided for credits backing up current and new investment in every sector of the economy. The guarantee cannot exceed 90% of the credit amount. The available budget for this scheme, estimated at €800 million, is limited by the capacity of public administrations, both central and regional, to cover for the beneficiary defaults. This regime will be in force until the end of 2010.

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5 Royal Decree-Law 7/2008, of October 13th, on Urgent Measures on economic and financial matters in connection with the Concerted Action Plan for the Countries of the Euro Zone.

6 Royal Decree-Law 9/2009, of June 26th, on bank restructuring and on strengthening the resources of the credit institutions.

6. Besides these horizontal measures, public support for the real economy has focused on labour intensive sectors such as the automotive and the construction sectors.

1.2.1 Automotive sector

- *State aid N 140/2009 Competitiveness plan for the automotive sector – Investments on manufacturing of more environment-friendly products*. Interest rate subsidies are granted for investment loans geared to the production of green products, i.e. "green cars", and car components which significantly improve environmental protection. Aid is only allowed for projects involving early adaptation to, or going beyond, EU product standards aimed at increasing environmental protection. The scheme applied to companies of all sizes during 2009 and amounted to €800 million (€100 million in aid and €700 million in loans).

- *Plan 2000 E*[7] was conceived to foster car demand, to maintain employment in the sector and to encourage the substitution of old cars (more than 5 years old) for new and less polluting ones. The plan consists of subsidies, coming from the central and regional administrations, to consumers for the purchase of new cars (an effort is also required from car manufacturers in the form of discounts). The aid from the Central Administration is to be granted from January 1st 2010, up to either September 30th 2010 or 200.000 new cars purchased.

7. Regarding the construction sector, with the aim of creating employment and easing the impact of the crisis, €33 billion have been invested through the State Fund for Local Investment, the Special Fund for the Economy and Employment, and the State Budget.

8. The State Fund for Local Investment has allocated €8 billion among Local Councils during 2009 in proportion to their population, for the financing of new local infrastructure. Then, a new package of measures was adopted in 2010 under the umbrella of the "Sustainable Economy Strategy", including several new funds:

- The State Fund for Local Employment and Sustainability, with a budget of €5 billion for local administrations to finance investments that foster economic performance, innovation sustainability and education.

- The State Fund for a Sustainable Economy has a budget of €20 billion, granted by ICO (the State credit agency) and commercial banks over 2010 and 2011. The Fund focuses on projects dealing with energy efficiency, R&D in the environmental field, waste treatment, health and biotechnology, among others.

2. Post crisis regulatory initiatives

9. Regulatory reforms of the Spanish financial sector include EU measures aimed at enhancing transparency, responsibility, supervision and crisis prevention in the sector, including the establishment of a new supervisory framework, the revision of rules on credit rating agencies' activities and the modification of Directives on capital requirements. Also, the EC is currently working on a proposal to create a set of common rules to be applied by the member States to their own resolution funds, whose objective is to ensure that bank failures are managed with due diligence, thus avoiding contagion.

7 Royal Decrees 898/2009, 1667/2009 and 2031/2009, on the direct granting of support to the purchase of vehicles, Plan 2000 E to support vehicle renovation in 2010.

10. As far as specific regulatory measures in Spain are concerned, the new "Institutional Protection System"[8], which has been established to facilitate the restructuring of the financial sector, is worth mentioning. The system allows for "cold mergers", that is, a partial pool of resources in order to comply with regulatory requirements and reduce the risks of the merged parties' balance sheets, which nevertheless allows them to maintain a certain degree of commercial independence.

11. From a broader perspective, the "Sustainable Economy Act", still to be approved, will permit to implement the "Sustainable Economy Strategy" which is expected to set the foundations for a more robust development model from an economic, social and environmental point of view. The Draft Act tries to foster competitiveness, strengthen financial supervision, establish new rules regarding defaults, increase transparency for listed companies, and ease public-private partnerships. It also favours R&D, non-university education and energy efficiency.

3. The role of the competition authorities in the design and implementation of exit strategies and of a new regulatory framework

12. The CNC remains vigilant about the potential distorting effects on competition that recent public intervention in the economy as a result of the crisis could be creating. Therefore, attention has focused on securing that public intervention in the markets does not go beyond what is necessary to reach its legitimate objective and that competition distorting measures are removed, either as soon as they have produced the desired results, or when they have proved ineffective.

13. State aids granted as a result of the crisis should be targeted, proportionate, non-distortionary and temporary. Any plan to unwind the measures adopted during the crisis should be also designed in a way that competitive asymmetries are reduced and the market level playing field is re-established. On competition grounds, the CNC believes that a number of general principles should apply:

- Priority should be given to exiting from support programmes that have limited effectiveness in reaching their goals and a significant distortionary impact on markets. Measures should be ranked on those two grounds and be removed accordingly. Policymakers have now experience to detect which measures have had limited effectiveness and high distortionary effects. The accumulated experience should help design the exit strategy. Competitive conditions should be re-established as soon as possible in those markets that have been affected by the adoption of special crisis measures.

- Competitive neutrality would require a co-ordinated approach across countries (and regions within a country), i.e. economic and financial support programmes should be unwound simultaneously across different countries in order to avoid competitive distortions and reduce the risk of arbitrage opportunities. The possibilities for this approach are limited however by some highly asymmetric characteristics of the crisis among countries, which would call for more tailor-made policy responses. . Nevertheless, exit plans should be as co-ordinated as the economic and financial context allows, avoiding creating artificial arbitrage opportunities across sectors or across national borders.

- Exit plans within a specific sector should be comprehensive and not partial, i.e. they should apply in the same way to all companies within a sector in order to reduce the risk of distorting competition between firms within an industry. Both in the financial sector and in the real economy, partial measures applying to specific firms or activities create market asymmetries with the subsequent competition distortions. The design of exit strategies should guarantee that firms within a sector compete on equal grounds and some firms are not discriminated against.

[8] Its origin lies on the solvency Directive 2006/48, which was transposed in Spain through Royal Decree 216/2008 and Bank of Spain Note 3/2008. It was recently modified through Royal Decree-law 6/2010.

- Public support to ailing companies should not be prolonged. Both companies and financial institutions whose financial problems go beyond the current crisis and present no risk of systemic contagion should be allowed to go bankrupt (in a controlled way if necessary). Putting barriers to exit could constitute an obstacle to economic recovery. The enforcement of state aid control policies should not be relaxed. Otherwise, existing inefficiencies or industry overcapacity might be perpetuated.

14. In those sectors where regulation is needed, the design and implementation of new regulation should also make sure that competition is not distorted. Regulation should be proportionate to the objective pursued and should not constrain competition beyond what would be strictly necessary to reach its legitimate objective. The efficient working of markets should be prioritised in any new regulatory regime.

15. Assigning competition authorities strong advocacy powers is essential to guarantee that the economy does not deviate from the economic growth long-term path, i.e. that the best framework for productivity and competitiveness growth is assured.

16. In this sense, the CNC has the capacity to issue non-binding reports on draft new regulation and on individual state aids or state aid schemes granted, or to be granted, by the central, regional and local governments. On the basis of such capacity, the CNC has paid special attention to the inclusion of competition concerns in the design of new pieces of regulation.

17. Most recently, on the basis of the advocacy functions assigned by the Competition Act in force, the CNC has produced a report on the above mentioned Draft Sustainable Economy Act[9], which called special attention to differences between the CNC and sector regulators as far the as the scope and the purpose of their respective functions is concerned.

18. Also, the CNC has elaborated many reports on draft legislation transposing the EU Services Directive, including those on the two general/horizontal acts -the “Umbrella Act”[10] and the “Omnibus Act”[11] -, as well as reports on pieces of draft legislation on a vast number of sectors, such as retail distribution[12], hydrocarbons, explosives, energy and mining, healthcare and pharmaceutical services, agriculture, environment, franchises, electricity, railway transport, etc[13]. The CNC considered the transposition of the Services Directive an excellent opportunity to implement good regulation principles, which would help overcome the crisis and prepare for the future. The job has been hard but the reward could be high. Generally speaking, the CNC’s recommendations have been followed. Nevertheless, there have been some divergences with certain public administrations, especially in the retail distribution field.

19. In addition, a Guide to Competition Assessment of draft regulation has been published [14] whose objective is to provide guidance to legislators on how to draft new law in the least competition-harmful way. A few months after the Guide was published, and following the CNC’s recommendations, a new *Law*

9 Available only in Spanish: http://www.cncompetencia.es/Administracion/GestionDocumental/tabid/76/Default.aspx?EntryId=35490&Command=Core_Download&Method=attachment.

10 Report and Press release in English.

11 Report in Spanish and Press release in English.

12 Report and Press release in English.

13 See all.

14 http://www.cncompetencia.es/Administracion/GestionDocumental/tabid/76/Default. aspx?EntryId=29518 &Command=Core_Download&Method=attachment.

regulating the Report on the impact of new legal provisions for the first time expressly established the obligation of law makers to assess competition issues when carrying out a report on the impact of any new piece of legislation. The Law entered into force on January 1st 2010, right after the elaboration of a *Methodological Guide for Impact Assessment of Regulation*, which contains the principles put forward in the CNC's Guide.

20. Regarding the monitoring of State aids awarded in Spain, the CNC issues annual reports, the first one of which, referring to 2008, was made public in July 2009[15]. In the second annual report, soon to be published, the CNC will present some examples in order to illustrate what should be considered "bad practices" in State aid, by applying the criteria established in the previous report, namely, that State aids must be justified -as a solution for a market failure or to achieve common interest goals-, proportional -the same results could not be achieved through other less intrusive instruments- and effective to achieve the planned goals, and that the damage caused to competition must be taken into account. In addition, the report will closely look into the automotive sector so as to examine whether public support is causing unjustified competition restrictions.

21. All these powers allow the CNC to monitor public interventions and to guarantee to a certain extent that they do not cause unnecessary and/or disproportioned distortions on competition in the markets.

15 Press release available in English at http://www.cncompetencia.es/Default.aspx?TabId=105&contentid=255000, report available only in Spanish at http://www.cncompetencia.es/Administracion/GestionDocumental/tabid/76/Default.aspx?EntryId=35211&Command=Core_Download&Method=attachment.