TUARASCÁIL ón gComhchoiste Fiosrúcháin i dtaobh na Géarchéime Baincéireachta

An tAcht um Thithe an Oireachtais
(Fiosrúcháin, Pribhléidí agus Nósanna Imeachta), 2013

REPORT of the Joint Committee of Inquiry into the Banking Crisis

Houses of the Oireachtas
(Inquiries, Privileges and Procedures) Act, 2013

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Dept. of Finance
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THEME: C4

Appropriateness and effectiveness of the domestic policy responses

LINE OF INQUIRY: C4c

Decision to recapitalise Anglo, Allied Irish Banks (AIB), Bank of Ireland (BoI), Educational Building Society (EBS), Permanent TSB (PTSB) and the alternatives available and/or considered

Statement by the Government on the Recapitalisation of Credit Institutions

The Government has today decided on an approach to the recapitalisation of credit institutions. The Government's objective is to ensure the long-term sustainability of the banking sector in Ireland and to underpin its contribution through the availability of credit to individuals and businesses in the real economy. This initiative will help to foster and encourage the flow of funds to the economy, and limit the impact of financial market difficulties on businesses and individuals.

The Government noted that recapitalisation is recognised by the European Commission as one of the key measures that may be used by Member States to preserve stability and proper functioning of financial markets, and that it believes that in current market conditions even fundamentally sound banks may require additional capital to respond to widespread market perception that higher capital ratios are appropriate for the sector internationally.

The Government decision followed the Minister for Finance's statement of 28 November 2008 which confirmed the State's willingness to supplement and encourage private investment in the recapitalisation of credit institutions in Ireland with State participation.

In that context, the Government has decided either through the National Pensions Reserve Fund or otherwise and subject to terms and conditions, to support, alongside existing shareholders and private investors, a recapitalisation programme for credit institutions in Ireland of up to €10 billion.

The State's investment may take the form of preference shares and/or ordinary shares and the State may where appropriate participate on an underwriting basis. In principle existing shareholders will be expected to have the right to subscribe for new capital on the same terms as the Government.

A key principle in the operation of such a fund will be to secure the interests of the taxpayers through an appropriate return on, and appropriate terms for, the investment.

The next step in this process will be for the Minister for Finance to initiate detailed engagement with the credit institutions themselves in respect of specific proposals.

In order to safeguard fully the interests of the taxpayer, State investment will be assessed on a case-by-case basis in an objective and non-discriminatory manner, having regard to the systemic importance of the institution, the importance of maintaining the stability of the financial system in the State, and the most effective and economical use of resources available to the State and each credit institution's particular requirement for capital. Any State investment will be undertaken in line with best practice in the EU and elsewhere and consistent with EU State aid rules and in particular the recent European Commission communication on recapitalisation.

Recapitalised institutions may be required to comply with such requirements as to transparency and commercial conduct as the Minister sees fit.

The National Pensions Reserve Fund Act, 2000 will be amended, as necessary.

Discussions with the relevant credit institutions are ongoing, and the institutions continue to progress proposals for private investment. Institutions are being asked to submit their proposals by early January.

The Government guarantee Scheme remains in place.

14 December 2008

SECRET
Oifig an Aire Airgeadais

Ref No **Date: 22nd April 2009**

Memorandum for Information of Government - Recapitalisation: Arrangements for Anglo Irish Bank and Statement of Allied Irish Banks

Decision sought:

The Minister for Finance asks the Government to:

1. Approve the putting in place of arrangements to make a capital injection to Anglo Irish Bank at short notice, if required, subject to approval by the Government of the level of funds involved.

2. Note the Statement issued by Allied Irish Bank on Monday 20th April 2009 following discussion with the Minister for Finance and his senior officials (copy attached at Appendix 1).

1. Anglo Irish Bank

1.1 Background

In September 2008, with severely stressed conditions on financial markets globally following the collapse of Lehman Brothers, the Government introduced a guarantee of the liabilities of the systemically important Irish banks, to ensure they could continue to raise funds to meet their liquidity needs. Anglo Irish Bank, as a major financial institution with a balance sheet of some €100bn, was among the covered institutions.

Following the introduction of the bank guarantee Scheme, the Financial Regulator commissioned PricewaterhouseCoopers (PwC) to conduct an analysis of the loan books of the six covered institutions. The report showed that Anglo, with a loan book of €72bn overall, was heavily exposed to commercial investment property (c. €40bn) and to the land and development sector (c. €20bn). The PwC report also assessed likely loan impairment rates in each of the covered institutions and the impact of various stress tests on the banks' capital levels.

In reaction to the financial crisis, international markets held increased expectations in relation to the level of capital to be held by banks to cover losses. In this context, the market perception of Anglo was that it had underprovided for its lending risks and that the bank's future viability was in question. Anglo's share price fell sharply in response to concerns about the adequacy of the bank's capital levels and the bank's funding position deteriorated.

In December 2008, as part of its broader bank recapitalisation programme, the Government announced proposals to invest an initial €1.5 billion of Core Tier 1 capital in Anglo Irish Bank with a commitment to making further capital available if required. However, the disclosures relating to loans to Directors at Anglo continued to undermine confidence in, and weaken the funding position of, the bank even after the announcement of the Government's proposed recapitalisation. Furthermore, the due diligence exercise undertaken as part of the planned recapitalisation brought to light further concerns around corporate governance at Anglo. The Government therefore decided to take Anglo into full public ownership, with effect from 21 January 2009, to ensure the stability of the bank and the financial system generally. As a consequence of Anglo being taken into State ownership, the Government decided not to proceed with the proposed capital injection of €1.5 billion into Anglo.

In recent months, there has been a general contraction in liquidity, which has particularly affected Anglo. Special funding facilities have been put in place for Anglo but these facilities are of a short-term nature and are not a long-term solution to the bank's funding difficulties, which are related to continuing market concerns about Anglo's capital position and the long-term viability of its business model.

1.2 Current position

The minimum regulatory requirement for Core Tier 1 capital - which is comprised of equity and reserves - is 4% of total assets (risk weighted). If this level of capital is breached by Anglo, a number of the bank's bonds will immediately become repayable and it is likely that other funding would be removed from Anglo as investors would be concerned about the bank's solvency. This would risk a call on the Government's guarantee and undermine the position of the other Irish banks.

Anglo's capital position is progressively deteriorating, as greater impairment provisions against capital are required to cover the losses that are being realised on the bank's loan book. In Anglo's December 2008 monthly accounts, the Core Tier 1 capital ratio stood at 5.7%. By February 2009, the Core Tier 1 ratio had declined to 4.9%. At this level, Anglo effectively had a €790m capital buffer to absorb further losses on its loan book, before it would be in breach of the minimum 4% regulatory capital requirement.

The Board of Anglo has indicated that the impairment provision for March may be of an order to bring the bank's Core Tier 1 capital ratio below the minimum 4% level. Anglo is currently fully assessing its loan book and overall risk position, to determine the final impairment charge to be shown in the bank's March accounts. Given the potential regulatory implications, the Financial Regulator has also commissioned PricewaterhouseCoopers consultants to conduct an independent analysis of the data which Anglo are basing their revised impairment figures on, and to make an assessment of the impairment provision required.

The outcome of these assessments will determine whether Anglo, in the absence of any capital injection, breached the 4% capital requirement in the bank's half-year accounts as at 31 March 2009, which are to be published in May. Even if Anglo did not breach the minimum 4% capital level in March, given the continued high rate of capital attrition which will result from impairment on Anglo's loan book, it is very likely that Anglo will fall below the minimum regulatory capital level by end-April.

The Anglo board have made a preliminary estimate that the total likely loss on their loan book over the three year period 2009-2011 will amount to €7.3bn. Much of the losses on the book may be crystallised if the National Asset Management Agency (NAMA) is set up and Anglo's development loans and related assets are transferred to the Agency. However, in the meantime it is essential that Anglo is sufficiently capitalised to meet minimum regulatory requirements.

1.3 Capital Provision

In this context, it is considered necessary to have the Government's approval in place to make a capital injection to Anglo at short notice to prevent a breach of regulatory requirements. The level of capital required is not certain at this stage and will depend on the scale of impairment declaration made by Anglo in the coming months. It is proposed that a significant amount of capital, of several billion, would be available for such purpose. The Minister for Finance will revert to Government when the final capital figure is determined.

The legal issues involved in making a capital injection to Anglo at short notice are currently being examined. However, given that the State has 100% ownership of Anglo, it is not anticipated that legal difficulties will present.

2. Allied Irish Bank

2.1 Background

On 11 February 2009 the Government announced its intention to invest €3.5bn capital in each of the main banks, AIB and Bank of Ireland, to be funded from the National Pensions Reserve Fund.

In the case of Bank of Ireland, the National Pensions Reserve Fund Commission with the assistance of PWC, completed a due diligence report which found no issue of sufficiently high risk to prevent the proposed investment. The Minister directed the National Pensions Reserve Fund Commission to make the investment on Tuesday 31 March 2009.

On 9 April 2009 Paul Carty, the Chairman of the NPRF wrote to the Minister in relation to the due diligence exercise on AIB which was undertaken also with the support of PWC and on the same basis as the due diligence on the Bank of Ireland. Mr Carty advised that the work carried out to date by PWC *"indicates that there is a high probability that, even allowing for the proposed issue of €3.5 billion in preference shares, AIB's Core Tier 1 Capital will fall below the current regulatory minimum of 4% in 2010 and 2011and that they will be unable in that year to pay in cash the coupon due on the preference shares"* and that under the PWC stress test scenarios *"AIB would need additional capital of up to €1.6 billion in 2010/11 over and above the €3.5 billion proposed."*

This is the NPRFC view, but the conclusion is sensitive to the assumptions used.
AIB have scheduled an egm to approve the recapitalisation for 13th May 2009 which requires a circular to issue to shareholders on Monday 20th April, setting out the terms of the recapitalisation. Mr Carty requested a direction from the Minister on whether

the recapitalisation should be allowed to proceed in light of the due diligence information now to hand.

2.2 Advice to Minister for Finance

The Minister for Finance has consulted extensively with his advisers. A key immediate concern is the liquidity position of AIB and of the Irish financial system generally. Three core options were considered:
Option A: Proceed with €3.5bn recapitalisation on the assurance that AIB will retain its capital above the minimum 4% requirement.
Option B: Renegotiate capital requirements now based on due diligence and in advance of NAMA.
Option C: Start AIB NAMA negotiation early, ahead of recapitalisation.

Given that the due diligence confirms that there is a significant risk that AIB will be unlikely to meet its minimum regulatory requirements the advice to the Minister was that he should not proceed with the €3.5bn capital investment as originally proposed. Instead a revised package to address AIB's capital requirements should be developed and on that basis the Minister consulted with AIB.

2.3 AIB advised of recapitalisation problem

On Thursday the Minister put it to AIB that in view of the reports from the due diligence and the advice available to him he was considering whether to proceed with the €3.5bn capital investment as originally proposed. He suggested to AIB that an alternative scenario would be to inject a minimum of €5bn to ensure it could meet its minimum capital requirements and that this could be made up of €2.5bn ordinary shares and €2.5bn preference shares. It was acknowledged that this could lead to a State ownership of between 70 and 75% and accepted that the immediate implication was that AIB would not be able to proceed with the issue of its circular on Monday 20th, which was required if the egm is to approve the recapitalisation, scheduled for 13th May 2009, was to proceed.

2.4 AIB Board response

The AIB board considered the capitalisation scenario put to it by the Minister and met with the Minister and his advisors on Saturday 18th to discuss options. AIB put it to the Minister that the market now accepted the €3.5bn State preference share investment and has factored in the likely additional capital impact of NAMA. They argued that for AIB to defer the issue of its circular on Monday 20th April and subsequent egm would cause huge uncertainty in the markets, would severely damage AIB funding and liquidity and raise unwarranted concerns about a huge hole not only in the finances of AIB but also in other financial institutions.

The Board made it clear that they were 'not contesting' the due diligence conclusion that there was a high risk of a capital shortfall nor that the additional sum to be made up was likely to be in the region of €1.5bn. The Board suggested however that this shortfall could be made up by the speedy disposal of AIB assets and other actions to raise capital which would avoid the risk of creating serious funding problems.

2.5 State shareholding in AIB

AIB confirmed that they would publicly confirm their commitment to NAMA and that it was their intention to see assets transferred to NAMA as soon as possible. The Board made it clear that they understand and accept that the implication of NAMA is that there could be a significant State shareholding in AIB. They accepted that this may mean converting some of the €3.5bn preference shares to ordinary shares if the quality of core tier one capital becomes an issue at a later date.

The Minister has also indicated to AIB that as the Board will shortly be up for re-election in the context of the forthcoming AGM, he will expect to be involved in determining the future shape of the Board.

2.6 Conclusion

The Minister considered the outcome of the discussions with AIB in consultation with his advisors. In the circumstances the advice to the Minister was that he should proceed with Option A but with the added assurances that the bank will be restructured to realise assets and that it will fully cooperate with NAMA recognising that this could entail a significant additional State equity stake. The Minister notes as progress that AIB are willing to formally acknowledge their need for additional capital and cooperation with NAMA. The added assurances from AIB will deal with a number of the cons associated with Option A and in particular move the Minister to a position where he is clearly responding to the concerns raised in the due diligence and cannot be seen as glossing over the problems. Any concern that AIB would not co-operate with potential recapitalisation arising from NAMA is also clearly being dealt with. These developments are considered essential to the continued credibility of the bank and the Government's actions to repair the banking sector.

2.7 Outcome

AIB released the attached press release to the Irish Stock Exchange on Monday morning, 20th April 2009. In the statement AIB publicly commits to transfer assets to NAMA and acknowledges the implications of this could be a significant State equity holding in the Bank.

2.8 Nationalisation

The Minister for Finance notes that there is much media debate proposing the nationalisation of Irish banks, particularly AIB and Bank of Ireland. It has been argued that if the banks are nationalised they are underwritten by the State so they can withstand large writedowns on their loan books without the need for large capital injections. As the banks would then be owned by the State, the argument is that there would be no need for NAMA to issue bonds because it would be a closed transaction – the State buying something from itself. This is simply not true. All loans in the banking system have to continue to be funded until they are repaid no matter who owns them. Furthermore, as can by seen by the section on Anglo above, banks which wish to continue functioning as banks must be adequately established, whether they are in State ownership or not.

The Government's strategy is to ensure that the lending needs of the real economy are met. A commercially focused banking system is best equipped to achieve this aim. The Minister for Finance considers that where banks are of systemic importance, viable and long-term sustainable, they should be maintained as market listed plcs open to private investment. Nationalisation is a long term policy that is very difficult to see any feasible exit strategy from. Internationally the prospect of wholesale nationalisation is very damaging to Ireland's reputation and attractiveness to international investors. No country is currently adopting a policy of wholesale bank nationalisation; there is no reason for Ireland to adopt such a policy. It is not Government policy to nationalise banks such as AIB but it could be that, similar to cases in the UK, the Government could end up with a majority shareholding.

Appendix 1

Allied Irish Banks, p.l.c. Capital Update

20th April 2009

On 12 February Allied Irish Banks p.l.c. ("AIB") [NYSE: AIB] announced an agreement with the Irish Government in relation to the proposed recapitalisation of the bank. Since then, market and public uncertainty about our capital adequacy has persisted despite the proposed addition of €3.5 billion in core tier 1 capital

'As previously announced, we will be seeking shareholder approval at an EGM on 13 May to accept the aforementioned capital. Furthermore following discussions with the Minister for Finance and reflecting his desire to ensure that systemically important banks would remain adequately capitalised, even in stressed scenarios, we have decided to take further action to strengthen our capital position as outlined in this announcement.

In cooperation with AIB, the Minister for Finance has been conducting due diligence and stress test scenarios. Arising from these stress tests the Minister for Finance and AIB have formed a view that to strengthen our capital position a total amount of €5.0 billion new core tier 1 capital is appropriate. As a consequence, in addition to the proposed €3.5 billion injection by the Government, we aim to increase core tier 1 capital by a further €1.5 billion before the end of 2009. Potential sources of this capital include the disposal of assets and marketable assets will be considered as part of this process. This commitment represents a reappraisal of our previous view in relation to asset disposal. The bank acknowledges that the Minister has said that if any further capital injections are required from the State these would be in the form of equity capital.

We also wish to state our support for what we believe is a positive step taken by the Government in its recent decision to create a National Asset Management Agency (NAMA) and AIB wishes to signal its intention to participate in this initiative. NAMA is currently at an initial planning stage. AIB will work closely with the authorities to achieve its implementation.

-Ends-

SECRET

Oifig an Aire Airgeadais

Ref No: F514/32 /10 **Date: 30 March 2010**

Memorandum for the Information of Government

Stabilising the Banking System

Decision Sought

1. The Minister for Finance asks the Government to note his intention to announce today the final phase of the stabilisation process of the banking system.

Background

2. The Government has already acted to address the banks liquidity problems through the introduction of the Bank Guarantee Schemes and to remove the riskiest loans from the balance sheets of the participating institutions through the NAMA process.

3. NAMA has decided on the price to be paid for the first tranche of loans to be transferred to the Agency, after detailed loan by loan analysis. The discount, or the so-called haircut, for the first tranche of loans and is as follows: AIB, 43%, Bank of Ireland, 35%; Anglo, about 50%; INBS, 58%, and EBS 37%. The weighted average haircut across these institutions is 47%.

4. While the first tranche is not necessarily reflective of future tranches, the Financial Regulator has determined the additional capital requirement of each NAMA participating institution, which must be in place in each of the institutions by the end of 2010 to meet the Regulator's new capital standards.

5. Bank of Ireland must raise additional core capital of €2.7 billion. While Bank of Ireland expects to be able to raise private capital, the State will commit to

converting part of its Preference Shares in Bank of Ireland into ordinary equity. This process requires no new investment of State funds.

6. Allied Irish Bank must raise additional core capital of €7.4 billion. The disposal proceeds will provide significant capital but it will not be sufficient to address the full requirement. To the extent that the gap is not filled by the private sector the State is willing to convert some or all of its preference shares as required on terms to be agreed to provide full value for the State. Any additional capital requirement will be met from the National Pension Reserve Fund.

7. INBS will need an injection of €2.7 billion. This will come from the State through a combination of €100 million in Special Investment Shares in the society and a Promissory Note for the balance issued to the Society. This Note will be payable over ten to fifteen years, which will reduce the impact on the Exchequer this year.

8. EBS will need an injection of €875 million. While EBS has had an expression of interest from a private party, the State will provide EBS with €100 million of capital through the issuance of Special Investment Shares. To the extent that private capital is not forthcoming, the remaining capital requirement of €775 million will be met either partly or fully through the issuance of a Promissory Note from the State to the institution.

9. In addition, the Minister will this week provide Anglo Irish Banks with €8.3 billion to support its capital position to take account of the bank's losses to date. He asks his colleagues to note that additional capital support of up to €10 billion is likely to be required depending on the NAMA discount on the first tranche of Anglo's loans.

10. These actions will put the banks in a much stronger position than heretofore. The Minister is imposing specific lending targets on AIB and Bank of Ireland so that they will make available not less than €3 billion each for new or increased credit facilities to SMEs in both 2010 and 2011.

agreed by Minister 14.5.09

Minister, from Ann Nolan

Anglo Capital Position

Decision Sought

You are asked to agree subject to legal clearance, the following actions in response to capital issues in Anglo:

1. Support for Anglo's application to the Financial Regulator for a derogation from capital requirements;
2. Issue of a letter to the Financial Regulator confirming that Anglo's capital position will be supported as necessary and appropriate; and
3. Alert Government to a likely capital requirement for Anglo of c€3bn, on an instalment basis, over the coming months.

These measures are required because Anglo faces a major impairment charge of €4.5bn for March 2009, meaning Anglo would be in breach of all of its minimum regulatory capital requirements, with an effective €3bn regulatory capital shortfall. Discussions with the Central Bank, Financial Regulator, NTMA have concluded that Anglo's regulatory capital shortfall for its March accounts can best be addressed in the short-term by way of derogations from the minimum regulatory capital requirements. This is a temporary solution. Regulatory derogations may be granted by the Financial Regulator only in temporary and exceptional circumstances and in a context where there is a clear path by which the capital position will be restored. Further, the Central Bank is of the view that any option other than a capital injection could worsen Anglo's liquidity position.

The details are set out below.

Background

The PricewaterhouseCoopers (PwC) review of impairment on Anglo's loan book has concluded that an impairment provision of €4.5bn (€3.6bn specific and €0.9 collective) is required for March 2009. The Board of Anglo, following an internal review, had also estimated total impairment of €4.5bn for March, (€3.7bn specific and €0.8bn collective), albeit with certain differences in terms of where impairment was judged to be required.

Beyond the impairment charge for March, very significant further losses remain to be realised on Anglo's loan book. For the second half of Anglo's financial year, to 30 September 2009, PwC forecast that Anglo face further specific impairment of €1.5bn - €3bn. While some of this second loss might be covered by a debt buy back, the maximum possible profit from such a buy back would be €1.2bn, so further capital is likely to be needed before the end of the year. The situation is compounded because Anglo's cost of funding has risen, and so their profitability has collapsed. In the longer term, PwC estimate a possible economic loss on Anglo's loan book over the next three years of €12.5bn. This estimate is based on the same stress tests that were applied to AIB and Bank of Ireland under the recapitalisation due diligence. PwC note that Anglo management's gross total stress provision estimate is €10.2bn.

In the short-term, the estimated €4.5bn impairment to be booked for March would leave Anglo's capital ratios as follows:

	Anglo 31/03/09	Regulatory minimum
Core Tier 1	0.48%	4.0%
Tier 1	0.96%	4.75%
Total capital	8.1%	9.5%

Anglo would be in breach of all of its minimum regulatory capital requirements, with an effective €3bn regulatory capital shortfall.

Possible Reponses

The immediate consequences of a regulatory breach can be addressed by way of:

- a capital injection;
- a guarantee of a portion of Anglo's loan book; or
- derogation from some or all of the regulatory capital requirements.

The advantages and disadvantages of each approach are as follows:

	Advantages	Disadvantages
Capital injection	▪ Positive market perception. ▪ No regulatory derogations.	▪ Immediate capital requirement. ▪ Removes pressure on Anglo to produce a credible business plan. ▪ No clear picture on Anglo's future prospects. ▪ Could impact on the treatment and transfer of assets to NAMA.
Asset guarantee	▪ No upfront capital requirement. ▪ Enforces need for Anglo to be pro-active in developing a credible business plan. ▪ Allows time to develop a structured approach to Anglo's capital issues. ▪ State would receive a guarantee fee.	▪ A significant amount of variable quality assets would have to be insured to meet the shortfall. ▪ Only a temporary measure in advance of addressing capital position. ▪ Indeterminate cost to the State. ▪ Market uncertainty on Government commitment to Anglo position. ▪ Anglo liquidity may be adversely affected. ▪ Market analysts may add contingent liability to Government debt. ▪ Lack of oversight of management of guaranteed assets.
Regulatory derogations	▪ No upfront capital requirement. ▪ Enforces need for Anglo to be pro-active in developing a credible business plan. ▪ Allows time to develop a structured approach to Anglo's capital issues.	▪ Only a temporary measure in advance of addressing Anglo's capital position. ▪ Market uncertainty on Government commitment to Anglo. ▪ Anglo liquidity may be adversely affected.

Liquidity Issues
Anglo's liquidity position is already very difficult. The Bank currently has €11bn of Emergency Liquidity Assistance (ELA), and this is likely to rise to €12bn by the end of the month. Following a re-assessment by Anglo of the credit quality of its loan book, the quality of the loans held by the Central Bank as collateral for ELA has deteriorated and now includes loans in arrears and impaired loans. The Central Bank is of the view that any option other than a capital injection could worsen Anglo's liquidity position.

Proposed Response
There are very significant disadvantages to all of the available options. It will be necessary over the coming period for Anglo to de-leverage and reduce costs. NAMA will help with this de-leveraging. It is proposed that we look in terms of a short-term solution to enable Anglo to develop an agreed business plan and to further consider the longer term options. Therefore, the Department, the Central Bank, the NTMA and the Financial Regulator have agreed that Anglo's regulatory capital shortfall for its March accounts can best be addressed in the short-term by way of derogations from the minimum regulatory capital requirements. The Financial Regulator has power to grant the necessary derogations under the terms of the Capital Requirements Directive, but Anglo would be required to remain in excess of the minimum 8% total solvency ratio.

This approach would enable Anglo to publish its March half-year accounts at the end May without a regulatory breach. Under the Transparency Directive, the publication of the March half-year accounts is required within two months of the period end, i.e. by 31 May.

Capital is Required
It must be emphasised that regulatory derogations alone are not a credible strategy for addressing Anglo's current capital shortfall and the future losses anticipated on the book, but merely a temporary solution. Such regulatory derogations may be granted by the Financial Regulator only in temporary and exceptional circumstances and in a context where there is a clear path by which the capital position will be restored. Also, the scale of the impairment being realised on Anglo's book is such that the Bank would be likely to breach the minimum 8% solvency requirement within a short period, which would trigger events of default on the Bank's bonds, resulting in a call on the guarantee.

The approach taken by the UK Government in relation to Northern Rock is indicative of the accompanying measures required to introduce derogations on regulatory capital ratios. In this case, the UK Government undertook to put additional capital in Northern Rock up to €3bn. The UK Government also provided a letter of undertaking to the UK Financial Services Authority (FSA) in respect of its continued support for the bank. This level of commitment from the UK authorities provided the foundation for the UK FSA to grant a waiver under Article 66 of the Capital Requirements Directive until 30 April 2009.

It is therefore considered necessary to accompany any introduction of regulatory derogations for Anglo with an announcement of a Government commitment to support Anglo's capital position. In the absence of a clear indication of how Anglo's requirement for capital is going to be addressed, Anglo's status as a going concern would be in question, with implications for Anglo's banking licence and its funding base.

Business Plan

The recommended approach would allow scope for the finalisation of Anglo's business plan, which is currently being drafted by Anglo, over the coming weeks. This business plan will enable assessment of Anglo's future and would be an important element of the proposal to restore Anglo's capital position. Matters for consideration include its business model, its potential profitability, its prospects for cost-reduction and improving its capital position. On the capital position, all options must be on the table, including a debt buy back programme and de-leveraging through both NAMA and asset-sales. This process will inform the final decision on the scale and means of capital support to Anglo. We intend to write to Anglo as part of this process and indicate what we want to see in Anglo's business plan.

NAMA

While it would be desirable to co-ordinate any capital injection to Anglo with the transfer of Anglo's Land and Development assets and connected exposures to the National Asset Management Agency, it is unlikely, even with this proposal to buy time, that we can postpone a capital injection to Anglo to that period.

Next Steps

Subject to your agreement to the proposed action, Anglo would make an application to the Financial Regulator to arrange for specific regulatory derogations from the Financial Regulator's requirements in relation to Own Funds and from the Capital Requirements Directive. The Financial Regulator has stated that a commitment on supporting Anglo's capital position, along the lines of that provided by the UK Authorities in respect of Northern Rock, would be an essential component of any application for regulatory derogations, so a letter of comfort to the Financial Regulator will need to be issued. Further, as the derogation would be a temporary solution, a memorandum for Government setting out the likely capital requirement, will be prepared.

13/5/09

Seen by Minister

Agreed to by Minister
[illegible] 30/7/09

Minister
From Ann Nolan

Capital Injection into Anglo Irish Bank

Decision Sought

Your agreement is sought:

a) to provide further capital, out of the balance of the agreed €1bn remaining, to Anglo to meet the cost of the buyback of debt instruments once the offer closes today and,

b) to provide the remainder of the €1bn to the bank once they have appointed a new CEO.

Background

The Government approved the recapitalisation of Anglo Irish Bank and agreed to the provision of up to €4bn for that purpose. The EU has also approved this.

€3bn was provided to the bank at the end of June and it was agreed that, as part of the Subscription Agreement underpinning this, the Exchequer would provide a further injection of up to €1bn for the bank to undertake a liability management exercise to buy back some of its debt instruments.

As you know the bank launched the buyback on Wednesday 22 July. Under the terms of the announcement 30 July is the date set for investors to sign up, with settlement on 4 August.

Estimates by the bank are that there will be a take up of about 40-50% although it could be higher or lower – the exact figure will not be known until the offer closes today. If the estimates are correct then the cash the bank will pay out will be of the order of €400-€500m. We will know tomorrow the exact take-up and the cost of that. The intention is to provide this money next week to the bank.

New CEO

As relayed to you yesterday the bank is progressing the appointment of a new CEO and is discussing contract details with one individual. The bank's projections are based on the full €1bn being provided to them and the public perception is that the Government commitment is to a full €4bn being injected. You indicated previously that you were agreeable to injecting the full amount subject to that appointment being made. Therefore, if you agree we will provide that balance of the remaining €1bn to the bank once they announce the appointment of the CEO which, hopefully, will be in the next week or so.

[illegible]
30 July 2009

cc Mr Cardiff

[LETTERHEAD OF THE DEPARTMENT OF FINANCE]

7 September 2009

Anglo Irish Bank Corporation Limited
Stephen Court
18 / 21 St. Stephen's Green,
Dublin 2

Draft.

FAO: The Company Secretary

Re: Subscription for Additional Shares

Dear Sirs,

We refer to the subscription agreement between The Minister For Finance and Anglo Irish Bank Corporation Limited dated 29 June 2009 (the "**Agreement**"). Terms used in this letter and not otherwise defined have the same meaning as in the Agreement.

~~Following the appointment of Mr Mike Aynsley as Group Chief Executive of the Bank,~~ I ~~i~~n reliance upon the Warranties and Post-Completion Covenants set out in the Agreement, the Subscriber hereby subscribes for 1,076,749,975 Ordinary Shares (the "**Further Shares**") on ● September 2009 (the "**Further Completion Date**").

In consideration for the Company's agreement to allot and issue the Further Shares, the Subscriber hereby undertakes to pay an aggregate subscription amount of EUR172,279,996 (the "**Further Subscription Amount**") to the Company on the Further Completion Date ("**Further Completion**").

The provisions of Clauses 4.2 and 4.3 of the Agreement shall apply to the Further Completion Date mutatis mutandis. References to the Initial Subscription Amount and/or the Additional Subscription Amount in Clause 5 of the Agreement shall be deemed to include references to the Further Subscription Amount.

Immediately before the time of Further Completion, the Company shall be deemed to represent and warrant to and undertake with the Subscriber that each of the Warranties is, by reference to the facts then existing, true and accurate and not misleading, at the Further Completion Date, save as disclosed in the Information. For this purpose only, where in a Warranty there is an express or implied reference to the "date of this Agreement" that reference is to be construed as a reference to the "date of Further Completion", and where in a Warranty there is an express or implied reference to "Completion" that reference is to be construed as a reference to "Further Completion"

We would be grateful if you could please confirm in writing:

1. that you accept and agree to the terms set out above; and

2. the details of the bank account into which the Further Subscription Amount should be paid on the Further Completion Date.

We look forward to hearing from you in due course.

Yours faithfully

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For and on behalf of
THE MINISTER OF FINANCE

Minister
From Ann Nolan

25/6/2009 Having examined submission - i.e. draft agreement I agree to the signature of same
Brian Lenihan

In line with the recent Government Decision to inject up to €4bn into Anglo Irish bank by way of an equity injection I attach a draft Subscription Agreement between the bank and you as subscriber.

The Subscription Agreement is similar to those completed for AIB and Bank of Ireland but contains changes to reflect the position of the bank as a nationalised institution.

The Agreement provides that €3bn will be injected immediately once EU approval is obtained which we hope will be tomorrow or Monday. In addition, the Agreement also provides that a further injection of up to maximum of €1bn can be made to enable the bank to engage in a liquidity management exercise as was envisaged when the decision to provide equity was made.

The main points of the Agreement are:

- The shareholder undertakes to provide the injection in the form of ordinary equity.
- The bank is required to fulfil certain obligations such as appointing a new leadership team, to be agreed with the Shareholder, within 1 month or else install a temporary external management team.
- It is also required to submit a restructuring plan for the bank by 30 September and they will not be allowed to engage in any new lending for 12 months except in limited circumstances.
- In addition, they will not be allowed to pay coupons on its Tier 1 bonds without our agreement.

The Agreement is a final draft but there may be some changes arising from the EU approval and/or drafting or minor changes and which, if you agree, we will approve if in order.

If you agree I will sign the agreement on your behalf.

A Nolan

Ann Nolan
25 June 2009

cc Secretary General

102

27/AN/125

Hunt, Aidan

From: Matthaeus, Andreas (IBK EMEA) [Andreas_Matthaeus@ml.com]

Sent: 21 December 2008 18:45

To: Kinsella, Sean

Cc: Beausang, William; Carrigan, Aidan; Nolan, Ann; Duffy, Eoghan; Baldock, Henrietta (IBK EMEA); BMcDonagh@ntma.ie; Cardiff, Kevin; Padraig.ORiordain@arthurcox.com

Subject: Re: Version 11 of Statement

Sean

Thank you for sending this to us. There are three changes we would recommend. Adding these will make the core tier 1 nature of these securities clearer to the market. The release would then have a lot of the key words associated with a share instrument rather than a fixed income instrument.

We would recommend:

1) Changing "annual fixed coupon amount" to "annual dividend". The security is a share in all respects and calling any payment associated with it a "dividend" will reinforce that to the market. Keeping it as coupon will give the wrong impression that the instrument is more fixed income in nature.

2) Changing "par value" to "issue price". Again this change will reinforce the equity nature of the instrument rather than a fixed income element.

3) Finally we would recommend adding the paragraph below in some kind of editor notes. It doe not need to be part of the release to the newspapers, but if any analyst or market participant were to download the release from a website (if this is how it works) then they would also see this paragraph:

"The preference shares rank parri passu to ordinary shares in liquidation. The annual dividend is non-cumulative and ranks pari passu with dividend claims of other preference shares. Should cash not be available to pay the preference share dividend then the bank must issue ordinary shares to the State as payment in kind. In the event that the preference share dividend is not paid in cash, no dividend may be paid on the ordinary shares."

Please let us know if you have any questions.

Regards,

Andreas Matthaeus
Director - IBK
Tel: +44 207 995 4914
Mob: +44 7799 583 041
Email: andreas_matthaeus@ml.com

From: Kinsella, Sean
To: Matthaeus, Andreas (IBK EMEA)
Cc: Beausang, William ; Carrigan, Aidan ; Nolan, Ann ; Duffy, Eoghan
Sent: Sun Dec 21 17:13:31 2008
Subject: Version 11 of Statement

Andreas

Latest version of statement attached.

Sean

01-6045531

<<Version 11 dated 21 December 13.15.pdf>>

Government Announcement on Recapitalisation

21st December 2008

Following on from Government Decisions of 28th November and 14th December on the recapitalisation of financial institutions, the Minister for Finance has this evening announced specific decisions in relation to three major financial institutions. Commenting on the announcement;

The Taoiseach said:

"The objective of these decisions is to ensure that the financial system in Ireland meets the everyday financial needs of individuals, businesses and the overall economy. As part of this recapitalisation package, I am very pleased that a number of measures to support small to medium businesses and mortgage holders have also been announced."

In relation to Anglo Irish Bank, the Minister for Finance announces an initial investment of €1.5 billion of core tier 1 capital to assist in restructuring the bank's capital. The Government will continue to reinforce the position of Anglo Irish Bank and will make further capital available if required so that it remains a sound and viable institution. The investment will be in the form of €1.5 billion of perpetual preference shares with a fixed annual dividend of 10%. The preference shares carry 75% of the voting rights of Anglo Irish Bank. The investment is subject to the approval of the ordinary shareholders at a general meeting which will be convened as soon as possible. On the basis of positive contact with the European Commission, the Minister said he was confident that the Anglo proposal will meet with EU State Aid requirements when formally notified in due course.

Good progress continues to be made in the capital discussions with other institutions. In particular, subject to shareholder and regulatory approval, the Government has agreed with Bank of Ireland and Allied Irish Banks plc that they will each issue €2bn of perpetual preference shares to the State with a fixed annual dividend of 8%. These shares will have voting rights in respect of change of control and any changes in the capital structure. They will also confer 25% of the voting rights in respect of appointments of directors and 25% of the directors on the board, currently including any directors to be appointed in connection with the Government's Guarantee Scheme.

All the institutions may redeem the preference shares within 5 years at the issue price or after 5 years at 125% of the issue price. The preference shares are non-convertible and will be treated as core tier 1 capital by the Financial Regulator and are replaceable only with other core/equity tier 1 capital.

The capital injection for Anglo Irish Bank is likely to take place following an Extraordinary General Meeting in mid-January, and for Allied Irish Bank and Bank of Ireland, by the end of the first quarter of 2009.

The Government has a substantial pool of additional capital available to underwrite and otherwise support the issuance of core tier 1 capital by the relevant institutions.
The Government need not be the principal source of this additional capital and encourages each institution to access private sources of capital. Nonetheless, the Government is prepared to underwrite further issuance of core tier 1 capital and both Allied Irish Banks plc and Bank of Ireland have indicated an interest in such an underwriting in an amount of up to €1 billion each.

The measures announced today have been designed having regarded to the recent European Commission Recapitalisation Communication and are subject to State aid approval.

Credit Package

The provision of credit to the economy is the most immediate and pressing issue for business and for the Government. The future health of our economy is inextricably linked with the supply of credit and a situation where banks are unwilling or are perceived to be unwilling to lend is damaging not only for the economy but also for the banks themselves. Banks have an important part to play in addressing this issue and a key objective of the Government's recapitalisation initiative is to ensure the continued flow of funds through the banks to individuals and businesses in the real economy.

In response to my earlier meetings with the banks many had already announced specific programmes to boost lending to small and medium enterprises. AIB and Bank of Ireland have announced new business support and start up funds and have provided commitments to support first time buyers and consumers. While these announcements are welcome the Government believes that it is appropriate as part of the agreed recapitalisation programme that the banks should further build on the commitments given in the banks guarantee scheme through specific credit policies targeted at small medium enterprises, first time buyers and consumers generally.

The recapitalisation announced today will provide the banks with the stability required to continue to lend to meet the needs of the Irish economy. The banks will be expected to contribute to the economy in a verifiable manner in relation to credit and in relation to the maintenance of a payments system which is socially inclusive. They will be expected to adopt an approach to customer relationships in a way which recognises that customers need support through difficult as well as good times. The banks assure the Government that they will continue to grow lending to small and medium sized enterprises and have agreed to the following credit package:

- **Small and Medium Enterprises:** The recapitalised banks will provide at least an additional 10% capacity for lending to small to medium enterprises in 2009 from which lending will be subject to demand from viable enterprises. (SMEs are to be defined in accordance with the requirements under EU State aid Regulations.)

- **Code of practice for business lending**: Business lending by the recapitalised banks will be supported by a new code of practice for business lending which will be developed by the Financial Regulator. The recapitalised banks have committed to work closely with the Financial Regulator and the IBF to develop this code which will be introduced before end of January 2009. The code will provide for issues such as appropriate notice before change of banking facilities, arrangements to work with small businesses in difficulty and reassurance that sustainable and productive business propositions will not be declined loan facilites.

- **Mortgages/First time buyers**: The recapitalised banks will provide an additional 30% capacity for lending to first time buyers in 2009. Take up will be subject to demand and the banks have committed to actively promote mortgage lending at competitive rates with increased transparency on the criteria to be met.

- **Mortgage Arrears**: The banks will take action to assist householders who are in arrears. The recapitalised banks already comply fully with the voluntary IBF Code on mortgage arrears and repossession and refer customers to the Money, Advice and Budgeting Service where appropriate. The banks have confirmed that those in default on their home loans will treated with respect and that they will work with mortgage holders to ensure that repossession is truly an option of last resort. Furthermore the recapitalised banks have confirmed to Government that they will wait at least six months from the time arrears first arise before the enforcement of any legal action on repossession of a customer's primary residence.

- **Basic bank account:** The recapitalised banks have committed to broaden the provision of basic or introductory bank accounts and will promote these accounts to socio-economic groups where the holding of bank accounts is less prevalent and to those who find that a current account does not suit their basic banking needs. The Department of Social and Family Affairs will continue its engagement with the financial institutions with a view to increasing availability and demand for basic bank accounts. Each bank can develop the form of its basic bank account in discussion with the Financial Regulator and in all cases it will provide cash card facilities. In support of this initiative the Government will arrange that stamp duty will not apply to cash cards for basic bank accounts. Detailed targets for basic bank accounts will be negotiated with each institution.

- **Environmental Improvements:** Each recapitalised bank will introduce a €100m fund to support environment friendly investments with a view to reducing energy usage, facilitating switching to renewable energies with a view to reducing Ireland's carbon footprint.

- **Financial education**: The recapitalised banks will provide funding and other resources, in cooperation with the Financial Regulator, to support and develop financial education for consumers and potential consumers. The resources to be made available will take account of the Financial Regulator's Financial Capability Study and the Report of the Steering Group on Financial Education.

- **Customer Communications**: The recapitalised banks will continue to improve the transparency of the terms and conditions of products, of charges, of marketing and of sales processes and procedures. Proposals in this regard will be submitted to the Financial Regulator in January 2009.

ENDS

Note for editors:

The Government's announcement today is the next step in the implementation of the recapitalisation programme for financial institutions announced last weekend.

It involves investment of high-quality share capital in the three main financial institutions in Ireland as follows:

AIB: €2bn investment at 8% return per annum

BOI: €2bn investment at 8% return per annum

Anglo Irish Bank: €1.5bn investment at 10% return per annum

The main objective of the initiative is to ensure that the major banks in Ireland are capitalised to meet the economy's financial needs. This capital investment will ensure that capital ratios in the Irish banks will meet the expectations of international investors.

The State will be remunerated on an annual basis in respect of this investment with the equivalent of almost €500m in dividends, either in cash or in ordinary shares.

Shareholder, regulatory and European Commission approval will be required.

The State will have significant voting rights, equivalent to 75% control in Anglo Irish Bank, and 25% in respect of key issues in AIB / BOI.

The remuneration structure to the State is designed to encourage institutions to redeem the State investment in due course.

Detailed terms and conditions for each proposed recapitalisation are attached in the Annex.

<u>Technical notes:</u>

Core Tier 1 Capital: This is capital which is equivalent to ordinary share capital, which a financial institution uses to absorb losses.

Preference Shares: This is a particular type of share capital which confers particular rights, including priority payment of any dividend.

The preference shares rank pari passu (equivalent) to ordinary shares in liquidation. The annual dividend is non-cumulative and ranks pari passu with dividend claims of other preference shares. Should cash not be available to pay the preference share dividend then the bank must issue ordinary shares to the State as payment in kind. In the event that the preference share dividend is not paid in cash, no dividend may be paid on the ordinary shares.

Non-convertibility: This means that preference shares are perpetual (no fixed maturity date), and at no stage convert into ordinary shares.

Coupon annual payment: This is the annual rate of return which is payable on a preference share.

Annex

Sunday 21 December

Indicative Preference Share termsheet

(Subject to approval by the EU Commission and AIB shareholders)

Form of Security:	Core Tier 1 non-cumulative Preference Share
Size:	€2.0bn
Transferability:	Transferable, if voting rights removed
Dividend:	• Fixed Dividend of 8% payable annually at the discretion of the bank • Dividends payable in cash. If not able to pay in cash then paid in the form of ordinary shares. Calculated on the basis of unpaid dividend divided by the Share Value. Share Value is calculated based on the average daily closing price over the 30 trading days preceding the dividend declaration date • Payment of dividends made in priority to dividends on ordinary shares
Term:	Perpetual, no step-up
Redemption:	• Redemption at issuers option • Bank can repurchase at par for 5 yrs and thereafter at 125% of par, subject to replacement of capital and IFSRA approval • Replacement Capital needs to be Core Tier 1
Ranking:	Pari Passu to ordinary share capital on liquidation and with other preference shares for dividends
Dividend Stopper:	Yes, if cash Preference Share dividend is unpaid
Voting and appointment rights	Right to appoint 25% of directors (currently including any directors appointed under the Government's Guarantee Scheme) Voting rights in respect of: • Changes in the capital structure or any capital issuance or redemption by the bank other than the redemption of these preference shares • Change of control transaction over 50% • Board appointments (so as to leave the Minister 25% of total ordinary voting rights)

Sunday 21 December

Indicative Preference Share termsheet

(Subject to approval the EU Commission and BOI shareholders)

Form of Security:	Core Tier 1 non-cumulative Preference Share
Size:	€2.0bn
Transferability:	Transferable, if voting rights removed
Dividend:	• Fixed Dividend of 8% payable annually at the discretion of the bank • Dividends payable in cash. If not able to pay in cash then paid in the form of ordinary shares. Calculated on the basis of unpaid dividend divided by the Share Value. Share Value is calculated based on the average daily closing price over the 30 trading days preceding the dividend declaration date • Payment of dividends made in priority to dividends on ordinary shares
Term:	Perpetual, no step-up
Redemption:	• Redemption at issuers option • Bank can repurchase at par for 5 yrs and thereafter at 125% of par, subject to replacement of capital and IFSRA approval • Replacement Capital needs to be Core Tier 1
Ranking:	Pari Passu to ordinary share capital on liquidation and other preference shares for dividends
Dividend Stopper:	Yes, if cash Preference Share dividend is unpaid
Voting and appointment rights	Right to appoint 25% of directors (currently including any directors appointed under the Government's Guarantee Scheme) Voting rights in respect of: • Changes in the capital structure or any capital issuance or redemption by the bank other than the redemption of these preference shares • Change of control transaction over 50% • Board appointments (so as to leave the Minister 25% of total ordinary voting rights)

Sunday 21 December 2008

ANGLO IRISH BANK

Indicative Preference Share termsheet

(Subject to approval by the EU Commission and Anglo Irish Shareholders)

Form of Security:	Core Tier 1 non-cumulative Preference Share with voting rights
Size:	€1.5bn
Transferability:	Not transferable
Dividend:	• Fixed Dividend of 10% payable, at the discretion of the bank, annually on January 16th • Dividends payable in cash. If not able to pay in cash then paid in the form of ordinary shares. Calculated on the basis of unpaid dividend divided by the Share Value. Share Value is calculated based on the average daily closing price over the 30 trading days preceding the dividend declaration date • Payment of dividends made in priority to dividends on ordinary shares
Term:	Perpetual, no step-up
Redemption:	• Redemption at issuers option • Bank can repurchase at par for 5 yrs and thereafter at 125% of par, subject to replacement of capital and IFSRA approval • Replacement Capital needs to be Core Tier 1
Ranking:	Pari Passu to ordinary share capital on liquidation and with other preference shares for dividends
Dividend Stopper:	Yes, if cash Preference Share dividend is unpaid
Voting rights	• Full voting rights as long as preference shares outstanding • Voting rights to represent 75% of total voting rights
Timetable:	Sunday, 21 Dec, 2008: Announce €1.5bn capital injection Tuesday, 23rd Dec, 2008: Anglo to publish Shareholder circular Friday, 16th Jan, 2009: EGM held to approve capital increase
Other Items:	• Management and Board change • Board will have Government representation • Restructuring plan after six months in line with EU Commission guidance

1. Recapitalise the banks

Are you going to recapitalise the banks?

We have put in place a wide guarantee for the banking system in Ireland

The legislative scheme setting out the terms and conditions for the guarantee to support the long-term viability of the banking system in Ireland and safeguard the interests of taxpayers will be presented to the Houses of the Oireachtas tomorrow.

The guarantee has to date been successful in stabilising the position of the banking system in Ireland during an unprecedented period in international financial markets.

It has been approved as being in compliance with the European Commission's requirements.

Sunday's euro group plan sets out a toolbox of measures which individual Member States may avail of according to their national circumstances in order to buttress their financial sectors.

Ireland had already taken effective and decisive action with the announcement of its guarantee scheme. The Scheme provides a detailed framework for the authorities to oversee and guide the assessment of strategic options by the banks themselves

The Irish Scheme is firmly aligned with the main themes of the euro group plan which contains an option to provide additional capital resources where appropriate to the banks.

If it is the case that an assessment is made by a particular institution that higher capitalisation would be appropriate, the first step is for the institution itself to consider all possible options to meet this requirement.

Is the Minister going to re-capitalise the banks?

The purpose of this Scheme is to provide for the provision of a guarantee to assist the covered institutions in accessing their required liquidity.

Ref No F513/40/09

8 February 2010

Memorandum for the Government
State Aid Notification of Capital Support for Anglo Irish Bank, Irish Nationwide Building Society and the Educational Building Society

Decision Sought

1. The Minister for Finance requests Government approval for notification to the European Commission for State aid approval for:-

   (i) The capital support measure for Anglo Irish Bank and Irish Nationwide Building Society (INBS) set out in Section 3 of this Memorandum below.

   (ii) The provision of capital into the Educational Building Society (EBS) and INBS through the Special Investment Share (SIS) mechanism put in place through the amendments to the Building Societies Acts contained in the NAMA Act.

2. The Minister requests the Government to note that:-

   (i) Final Government approval will be sought for the implementation of the above measures shortly once:-

   - the extent of the capital support required for each institution is confirmed through the process finalising their end-year (2009) financial accounts;

   - confirmation is received from the Financial Regulator regarding the regulatory capital treatment of the proposed capital support measures; and

   - the Central Statistics Office finalises its position on the treatment of the measures in the General Government accounts.

   (ii) It is proposed that the announcement of these measures will coincide with a broader announcement in early March regarding the capital needs of the domestic banking sector as a whole in the context of the implementation of NAMA and how it is expected that these capital requirements would be met.

3. Proposal

It is proposed that the Minister will issue Promissory Notes to Anglo and INBS that will enable them to meet regulatory capital requirements at end-2009 and also in the context of the capital write-downs and the reduction in the institutions' assets following the loan transfers into NAMA. The Note will, therefore, underpin the institutions' capital positions which might otherwise create the risk of a call under the

Bank Guarantee. Under the proposed terms of the Note the institutions could call on cash payments of a proportion of its principal value for a period of up to 10 years. The Note would be payable in full on wind-up of the institutions should that happen.

The proposal will allow the State to spread the expected capital requirements of Anglo and INBS arising from the incurred losses arising mainly from the transfer of assets into NAMA over an extended period rather than having to provide this level of capital in the first quarter 2010 which would create a major additional burden on the State's funding requirements and would also give rise to a significant increase in the 2010 General Government Deficit.

The timeframe for the implementation of the proposal will be determined by the State aid approval process, the implementation of the NAMA Scheme, the finalisation of the end-year accounts of the institutions and the Minister's proposed announcement on capital requirements in the Irish banks.

4. Background

The Minister stated in his Second Stage Speech on the NAMA Bill on 16 September 2009, that it is likely that some institutions will require additional capital in order to absorb the losses arising from the transfer of their impaired assets to NAMA and in order to maintain appropriate levels of capital. The Minister confirmed that to the extent that sufficient capital cannot be raised independently or generated internally, the Government was committed to providing such banks and building societies with an appropriate level of capital to continue to meet their requirements. This statement has played an important role in maintaining confidence and providing stability and certainty regarding the capital position of institutions which it is expected will participate in NAMA. In addition, the Minister has made clear that additional capital would be required in Anglo once a determination of its losses for 2009 was made.

5. Anglo

In the case of Anglo, it has been clear that the bank would need further support over and above the €4bn injected in mid-2009. The bank has been undertaking a detailed Asset Quality Review for some time to help quantify the scale of its end-year impairments for some time. Prior to end-year the Bank advised that preliminary numbers indicted that the level of likely impairments was such that a capital gap would arise in the bank's end-year accounts and give rise to a risk that a call would be made in respect of debt securities guaranteed by the State. The Bank has been revising its estimates in the light of a through review of its loan book, the NAMA valuations coming through and the continued difficult economic conditions and expects to confirm the final figures shortly.

6. INBS

The Minister's accounting advisors, PwC, confirmed in December that INBS has very significant impairments. The magnitude of these impairments is such that, if all the necessary provisions were included in the institution's end year accounts a capital gap would arise and could trigger a call on the bonds and ultimately the State guarantee.

7. Support Letter

A support letter was provided by the Minister to the Boards of Anglo and INBS on 22 December 2010 to safeguard their balance sheet position. This letter gave a commitment to finding a method to support their capital position in order to maintain minimum levels of regulatory capital.

8. European Commission State Aid

The European Commission was made aware of the proposed measure before Christmas and a draft State aid notification was recently submitted to the Commission. Subject to Government approval for the measure a formal notification will be made to the Commission this week. It is expected that once the measure is notified that State aid approval will be forthcoming within two weeks. It has been indicated that the European Commission in approving the measure will initiate procedures for a formal investigation of the measure under State aid rules.

9. General Government Accounts Treatment

In terms of reporting on the fiscal position under Ireland's Stability Programme, the key consideration will be the impact of the measure on the General Government sector, both in terms of the General Government Balance (GGB) and the level of General Government Debt (GGD). The Department has had an initial discussion with the Central Statistics Office (CSO) and the CSO's preliminary view is that the issue of a Promissory Note would not be included in the measurement of the GGB. However it will need to be recognised in full as part of the GGD to balance the recording of the Promissory Note as an asset in the balance sheets of the institutions. In essence, if the assumption is confirmed by the CSO in line with Eurostat rules, then only cash payment for any annual injections will impact on the deficit.

10. Accounting Advice

The Minister's accounting advice is that the Promissory Note issued will be recognised as capital for accounting and regulatory capital purposes. However, the accounting treatment must be endorsed by the auditors of the respective institutions and the Financial Regulator must confirm the regulatory capital treatment. Discussions are ongoing with these bodies.

11. Views of the Attorney General's Office and the Governor of the Central Bank

[redacted]

The Governor of the Central Bank's view is that there is a benefit in spreading the costs over a number of years but the transaction should not over-capitalise Anglo or INBS. He was also concerned that the proposal also should not effectively pre-empt aspects of the Government's Decision on the long-term future of Anglo or narrow the Government's options in this regard which could potentially result in a higher ultimate Exchequer cost. This risk of overcapitalisation will be addressed through making the value of the Note variable to match only the needs to meet minimum regulatory capital requirements.

12. Special Investment Shares Investment in EBS/INBS

The Minister also proposes to take up Special Investment Shares (SIS) in EBS to recapitalise that institution. EBS are currently in merger discussions with INBS but whether a merger is allowed to go ahead will depend on European Commission State aid approval of the restructuring plans that both institutions will be required to produce.

Similarly, it is intended that the State will also provide capital to INBS through SIS. This capital injection will be undertaken on a de minimis basis to provide the Minister with control over the strategic direction of the Society. It is then planned to provide the majority of the capital support required by INBS by way of the Promissory Note mechanism as explained above.

13. Other Banks

The method proposed by the Minister to support Anglo and the INBS through the issue of a Promissory Note is certainly not an avenue available for AIB and Bank of Ireland who are in need of further capital and may be required to receive this from the State for example through the conversion of the State's Preference Shares or further purchases of bank equity by the NPRF. This is because, unlike Anglo and INBS, the State would wish to demonstrate that the investment into the two banks was a commercial investment into viable institutions and the banks were viable in the medium-term and capable of remunerating or re-paying the capital injected into them.

Government Announcement on Recapitalisation

Speaking Points

- Following its decision of 14 December 2008 to support a programme of recapitalisation for credit institutions in Ireland, the Irish Government announced on 21 December that it proposed to invest a combined €5.5bn core tier 1 capital into 3 institutions:
  - Anglo Irish Bank
  - Allied Irish Banks
  - Bank of Ireland

- The Government has asked the relevant institutions to explore private sources for further capital but is prepared to underwrite further issuance of core tier 1 capital and both Allied Irish Banks plc and Bank of Ireland have indicated an interest in such an underwriting in an amount of up to €1 billion each.

- As part of its investment the Government has taken on certain voting rights and has required compliance by the participating institutions with a credit package to ensure the continued flow of funds through the banks to individuals and businesses in the real economy.

- The proposed investments are subject to shareholder, regulatory and State Aid approval.

Background Briefing

Following on from Government Decisions of 28th November and 14th December on the recapitalisation of financial institutions, the Minister for Finance announced on 21 December specific decisions in relation to three major financial institutions – Anglo Irish Bank, Allied Irish Banks and Bank of Ireland. It is important to note that the investment is subject to shareholder, regulatory and Commission approval.

The breakdown of the proposed investment is as follows:

1. In relation to Anglo Irish Bank, an initial investment of €1.5 billion of core tier 1 capital to assist in restructuring the bank's capital. The Government will continue to reinforce the position of Anglo Irish Bank and will make further capital available if required so that it remains a sound and viable institution. The investment will be in the form of €1.5 billion of perpetual preference shares with a fixed annual dividend of 10%. The preference shares carry 75% of the voting rights of Anglo Irish Bank.
2. The Government has agreed with Bank of Ireland and Allied Irish Banks plc that they will each issue €2bn of perpetual preference shares to the State with a fixed annual dividend of 8%. These shares will have voting rights in respect

of change of control and any changes in the capital structure. They will also confer 25% of the voting rights in respect of appointments of directors and 25% of the directors on the board, currently including any directors to be appointed in connection with the Government's Guarantee Scheme.

3. The Government is also prepared to <u>underwrite further issuance</u> of core tier 1 capital and both Allied Irish Banks plc and Bank of Ireland have indicated an interest in such an underwriting in an amount of up to €1 billion each.

The objective of these decisions is to ensure that the financial system in Ireland meets the everyday financial needs of individuals, businesses and the overall economy. As part of this recapitalisation package the relevant institutions have agreed to a credit package that will help the continued flow of funds through the banks to individuals and businesses in the real economy.

See the attached Statement which contains extensive details on the terms of the investments and the credit package etc.

Annex

Government Announcement on Recapitalisation

21st December 2008

Following on from Government Decisions of 28th November and 14th December on the recapitalisation of financial institutions, the Minister for Finance has this evening announced specific decisions in relation to three major financial institutions. Commenting on the announcement;

The Taoiseach said:

"The objective of these decisions is to ensure that the financial system in Ireland meets the everyday financial needs of individuals, businesses and the overall economy. As part of this recapitalisation package, I am very pleased that a number of measures to support small to medium businesses and mortgage holders have also been announced."

In relation to Anglo Irish Bank, the Minister for Finance announces an initial investment of €1.5 billion of core tier 1 capital to assist in restructuring the bank's capital. The Government will continue to reinforce the position of Anglo Irish Bank and will make further capital available if required so that it remains a sound and viable institution. The investment will be in the form of €1.5 billion of perpetual preference shares with a fixed annual dividend of 10%. The preference shares carry 75% of the voting rights of Anglo Irish Bank. The investment is subject to the approval of the ordinary shareholders at a general meeting which will be convened as soon as possible. On the basis of positive contact with the European Commission, the Minister said he was confident that the Anglo proposal will meet with EU State Aid requirements when formally notified in due course.

Good progress continues to be made in the capital discussions with other institutions. In particular, subject to shareholder and regulatory approval, the Government has agreed with Bank of Ireland and Allied Irish Banks plc that they will each issue €2bn of perpetual preference shares to the State with a fixed annual dividend of 8%. These shares will have voting rights in respect of change of control and any changes in the capital structure. They will also confer 25% of the voting rights in respect of appointments of directors and 25% of the directors on the board, currently including any directors to be appointed in connection with the Government's Guarantee Scheme.

All the institutions may redeem the preference shares within 5 years at the issue price or after 5 years at 125% of the issue price. The preference shares are non-convertible and will be treated as core tier 1 capital by the Financial Regulator and are replaceable only with other core/equity tier 1 capital.

The capital injection for Anglo Irish Bank is likely to take place following an Extraordinary General Meeting in mid-January, and for Allied Irish Bank and Bank of Ireland, by the end of the first quarter of 2009.

The Government has a substantial pool of additional capital available to underwrite and otherwise support the issuance of core tier 1 capital by the relevant institutions.
The Government need not be the principal source of this additional capital and encourages each institution to access private sources of capital. Nonetheless, the Government is prepared to underwrite further issuance of core tier 1 capital and both Allied Irish Banks plc and Bank of Ireland have indicated an interest in such an underwriting in an amount of up to €1 billion each.

The measures announced today have been designed having regarded to the recent European Commission Recapitalisation Communication and are subject to State aid approval.

Credit Package

The provision of credit to the economy is the most immediate and pressing issue for business and for the Government. The future health of our economy is inextricably linked with the supply of credit and a situation where banks are unwilling or are perceived to be unwilling to lend is damaging not only for the economy but also for the banks themselves. Banks have an important part to play in addressing this issue and a key objective of the Government's recapitalisation initiative is to ensure the continued flow of funds through the banks to individuals and businesses in the real economy.

In response to my earlier meetings with the banks many had already announced specific programmes to boost lending to small and medium enterprises. AIB and Bank of Ireland have announced new business support and start up funds and have provided commitments to support first time buyers and consumers. While these announcements are welcome the Government believes that it is appropriate as part of the agreed recapitalisation programme that the banks should further build on the commitments given in the banks guarantee scheme through specific credit policies targeted at small medium enterprises, first time buyers and consumers generally.

The recapitalisation announced today will provide the banks with the stability required to continue to lend to meet the needs of the Irish economy. The banks will be expected to contribute to the economy in a verifiable manner in relation to credit and in relation to the maintenance of a payments system which is socially inclusive. They will be expected to adopt an approach to customer relationships in a way which recognises that customers need support through difficult as well as good times. The banks assure the Government that they will continue to grow lending to small and medium sized enterprises and have agreed to the following credit package:

- **Small and Medium Enterprises:** The recapitalised banks will provide at least an additional 10% capacity for lending to small to medium enterprises in 2009 from which lending will be subject to demand from viable enterprises. (SMEs are to be defined in accordance with the requirements under EU State aid Regulations.)

- **Code of practice for business lending**: Business lending by the recapitalised banks will be supported by a new code of practice for business lending which will be developed by the Financial Regulator. The recapitalised banks have committed to work closely with the Financial Regulator and the IBF to develop this code which will be introduced before end of January 2009. The code will provide for issues such as appropriate notice before change of banking facilities, arrangements to work with small businesses in difficulty and reassurance that sustainable and productive business propositions will not be declined loan facilites.

- **Mortgages/First time buyers**: The recapitalised banks will provide an additional 30% capacity for lending to first time buyers in 2009. Take up will be subject to demand and the banks have committed to actively promote mortgage lending at competitive rates with increased transparency on the criteria to be met.

- **Mortgage Arrears**: The banks will take action to assist householders who are in arrears. The recapitalised banks already comply fully with the voluntary IBF Code on mortgage arrears and repossession and refer customers to the Money, Advice and Budgeting Service where appropriate. The banks have confirmed that those in default on their home loans will treated with respect and that they will work with mortgage holders to ensure that repossession is truly an option of last resort. Furthermore the recapitalised banks have confirmed to Government that they will wait at least six months from the time arrears first arise before the enforcement of any legal action on repossession of a customer's primary residence.

- **Basic bank account:** The recapitalised banks have committed to broaden the provision of basic or introductory bank accounts and will promote these accounts to socio-economic groups where the holding of bank accounts is less prevalent and to those who find that a current account does not suit their basic banking needs. The Department of Social and Family Affairs will continue its engagement with the financial institutions with a view to increasing availability and demand for basic bank accounts. Each bank can develop the form of its basic bank account in discussion with the Financial Regulator and in all cases it will provide cash card facilities. In support of this initiative the Government will arrange that stamp duty will not apply to cash cards for basic bank accounts. Detailed targets for basic bank accounts will be negotiated with each institution.

- **Environmental Improvements:** Each recapitalised bank will introduce a €100m fund to support environment friendly investments with a view to reducing energy usage, facilitating switching to renewable energies with a view to reducing Ireland's carbon footprint.

- **Financial education**: The recapitalised banks will provide funding and other resources, in cooperation with the Financial Regulator, to support and develop financial education for consumers and potential consumers. The resources to be made available will take account of the Financial Regulator's Financial Capability Study and the Report of the Steering Group on Financial Education.

- **Customer Communications**: The recapitalised banks will continue to improve the transparency of the terms and conditions of products, of charges, of marketing and of sales processes and procedures. Proposals in this regard will be submitted to the Financial Regulator in January 2009.

ENDS

Note for editors:

The Government's announcement today is the next step in the implementation of the recapitalisation programme for financial institutions announced last weekend.

It involves investment of high-quality share capital in the three main financial institutions in Ireland as follows:

AIB: €2bn investment at 8% return per annum

BOI: €2bn investment at 8% return per annum

Anglo Irish Bank: €1.5bn investment at 10% return per annum

The main objective of the initiative is to ensure that the major banks in Ireland are capitalised to meet the economy's financial needs. This capital investment will ensure that capital ratios in the Irish banks will meet the expectations of international investors.

The State will be remunerated on an annual basis in respect of this investment with the equivalent of almost €500m in dividends, either in cash or in ordinary shares.

Shareholder, regulatory and European Commission approval will be required.

The State will have significant voting rights, equivalent to 75% control in Anglo Irish Bank, and 25% in respect of key issues in AIB / BOI.

The remuneration structure to the State is designed to encourage institutions to redeem the State investment in due course.

Detailed terms and conditions for each proposed recapitalisation are attached in the Annex.

Technical notes:

Core Tier 1 Capital: This is capital which is equivalent to ordinary share capital, which a financial institution uses to absorb losses.

Preference Shares: This is a particular type of share capital which confers particular rights, including priority payment of any dividend.

The preference shares rank pari passu (equivalent) to ordinary shares in liquidation. The annual dividend is non-cumulative and ranks pari passu with dividend claims of other preference shares. Should cash not be available to pay the preference share dividend then the bank must issue ordinary shares to the State as payment in kind. In the event that the preference share dividend is not paid in cash, no dividend may be paid on the ordinary shares.

Non-convertibility: This means that preference shares are perpetual (no fixed maturity date), and at no stage convert into ordinary shares.

Coupon annual payment: This is the annual rate of return which is payable on a preference share.

Annex

Sunday 21 December

<u>Indicative Preference Share termsheet</u>

(Subject to approval by the EU Commission and AIB shareholders)

Form of Security:	Core Tier 1 non-cumulative Preference Share
Size:	€2.0bn
Transferability:	Transferable, if voting rights removed
Dividend:	• Fixed Dividend of 8% payable annually at the discretion of the bank • Dividends payable in cash. If not able to pay in cash then paid in the form of ordinary shares. Calculated on the basis of unpaid dividend divided by the Share Value. Share Value is calculated based on the average daily closing price over the 30 trading days preceding the dividend declaration date • Payment of dividends made in priority to dividends on ordinary shares
Term:	Perpetual, no step-up
Redemption:	• Redemption at issuers option • Bank can repurchase at par for 5 yrs and thereafter at 125% of par, subject to replacement of capital and IFSRA approval • Replacement Capital needs to be Core Tier 1
Ranking:	Pari Passu to ordinary share capital on liquidation and with other preference shares for dividends
Dividend Stopper:	Yes, if cash Preference Share dividend is unpaid
Voting and appointment rights	Right to appoint 25% of directors (currently including any directors appointed under the Government's Guarantee Scheme) Voting rights in respect of: • Changes in the capital structure or any capital issuance or redemption by the bank other than the redemption of these preference shares • Change of control transaction over 50% • Board appointments (so as to leave the Minister 25% of total ordinary voting rights)

Sunday 21 December

Indicative Preference Share termsheet

(Subject to approval the EU Commission and BOI shareholders)

Form of Security:	Core Tier 1 non-cumulative Preference Share
Size:	€2.0bn
Transferability:	Transferable, if voting rights removed
Dividend:	• Fixed Dividend of 8% payable annually at the discretion of the bank • Dividends payable in cash. If not able to pay in cash then paid in the form of ordinary shares. Calculated on the basis of unpaid dividend divided by the Share Value. Share Value is calculated based on the average daily closing price over the 30 trading days preceding the dividend declaration date • Payment of dividends made in priority to dividends on ordinary shares
Term:	Perpetual, no step-up
Redemption:	• Redemption at issuers option • Bank can repurchase at par for 5 yrs and thereafter at 125% of par, subject to replacement of capital and IFSRA approval • Replacement Capital needs to be Core Tier 1
Ranking:	Pari Passu to ordinary share capital on liquidation and other preference shares for dividends
Dividend Stopper:	Yes, if cash Preference Share dividend is unpaid
Voting and appointment rights	Right to appoint 25% of directors (currently including any directors appointed under the Government's Guarantee Scheme) Voting rights in respect of: • Changes in the capital structure or any capital issuance or redemption by the bank other than the redemption of these preference shares • Change of control transaction over 50% • Board appointments (so as to leave the Minister 25% of total ordinary voting rights)

Sunday 21 December 2008

ANGLO IRISH BANK

Indicative Preference Share termsheet

(Subject to approval by the EU Commission and Anglo Irish Shareholders)

Form of Security:	Core Tier 1 non-cumulative Preference Share with voting rights
Size:	€1.5bn
Transferability:	Not transferable
Dividend:	• Fixed Dividend of 10% payable, at the discretion of the bank, annually on January 16th • Dividends payable in cash. If not able to pay in cash then paid in the form of ordinary shares. Calculated on the basis of unpaid dividend divided by the Share Value. Share Value is calculated based on the average daily closing price over the 30 trading days preceding the dividend declaration date • Payment of dividends made in priority to dividends on ordinary shares
Term:	Perpetual, no step-up
Redemption:	• Redemption at issuers option • Bank can repurchase at par for 5 yrs and thereafter at 125% of par, subject to replacement of capital and IFSRA approval • Replacement Capital needs to be Core Tier 1
Ranking:	Pari Passu to ordinary share capital on liquidation and with other preference shares for dividends
Dividend Stopper:	Yes, if cash Preference Share dividend is unpaid
Voting rights	• Full voting rights as long as preference shares outstanding • Voting rights to represent 75% of total voting rights
Timetable:	Sunday, 21 Dec, 2008: Announce €1.5bn capital injection Tuesday, 23rd Dec, 2008: Anglo to publish Shareholder circular Friday, 16th Jan, 2009: EGM held to approve capital increase
Other Items:	• Management and Board change • Board will have Government representation • Restructuring plan after six months in line with EU Commission guidance

SECRET
Oifig an Aire Airgeadais

Ref No **Date: 11th February 2009**

Memorandum for Government
Recapitalisation of the Banking System

Decision sought

1. Approval is sought for
   (i) terms for the recapitalisation of Bank of Ireland and AIB to be announced this evening, as summarised at paragraph 3 and set out in the term sheet attached at Appendix 1. A summary of the term sheets is attached to the announcement at Appendix 2. The total recapitalisation purchase is €7bn - €3.5bn for each bank. The term sheet is subject to EU State aid approval and amendments agreed by the Minister for Finance and the Banks;
   (ii) The €7bn will be provided from the National Pensions Reserve Fund, €4 billion of which will come from the Fund's existing resources and €3bn by means of a frontloading of the 2009 and 2010 Exchequer contributions;
   (iii) the Bank Customer package which has been negotiated with the banks in the context of the recapitalisation as set out at Paragraphs 25-30 below;
   (iv) an announcement that at the end-March review of the guarantee Scheme, we intend to engage with the European Commission to discuss revision of the Scheme to encompass longer-term bond issuance by the Banks, consistent with State aid requirements;
   (v) an announcement that, taking into account EU and market developments, the Government will examine various options to deal with riskier parts of the banks' loan books, i.e. land and development, on a basis which would eventually lead to a favourable outcome for the taxpayers; and
   (vi) the broad terms of the proposed announcement (Appendix 2)

   Government is also asked to note that the banks have agreed that total remuneration for all senior executives will be reduced by at least 25%. No performance bonuses will be paid for these senior executives and no salary increases will be made in relation to 2008 and 2009. The two banks have also accepted that, for non-executive directors, fees will be reduced by at least 25%.

Why Recapitalise the Banks

2. The international financial crisis which led to numerous State interventions in national banking systems across the world is proving to be acute and prolonged.

   Against this background, particularly in a situation where there is extensive exposure to land and development loans in the Irish banking sector, the funding positions of Irish banks have weakened significantly in recent weeks. One effect of increasing loan impairments, whether already acknowledged or expected in the next few years, has been increased market expectations of the levels of quality capital (i.e Core Tier 1) banks require.

Higher levels of capital are required not only in response to market demands to provide a buffer for expected losses and underpin the solvency of the banks but also to allow for continued lending and to support our banking sector in attracting the funding needed to help the economy deal with the very unfavourable international climate.

Significant falls in the share prices of Irish banks in recent months are evidence of the market's belief that the Irish banks are undercapitalised.

3. Against the background of increasing concern about impairments and in the context of the taking into State ownership of Anglo Irish Bank, it has become clear that the Banks require an increased level of capital and at an accelerated rate. While the immediate proposals are aimed at addressing difficulties for Bank of Ireland and AIB, appropriate measures will have to be taken with regard to INBS, ILP and EBS. The situation regarding these banks is set out below.

4. Capitalisation of AIB and BOI, and measures aimed at the other institutions, will help the current situation. It is absolutely necessary to prevent our banks from being significantly downgraded by the rating agencies, which would have an immediate effect on funding and thereafter on lending capacity and the economy. Such downgrades could have a knock-on effect on the State's own credit rating. However recapitalisation can only be one part of an overall response.

Capitalisation

5. The main features of the proposed recapitalisation are:
    - The Government will provide €3.5bn in Core Tier 1 capital for each bank.
    - In return for the overall investment the Minister will get preference shares with a fixed dividend of 8% payable in cash or ordinary shares in lieu. These preference shares can be redeemed at par up to the fifth anniversary of the issue and at 125% of face value thereafter.
    - The Minister can appoint, in total, 25% of the directors to both banks.
    - The Minister also gets 25% of total ordinary voting rights in respect of certain functions including change of control and board appointments.
    - Warrants attached to the Preference Shares give an option to purchase 25% of the ordinary share capital of each bank existing on the date of issue of the New Preference Shares. The strike price of the first 15% of the Warrants exercised by the State shall be €0.975 for AIB and €0.52 for BOI. The strike price of the balance of the Warrants shall be €0.375 for AIB and €0.20 for BOI.
    - If the bank redeems up to €1.5bn of the State investment in New Preference Shares from privately sourced Core Tier 1 capital prior to 31 December 2009, then the Warrants will be reduced pro rata to that redemption to an amount representing not less than 15% of the ordinary shares of the bank.

6. The original proposed Capitalisation Scheme was announced in December. At that time, it was proposed that the State would provide €2bn upfront and underwrite another €1bn to be sought by the banks from existing and new investors. Market conditions in relation to such share subscription are such that private investors will not subscribe to such equity on acceptable terms at present.

7. An additional €500m is now provided to each bank because the continued turbulence in the market means that more capital is needed to ensure the banks' position. Furthermore, the banks now consider that they need the money upfront, but they would still like the opportunity to seek to raise some of the money before the end of the year and this is provided for in this deal. The additional €[500]m has been agreed as appropriate by the Banks themselves and is recommended by the Governor of the Central Bank, the NTMA and my officials in the Department of Finance.

8. The terms have also been amended to provide the banks with some discretion as to when the coupon is paid. This strengthens the position of the banks in the market, which is the purpose of the investment. However, the requirement for the allocation of shares in lieu and the accrual of related voting rights is a firm incentive to ensure prompt settlement by the banks.

9. A further change from the 21 December 2008 package is the issuing of warrants (i.e. options to purchase shares). This significantly strengthens the Minister's position and ensures that the State will benefit from any increase in the share price if the Banks recover while indicating clearly that the State does not intend to nationalise these banks.

Position of Other Covered Institutions

10. The Minister is also in discussions with the other covered institutions regarding appropriate provision. These institutions do not all have the same capitalisation requirements. Their financial positions differ significantly.

11. **EBS** has a land and development loan book which, though small, is of poor quality. They also have a commercial loan book of €1.8 billion which is of variable quality. As a result, EBS will declare large losses of about €30-35m in March 2009 for 2008 due to high loan impairment levels. However losses in future years could bring their total losses to €500m which is equivalent to 10 years pre loss earnings and would be a significant proportion of existing reserves. This announcement will trigger further downgrades by the credit rating agencies and will result in funding problems for EBS which will lead to questions as to its future viability and to consideration of the need for a merger with another institution. The Minister is in discussion with the society and will revert to Government with proposals in the near future.

12. **Irish Life and Permanent (ILP)** is adequately capitalised currently but has a very high loan to deposit ratio. Much of its loan book is secured through short term interbank borrowing that has posed significant challenges for ILP given pressures on the interbank market. It has had recourse to significant collateralised funding from the ECB which needs to be addressed. The Minister will continue to examine the position in relation to ILP.

13. In the case of **Irish Nationwide**, as with other covered institutions, the funding position remains weak. Though currently in a strong cash position, the prospect of further ratings downgrades and resulting deposit outflows could seriously weaken the Society's position over a short period. The society has a very large development loan book. My Department is closely monitoring the position with a

view to exploring contingency arrangements for dealing with Irish Nationwide in the coming months.

Review of Guarantee Scheme

14. Many countries have introduced guarantee schemes that facilitate their banks in issuing longer term debt, e.g. up to five year bonds in limited and exceptional circumstances. Irish banks owing to the end-September 2010 legislative deadline applying to the guarantee Scheme have in practice have been unable to issue new bonds for a period extending beyond the guarantee. It is clearly in the interests of the stability of the financial system that banks are able to raise longer-term money and reduce their dependency on short term money markets. It is not proposed to increase the State's exposure under the guarantee Scheme but to announce that as part of the review of the guarantee Scheme to be completed by end-March this year, we intend to engage with the European Commission to discuss revision of the Scheme to encompass longer-term bond issuance by the banks, consistent with State aid requirements.

Loan Impairments

15. The primary concern surrounding the Irish banking sector is the potential for heavy losses on loans on the banks' balance sheets. As long as this issue remains unaddressed the banks have argued that markets will continue to have doubts about the ability of the Irish banks to absorb these losses resulting in continued funding difficulties and an incentive not to engage in further lending. The primary area of concern is the land and development loan books of the banks. The total value of the loans in this category is €34bn for AIB and BOI, as illustrated in the table below. The table highlights the level of land and development loans in these institutions as well as likely level of impairments on these books as assessed by PricewaterhouseCoopers and Jones Lang LaSalle in reviews undertaken for the Regulator and the NTMA. Increasingly, markets and other countries are looking to asset side solutions to supplement other actions taken to address the current crisis. A common EU framework has been proposed for asset protection scheme. Large projected falls in the value of property here makes the issue even more pressing in the view of Irish banks

Institution €B	BOI	AIB	**Total**		Anglo	INBS	EBS	**Total**
Total Land & Development Loans	13	21	**34**		19.7	5.6	0.5	**25.8**
Impairment Over 3-5 years	2.9	4.6	**7.5**		5	1.6	0.2	**6.8**

16.

The Minister for Finance considers that some action may have to be taken to deal with the riskier parts of the banks' loan books, i.e. land and development but he does not favour arrangements which leave the taxpayer exposed to undue risks which should be borne by the banks' shareholders. Any such arrangement should ensure a commercial outcome for the State. The Minister proposes that in examining the options, he will take into account EU and market developments. The UK has announced, in outline, a risk insurance scheme but will not be announcing the terms until end of February. The Minister proposes that the announcement today will indicate that we are looking at risk on the land/development part of the banks' loan books but will not commit us to any particular model or scheme. The banks themselves have made a proposal for risk insurance and this is analysed at Appendix 3.

EU Commission

17. The Minister's Department and its commercial legal advisers Arthur Cox have consulted with the Commission on the recapitalisation proposals. The Commission have expressed concerns that the proposed 8% remuneration level for the State's investment is low and have requested analysis of the rate of return when account is taken of the warrants, redemption and other terms. They have also highlighted the requirement for a viability plan subject to Commission approval in respect of both institutions on the basis that they do not regard the banks as meeting the Commission's risk profile for "fundamentally strong" institutions.

18. The Department's assessment is that the coupon rate is appropriate and within guidelines set down in this regard by the European Commission. It also considers that agreement on the restructuring plan requirement, and provision to the Commission of the additional information required on the rate of return, will allow us to meet Commission requirements for approval of the recapitalisation measure.

19. The proposal to revise the guarantee Scheme has been raised with the Commission. EU officials stressed that they would require specific details of the proposals and that Member States cannot select the most favourable elements of different guarantee models. The draft announcement addresses this point by noting that the Government will examine how the Scheme could be revised subject to European Commission approval and consistent with EU State aid requirements to achieve a reduction in risk overall, including by supporting longer-term bond issuance by the covered institutions.

20. Options to deal with risk on banks' loan books have not been raised formally with the Commission to date. The Commission have, however, been advised that in line with other EU Member States various options are under examination. The Department of Finance's assessment is that the Commission would not object to a statement which said that the Government intends to examine various options to address, this providing the statement highlights the intention to consult with the Commission and conform to State aid requirements.

Remuneration

21. In conjunction with this support, it is proposed that significant reductions be made in remuneration of Directors and senior executives of the covered institutions ie AIB, BOI, Anglo, ILP, EBS and INBS. The banks accept that pay restraint is important in the overall context of the economy and the supports being provided by the taxpayer, and will act accordingly. As a step in this direction, both AIB and Bank of Ireland accept that the pay of senior executives will be curtailed. Total remuneration for all senior executives will be reduced by at least 25%. No performance bonuses will be paid for these senior executives and no salary increases will be made in relation to 2008 and 2009. The two banks have

also accepted that, for non-executive directors, fees will be reduced by at least 25%.

22. The question of bonuses and pension arrangements will be reviewed further following the report of the independent committee appointed to advise the Minister for Finance under the Guarantee Scheme. The CIROC report on remuneration in banks is expected shortly. The role of CIROC is to consider the remuneration plans of each of the institutions covered by the Government guarantee and make recommendations to the Minister.

Governance

23. The Minister intends to review governance arrangements for financial institutions, including the question of renewal of their boards. The banks have indicated that they are agreeable to the issue of a statement of intent regarding such a review.

Implementation

24. Funds required to meet recapitalisation will be provided by the National Pension Reserve Fund over the course of 2009 and 2010 subject to the enactment by the Oireachtas of the NPRF Amendment Bill. The fund at end of 2008 had liquid assets of €4bn. The Exchequer will fund the remaining €3bn for the moment, but this will be recouped by the Exchequer by offsetting it against the annual contribution to the NPRF. Interest and shares received on foot of the preference shares investment will accrue to the NPRF.

Bank Customers Package

25. The banks have reconfirmed their December commitment to increase lending capacity to small and medium enterprises by 10% and to provide an additional 30% capacity for lending to first time buyers in 2009. The banks have committed to public campaigns to actively promote their lending to these sectors. A €100m environmental improvement fund is also being established by each bank.

26. Statutory codes of practice on business lending and mortgage arrears have been finalised and will be published by the Financial Regulator in the coming days. The business lending code will require banks to offer annual review meetings, to inform customers of the basis for decisions made and to have written procedures for the proper handling of complaints. Where a customer gets into difficulty the banks will seek to agree an approach to resolve problems and provide reasonable time and appropriate advice.

27. Under the mortgage arrears code where a borrower is in difficulty the lender will make every reasonable effort to agree an alternative repayment schedule and will only commence legal action for repossession after six months from the time arrears first arise. Furthermore the two recapitalised banks will not enforce repossession of a principal private residence within 12 months of arrears appearing, where the customer continues to cooperate reasonably and honestly with the bank. The banks have assured Government that in the normal course of events they will make every effort to avoid repossessions, as has been evidenced by the low level of repossessions by them to date.

28. The availability of a pool of skilled support for major companies and construction projects is an essential component of Ireland's attraction as a business location. The recapitalised banks have agreed to work closely with the IDA, Enterprise Ireland and with State agencies to ensure the supply of appropriate finance to contractors engaged on major projects sponsored by them.

29. More generally, the banks have agreed to engage in a 'clearing group' chaired by a Government representative and including representation from business interests and State agencies. The purpose of this group will be to identify specific patterns of events or cases where the flow of credit to viable projects appears to be blocked and to seek to identify credit supply solutions. The recapitalised banks have also agreed to fund and cooperate with an independent review of credit availability which will be managed jointly by the banks, Government and business representatives.

30. The banks have also agreed to each provide €15m to a new seed capital fund with Enterprise Ireland, and have also committed to abide by prompt payment rules requiring payment within 30 days and an interest charge on late payments. Full details of the customer package are attached at Appendix 2 along with the proposed announcement and summary term sheet.

Conclusion

31. This overall package deals with the main issues facing the two big banks at present and should assist in efforts to provide lending into the Irish economy.

32. Recapitalisation will support stability because improving the capital position of the two banks will help build market confidence, secure their funding position and allow them to engage in new lending. In the current environment, an 8% coupon offers the State appropriate return, and the State gets shares in lieu if the payment is not made.

33. Additionally, the warrants give the State an opportunity to benefit from any improvement in either bank's share price. Further, risk reduction options for discussion with the banks should offer substantial upside access to movements in the banks' share prices. This is because if the State's capital is not redeemed within a 5 year period, there is option to purchase a 25% stake in the banks at a strike price for the Core Tranche of warrants €0.975 for AIB and €0.52 for BoI – the strike price of the balance of the warrants shall be €0.375 for AIB and €0.20 for BoI.

34. A signal that the Government is looking at risk should be of some help to the market assessment of the banks. Stability and confidence are needed at this time because the markets are fragile and there is significant negative sentiment about Ireland. The proposals in relation to capitalisation, the Guarantee arrangements and dealing with risk in relation to land and development loans have been recommended to the Minister for Finance and the Government by the Governor

of the Central Bank, the Financial Regulator, the NTMA, his own Department officials and his financial and legal advisors.

An Roinn Airgeadais
Department of Finance

BANKING IMPLEMENTATION GROUP

BRIEFING PACK

RESTRUCTURING AND REORGANISATION OF THE CERTAIN IRISH BANKS

UNDER

EU/IMF PROGRAMME OF FINANCIAL SUPPORT FOR IRELAND

AUGUST 2011

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TABLE OF CONTENTS

1. INTRODUCTION – BANKING IMPLEMENTATION GROUP

1.1 The Banking Implementation Group

In March 2010 the Government delegated to the NTMA certain banking system functions of the Minister for Finance (the "**Minister**"), related to the oversight and management of the State's interest and holdings in those financial institutions covered by the 2008 Government guarantee.

The main functions delegated to the NTMA and the parameters set out in the directions issued by the Minister can be summarised as follows:

- to lead discussions with the covered credit institutions to determine their likely capital requirements;
- to negotiate the terms and conditions on which any capital support provided by the State will be invested;
- to manage any Ministerial shareholdings in these institutions.

Following the change of Government, in April 2011 the Minister announced that a stand-alone unit accountable to him through the Department of Finance (the "**DoF")** would be created to provide State oversight of the banking system and that this Unit would be strengthened as necessary and draw on the resources of the NTMA to carry out its work. The NTMA has worked closely with the DoF on the implementation of the new structure which involved the secondment of the NTMA Banking Unit to the Department and the ending of the delegation of banking system functions to the NTMA in August 2011.[1] The NTMA Banking Unit seconded to the department has now come to constitute the DoF Banking Implementation Group.

2. PROGRAMME OF FINANCIAL SUPPORT AND PCAR/PLAR

2.1 Programme of Financial Support

The EU/IMF Programme of Financial Support for Ireland (the "**Programme**") is the collective name for the documents agreed with European Commission, the ECB and the IMF setting out the policy conditions for the provision of financial support to Ireland by the EU member states (via the European Financial Stabilisation Mechanism, the European Financial Stability Facility and the bi-lateral loans from the UK, Sweden and Denmark) and the International Monetary Fund.[2]

[1] Source: http://www.ntma.ie/BankingSystemFunctions/BSFhome.php

[2] Source: "Statement by Minister for Finance, Brian Lenihan T.D. on the EU/IMF Programme for Ireland and the National Recovery Plan 2011 to 2014" – 1 December 2010 as found at http://www.finance.gov.ie/viewdoc.asp?DocID=6602&CatID=54&StartDate=01+January+2010

The Programme has two parts – the first part deals with bank restructuring and reorganisation and the second part deals with fiscal policy and structural reform.

In relation to bank restructuring and reorganisation the Programme provides for a fundamental downsizing and reorganisation of the banking sector so it is proportionate to the size of the economy, the recapitalisation of Irish Banks to the highest international standards, and to return Irish Banks to a position of normal market funding.[3]

The main elements of the Programme[4] in relation to the banking sector is set out below. The list has been segregated into actions in connection with (1) restructuring and reorganisation and (2) regulation and legislation:

Restructuring and reorganisation

- Further recapitalisations to take place in the first half of 2011 as necessary based on the results of a detailed review and updating of the banks' capital needs following a revised Prudential Capital Assessment Review ("**PCAR**") exercise undertaken by the Central Bank of Ireland and involving stringent stress testing. See 2.2 below for further details.

- A Prudential Liquidity Assessment Review ("**PLAR**") to be implemented by the Central Bank of Ireland for the domestic banks to identify deleveraging actions necessary to significantly reduce their reliance on short term funding .See 2.2 below for further details.

- A substantial downsizing of the banking system to be achieved through early and decisive actions including:

    - Banks will be required to run down non-core assets, securitize and or sell portfolios or divisions with credit enhancement provided by the State, if needed.

    - The NAMA Scheme will be extended to remove remaining vulnerable land and development loans from Bank of Ireland and Allied Irish Bank by end-Q1 2011

  This process will be carried out in a carefully balanced and controlled manner with the benefit of the substantial resources available to the banks for their funding and capital needs.

- Banks will be required to promptly and fully provide for all nonperforming assets.

- The restructuring of Anglo Irish Bank and Irish Nationwide Building Society will be swiftly completed and submitted for EU State aid approval.

Regulation and legislation

- A significant strengthening of the regulation and stability of the credit union sector will be carried out by end-2011

- A special legislative regime to resolve distressed credit institutions will be introduced early in 2011.

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[3] Source: "*Government Statement - Announcement of joint EU - IMF Programme for Ireland*" 28 November 2010 as found at http://www.finance.gov.ie/viewdoc.asp?DocID=6600&CatID=1&StartDate=01+January+2010

[4] Source: "*Government Statement - Announcement of joint EU - IMF Programme for Ireland*" 28 November 2010 as found at http://www.finance.gov.ie/viewdoc.asp?DocID=6600&CatID=1&StartDate=01+January+2010

2.2 PCAR/PLAR

Based on the Central Bank's work, as set out in the Financial Measures Report of 31 March 2011[5] (the "**FMP**"), a further €24bn, including €3bn of contingency funds, was required by the AIB, Bank of Ireland ("**BOI**"), EBS and Irish Life and Permanent ("**ILP**") for capital purposes. The split across the Covered Banks is as follows:

	AIB	BOI	EBS	ILP	Total
Capital required 2011- 2013 pre-buffer	10.5	3.7	1.2	3.3	**18.7**
Additional capital buffer (equity) imposed by the Central Bank	1.4	0.5	0.1	0.3	**2.3**
Additional capital buffer (contingent capital) imposed by the Central Bank	1.4	1.0	0.2	0.4	**3.0**
Total capital required 2011-2013	**13.3**	**5.2**	**1.5**	**4.0**	**24.0**

The process to recapitalize four domestic banks was expected to conclude by end-July. Of the total need for €24bn, the authorities expected to meet a significant portion (assumed to be about €5bn) through liability management exercises ("**LME**(s)") on subordinated bank debt.[6]

Neither Anglo Irish Bank ("**Anglo**") nor Irish Nationwide ("**INBS**") were subject to the PCAR/PLAR review announced on the 31 March 2011. The Central Bank published an addendum to the FMP on 31 May 2011 addressing whether Anglo and INBS had additional capital requirements in addition to the capital injected into each institution in 2010 (Anglo €29.3bn and INBS €5.4bn). The Central Bank sought to develop an independent view on the loss estimates that were used in the last capital estimation exercises for both Anglo and INBS which were the key drivers of the requirement for capital at that time. The Central Bank concluded that the previous analytical results were reasonable and that Anglo and INBS did not require additional capital in order to cover future losses.

3. RESTRUCTURING AND REORGANISATION OF THE IRISH BANKING SYSTEM TO DATE

Set out below are details of the main restructuring and reorganisation events in the Irish Banking System following on from the Programme and the PCAR/PLAR.

3.1 Sale of the Anglo deposit book to AIB and the INBS deposit book to ILP

Following an application by the Minister on 24 February 2011, the High Court issued two Transfer Orders on 24 February 2011 under Part 5 of the Credit Institutions (Stabilisation) Act 2010 for the immediate transfer of the deposit books and corresponding assets of Anglo and INBS to AIB and ILP respectively.

[5] Source: "The Financial Measures Programme Report" Central Bank of Ireland 31 March 2011 as found at http://www.centralbank.ie/regulation/industry-sectors/credit-institutions/Documents/ The%20Financial%20Measures%20Programme%20Report.pdf

[6] Source: "*First and Second Reviews Under the Extended Arrangement and Request for Rephasing of the Arrangement*" - 2 May 2011 - IMF as found at http://www.imf.org/external/pubs/ft/scr/2011/cr11109.pdf

The Minister, having consulted with the Governor of the Central Bank of Ireland, was of the opinion that these Transfer Orders were necessary to ensure that both Anglo and INBS are in a position to continue the process for their restructuring in accordance with the provisions of the Programme.[7]

ILP acquired €3.6bn of INBS deposits and the shares in the Isle of Man ("IOM") subsidiary of INBS[8]. AIB acquired €7.1bn of Anglo deposits located in Ireland and the UK and shares in IOM subsidiary of Anglo, which held €1.6bn of deposits[9].

3.2 Merger of Anglo and INBS

A Transfer Order was made on 1 July 2011 by the High Court in Dublin under the Credit Institutions (Stabilisation) Act 2010 transferring the assets and liabilities of INBS to Anglo with immediate effect. This achieves the legal merger of the INBS business into Anglo consistent with directions provided to both entities.

As a result, former INBS business units will be positioned in Anglo's operating model as a stand-alone division and INBS as a brand ceased to exist from 1 July 2011 onwards.

Under the terms of the Transfer Order, all INBS employees automatically transferred to Anglo, with their terms and conditions safeguarded in accordance with applicable employment legislation.[10]

3.3 Merger of AIB and EBS

AIB completed the acquisition of EBS on 1 July 2011 which was a significant milestone in the formation of one of two pillar banks in Ireland. EBS, which will now be called EBS Limited, will initially operate as a standalone, separately branded subsidiary of AIB with its own branch network. [11]

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[7] Source: Press Release – Department of Finance – 24 February 2011 – "*Transfer of Anglo Irish Bank's and Irish Nationwide Building Society's deposit books*" as found at http://www.finance.gov.ie/viewdoc.asp?DocID=6704&CatID=1&StartDate=1+January+2011

[8] Source: RNS Irish Life & Permanent Group Holdings plc – "*Statement on the Transfer of selected assets and liabilities from Irish Nationwide Building Society*" - 25 February 2011 as found at http://otp.investis.com/clients/uk/irish/rns/regulatory-story.aspx?cid=121&newsid=196841

[9] Source: AIB Press Office "Transfer of business from Anglo Irish Bank" – 24 February 2011 as found at http://www.aib.ie/servlet/ContentServer?pagename=PressOffice/AIB_Press_Releas/aib_po_d_press_releases-0_08&cid=1298044873956&poSection=AR&poSubSection=paDA&position=notfirst&rank=top&month=02&year=2011

[10] Anglo Press Release – 1 July 2011 – "*Merger of Irish Nationwide Building Society and Anglo Irish Bank*" as found at: http://www.angloirishbank.com/Media-Centre/Press_Release_HTML/ Merger_of_Irish_Nationwide_Building_Society_and_Anglo_Irish_Bank_.html

[11] Source: AIB Press Office "AIB and EBS come together to form one of two Irish pillar banks" 1 July 2011 as found at: http://www.aib.ie/servlet/ContentServer?pagename=PressOffice/AIB_Press_Releas/aib_po_d_press_releases-0_08&cid=1308217019097&poSection=AR&poSubSection=paDA&position=notfirst&rank=top&month=07&year=2011

3.4 Recapitalisation of AIB and EBS

Following the acquisition of EBS Limited by AIB, AIB was required to raise both the AIB PCAR and EBS PCAR requirements, by 31 July 2011 to achieve the capital targets set out under the March 2011 PCAR/PLAR.[12]

This resulted in a total capital requirement of c. €14.8bn (AIB €13.3bn and EBS €1.5bn) of core tier 1 capital (of which c. €1.6bn could take the form of contingent capital).

AIB achieved the recapitalisation though a combination of burden sharing (€2.1bn as set out in 3.4.1 below) and capital raising (€12.7bn in total) as set in 3.4.2 below.

Following the capital raising and the 2011 Bonus Issue, the National Pensions Reserve Fund Commission (the "NPRFC") shareholding in the enlarged total issued ordinary share capital of AIB has increased from c.93.1% to c.99.8%[13].

3.4.1 AIB - Burden sharing

On 13 May 2011, AIB launched a tender offer for cash for all its outstanding subordinated liabilities and other capital instruments. Under this offer AIB agreed to purchase these instruments at prices ranging from 10% to 25% of their face value. The total capital gain under the LME (including EBS) amounted to €2.1bn . [14]

3.4.2 AIB - Residual Capital Requirement

3.4.2.1 Placing of €5bn

On 27 July 2011 AIB issued 500,000,000,000 Ordinary Shares of €0.01 each to the NPRFC at a subscription price of €0.01 per share raising in aggregate proceeds of €5.0bn. [15]

3.4.2.2 Contingent Capital Notes

On 27 July 2011 AIB issued €1.6bn of contingent capital notes at par to the Minister. The contingent capital notes are a subordinated tier 2 capital instrument issued at par with a five year and one day maturity and an aggregate principal amount of up to €1.6bn. The contingent capital notes will convert immediately and mandatorily in their entirety into ordinary shares should a predefined capital deficiency or non-viability event occur. [16]

3.4.2.3 Capital Contribution

On 27 July 2011 the Minister and the NPRFC made capital contributions in the aggregate amount of c. €6.054bn to AIB for no consideration. Accordingly, no new Ordinary Shares were issued by AIB to the Minister and the NPRFC in return for the Capital Contributions[17]

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[12] Source: *"AIB Group preliminary interim results announcement June 2011"* http://www.aib.ie/servlet/BlobServer/document.pdf?blobkey=id&blobwhere=1308217196471&blobcol=urlfile&blobtable=AIB_Download&blobheader=application/pdf&blobheadername1=Content-Disposition&blobheadervalue1=document.pdf

[13] Ibid

[14] Ibid

[15] Ibid

[16] AIB Press release *"AIB – Capital raising update"* as found at http://www.aib.ie/servlet/ContentServer?pagename=AIB_Investor_Relations/AIB_Press_Releas/aib_d_press_releases&cid=1311339854604&c=AIB_Press_Releas&channel=IRCA&position=notfirst

[17] Source: *"AIB Group preliminary interim results announcement June 2011"* http://www.aib.ie/servlet/BlobServer/document.pdf?blobkey=id&blobwhere=1308217196471&blobcol=urlfile

3.5 Recapitalisation of BOI

Under the March 2011 PCAR, BOI was required to generate incremental equity capital of €4.2bn including a regulatory buffer of €0.5bn, together with an additional €1.0bn of contingent capital. Accordingly, BOI commenced a capital programme comprising a LME and a rights issue.

The most significant elements of the capital programme were completed in July 2011 and generated a total of €3.9bn (gross of fees and costs of c.€150m) comprising €2.1bn from LMEs (see 3.5.1 below) and €1.9bn in equity capital following the completion of the Rights Issue (see 3.5.2.1 below). Further equity capital of up to €0.4bn is anticipated from liability management and further subordinated debt burden sharing by year end.

As part of the capital programme, a group of significant institutional investors and fund managers have agreed to acquire c.10.5bn units of ordinary stock in the Bank from the State for c.€1.05bn on receipt of normal regulatory approvals which will give them a stockholding of 34.9%. See 3.5.2.2 below for further detail.

On completion of the capital raising programme, existing shareholders, former bondholders (who accepted the equity exchange in our June 2011 LME) and new investors will own 84.9% of the Bank, with the State maintaining a minimum 15.1% stockholding in the Bank.[18]

3.5.1 BOI - Burden sharing

On 8 July 2011, the Group announced the results of the Debt for Equity offers (excluding certain Canadian Dollar 2015 notes and £75m 13 $^{3}/_{8}$ % perpetual securities). A total of 78.7% of eligible note holders (representing €1.9bn nominal value) elected to exchange their securities, of which 74.3% elected to receive ordinary equity and 4.4% cash. This resulted in a capital increase of €1.96bn. A further €0.1bn of equity was raised from the Canadian Dollar LMS when it closed in August 2011. [19]

3.5.2 BOI - Residual Capital Requirement

3.5.2.1 BOI – Rights Issue

On 8 July 2011 BOI announced a rights issue, underwritten by the NPRFC, of 19.1bn units of ordinary stock at a price of €0.10 per unit to generate gross proceeds of €1.9bn.

The rights issue closed on 26 July 2011 and the results were as follows:

- Valid acceptances were received from the State in respect of its 36% holding of ordinary stock (representing 6.9bn units).
- Valid acceptances were received from other non-Government shareholders in respect of their 23.5% holding of ordinary stock (representing 4.5bn units)
- 1.4bn units of ordinary stock (7.5%) was placed in the rump issue.

&blobtable=AIB_Download&blobheader=application/pdf&blobheadername1=Content-Disposition&blobheadervalue1=document.pdf

[18] Source: "*Bank of Ireland Interim Report for the 6 months ended 30 June 2011*" as found at http://www.bankofireland.com/fs/doc/publications/investor-relations/interim-report-for-the-six-months-ended-30-june-20111.pdf

[19] Source: Ibid

- In accordance with the transaction agreement with the State, the State subscribed for the remaining 6.3bn units of ordinary stock (33%) at the issue price of €0.10 cent per unit. [20]

3.5.2.2 BOI- Significant 3rd party investment in BOI

On 25 July 2011, the Irish Government announced its agreement to sell up to 11.2bn units of ordinary stock at €0.10 per unit (subject to certain conditions) to a group of significant institutional investors and fund managers. These investors are Fairfax Financial Holdings, WL Ross, Capital Research, Fidelity Investments and Kennedy Wilson. The Bank has been advised that each of these investors will manage their individual stockholdings independently. Certain elements of this transaction requires the approval of stockholders at an Extraordinary General Court which is expected to be held on 9 September 2011.

Following the completion of the 2011 capital raise and the significant investment in Bank of Ireland, the State's shareholding in the Bank is expected to be 15.1% of BOI's fully diluted ordinary stock while the combined stockholding of the new group of significant institutional investors and fund managers is expected to be 34.9%.[21]

3.5.2.3 BOI – Contingent Capital

In July 2011 BOI issued a contingent capital note to the State with a nominal amount of €1bn and a maturity of five years. This Contingent capital note is classified as a subordinated liability and it qualifies as Tier 2 capital. [22]

3.6 Recapitalisation of IL&P

Irish Life & Permanent Group Holdings plc ("IL&PGH") is quoted plc which owns Irish Life & Permanent plc (IL&P). IL&P is also a 100% owner of Irish Life Limited, the holding company for the Irish Life group of businesses.

The PCAR/PLAR identified a total gross capital requirement of €4.0bn for IL&P in order to: (i) achieve a core tier 1 capital ratio of 6 per cent. (plus an additional buffer) in a stressed scenario by 31 December 2013; and (ii) cover losses associated with the requirement to deleverage the bank's balance sheet in order to achieve a loan to deposit ratio of circa 122.5% by 31 December 2013.

[20] Source: Ibid
[21] Source: Ibid
[22] Source: Ibid

3.6.1 IL&P - Burden sharing

On 17 May 2011 IL&P bought back three upper tier 2 perpetual subordinated notes made to IL&P representing original aggregate nominal amounts of €320m, which generated €290m of core equity tier 1 capital. These buybacks realised net gains of €318m against the carrying values of the notes based on a discounted price of 8.5% being paid on the JPY 37bn yen principal balances. Additional gains were made when closing out the foreign currency hedges associated with the Yen notes.

In June 2011 IL&P launched a cash tender offer in respect of up to c. €798m nominal value of its subordinated liabilities (subsequently increased to cover €878m of nominal value). Cash prices under the exercise were 20 per cent of nominal for the relevant subordinated liabilities, with the exception of one series of zero coupon subordinated liabilities where the cash price was 8.635 per cent of the nominal amount. The tender offer was completed in August 2011.

The burden sharing outlined above generated c €998m of core tier 1 capital from c €1.2bn of subordinated liabilities, of which €763m was reflected in the interim accounts to 30 June 2011 with the balance to be recognised thereafter.

Of the 18 subordinated bond exercises targeted 16 were fully redeemed as any amounts outstanding following the tenders were called at a nominal price. In the case of the 2 other bonds no quorum was achieved to enforce the call option. The amounts outstanding are (1) €10.5m – maturing on 30 August; and (2) €23.9 nominal (€14m book value) – zero coupon bonds issued exclusively to credit unions.

There will be no subordinated debt held by IL&P post 31 August 2011, other than €23.9m nominal value of the zero coupon bond.

3.6.2 IL&P - Other Internal Capital

In May 2011, IL&P received a dividend from [Irish Life Assurance plc] of €143m. During June and July a further €3m and €19m respectively in dividends were also received by IL&P from other divisions of the Irish Life group.

3.6.3 IL&P - Residual Capital Requirement

On 26 July 2011 IL&PGH was directed by the High Court of Ireland under a Direction Order on the application of the Minister under the Credit Institutions (Stabilisation) Act 2010 to issue €2.3bn of new equity capital to the Minister and immediately following the share subscription, to pay an amount equal to €2.3bn, less subscription fees and expenses, to IL&P, a 100% subsidiary of ILPGH, to increase the Core Tier 1 Capital of IL&P. IL&P was also directed to issue €0.4bn of convertible contingent Tier 2 capital notes to the Minister.

In order to address the requirements of the Order, ordinary shares were issued to the Minister for a consideration of €2.3bn at an issue price of €0.06345 per share, and potentially up to a maximum of €0.4bn of further ordinary shares at an issue price of €0.031 per share if the Contingent Capital Notes convert.

By the end of July 2011 IL&P had also received €165m of dividends from the Irish Life group, which reduced its external capital requirements by an equivalent amount. See 3.6.2 above for further details.p

The State investment and Irish Life dividends outlined above ensured that IL&P met the additional capital requirements, adjusted for asset sales, set by the Central Bank of Ireland following the PCAR and PLAR exercises which were required to be met by 31 July 2011.

The Minister currently owns 99.24% of the IL&PGH. IL&PGH is currently listed on the ESM of the Irish Stock Exchange[23].

The remaining capital requirement is being funding through the disposal of the Life Group and the LME outlined above. It is expected that the LME combined with the disposal of Irish Life group will generate €1.1bn of core tier 1 capital. Should these initiatives not generate sufficient funds to meet the additional requirement, the state has indicated that they will provide the necessary support.[24].

4. NEXT STEPS

4.1 Deleveraging[25]

The non –core assets of the banks covered by the PLAR review are being deleveraged through a combination of run offs, from amortisation or prepayments and a carefully coordinated programme of phased asset disposals. While avoiding fire sales, this will deliver a small more robust banking system, with a target loan to deposit ratio of 122.5 percent by end 2013. In the near tem, the focus will be on assessing bank targets for the quantum of assets disposal requirements, derived from their deleveraging programmes established to meet the PLAR target loan to deposit ratios, which will be closely monitored. As set out below, a framework for the governance of deleveraging has been developed, which will be kept under review based on experience.

Following the identification of the non-core assets, the bank, with the assistance of international consulting firms, are completing due diligence on their inventories to establish the phasing and pricing of non-core assets identified for sale. Banks have also established deleveraging committees (chaired by a non-executive Directors) to make decisions on larger transactions, and will report to the authorities on progress towards the semi-annual interim targets for key liquidity indicators on a quarterly basis.

A representative of the DoF will participate in a non-voting capacity in each bank's Deleveraging Committee to promote the observance of agreed goals, report regularly to the DoF Review Committee, and have the authority to refer material transactions to the DoF Review Committee. Any such transactions would automatically be reviewed if the price falls below a certain threshold based on the PCAR/PLAR exercise. The Minister would use his powers to either enforce or veto transactions with a view to advancing deleveraging while avoiding fire sales.

Details of deleveraging on completed to date on a bank by bank basis is set out below.

[23] Source: IL&P Group Holdings plc Press release "*Recapitalisation – High Court Order*" 26 July 2011 as found at: http://www.irishlifepermanent.ie/media-centre/press-releases/2011/26-07-2011.aspx

[24] Source: Irish Life and Permanent plc 2011 Half Year Report for the six months ending 30 June 2011 [Draft]

[25] Source: "*Memorandum of Economic and Financial Policies*" *Department of Finance*", 28 July 2011 as found at http://www.finance.gov.ie/documents/publications/other/2011/EU%20imf/EUimfJul2011.pdf

4.1.1 *AIB- Deleveraging*[26]

The AIB Non Core Unit was established on 1 July 2011 to formulate and implement AIB's strategy of deleveraging of its non core assets through a combination of disposals, run-off, refinancing and other forms of deleveraging. Non core assets are managed as a distinct portfolio within the business by a dedicated management team. The structure and operational framework for the non core management team is now implemented with strong focus on governance, risk, performance measurement and oversight reporting to the key stakeholders. The team has an explicit performance mandate to realise optimum value from the portfolio while also preserving AIB's core customer franchise within the overall objective of meeting the defined deleveraging targets as agreed with the authorities.

Total net loans of €25.1bn have been designated as non core assets, of which it is planned to deleverage €17.4bn over a three year period to the end of 2013.

Deleveraging of non core assets amounted to €8.3bn during the half year to June 2011. This was achieved through a combination of disposals of specific asset pools, repayments and redemptions, increased provisioning and other deleveraging impacts.

Asset disposals to date of €1.5bn were achieved, principally in property and project finance related assets located in the United States, United Kingdom and Europe. Repayments and redemptions to date amounted to €3.6bn principally in the United Kingdom and overseas, while increased impairment provisions, foreign exchange movements and other deleveraging impacts amounted to €3.2bn.

The impact on capital as a consequence of deleveraging to date, including losses on disposal of €131m on non core assets, has been positive, due to the resulting reduction in risk weighted assets. The pipeline for further asset disposals in the second half of the year remains strong with a number of additional non core asset pools identified and in the course of disposal.

4.2 BOI – Subordinated Debt Burden Sharing

4.3 Anglo – Senior Debt Burden Sharing

4.4 Sale of Irish Life

4.5 Strategic Future of ILP

4.6 Integration of AIB and EBS

[26] Source AIB Group Interim Results 2011 as found at [ ]

[Draft – subject to finalisation]

Appendix 1 – Summary of recapitalisation of Irish Banks under The Programme of Financial Support and PLAR/PCAR

All figures stated in €bn

AIB	Capital Requirements	Total State Investment	Internal Capital Raise (a)	Private Investment
Equity Placing	5.0	5.0	-	-
Contingent capital instrument	1.6	1.6	-	-
Capital Contribution	6.1	6.1	-	-
Liability management exercise	2.1	-	2.1	-
Capital requirements	**14.8**	**12.7**	**2.1**	**-**

BOI	Capital Requirements	Total State Investment	Internal Capital Raise (a)	Private Investment
Rights Issues (adjusted for private investment)	1.3	0.2	-	1.1
Rump + Non NPRF Rights takeup	0.6	-	-	0.6
Contingent capital instrument	1.0	1.0	-	-
Liability management exercise	2.1	-	2.1	-
Further Capital Raising Measures (b)	0.4	-	0.4	-
Transaction fees, legal and corporate finance costs	(0.2)	(0.1)	-	(0.1)
Capital Requirement	**5.2**	**2.3**	**2.5**	**1.6**

ILP	Capital Requirements	Total State Investment	Internal Capital Raise (a)	Private Investment
Equity Placing	2.3	2.3	-	-
Contingent capital instrument	0.4	0.4	-	-
Internal Capital Raising	0.2	-	0.2	-
Sale and LME (b)	1.1	-	1.1	-
Capital Requirement	**4.0**	**2.7**	**1.3**	**-**

Total recapitalisation	Capital Requirements	Total State Investment	Internal Capital Raise (a)	Private Investment
AIB	14.8	12.7	2.1	-
BOI	5.2	1.1	2.5	1.6
ILP	4.0	2.7	1.3	-
Total	**24.0**	**16.5**	**5.9**	**1.6**

Note (a) Includes capital raised via LMEs and asset disposals.
Note (b) to be finalised

Appendix 2 – Summary of recapitalisation of Irish Banks - 2009 to date

Amount invested by institution and by year

€ in millions	Anglo	INBS	AIB	BOI	EBS	ILP	Total
State investment							
2009							
Equity	4.0	-	-	-	-	-	**4.0**
Special Investment shares	-	-	-	-	-	-	**-**
Preference shares	-	-	3.5	1.8	-	-	**5.3**
2010							
Equity	-	0.1	3.7	1.7	-	-	**5.5**
Special Investment shares	-	-	-	-	0.6	-	**0.6**
Capital contribution	25.3	5.3	-	-	0.3	-	**30.9**
2011							
Equity	-	-	5.0	0.3	-	2.3	**7.6**
Capital contribution	-	-	6.1	-	-	-	**6.1**
Contingent capital	-	-	1.6	1.0	-	0.4	**3.0**
	29.3	**5.4**	**19.9**	**4.8**	**0.9**	**2.7**	**62.9**
LME							
2009	2.1	0.3	1.2	1.0	0.0	-	**4.6**
2010	1.6	-	0.4	1.4	0.0	-	**3.4**
2011	-	0.1	3.7	2.1	0.1	1.0	**7.0**
	3.6	**0.4**	**5.2**	**4.5**	**0.2**	**1.0**	**15.0**
Private capital raised							
2010	-	-	-	1.5	-	-	**1.5**
2011	-	-	-	1.6	-	-	**1.6**
	-	**-**	**-**	**3.2**	**-**	**-**	**3.2**
	32.9	**5.8**	**25.1**	**12.5**	**1.0**	**3.7**	**81.0**
As at August 2011							

DÁIL QUESTION

NO

To ask the Minister for Finance the status of the additional □24 billion needed for Irish banks as a result of the stress tests in early 2011; if the funding has been paid to any Irish bank and if so, the percentage that is being used to provide write-downs for personal and commercial debt, the percentage for boosting reserves at the banks; if it is his intention to formulate an adequate credit policy which will give a clear direction to the banks on personal and commercial debt; and if he will make a statement on the matter.

\- Noel Grealish.

* For WRITTEN answer on Wednesday, 18th April, 2012.

Ref No: 18719/12

REPLY

Minister for Finance (Mr Noonan) :

The bank recapitalisation commitments made by the State to date are set out in the following table:

€bn	AIB/EBS	BoI	IL&P	IBRC (Anglo/INBS)	Total
Government preference Shares (2009) - NPRF	3.5	3.5*	-	-	**7.0**
Capital contributions (with Promissory Notes as consideration) /Special Investment Shares (2010) – Exchequer **	0.9	-	-	30.7	**31.6**
Ordinary Share Capital (2009) – Exchequer	-	-	-	4.0	**4.0**
Ordinary Share Capital (2010) - NPRF	3.7	-	-	-	**3.7**
Total pre-PCAR 2011 (A)	**8.1**	**3.5**	**0**	**34.7**	**46.3**
PCAR 2011:	**AIB/EBS**	**BoI**	**IL&P**	**Anglo/INBS**	**Total**
Capital from Exchequer***	3.9	-	2.7	-	**6.5**
NPRF Capital	8.8	1.2	-	-	**10.0**
Total PCAR (B)	**12.7**	**1.2**	**2.7**	**-**	**16.5**
Total Cost of Recap for State (A) + (B)	**20.7**	**4.7**	**2.7**	**34.7**	**62.8**

* €1.7bn of BoI's government preference shares were converted to equity in May/June 2010 (€1.8bn still left in existence). The government also received €0.5bn from the warrants relating to BoI's preference shares (excluded from table above).

** The IBRC amount is made up of a total capital contribution for Anglo / INBS of €30.6bn and a special investment share of €0.1bn (INBS). The Anglo / INBS capital contribution impacted in full on the GGB in 2010. The consideration for the Anglo / INBS capital contribution was €30.6bn of promissory notes. These Promissory Notes are an amount due from the State to IBRC. Each year, on 31 March, €3.06bn is paid by the Exchequer to Anglo / INBS as part of the scheduled repayments of the promissory notes. The first such repayment was made on 31 March 2010.

*** The Exchequer cost of the 2011 BoI recap is shown net of share sale to private investors (Completed in October, 2011)

As the Deputy will be aware, the banks were required to raise a total of €24bn as a result of the Central Bank's 2011 Prudential Capital Assessment Review (PCAR). However, primarily as a result of successful private equity contributions, asset sales and burden sharing with bondholders the Government only had to inject €16.5bn into the relevant institutions.

In addition, the State is committed to acquiring Irish Life for €1.3bn to complete the recapitalisation of Irish Life & Permanent. It is expected that the proceeds of an onward sale of Irish Life in due course will reduce the amount the State has committed to the bank recapitalisation.

In relation to personnel and commercial debt, there is on-going and detailed engagement between my Department and the covered institutions. The current and projected capital requirements of the institutions form part of this engagement and these are monitored and assessed on an on-going basis. The PCAR carried out in 2011 by the Central Bank independently assessed the capital requirements having regard, among other things, to the asset quality and the potential impact of such asset value/quality in base and stressed case scenarios.

However, the Banks' policy in relation to credit decisions is a matter for the management and board of the institution. I have no role in the day-to-day commercial and operational decisions of the banks, which include these matters. These decisions are taken by the board and management of the institutions. Notwithstanding the fact that the State is a significant shareholder in the institutions, the banks are run on a commercial arm's length basis as per the Memorandum on Economic and Financial Policies agreed with the EU Commission, the ECB and the IMF.

To: Michael Torpey

Secretary General

From: Ciaran Callaghan

PQ 18719/12

Please find attached a draft response for the above PQ which is for WRITTEN answer on Wednesday 18th April 2012.

THEME: C4

Appropriateness and effectiveness of the domestic policy responses

LINE OF INQUIRY: C4d

CISA* – effectiveness of the actions to merge AIB and EBS, Anglo and INBS and deposit transfers

* Credit Institutions Stabilisation Act (2010)

(10) On 31 August 2010, Ireland submitted a new proposal to the Commission on the restructuring of Anglo which set out a split and wind-down of the bank over ten years.

(11) In light of a detailed assessment of the prospects of Anglo, the Irish Minister of Finance announced on 30 September 2010 that the resolution of Anglo would require in total a cumulated capital injection of EUR 29,3 billion under base projections, and an additional EUR 5 billion under a stress scenario.

(12) On 26 October 2010, Ireland submitted a work-out plan for Anglo (hereinafter referred to as "the third Anglo restructuring plan"), explaining in detail how it would implement the work-out of the entity which had been presented for the first time in its submission of 31 August 2010.

(13) In the subsequent weeks, the Commission services requested some clarifications and sought additional information on 29 October 2010. The Irish authorities replied in a number of e-mail exchanges and conference calls.

(14) On 8 December 2010, Ireland notified to the Commission an additional recapitalisation of EUR 4 946 million (hereinafter referred to as "the fourth recapitalisation") and State guarantees in respect of certain liabilities in favour of Anglo.

(15) By Decision of 21 December 2010[9], the Commission approved the fourth recapitalisation and guarantees in respect of certain liabilities in favour of Anglo on a temporary basis until the approval of Anglo's final restructuring plan.

1.2 Irish Nationwide Building Society

(16) By Decision of 30 March 2010, the Commission temporarily approved a EUR 2,7 billion recapitalisation of Irish Nationwide Building Society (hereinafter referred to as "INBS") for six months as of the date the recapitalisation was put into effect (22 December 2009), or, if Ireland submitted a restructuring plan before that date, until the Commission had adopted a final decision on INBS' restructuring plan (hereinafter referred to as "the first INBS recapitalisation")[10].

(17) Furthermore, on 30 March 2010, the Irish Minister of Finance announced that, in the light of the reduction of the INBS' balance sheet resulting from transfers to the National Asset Management Agency (hereinafter referred to as "NAMA"), that institution did not have a future as an independent stand-alone entity.

(18) On 22 June 2010, Ireland notified a restructuring plan for INBS to the Commission (hereinafter referred to as "the INBS restructuring plan"). That plan envisages the continued management of the society as a going concern in anticipation of a sale to a trade buyer.

(19) In the following weeks, Ireland informally informed the Commission that it was assessing other options for the future of INBS. In particular, Ireland was planning to test the market appetite for acquiring parts of INBS.

[9] Commission Decision in Case SA.32057 (2010/NN), Ireland - Temporary approval of the fourth recapitalisation and guarantee in respect of certain liabilities in favour of Anglo Irish Bank, (OJ C 76, 10.3.2011, p. 4.).

[10] Commission Decision in Case NN 11/2010, Ireland - Rescue measures in favour of INBS, (OJ C 143, 2.06.2010, p. 23.).

while its lending activities will be limited to the normal management and work-out of the legacy loan book of Anglo and INBS. The merged entity will eventually fully disappear from the Irish lending and deposit markets, and therefore no longer distort competition. In addition, the merged entity will apply a ban on acquisitions.

6.3.4.4 Monitoring

(188) Point 46 of the Restructuring Communication indicates that, in order to verify that the restructuring plan is being implemented properly, detailed regular reports from the Member State are necessary. Accordingly, Ireland should provide the Commission with such reports every six months, starting from the date of notification of this Decision.

(189) In the case of the restructuring of Anglo and INBS, a monitoring trustee will also be nominated for a period of three years to monitor the application of the commitments undertaken by Ireland. The monitoring trustee will be in charge of monitoring all the commitments (see Annex II). In particular the monitoring trustee will monitor on a regular basis whether the merged entity manages the legacy loan books of Anglo and INBS in line with the terms of the commitments and will ensure that the management of the Anglo and INBS loan books does not result in distortion of competition in the market.

6.3.4.5 Conclusion

(190) It should be concluded that the joint restructuring plan of Anglo and INBS fulfils the requirements of the Restructuring Communication. The plan foresees an orderly work-out of Anglo and INBS assets. The own contribution of the banks is sufficient, while the burden-sharing is substantial and the State aid is limited to the minimum. The measures addressing distortion of competition are appropriate, and finally proper monitoring will be implemented.

7 CONCLUSION

(191) The measures (a) to (v) referred to in recitals 66 to 69 and listed of Table 1 are considered to be restructuring aid. Concerning the aid measures covered by the opening decision of 31 March 2010, the Commission finds, pursuant to Article 7(3) of Council Regulation No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty[66], that those measure are compatible with the internal market under Article 107(3)(b) TFEU. As regards the remaining measures covered by this Decision, the Commission, pursuant to Article 4(3) of the Regulation No 659/1999, raises no objections to those measures as they are compatible with the internal market under Article 107(3)(b),

[66] OJ L 83, 27.3.1999, p. 1.

Memo

To:	John Moran
Copy to:	Michael Torpey / Banking Implementation Unit
From:	Gary Hynds / Enda Johnson
Date:	16 September 2011
Subject:	Alpha/Ebony Integration Approach

NOTE: The following is subject to approval by the Boards of both Alpha and Ebony

1. Introduction

Alpha and Ebony have put forward a recommended medium term approach for the integration of the two businesses. The proposal was submitted to the Ebony board on 14th September and is due to be considered at the Alpha board meeting on 14th October

2. Summary of proposed approach

The proposal is to retain two full retail offerings for the next 3 – 4 years after which the strategy would be reassessed. Two separate networks and front office systems would be maintained with all back and middle office functions and IT systems being fully integrated. The Ebony Brand, Branches and Agent network would be maintained throughout. As part of the analysis of the optimal strategy, Alpha considered six options ranging from maintaining full independence of the two banks to a fully integrated platform. Further detail on the options considered and the rationale underpinning the final choice can be referenced in the attached presentation (**Tab A**).

3. Retention of Ebony Banking Licence

The proposal would involve maintaining two separate banking licences. The primary benefit in retaining the banking licence for Ebony stems from the continued participation in the Deposit Guarantee Scheme. Ebony estimates that circa 40% of their customers also have accounts with Alpha. The existence of the two banking licences allows customers with accounts in both institutions to have deposits of up to €100,000 guaranteed in each individual institution. As a result Alpha has made it clear that there is a significant risk that moving to one licence would result in additional deposit losses. The proposal would be that once this risk reduces and the need for two deposit guarantees subsides then the Ebony licence would in theory no longer be required. Given the current market environment, no timetable for this has been considered further at this stage.

4. Sales and Distribution Network

All sales and distribution outlets would be left independent with the call centres, internet and other intermediaries merged. Mortgage and deposit servicing and customer service facilities would also be merged. The current expectation is that this would see a c.20% reduction (c. 140) FTEs in Ebony. The intention would be to include these redundancies as part of the overall Alpha Group redundancy package. [1]

Ebony currently has 14 Branches, 41 Tied Branch Agents (TBAs) and 38 Agents. The proposal would be to maintain this network where it makes sense to do so. Ebony is exploring the possibility of converting some or all of the remaining branches into TBAs in order to reduce operating costs. Work will also continue to assess opportunities to optimise the combined network through the merging of underperforming branches or converting Alpha branches into TBAs however decisions will **not** be taken on the basis of proximity to existing Alpha branches and the intention is to retain the exiting sale and distribution network on a stand-alone basis to the maximum extent possible.

5. Product Management

Work is already underway to develop joint product and channel strategies. A Group Product Manager will be assigned with separate Alpha and Ebony teams reporting to him. The Group Product Manager will be responsible for developing product and network strategies that optimise both networks. Offerings such as Ebony's current 'National Savings Week' have been developed in cooperation to ensure that they align with Alpha plans.

In future the intention would be to develop 'white label' Alpha products that could be also offered under the Ebony brand. There is also potential for cross selling of other Alpha products such as credit cards and personal loans however there are currently no plans to offer current accounts through the Ebony network. In relation to other services that are provided in both Alpha and Ebony (banc assurance etc.) the intention is to allow existing contracts to expire and explore any potential synergies that can be achieved as these contracts are put up for re-tender.

6. Management / Governance

The proposal is to retain the Ebony Board along with the Risk and Audit committees of Ebony. Dual reporting lines with be maintained and a formal SLA to be agreed between Ebony and the Alpha Group. The intention would be that the Ebony CEO role would transform into more of a general manager role, with the exact nature of that role being decided as part of the broader organisation design. Current Ebony management have endorsed this proposal.

[1] Note these figures are draft and are highly confidential. These figures have not been agreed at board level, are indicative only and have not been disclosed to Alpha / Ebony general staff.

7. Synergies

Significant synergies have been identified as part of this integration proposal. Alpha are targeting synergies of 19-20% at the base level. These are set out in the table below;

Workstream	***Identified Savings***	***Comment***
Integrated Organizational Structure	€9.1m	Corporate spend, Marketing/PR etc.
Streamlined Facilities	€0.8m	Will increase over time, Ebony Head Office - first break clause 2017. Alpha intends to relocate Ebony staff to their headquarters in 12 – 24 months and potentially sub let the existing Ebony head office on reduced terms.
Business Targets	€7m	Integrated targets for mortgage and deposit businesses
Procurement	€0.7m	
IT Savings	€2.7m	Contractors + system maintenance
Cross Selling	€2m	Alpha products (personal loans/credit cards), 3rd party providers

8. Other Points to Note

- There are still significant HR issues that remain to be resolved. It was made clear in our meeting with Maurice Crowley that there is a significant discrepancy between overall pay and fringe benefit levels within the organisation with staff in Ebony currently being remunerated at a higher level generally. This will need to be addressed as part of the rationalisation. Alpha has appointed a senior member of their HR team to handle this particular issue, amongst others.

- The engagement with Bain and Company in relation to the integration has now been completed. We have requested a copy of the final report produced.

- The integration of Ebony into Alpha has led to a sharp increase in Ebony's provisioning levels as standards and risk strategies are aligned

- To date, Ebony has seen only one material resignation as a result of the merger. The former head of treasury has departed since the merger was completed. However, under the integration plans implanted to date, the majority of Ebony's treasury functions have already been integrated under existing Alpha functions.

9. Relevant follow on actions

The shareholding management unit met with Maurice Crowley (Head of Alpha/Ebony Integration) on Tuesday 13th September to discuss the contents of the integration plan. At that meeting we discussed the proposed integration and specifically the contents of the attached presentation. The proposal is to be considered by the Alpha Board on 13th October next. Ebony and Alpha management have been involved in arriving at this position and the Ebony management has endorsed the proposals. Separately, Alpha engaged Bain & Co to advise on the integration strategy, particularly in light of concerns over deposit attrition.

We are of the opinion that the integration plan as proposed is reasonable given the risk of significant deposit losses at Ebony if the branch network were to close, brand was to be removed or if the banking license was removed. External benchmarks along with the Bain analysis suggest that 25-35% of deposits could be lost if the Ebony brand was removed and network were closed. A similar level of attrition was witnessed in the transfer of the Anglo and INBS deposit books. The shareholder management unit will actively monitor the successful implementation of the integration plan as part of the overall reorganisation of the Alpha Group. The continued need for a separate banking licence for Ebony will also be closely monitored.

If agreed we would propose indicating we have no objection to the plan to Alpha ahead of the upcoming Board meeting in October. As part of arriving at this view, it should be noted that the strategy chosen for the integration of the 2 businesses is, in the first instance, a matter for the board and management of the bank. The proposal that Alpha has put to the State appears entirely reasonable on a number of different fronts, however it is ultimately the responsibility of the board and the management team to ensure that the integration strategy chosen delivers maximum benefit to the State as 99.8% shareholder. Or discussions with Maurice Crowley made this point very clear and he indicated that the medium strategy will remain under constant review as economic conditions evolve and the performance of the businesses stabilise post merger.

Sale of Anglo and INBS deposit books
Note for the Minister
28 January 2011

agreed by Minister
28/1/11

To: Minister

From: Ann Nolan

Decisions required

1. To proceed with the sale of the deposit books held by Anglo and INBS and their NAMA bonds in advance of securing a commitment to a long term funding solution for these entities within the next 2-4 weeks (subject to the receipt of compliant bids and clarity over the legal process)
2. To sell the NAMA bonds as the matching asset to the deposits as required under the IMF/EU programme (the Programme)
3. To proceed with an expedited rapid sale process rather than the more orderly process requested by Anglo management
4. Agree to submit the Restructuring Plan for the remaining combined Anglo and INBS to the EU by 31 January 2011 in line the Programme requirement.

Background

We have agreed as part of the Programme to sell the deposits in these institutions together with their NAMA bonds in a swift and decisive manner. Separately we have committed to submitting a restructuring plan for the remaining, combined entity to the EU by 31 January 2011. While it was envisaged that we would sell the deposits and bonds in January in advance of the submission of the EU plan, there is nothing in the Programme that requires this, other than the commitment for "swift and decisive action".

Since the signing of the Programme a significant project has been underway on this objective.

- A steering committee, chaired by the NTMA, and including senior management from both banks, their advisors and the Department has been meeting twice a week to oversee the project
- Numerous work streams in areas such as legal, regulation, operations, HR have been assessing the many issues involved and developing plans to implement the transaction process itself and the expected transfer once a deal is concluded.
- At this point the data rooms are ready to be opened to the identified prospective bidders to enable them to carry out the necessary due diligence.

However as noted above a number of significant decisions are required before we progress any further.

1. Funding of remaining entity

As yet we do not know how the remaining combined entity is to be funded. Proceeding with the transaction in advance of getting an agreed funding solution will further weaken both banks' existing funding capability and make them more reliant on ELA.

(It should be recognised that any weakening of Anglo or INBS funding should be somewhat offset by a reduction of ELA in the acquiring bank)

While the IMF has stated that it was implicit in the Programme that such a funding solution for Anglo and INBS would be provided, the Troika is pressing us to progress the transaction without this commitment. When ECB was asked recently whether we should proceed on the assumption that a funding solution would be concluded in due course, no answer was forthcoming. The ECB should either provide the funding or explicitly agree that the CBI can do so.

Any funding commitment will need to include a commitment to fund Anglo's significant Sterling (c£8-9bn) and USD (c€6-7bn) loan books. These are currently funded/hedged by deposits (which will be sold) and counterparty hedges (which may not always be available to Anglo).

2. Structure of deal – inclusion of NAMA bonds

The inclusion of NAMA bonds in the transaction makes the deal unattractive to the acquiring bank as they give rise to liquidity and capital risk.

Liquidity
While the initial impact on liquidity should be to enable an Irish acquiring bank to replace ELA funding with ECB collateralised funding, there are several risks and implications that arise.

- The bank will have increased its balance sheet size which is contrary to the de-leveraging obligations as set out in the Programme
- It is possible that the ECB will change its repo assessment of these bonds and hence this liquidity benefit could be significantly eroded
- There is no assurance that the deposits will stick and the absence of cash to fund any repayments will also reduce the positive liquidity impact.
- The future treatment of NAMA bond to meet Liquidity Coverage Ratio requirement is uncertain

Impact on capital
There is a risk that these bonds will be written down in value by the ECB and this will likely result in write offs and capital shortfalls in all of the banks holding these bonds. Increasing a viable bank's holding in NAMA bonds will therefore increase its exposure to this issue.

Additionally, given the reluctance of bidders to acquire these bonds, irrespective of any ECB action, any transaction in the bonds is likely to result in the creation of a market value below par which would also result in write off and capital shortfalls. We have agreed with DG Competition that we can set minimum bid values for these bonds which should somewhat mitigate this risk. (Discussed further below).

We have been in extensive discussions with the Troika (and in particular the ECB) on a cash supported sale (meaning replacing the NAMA bonds with cash) which would fully deal with this issue. However the ECB was adamant that it did not wish to increase its exposure to wind down, defunct banks.

Accordingly the only way of selling the deposits in a swift and decisive manner is to include NAMA bonds in the deal.

3. Operational issues

You will be aware that Anglo has recently highlighted its concerns that the operational risks associated with the transaction are very significant. Anglo pointed out that there are significant payment default and other risks with the proposed approach and would therefore prefer a more orderly sale process.

In any transaction of this nature numerous operational risks arise. Over the past week we have worked with Anglo management, the Central Bank and the NTMA to get a better understanding of these risks and the various mitigants that can be used. Most of the risks identified by Anglo have been adequately addressed but the following require your attention.

Foreign exchange risk

The are three important foreign exchange issues

Day 1 risks: Anglo will need to access sterling and US$ Central Bank/ECB foreign exchange lines to ensure it has the foreign currency to allow it to hedge the exposure that will be created by selling its Sterling (c£3.6bn) and US$ ($750m) deposits. The CBI has advised that these lines will be available. However these lines expire in September 2011 and July 2011 respectively and there is no commitment to extend them. (This expiry issue should be considered in the context of the overall funding commitment discussed above).

Day 2-30 risks: If we adopt an immediate or quick sale process Anglo will need to fund any customer withdrawals on behalf of the acquirer, as it will continue to process the deposit transactions until they are transferred to the acquirer's system. This risk could be mitigated by requiring the acquiring bank to pre-fund euro, sterling and US$ accounts with Anglo. Currently most banks are reluctant to deal with Anglo. Therefore this pre-funding requirement needs to be considered in the context of the acquiring bank's overall appetite for the transaction given inclusion of the NAMA bonds.

Foreign Exchange hedge counterparties: Anglo only has 5 remaining hedge counterparties. Management is concerned that any shock information, such as an overnight sale process, could cause some or all of these counterparties to pull their lines. This risk may be mitigated by having some upfront communication with these counterparties. However management would need a Ministerial instruction to communicate with these counterparties, as otherwise they could be in breach of the CIS Act.

Counterparty payment clearers

As with Foreign exchange counterparties Anglo has a limited number of payment clearers. Any shock information could result in them withholding payment. Even a temporary delay in payments could result in significant systemic issues. Again this risk could be mitigated by upfront communication following a Ministerial order.

The above risks can be further reduced by the inclusion of 2 extra days in the process between the time the deal is struck and the time the transfer order and public communications are made.

Anglo's suggestion

Anglo has requested us to consider an "orderly" sale process rather than the more immediate sale process currently envisaged. This would involve a process of disposals over a longer period with a targeted legal completion by mid-March and a final transfer by mid-April. In additional it would involve separate transactions for the Irish, UK and Isle of Man businesses. Anglo presented a suggested version of this longer process to the Authorities yesterday. Anglo management was not in full agreement on what was presented and further detail of this process would need to be developed. While undoubtedly the longer sale process does reduce some of these operational risks further, the various Authorities were not convinced that the risks were so significantly reduced when considered in the context of the potential outflows of deposits that will arise during the extended process.

29|1|4

4. Requirement for a Transfer Order and Direction Order

In order to reduce the cessation of business and cross default risk in the senior bonds, Anglo management, its legal advisors and Arthur Cox advise that we should proceed with both a Transfer Order for the deposits and NAMA bonds concurrently with a Direction Order under the CIS Act. The Direction Order would require the boards to undertake specific actions designed to facilitate the wind-down of the banks on a gradual, orderly, solvent basis over a number of years in accordance with the State's agreement with the Troika and the EU State aid restructuring plans. It would also provide protection from creditors seeking to invoke cessation of business clauses. The NTMA also considers this to be the most appropriate course of action.

A Transfer Order without a Direction Order could increase the risk of triggering an event of default (other than specifically related to the transfer which will be protected under S.61), as the institutions will be beginning the wind down process.

Bank management, Arthur Cox, the AGO, the NTMA and the Department continue to work on the specific details of each of these orders and should be in a position to issue them once the due diligence period has concluded. However given the unprecedented nature of the legal aspects of the Direction Order, the AGO will need time to perfect its approach.

5. Agreement with DG Competition

Under State aid rules it is important that an open sales process is conducted and that no one party is advantaged over another. Given some of the issues referred to above we have agreed with DG Competition that we can set the following bid criteria to all bidders in order to mitigate some of the risks associated with the transaction:

- Bidder must bid for the NAMA bonds - *to comply with Programme requirement*
- A minimum bid price for the bonds will be set in advance - *to reduce the risk of setting a low market price*
- Bid must bid for all of the deposits (Irish and overseas) – *to ensure a speedy and single sale transaction*
- Bidders must commit to a very short close period – *to comply woth Troika expectations*
- Bidder must agree to pre-fund Anglo – *to reduce risk of payment default*

Given the extent of these conditions it is possible that no fully compliant bids will be received. We have agreed with DG Competition that if this situation arises that it would be allowable under EU State aid rules for us to instruct one of the banks to complete the transaction, as long as we consult with them and the Troika in advance and as long as the acquiring bank was not given an unfair advantage.

Conclusion

It is recommended that the transfer of the deposits and NAMA bonds should proceed despite the operational risks involved and that once the legal aspects of the Transfer Order and the Direction Order have been settled the sale process should commence. The NTMA accepts that this approach is appropriate in the absence of agreement by the Troika to vary the commitment to this effect in the Programme.

This is despite the lack of formal agreement from the ECB to fund the remaining entity over the longer term. This is a risk but given the insistence of the Troika we appear to have no other option.

Anglo Irish bank/INBS Restructuring Plan

In line with our commitment under the Programme a plan for the amalgamation and orderly wind down of Anglo Irish Bank and INBS has been prepared and is to be submitted to the EU Commission under state aid rules on 31 January 2011 subject to your agreement.

The Plan will continue to be refined in detail but the broad outlines will remain the same and follows the parameters agreed with the Troika.

The Plan assumes that the majority of deposit and the NAMA bonds in both institutions will be transferred in Q1 this year. In addition it assumes that funding will be provided on an ongoing basis by the Central Bank and a low cost of funds.

The other main points are

- €27 bn customer loan book and €31bn Government promissory notes are main assets of the merged entity
- The commercial loan book will be run off within 10 years. ~41% of net book in the first 5 years
- The IBNS mortgage book will be run down and sold
- Run-offs, disposals and loan refinancing will be managed to minimise capital losses in accordance with best practices and commitments agreed with the EU
- In the early years the focus will be on extracting value from "higher quality" loans e.g. US and UK loans, where faster recovery is expected
- If market conditions allow, the merged entity will seek to accelerate work-out through early asset disposal
- As agreed with the Troika, the combined entity will retain some €800m of deposits which are linked to loans
- The capital cost to the State is in line with the Sept 2010 announcement - €34.7bn in the base case (€29.3bn Anglo/€5.4bn INBS) and €37.3bn in a stress case. Compared to previous plans the base case is in line with the previous estimates while the stress case is c€2bn lower expected.

The main financial risks are:

- Additional loan losses could occur – but stress scenarios have been analysed to reflect this risk (as referred to above)
- The bank has a very significant fixed rate pronote which it cannot swap to floating. Therefore the bank is very exposed to any increase in interest rates unless this position can be hedged.
- The deposits and NAMA bonds are assumed to transfer at par. This may not occur.
- The plan assumes CB funding at certain rates which may prove to be inaccurate.
- Without the protection of a Direction Order the bank will run the risk of a cessation of business claim.

Attachment: Analysis of the advantages of Anglo's orderly process

Anglo has requested us to consider an orderly rather than the rapid sale process. While the detail of this orderly process needs some further development by Anglo, the following table illustrates the advantages and disadvantages of the two approached.

Risk	**Rapid**	**Orderly**
	Mitigants	
FX – Day 1	CBI lines	CBI lines
FX – Day 2-30	Acquirer prefunds accounts (further deal inhibitor)	Risk dealt with as all transferred
FX – hedge counterparties	Upfront communication	More communication
Counterparty payments	Upfront communication	More communication
	Pros and cons	
Pros	• Clearly a "swift and decisive transfer" • Limits deposit outflow due to "Anglo/INBS effect" • Potential to keep some of the UK sterling retail deposits in the Irish system • Bank union already raising issues in INBS. A rapid process limits their options	• Above risks are more fully mitigated • Staff can be fully consulted in line with TUPE requirements • Could avoid "work to rule" type situations
Cons	• Higher operational risk • Risk of industrial action which would increase the operational risk issues	• Will miss deadline of 11 February when decision has to be made to wind down the UK sterling book and c£1bn of deposits will need to be repaid • Potential for significant outflows of deposits from both banks over period (upto €3bn)

Joint EC Restructuring and Work Out Plan for Anglo Irish Bank and Irish Nationwide Building Society

31 January 2011

Introduction

- The following document outlines the **Joint EC Restructuring Plan for Anglo Irish Bank ("Anglo") and Irish Nationwide Building Society ("INBS")**, and has been **developed by a working group** including representatives from the Department of Finance, NTMA, the Central Bank of Ireland (the "Authorities"), Anglo and INBS

- The Joint Restructuring Plan is **primarily guided by the agreement reached between the Irish Authorities, the EU, IMF and ECB in November 2010** and seeks to provide further detail and specification on the restructuring and work out solution for Anglo and INBS outlined therein

- This plan assumes **a merger of the two entities in H1 2011** and the numbers that are presented are for the combined institution. The 2010 **Year End numbers are a pro-forma** of actual year end numbers, excluding deposits franchises and NAMA bonds planned for transfer

- Implementation of the Joint Restructuring Plan is **subject to approval by the European Commission**

Contents

Context

- **Anglo Irish Bank (Anglo) has historically focussed predominantly on commercial property lending** in Ireland, the UK and US. Anglo was fully nationalised on 21 January 2009 following unprecedented market events and mounting loan losses. The Bank has since required substantial State aid
- **Irish Nationwide Building Society (INBS) was established primarily as a residential property lender**, but increased its focus on commercial property lending from 2004-08. It has required substantial State aid since September 2008, as a result of issues identified in the June 2010 Restructuring Plan and is now fully state owned
- **Anglo and INBS have recently submitted standalone restructuring plans to the European Commission:**
  - **Anglo submitted a Revised Restructuring Plan on 22 October 2010** (developed with the Irish Authorities) proposing a split into a Recovery Bank and a Funding Bank. This Plan required a total State capital injection of €29.3B, in base and €34.0B in stress
  - **INBS submitted a Restructuring Plan on 22 June 2010** recommending a "preparation for sale" strategy, with a view either to completing a sale (contingent on performance and the market environment) or to pursuing other strategies such as wind-down or merger in the future. This Plan required total government injections of €10.1B under the "wind down until 2020" case (consisting of capital of €4.6B and funding of €5.5B) and €11.4B under the wind down stress case. INBS has received capital injections of €5.4B to date
- **On 28 November 2010, the EC, IMF, ECB and Irish National Authorities agreed on a €85B programme for Ireland** including a National Recovery Plan and a financing package to strengthen the economy, financial system and public finances
- **Consistent with the terms of this programme, the Joint Plan assumes that the Irish Authorities will transfer the deposit franchises and NAMA bonds of both entities.** Deposit franchises (~€14B of deposits) will include associated capabilities, (but exclude up to €1B of deposits currently in secured or related to borrower accounts[1])
- **This Joint Plan proposes to combine what remains within both Anglo and INBS to create a single licensed, fully regulated and Government-owned bank**, focussed on working-out legacy commercial property and other loans within 10 years to minimise capital losses and managing residential property loans for eventual sale

1 Secured deposits are either secured to the Bank (i.e. charge over deposit), or secured to NAMA; Related deposits are unsecured but held by borrowers whether subject to a contractual set off right of the Bank or not

Executive Summary

- Anglo and INBS will be merged into a single entity:
  - The merged bank will be legally independent (within limitations of the law) with its own Board, governance functions and management team
  - A prudent transition period is required to manage towards full merger, recognising the risks of combining operations/systems
- The merged bank will be a licensed, fully regulated and 100% Government owned bank which will:
  - Wind down commercial property and other loan assets of Anglo/INBS within 10 years to minimise capital losses
  - Manage the residential property assets of INBS for eventual sale (assumed in the plan after 5 years)
  - Rely fully on Central Bank or similar funding (e.g. CBI/ELA) supplemented by existing wholesale liabilities (running off in the near term according to existing schedules). Will not hold retail or corporate deposits (except €1B of deposits secured or related to borrower)
- The objective of this proposed model is to avoid the risk of further losses from new lending and concentrate expertise in managing effective wind downs and minimising capital losses in a single entity. As far as possible – the merged entity will seek to minimise and place a cap on State aid requirements
- The proposed Joint Restructuring Plan is not expected to require any additional capital beyond that injected to date in the base case providing the assumptions set out in this Plan are realised (see reference to key risks and assumptions below). The on-going funding requirement will be reduced by asset realisations over the life of the plan:
  - Capital: €34.7B has been injected to date (€29.3B in Anglo and €5.4B in INBS) satisfying the capital requirements for the merged entity in the forecast base case scenario. Capital requirements would increase to €37.9B in a stress scenario (with an additional €3.2B capital to be injected over the plan period).
  - Funding: €49.1B of Central Bank or similar (e.g. CBI/ELA) funding will be required immediately following the transfer of deposits and NAMA bonds[1]. There will be an ongoing funding requirement for the life of the bank (€36B-€47B up to 2015)
  - Guarantees: No guarantee fees paid except on secured, or related to borrower deposits (50 bps fee for the duration of the ELG scheme) and bonds outstanding (95-125bps fee in 2011)
- Several significant risks and assumptions have been identified for which management and the Authorities are identifying feasible mitigating actions. In the near-term, the most significant risks include (see page 13 for overall summary of risks):
  - Triggering default: any action related to this plan may trigger event of default which would lead to a cessation of business challenge
  - Deposit and NAMA bond transfers: may occur below book value, or require additional costs, while increasing operational risks
  - Funding: may not be able to access €49.1B of Central Bank funding in the required currencies at the pricing and duration required
  - Currency risk: Merged entity may have limited/restricted market access, compromising ability to manage structural currency mismatch

1. Assumes NAMA bonds are successfully sold or funding requirement rises by ~€15B

QUESTIONS AND ANSWERS

Transfer of Anglo Irish Bank's and Irish Nationwide Building Society's deposit books

What action is the Minister taking?

The Minister is taking action in connection with the restructuring of Anglo Irish Bank Corporation Limited and Irish Nationwide Building Society. The purpose of the Court Orders is to transfer with immediate effect the deposits and certain assets from both institutions, following an auction process that was commenced under the Direction Orders previously issued on 8 February.

Why is it necessary to take this action?

The continued and on-going existence of Anglo and INBS has been a factor in the destabilisation of the Irish banking system in recent years. There is now a need for the State to take action to resolve the future of Anglo and INBS so as to help restore the Irish financial sector. The State's principal position is that, as a matter of public policy, Anglo position should be worked out in an orderly manner over a period of years, as set out in the Minister's statement of 8 September 2010 and has been endorsed by the External Authorities (IMF/EU/ECB) who are co-ordinating the financial support programme for the State.

What is the restructuring plan for Anglo and Irish Nationwide?

In accordance with the Programme, a joint restructuring and work out plan for these two institutions was submitted on 31 January 2011 to the EU Commission for approval under State Aid rules. The plan envisages the orderly work out of Anglo and INBS over a period of years and, as part of that process, the immediate transfer of deposits from Anglo and INBS to third party credit institutions, namely AIB and IL&P respectively. This plan is now being considered by the Commission, in consultation with the other External Authorities as necessary.

What does the restructuring plan provide for?

In accordance with Government policy the plan provides for the work out of the assets that remain in these institutions after transfers to NAMA in a manner that seeks to protect the financial system as a whole and also to minimise the capital losses associated with this work out. The sale of deposits and corresponding assets are included as a first step in the plan. The Government policy in this regard has been endorsed by the External Authorities.

When do you expect a decision on the restructuring plan?

This is a matter for the European Commission in the first instance. A restructuring plan for Anglo Irish Bank and INBS was submitted to the European Commission on 31 January in line with the timelines agreed with the IMF, ECB and EU for approval under State Aid rules. The national authorities continue to engage closely with the European Commission and the other bodies on this plan. The current expectation is that there should be an indication of the Commission's assessment as to the restructuring outcome later in the spring.

What is intended in respect of deposits in the two institutions?

As a result of the Transfer Orders, substantially all of the deposits of Anglo and INBS have transferred to AIB and ILP respectively.

It is a fundamental objective of the Joint Restructuring Plan that the restructuring of Anglo and INBS protects depositors. The position of Irish depositors is fully protected under the Deposit Guarantee Scheme and the Eligible Liabilities Guarantee Scheme (ELG). UK deposits will retain the protection of the ELG and will be protected under the UK Financial Services Compensation Scheme. Isle of Man deposits will also retain the protection of the ELG and also be protected by the Isle of Man Depositors' Compensation Scheme. The terms and conditions of deposits previously held in Anglo and INBS, including inter alia, maturity and interest rate, will be unaffected by the transfer.

Individual queries on the question of savings and deposits should be addressed to Anglo or INBS in the first place. See contact numbers for Customer relationship teams.

Anglo's relationship team: +353 1 616 2618 (Monday to Friday, 9am – 5pm)

Irish Nationwide Building Society's relationship team: 1850 522 522 (Monday to Friday, 8am – 8pm and Saturday 9am-1pm from Friday 25 February)

How much did AIB pay for the Anglo deposits?

As a result of the transfer, AIB has received Anglo deposits (including deposits in Ireland, the UK and the Isle of Man) of approximately €8.6 billion. It has purchased Senior NAMA bonds with a nominal value of approximately €12.2 billion and the share ownership of Anglo's Isle of Man subsidiary. AIB has also made a cash payment of €3.5 billion.

How much did IL&P pay for INBS deposits?

As a result of the transfer, IL&P has received INBS deposits (including deposits in Ireland, the UK and the Isle of Man) of over €3.6 billion. It has purchased Senior NAMA bonds and other bonds with a nominal value of approximately €3.7 billion in addition to share ownership of INBS' Isle of Man subsidiary. IL&P has also made a cash payment of €2.3 million.

What action will I be required to take as a customer of INBS (Anglo)?

No action is required as a result of this transfer. The respective institutions (IL&P and AIB) will keep customers updated on their transfer of deposits in due course. IL&P and AIB have stated that they are committed to honouring each of the terms and conditions of the savings products as if customers still remained with INBS and Anglo Irish Bank. All savings will also retain the full level of protection under the relevant deposit guarantee schemes as described earlier.

Will my existing terms and conditions remain in place in AIB and IL&P?

Yes, the existing terms and conditions of deposits will be unaffected by the transfer.

I do not wish to bank with AIB/IL&P, can I break my contract without any penalty?

The terms and conditions of deposits, including in relation to matters such as maturity, will be unaffected by the transfer. All depositors will retain the full level of protection under the existing deposit guarantee schemes as described earlier. Any penalties arising from breaking fixed term contracts will be as set out in the terms and conditions applicable to the relevant deposit account.

Will you inform depositors about the outcome of the auction process and the transfer process?

Both institutions INBS/Anglo will update their deposit customers regarding the outcome of the process.

Will I be able to withdraw money at my local INBS branch or Anglo branch or call centre?

Yes, INBS and Anglo branches and call centres will continue to operate as normal and will be available to transact deposit business in accordance with normal terms and conditions. INBS and Anglo will continue to communicate with its customers and will clearly set out the transitional arrangements that will apply.

Will my mortgage in INBS be affected by this court order?

The Court Order in respect of INBS does not affect the mortgage assets of INBS. Accordingly, any mortgage loan a person has with INBS is not affected by the Court Order.

24 February 2011

THEME: C4

Appropriateness and effectiveness of the domestic policy responses

LINE OF INQUIRY: C4E

Cost of crisis and sharing of the impact

Ireland: Housing loans

2.20 Ireland: Housing loans[1], 2004-2013

Year	New Houses	Other houses	Total Number	Total value (€m)	Average value of mortgage (€000)	Representative mortgage interest rate (%)[2]
2004	44,231	54,478	98,709	16,933	171.5	3.48
2005	53,758	53,922	107,680	21,536	200.0	3.49
2006	55,737	55,516	111,253	25,495	229.2	4.20
2007	46,588	37,698	84,286	22,457	266.4	5.25
2008	24,467	29,224	53,691	14,508	270.2	5.51
2009	9,832	15,340	25,172	5,831	231.6	3.46
2010	6,923	11,459	18,382	3,799	206.7	3.66
2011	3,033	8,204	11,237	2,105	187.3	4.18
2012	3,229	11,080	14,309	2,484	173.6	4.24
2013	2,522	11,093	13,615	2,368	174.0	4.36

Source: Department of the Environment, Community and Local Government

[1] These data contain an unquantified element of refinancing of existing mortgages.

[2] See Appendix 1 for more details.

Open in Excel: Measuring Ireland's Progress, 2013 Table 2.20 (XLS 19KB)

- The average value of a housing loan in Ireland increased strongly from €171,500 in 2004 to €270,200 in 2008 before falling sharply over the following five years to €174,000 in 2013.
- The mortgage interest rate rose from 3.48% in 2004 to 5.51% by 2008. The rate then dropped sharply to 3.46% in 2009 and has gradually increased each year since then to stand at 4.36% in 2013.

Central Statistics Office, Skehard Road, Cork, Ireland
Tel: 353-21-4535000 | Fax: 353-21-4535555 | email: information@cso.ie
Contact Census: Tel: 353-1-8951460 | email: census@cso.ie

DÁIL QUESTION

NO

To ask the Minister for Finance if his estimates for interest payments on public debt in 2009 has been revised; and if he will make a statement on the matter.

- Leo Varadkar. (Nominated by: Richard Bruton).

For ORAL answer on Wednesday, 18th February, 2009.

Ref No: 6260/09

REPLY

Minister for Finance (Mr Lenihan) :

The National Treasury Management Agency (NTMA) have advised me that Ireland has a net financing need of some €24½ billion in 2009. This is based on;

- the forecast Exchequer Borrowing Requirement of €18 billion as set out in the Addendum to the Stability Programme Update;
- the refinancing of a €5 billion bond which matures in April; and
- some €1.4 billion in respect of the frontloading of the Exchequer contribution for 2010 for the National Pensions Reserve Fund in relation to the bank recapitalisation programme.

The NTMA have estimated that the associated debt servicing cost in 2009 is €4.5 billion and have advised me that they consider that the revisions to the debt service estimate included in the Addendum are adequate in the context of the current market conditions.

The NTMA have advised me that the main reasons for the increase in the forecast cost of servicing the national debt for 2009 over previous years are the increase in the Exchequer Borrowing Requirement and the higher interest rates currently prevailing on Government bonds. While the increase in borrowing is the major factor, the current elevated yields on Irish Government bonds also contribute to increased debt service costs. There are many factors underlying these yields.

These include global factors which are affecting all euro sovereign borrowers benchmarked to the German bond, and national specific factors.

The NTMA intends to raise funds on the long-term government bond market through a combination of auctions and syndicated loans. It already successfully raised a 5-year €6 billion bond at a coupon of 4 per cent in early January.

It is important to note that Ireland is rated as AAA by the credit rating agencies. In addition we have a relatively low debt level. The General Government Debt to GDP ratio was 41% at end 2008, which is well below the EU average of 60%. At end 2008 when account was taken of the cash balances held by the NTMA and the value of the National Pensions Reserve Fund and other funds managed by the NTMA, the Debt to GDP ratio was reduced to around 20% of GDP. Ireland's debt level will remain below the EU and euro area averages over the coming years. While our debt level will increase in the coming years, our low starting point will provide us with the leeway to target a restoration of balance to the public finances over a number of years. In this way, we can avoid placing too great a shock upon the system as we restore order to the public finances and re-position our economy.

What is our current debt position?
At end January 2009 the National Debt stood at just over €51 billion.

What is the difference between National Debt and General Government Debt?
National Debt is a presentation of the indebtedness of the Exchequer. It should be noted that it is calculated net of liquid assets and excludes certain liabilities recognised in the General Government Debt.

The **General Government Debt** (GGD) is the standard measurement of gross indebtedness used for comparative purposes within the EU. It includes the debt of the Exchequer, the extra-budgetary funds, the non-commercial state-sponsored bodies, as well as the debt of local authorities. It does not allow the offset of liquid assets (Exchequer deposits) held at year end.

What are the forecasted costs of servicing the national debt in 2009?
My Department is informed by the NTMA that the debt service estimate for 2009 is €4.5 billion, broken down as follows:

Cost of Servicing National Debt in 2009	€ million
Interest	3,839
Sinking Fund	573
Other Debt Management Expenses	88
Total	**4,500**

What is the sinking fund?
The Sinking Fund item refers to payments to the Capital Services Redemption Account (CSRA) which was established under section 22 of the Finance Act 1950 to set aside funds for paying off the National Debt. The Sinking Fund provision is a transfer from the current account to the capital account to reduce national debt. The overall Exchequer Balance remains unaffected by the provision because, while the Sinking Fund contribution is recorded as current expenditure, it is balanced out by being recorded also as a capital receipt.

Is Ireland going to lose its AAA credit rating?

The credit rating agencies regard Irish Government debt as among the safest in the world. In January 2009 Moody's, Standard & Poor's and Fitch all re-affirmed Ireland's AAA rating, the highest credit rating.

While reaffirming Ireland's AAA status, S&P and Moody's changed the outlook on Ireland to negative. This suggests a possible medium to long term change in our assessment if no policy changes are made in the intervening period. A change in outlook is not necessarily a precursor of a rating change. "Positive" means that a rating may be raised, "Negative" means that a rating may be lowered, "Stable" means that a rating is not likely to change, and "Developing" means a rating may be raised or lowered.

The National Treasury Management Agency keeps in constant contact with the credit rating agencies to ensure that they are informed of the NTMA's funding plan, developments in the Irish economy and any other relevant matters.

Increased spread in credit default swaps for Ireland? Is Ireland going to default?

There is no question of Ireland defaulting on its obligations and any suggestion in that regard is reckless and without foundation. My understanding from the NTMA is that the credit default swaps market for Ireland's Government bonds is relatively small and is opaque and unregulated. I am advised that the CDS market is generally used as a speculative tool by a small number of market participants to take positions on movements in the CDS market itself rather than to insure against default. Hence, drawing any inference about the soundness of Ireland's public finances from the CDS market would be incorrect. We are an AAA rated country, committed to ensuring the sustainability of our finances and we have no difficulty in servicing our debt position. I again remind you of the fact that we have a low debt ratio and meet our current problems from a position of strength.

Why are our spreads so high compared to Germany? What is this costing us?
The yield on Ireland's 10 year government bonds is currently about 275 basis points over the German equivalent. This spread over Germany is due to a number of factors and it is impossible to quantify the impact of each. These include global factors which are affecting all euro sovereign borrowers benchmarked to the German bond, and national specific factors.

The current spread would add about €27.5 million in interest costs over a full year on every €1 billion borrowed.

Irish bond spreads have widened dramatically - why?
I acknowledge that Irish bond spreads have widened against the benchmark German bond over recent months. However it must be borne in mind that with increased global risk aversion, this widening of spreads is affecting the vast majority of countries and is not specific to Ireland only.

In our case I am aware that the banking guarantee may be a factor in relation to widening spreads. That said, there are actually a variety of factors at play, most notably the international economic environment and the general government deficit. To this end, I have already outlined the necessity to reign in public spending in order to bring balance to the public finances and in line with EU rules.

There is provision in Paragraph 19 of the Credit Institutions (Financial Support) Scheme 2008 to revise the charge if the long term cost to Exchequer funding proves higher than initially estimated.

Have the NTMA had difficulties in raising financing since the guarantee scheme was announced?
The NTMA has continued to be successful in raising finance for the Exchequer. In January the NTMA issued a new five-year €6 billion bond at a coupon of 4 per cent. Strong demand from more than 140 investors across Europe enabled the NTMA to issue double the €3 billion originally intended.

Has the forecast for debt servicing costs increased following the bank recapitalisation programme?

My Department is informed by the NTMA that the debt service estimate for 2009 is €4.5 billion. While the Exchequer's contribution to the NPRF for 2010 will be brought forward into 2009 the NTMA have advised me that this will not lead to additional debt servicing costs this year but it will have an impact in future years.

How much does an extra €1 billion on the EBR cost i.e do you have a ready reckoner for debt service costs?

At current rates on Irish Government bonds, the NTMA have advised me that an extra €1 billion on the EBR would add about €58.5 million in interest costs over a full year.

What is the additional volume and cost of servicing of debt since the Budget?

At Budget time in October last an Exchequer Borrowing Requirement of €13½ billion in 2009 was forecast. The expected cost of financing the national debt in 2009, based on the Budget day forecast for borrowing, was €4 billion. The Addendum to the Stability Programme Update, which was published in early January, presented revised forecasts for the Exchequer Borrowing Requirement. The 2009 requirement is now forecast at €18 billion and there will be an additional €1.4 billion required in respect of the frontloading of the Exchequer contribution for 2010 for the National Pension Reserve Fund in relation to the bank recapitalisation programme. In terms of financing costs the estimate has increased by €544 million over the Budget day forecast to €4.5 billion.

Why has the cost of funding the national debt in 2009 increased by €544 million since Budget 2009?

The Addendum to the Stability Programme Update, which was published in early January, presented revised forecasts for the Exchequer Borrowing Requirement. The 2009 requirement was forecast at €18 billion. Since then this has increased by some €1.4 billion in respect of the frontloading of the Exchequer contribution for 2010 for the National Pension Reserve Fund in relation to the bank recapitalisation programme. In terms of financing costs the estimate has increased by €544 million over the Budget day forecast.

The National Treasury Management Agency have advised me that the main reasons for the increase in the forecast cost of servicing the national debt for 2009 are the increase in the estimate for the 2009 Exchequer Borrowing Requirement and the higher interest rates currently prevailing on Government bonds. While the increase in borrowing is the major factor, the current elevated yields on Irish Government bonds also contribute to increased debt service costs.

The NTMA have advised that certain timing factors also contributed to the increase – as a result of the build up in Exchequer balances, additional interest costs were accrued toward the end of 2008 but did not fall due for payment until 2009. In addition deposit interest rates have fallen since Budget time and this also increases the debt service costs.

How much more is the cost of financing the debt in 2009 than in 2008?
The National Treasury Management Agency have advised me that the expected cost of financing the national debt in 2009 is estimated at €4.5 billion, which represents an increase of €2.4 billion on that for 2008. The NTMA have advised me that the reasons for this increase are;

- the costs of funding the now larger Exchequer deficits for 2008 and 2009
- higher interest rates on Government bonds and
- timing differences arising from interest accrued in 2008 but payable in 2009.

How much cash has the NTMA?
As a prudent measure, the NTMA accumulated cash balances of more than €20 billion during 2008. The associated short-term borrowings are currently refinanced on an ongoing basis as they mature. The NTMA also successfully issued a 5-year €6 billion bond in January. As a result, Exchequer free cash balances currently stand at over €26 billion. The NTMA will decide on the timing of its longer term debt issuance programme for the remainder of the year in the light of market conditions.

What is the estimated premium over the ECB rate for borrowing?
The European Central Bank has two lending rates - the interest rate on main refinancing operations (which provide the bulk of liquidity to the banking system)

currently stands at 2 per cent; the interest rate on the marginal lending facility (which offers overnight credit to banks from the Eurosystem) currently stands at 3 per cent. These rates are short-term rates available to banks.

The NTMA intends to raise funds on the long-term government bond market through a combination of auctions and syndicated loans. It already successfully raised a 5-year €6 billion bond at a coupon of 4 per cent in early January. The yield on 10-year Irish Government Bonds is currently around 5.6 per cent. For commercial reasons, the expected yield on bonds to be issued in 2009 is not disclosed.

Does the forecast for debt service costs take account of the €2 billion in required savings on expenditure?

The Addendum to the Stability Programme Update forecast an Exchequer Borrowing Requirement of €18 billion for 2009. This took into account the requirement for a €2 billion adjustment. The forecast for debt service costs in 2009, estimated at €4.5 billion, takes into account the fiscal consolidation objective.

Will there be a reduction in borrowing in 2009 as a result of the expenditure control measures announced on 3 February 2009?

The expenditure adjustments announced on 3rd February last will yield €1.8 billion in 2009 and €2 billion in a full year. This is broadly in line with the indicative annual adjustment as set out in Table 4 of the Addendum to the Stability Programme Update. As such it is consistent with the overall macro-economic and fiscal forecasts published in early January including those for Government borrowing.

Surely increasing the amount of borrowing is the wrong approach to take? / Should we not borrow our way out of difficulty?

As I have already stated we have a low debt level. The General Government Debt/GDP ratio was 41% at end 2008, which is well below the EU average of 60%. At end 2008 when account was taken of the cash balances held by the NTMA and the value of the National Pensions Reserve Fund and other funds managed by the NTMA, the Debt/GDP ratio was reduced to around 20% of GDP. This affords us some leeway to deal with the current challenges.

However borrowing is not a long-term solution. The recently published Addendum to the Stability Programme update set out to address the fiscal and economic situation over a five-year period to 2013. Since then we have announced expenditure savings of €1.8 billion in 2009 and €2 billion in a full year. The Government has also signalled that further fiscal consolidation measures will be necessary in the period 2010-2013 and that these adjustments will, as necessary, include measures to reduce and prioritise expenditure and to adjust taxation levels to reflect the changed realities. The work of the Special Group on Public Service Numbers and Expenditure and that of the Commission on Taxation will inform decisions taken by the Government in this regard.

Will the NTMA have savings this year in respect of debt servicing costs?

The forecast for debt servicing costs for 2009 is €4.5 billion. This estimate was prepared for the Addendum to the Stability Programme Update published in January. It has been stress-tested and the NTMA have advised me that they consider it adequate in the context of current market conditions.

But the NTMA had debt savings in 2008?

The NTMA reported savings on debt servicing costs at the end of 2008 of €396 million over the Budget 2008 forecast due mainly to timing issues related to the payment of interest on new borrowings issued in 2008, higher than anticipated deposit interest on Exchequer cash balances, reduced interest rates on borrowings, and certain debt management initiatives.

What is your forecast for General Government debt over the period to 2013?

As set out in the Addendum to the Stability Programme Update the forecast for General Government debt as a percentage of GDP over the period to 2013 is as follows

2008	2009	2010	2011	2012	2013
40.6%	52.7%	62.3%	65.7%	66.2%	64.5%

While the General Government debt-to-GDP ratio will rise over the forecast period, Ireland's net debt position will still be significantly lower than implied by the gross level.

The General Government Debt to GDP ratio was 41% at end 2008, which is well below the EU average of 60%. At end 2008 when account was taken of the cash balances held by the NTMA and the value of the National Pensions Reserve Fund and other funds managed by the NTMA, the Debt to GDP ratio was reduced to around 20% of GDP.

What is the 2009 Exchequer contribution to the National Pensions Reserve Fund?

The 1% of GNP payment in 2009 will be €1.584 billion. Under the Government's proposal to recapitalise Allied Irish Banks and Bank of Ireland, it is envisaged that the NPRF will invest some €4 billion from its own funds and a further €3 billion made up of this year's Exchequer contribution of €1.584 billion with the balance provided by the Exchequer as a pre-payment towards next year's contribution.

NPRF and recapitalisation of the banks

The National Pensions Reserve Fund (NPRF) was established on 2 April 2001 under the National Pensions Reserve Fund Act 2000 with the objective of meeting as much as possible of the cost to the Exchequer of social welfare and public service pensions to be paid from the year 2025 until at least 2055. The National Pensions Reserve Fund Commission controls, manages and invests the assets of the Fund, to which the Exchequer contributes an amount equivalent to 1% of GNP each year, in accordance with the Fund's investment policy.

On 11 February 2009, I announced details of a scheme designed to recapitalise the two main Irish banks, Allied Irish Bank and Bank of Ireland. The recapitalisation programme will be funded from the NPRF. €4 billion will come from the Fund's current resources while €3 billion will be provided by means of a frontloading of the Exchequer contributions for 2009 and 2010. The necessary amending legislation to the National Pensions Reserve Fund Act 2000 will be introduced shortly.

I expect that this participation by the NPRF in the recapitalisation exercise will yield a satisfactory return for the Fund over time and will assist the Fund in its purpose of meeting as much as possible of the cost to the Exchequer of social welfare pensions and public service pensions, to which the Fund will start to contribute in 2025.

What is the value of the Fund today?

The market value of the Fund at end-2008 was €16.4 billion, giving an annualised return of 0.6%, while total contributions amounted to €16.9 billion.

What is the projected value of the Fund at end-2009?

The investment and management of the Fund is a matter for the National Pensions Reserve Fund Commission. I have no function with regard to making projections in relation to the future performance of the Fund, but see no reason why the long-term performance of the Fund should not equal or exceed that of Irish pension funds generally.