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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January 2016

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THEME: C4

Appropriateness and effectiveness of the domestic policy responses

LINE OF INQUIRY: C4a

Decision to nationalise Anglo in 2009 and a review of the alternatives available and/or considered

SECRET
Offig an Aire Airgeadais

Ref No **Date: 15 January 2009**

Decision Sought on the Nationalisation of Anglo Irish Bank

1. Decision Sought

The Minister for Finance asks the Government today to approve:

(a) That Anglo Irish bank should be nationalised and that this should be done by way of a Bill, the indicative text of which is attached; this will be subject to amendment to be agreed between the Minister for Finance and the Attorney General. The Bill, when finalised, is to be published.

(b) That the Houses of the Oireachtas be recalled with a view to sitting on Tuesday 20 January, with a view to taking all stages on Tuesday.

(c) That there be an early signature motion to incorporate the Bill.

(d) That the Government notes that it would be the intention of the Minister that the newly appointed Chairman and the public interest Directors would be reappointed after nationalisation and that the Minister would consider the position of the other Directors giving due regard to the need for continuity.

(e) That a statement will be issued this evening and the draft of the Bill will be made available publicly.

(f) Finally, the Minister will be informing the opposition spokespersons.

2. Background

Last night, the Central Bank, the Financial Regulator, the NTMA, and the Department of Finance recommended that nationalisation of Anglo Irish Bank provides the better prospect of stability in the Irish banking system and should be pursued in preference to the planned recapitalisation of Anglo on Friday.

This morning AIB and BOI gave their view that a nationalisation of Anglo should not de-stabilise their position, provided a clear distinction is made between their financial and market position, and that of Anglo, and each bank said that in their opinion, on balance, nationalisation was the best option available.

This advice was given because of a number of serious corporate governance concerns at Anglo, and because of Anglo's progressively deteriorating liquidity position.

3. Corporate Governance

There is continuing concern about governance issues including Directors loans, loans to buy Anglo shares and other financial arrangements in the Bank. The ODCE has commenced an investigation and it is possible that the ODCE would appoint a court inspector on these and other company law matters.

The Financial Regulator is concerned about all of the governance issues and is conducting a number of investigations. However, the disclosure of some or all of these issues would have the effect of further destabilising the position of Anglo Irish Bank. This is in a context where, following the resignations of the Chair and CEO, market confidence in Anglo is already extremely low, which has meant that Anglo is encountering increasing liquidity difficulties.

4. Liquidity

Anglo's liquidity has disimproved since early December, with the bank losing €3bn in corporate deposits. Anglo's liquidity position is now very fragile.

Fitch's are expected to downgrade Anglo's credit-rating today, leading to a potential further €1bn -€2bn outflow of corporate deposits. Downgrades from S&P are also expected to result in even greater corporate outflows. A total of €6bn or more could flow out from Anglo and it is clear that this flow is not being stemmed by our announcement on recapitalisation and government voting rights in Anglo.

Using Central Bank and NTMA options to replace this liquidity would put at risk a disproportionate amount of liquidity reserves to protect Anglo. It is considered unlikely that this public liquidity support could be repaid in the foreseeable future by the bank.

As a result of these new developments, it is necessary to re-evaluate the approach to be taken with Anglo. The alternative to the planned recapitalisation is nationalisation. While neither option can quickly resolve Anglo's difficulties, on balance nationalisation mitigates the risks that the Anglo now presents to the public finances and to financial stability.

5. Pros and Cons of Nationalisation

<u>Pros:</u>

- Should mitigate the risk of an S&P ratings downgrade
- Minimises deposit outflows
- Reduces risks of significant demands on the liquidity reserves available to the NTMA and the CBFSAI
- Introduces certainty in the market on Anglo
- €1.5bn can be used for liquidity funding, with a better chance of recovery
- Even with recapitalisation and liquidity support, continuing bad news could lead to a requirement to nationalise Anglo, but from a weaker position
- De-listing ends share speculation about the bank on the market
- Allows for orderly work-out of the loan book
- Allows Minister direct control to deal with the governance issues

Cons:

- Introduces perception of confused approach to Anglo problems
- Contagion risk to other banks
- Liquidity support likely to still be required
- May be perceived as a reaction to significant negative issues arising from the due diligence process
- Asset realisation values may be negatively impacted

6. Taking all of the above factors into account, I am therefore seeking your approval to nationalise Anglo Irish Bank.

THEME: C4

Appropriateness and effectiveness of the domestic policy responses

LINE OF INQUIRY: C4b

Establishment, operation and effectiveness of National Asset Management Agency (NAMA)

OIFIG AN AIRE AIRGEADAIS

Ref No: **March 2009**

SECRET

Memo for Government

Proposal for a National Asset Management Agency

1. Decision Sought

The Minister for Finance requests the Government to note:

- the summary of the report from Mr. Peter Bacon acting as the Minister's adviser to the NTMA which is given at Appendix 1;
- the liquidity support arrangement as set out in paragraph 10 and the initial conclusions of a review of the banks guarantee scheme, as set out in this Memorandum and the further Appendices.

The Minister for Finance asks the Government to note that he is working on a proposal as follows:-

- he will announce on Budget Day that he intends to set up a National Asset Management Agency (NAMA) under the auspices of the National Treasury Management Agency
- that NAMA will purchase the land and development books of the six main covered institutions and the loans of the 22 largest borrowers from these institutions; this purchase will be at a discount, will be of the order of €60bn and will be funded by the issue of Government Bonds.

The Minister for Finance asks the Government to note that there is a consensus among his advisers in favour of the establishment of a National Asset Management Agency, although there is considerable further work needed on the detail before the Budget Day announcement and that the Minister will return to Government on this issue. It will also be necessary to consult the Commission and the ECB on this matter.

2. Background

At present Irish banks face an extremely unstable outlook. In recent times they have experienced major withdrawals of deposits and established credit lines leading to substantial recourse to the Central Bank for short-term liquidity support. This is not a sustainable trend and if it persists would be expected to lead to a serious systemic issue for the Irish banking system over the coming weeks. According to some

projections the six guaranteed credit institutions face cumulative economic impairment on their property loan exposures to 2011 of around €34bn, or 20 per cent of the total value of property loans of €158bn; this is before account is taken of offsetting earnings.

The initiatives taken to date by Government have been insufficient to encourage the retention of liquidity in the Irish banking system. Share values have remained depressed, deposits are continuing to fall and access to debt capital markets is very restricted. This is undermining banks' capacity to grow lending, now in the future, in support of the recovery of the real economy. The Bacon report concludes that, unless there is a restructuring, even a very considerable additional capital injection, over and above the €7bn recently announced, would do no more than maintain the banks in their current 'zombie' status till 2011 and leave Ireland's international credit rating subject to downward pressures and speculative attacks. Therefore additional and far reaching measures need to be undertaken, as soon as possible to seek to place the banking system on a sound footing.

The deterioration in Ireland's credit terms associated with the national fiscal position has been compounded by the additional contingent liabilities of c.€440bn under the bank guarantee scheme and the fact that deposits and access to international credit markets have not been stabilised as a result of the Guarantee is compounding the perception that the contingent liabilities could be realised through a bank default which would impact very severely on the State's financial position and creditworthiness.

Bacon concludes that, to achieve stability in banks deposit and term debt liabilities, doubts about capital adequacy of the credit institutions and their capacity to deal with prospective loan impairment must be removed. Additional supports should focus on the asset impairment issue and associated implications for capital adequacy.

3. Options Available to Government

There are a number of options available to Government in dealing with the current liquidity difficulties and the overall threat to the stability of the Irish banking system.

Maintain Status Quo: This option is to continue with the present recapitalisation strategy and not to undertake additional measures on the basis that they run the risk of further undermining the State's fiscal position and international credit rating. In the current circumstances, there is no apparent benefit to doing nothing. Not acting now increases the risk of a sovereign default and threatens the stability of the banks. Moreover it will not address the current liquidity shortage or promote vital lending into the economy.

Insurance: The State could establish an insurance scheme for certain assets, such as the land and development portfolio valued at €60bn. The State could then provide insurance to the banks against the majority of the losses they incur on the relevant loans above a certain "first loss" position (for example, 20 per cent.). The loans would remain on the books of the Bank who would continue to manage them over time. It is also likely that the banks would be required to share a proportion of the losses above that first loss amount (perhaps another 10 per cent. of all amounts covered by the

insurance) to incentivise them to achieve the best recovery for the loans. The banks will pay a relatively small fee of c2.5% to the State for providing the insurance. The main benefit to the insurance scheme is that there is no upfront cost. However, the success of the insurance scheme depends on the market's faith in the Government's ability to cover future losses. The contingent liability element of the insurance scheme parallels the bank guarantee scheme and provides no direct method to deal with the current severe liquidity problems faced by the covered institutions who have lost over €43bn since the start of 2009. It also fails to create a strong incentive for the banks to work out their impaired loan book once their first loss has been incurred.

Asset Management Agency: An Asset Management Agency could be established. The agency would purchase a portfolio of loans from the banks focusing on the riskiest loans. The purchase could be done by issuing government bonds to the banks. The Agency would then manage the loan assets over time to ensure the minimum loss for the State. This option would be expected to cleanse the balance sheets of the banks, considerably reducing uncertainty over bad debts and allowing them to increase lending to the real economy. It would also address the liquidity difficulties the banks face as Government bonds could be used as collateral to access ECB funds. On the downside there would be a very considerable upfront cost to the State impacting the Government debt and instantly inflating the debt with related implications which are discussed elsewhere. There would also be significant logistical implications to taking this course of action. As with the risk insurance option the markets will be required to maintain faith in the Government's ability to maintain its own position. It would also be important to ensure this is consistent with the EU framework in order to maintain Ireland's capacity to work closely with the EU and our Eurozone partners as we seek to resolve the financial crisis.

A more detailed assessment of these options is at Appendix 2

4. Bacon favours an Asset Management Agency

The key conclusion in the Bacon report is that an Asset Management Agency should be established to take over the banks' Land and Development books of **c€63.5bn**.

The Bacon report however goes further and recommends that the banks commercial property books should also be taken over bringing the total value of the assets to be managed to **€158.3bn,** although these would be purchased by the State at a discount. While the report does not provide a detailed rationalisation for the extension of the assets to be purchased by the State to the banks commercial property books, Mr. Bacon did advise at an oral briefing that he was taken aback at the pace of decline in the performance of the commercial property books and had concluded that these loans must be removed from the banks to ensure the creation of clean banks which will again be in a position to lend into the economy.

Economic impairment of the combined property books to 2012 is estimated at **€34bn**. Bacon recommends this amount be written off immediately by the banks and that consequently the cost to the State of taking the property books into the Asset Management Agency will be in the region of **€120bn**. Immediate write offs on this scale will give rise to further capital investments and bank restructuring, as considered below.

The report recommends that the asset management agency be located in NTMA and funded by means of an exchange of assets; the banks would receive Government paper in return for the loan books they hand over.

5. Consensus in favour of asset management over risk insurance solution
The Bacon report has been considered by the Department, the Central Bank, the Financial Regulator, NTMA and Merrill Lynch. While the risk insurance has certain attractions in terms of deferring realisation of the impairments and funding requirements of the insurance, there is a consensus that the asset management agency is preferable as it would:

- Deal with the issue of impaired property loans more decisively and definitively, providing the banks with cleaner balance sheets and reducing the risk of further impact of impairments from property loans on the banks
- Improve the funding position of the banks by providing them with assets that can be used to access ECB funding
- Remove management of the problem loans from the banks, which should provide greater control of the work-out of the loans, address public suspicion regarding the relationships between the banks and developers and deal with market concerns that the banks are not realistic about the extent of likely losses
- The asset manager should have limited regulatory capital requirements in respect of losses on impaired loans and can manage the assets without the focus on impairment disclosure that the banks face
- Should improve sentiment towards the banks and represent the start of the repositioned investment case. It would allow management time to be refocused on rebuilding strength particularly in core retail businesses and maintaining their deposit bases, during an extended period during which it will be very challenging to raise funding.

6. The scale and cost of assets to be transferred
While there is a strong argument in favour of the creation of an Asset Management Company it is not clear that this should include all of the commercial property books of the banks as recommended by Bacon.

There are three identifiable options for what assets could be purchased by the Asset Management Agency. These are:-

i. All land and development and property development loans as recommended by Bacon – these are currently valued at c€160bn but Bacon envisages that the Asset Management Agency would pay circa €120bn for this total loan portfolio, with the banks writing off the balance of 25%;

ii. Land and Development loans only, which is the riskiest part of the banks loan portfolio – these are currently valued at c€60bn but it is envisaged that the Asst Management Agency would take these at considerable discount to the book value, perhaps of the order of 33%, and would cost circa €40bn;

iii. Land and development loans plus a certain portion of the commercial loan book (following a risk assessment to incorporate the largest exposures in the system and other risk assessment criteria) – this portfolio would amount to circa €85bn, but again there would be significant discount and would cost circa €60bn.

7. **Impact on National Debt**

The main disadvantage of the Asset Management Agency is the up front impact it will have on the national debt. At the end of 2008 the General Government Debt stood at €76.1bn (inclusive of Exchequer cash balances of €21bn) which was equivalent to 40.6% of GDP. The addendum to the Irish Stability Programme Update, presented to the Commission last January, provided for a further decline in the fiscal position in 2009. Taking account of the recent €2bn adjustment, and before supplementary measures to be decided in the coming weeks, it provided for a General Government Deficit of €17.2bn in 2009 and an increase in the debt/GNP ratio to 52.7%.

The Asset Management Agency proposal will significantly increase the level of the General Government Debt, unless a mechanism can be found to put it "off balance sheet". The scale of the impact will be determined by the amount of the banks assets transferred and the price paid for those assets. Based on the figures recently contained in the Stability Programme Update for 2009, the three options set out above would have the following impact on the level of General Government Debt in 2009:

	Stability Programme Update position	All land & development and commercial property loans (Option i)	All land & development loans only (Option ii)	All land & development loans plus a portion of the commercial loan book (Option iii)
Book value of loans (€bn)	-	160	60	85
Assumed price paid by the AMA for the loans (€bn)	-	120	40	60
General Government Debt (GGD) level (€bn)	94.7	214.7	134.7	154.7
GGD/GDP ratio (%)	**52.7**	**119.4**	**74.9**	**86.1**

The above GGD/GDP ratios would compare with an EU average of 59.8% and 104% for Italy, the highest in the EU. (2008 position in each case). Consideration will be given to whether there are structures which allow these liabilities to be kept off the GGD, but of course the markets will look through these.

8. Consensus in favour of scaled back option

The consensus view of the Central Bank, Financial Regulator, NTMA and Merrill Lynch is that the 'scaled back' option which would see the transfer of the land and development books of c€60bn, plus a certain portion of the commercial loan book, amounting to around €25bn, would be the one that provides the best balance between the objectives of stabilising the banking system while seeking to constrain the impact on the national debt.

9. Implications of creating an Asset Management Agency

With regard to the banks the implication of the transfer of a large part of their loan portfolios will see the operations of Anglo Irish Bank and INBS significantly scaled back. The option of selling on INBS remaining interests would have to be looked at after the relevant assets were removed. Anglo would either have to be recapitalised and reoriented or sold.

Further recapitalisation may also be required. The 'scaled back' asset transfer option above is based on a projected economic impairment estimate for the six institutions combined property development and part of the investment book of €25bn now. The effect of realising this kind of shortfall would require further capital injections, over and above the €7bn already announced for AIB and Bank of Ireland. It is estimated that AIB would require a further recapitalisation of about €1.5bn with €0.2bn required by EBS. Bank of Ireland would not require any further capital, over and above that already agreed.

Balance sheets at Appendix 3 indicate the aggregate impact on the six banks, the Asset Management Agency and on the State.

10. Immediate Liquidity needs.

Neither the 'status quo' nor the risk insurance options provide the banks with further access to ECB liquidity. The Asset Management Agency option does provide Government bonds which can be repo-ed at the ECB to replace lost liquidity. However, an AMA would take time to set up, so some interim liquidity support may be necessary. A short term Collateralised Lending Scheme (CLS) could be provided to the bank as a 'bridge' to the AMA. Under this scheme the NTMA and Central Bank would swap (new) short term government bonds for loans provided by the banks. These bonds could then be used as collateral with the ECB. A summary of the draft CLS scheme is provided in Appendix 4. This scheme would add to the Government debt as the banks needed liquidity. In the event that the risk insurance or status quo options were pursued, it is likely that a CLS scheme will have to be put in place also as an alternative to special liquidity facilities provided by the Central Bank to institutions that have exhausted their ECB collateral. However, it is not clear how the Government would exit such a scheme in these cases.

11. Review of the Bank Guarantee Scheme

A review of the Guarantee is currently underway, as required by the European Commission and the terms of the Guarantee Scheme itself, with the purpose of establishing whether the Guarantee continues to assist in achieving the objectives of the Credit Institutions (Financial Support) Act of 2008. While the Guarantee had a successful short-term impact, several long-term deficiencies have been identified including in particular that as demonstrated by recent liquidity outflows the Guarantee has lost credibility in the market. The Government has already agreed to seek the extension of the Guarantee to encompass longer-term bond issuance (up to five years) to support the banks in accessing longer-term funding. This would be consistent with the common EU framework. The possibility of enhancing the credibility of the Guarantee by reducing the contingent liability assumed by the State is also being examined. There are several instruments covered by the Guaranteed that have not practical benefits for the banks in supporting their funding but impact on the size of the Guarantee (e.g. covered bonds,). Very careful examination would however be required of the possible impact of a restructuring in the Guarantee on Ireland's international reputation and creditworthiness. An update on the review of the Guarantee is included at Appendix 5.

12. EU implications

The Bacon proposal would raise a number of significant issues in light of the Commission's recent Communication on the Treatment of Impaired Assets, including the assessment of assets eligible for transfer to the asset management agency, the valuation process and methodology and consistency with the sustainability of Ireland's overall fiscal position. The Commission has confirmed this in an initial response to the Bacon proposal, which identifies several issues that would need to be discussed and addressed, and the process that would need to be followed in a review of these issues. These issues are noted at Appendix 6.

Appendix 1:

Bacon Report on Options for Resolving Property Loan Impairments and Associated Capital Adequacy of Irish Credit Institutions

Overview:

The Bacon report identifies and seeks to address two critical issues:

1. That the lack of market confidence in Irish banks - reflected in low share prices and funding outflows despite the guarantee - is founded on uncertainty about the adequacy of capital levels in the banks to meet future loan impairments.
2. That a large part of the increase in sovereign borrowing costs is based on market uncertainty around the State's exposure to the c. €440bn contingent liability assumed with the guarantee of all bank liabilities.

Bacon recommends the establishment of a National Asset Management Agency (NAMA) to take over and manage all the Land and Development loans and Investment Property loans currently held by the covered banks, totalling some €158bn. These assets would be mandatorily purchased by the State, at discounted rates to their original book values, by the issue of c.€124bn worth of Government bonds to the banks. A further €7.5bn recapitalisation of the covered institutions, the sale or controlled winding down of a merged Anglo-INBS entity, and a review of the guarantee Scheme, also form part of Mr. Bacon's proposals.

This approach would address market uncertainty around future capital levels in the banks. This should allow the banks to raise and retain funding, and lend to the economy. In addition, subject to the agreement of the ECB, the banks could use the Government bonds to access c. €118bn in funding from the ECB, thereby addressing current liquidity constraints in the Irish system.

The proposal would involve a sharp increase in the level of national debt (from 41% to 111% of GDP). However, the definitive transfer of all risky bank assets to the State, would bring certainty to the market on the Government's borrowing requirement to address the banking crisis (c.€130bn rather than c.€440bn). Returns from the assets held by the NAMA would accrue to the State. As the assets transferred would be discounted and would include both performing and non-performing loans, the State could expect to recover, over time, at least the greater part of the cost of acquiring these assets.

Summary:

1. Crisis in Irish Banking:

The expansion of credit in recent years has been funded by growth in external funding sources of the banks. The downturn in the economy has brought a lack of market confidence in the ability of the banks to cover losses arising from the credit they extended, which has resulted in funding outflows of €45bn to date in 2009, and a consequent deterioration in the day-to-day liquidity positions of the banks.

It is estimated that between now and 2011, the six covered institutions face a cumulative impairment on their property-related loan exposures of around €34bn, or

20% of the total value of the property loans outstanding at September 2008 of €158.3bn. Of this loss, €20bn relates to land and development lending, and €14bn relates to lending for property investment. These figures are based on the assumption of a 55% peak-to-trough decline in the value of development assets, and a 32% reduction in the value of investment assets, and are broken down as follows:

Projected impairment of Development & Investment Property loans (€bn):

Total	AIB	Anglo	BoI	INBS	IL&P	EBS
34	10.8	12.9	7.6	2.2	0.2	0.3

Using these estimates, retaining the 6 banks' capital levels at above 7.5% in the absence of a transfer of risky assets to the State, would require a further recapitalisation of the banks of €8.4bn, as follows:

Projected <u>additional</u> capital required to raise Tier1 Capital Ratio to 7.5% following projected impairment (€bn):

Total	AIB	Anglo	BoI	INBS	IL&P	EBS
8.4	1.5	5.6	-	1.0	-	0.3

However, because of continuing market uncertainty around eventual losses on the risky assets, even if this projected capital requirement was met by the State, the banks would retain their current 'zombie' status, with depressed share prices, no prospect of private capital-raising, under continued funding pressure and consequently with no capacity to grow lending, thus hindering economic recovery. In addition, market concerns around the sovereign exposure to the banks under the guarantee would remain, complicating further the required adjustment of the public finances and leaving Ireland's international credit rating subject to downward pressures and speculative attacks. Bacon suggests therefore that additional measures need to be undertaken to place the banking system on a sound footing.

2. Constraints on the Public Finances:

From a high of almost 100% of GDP in the early 1990s, national debt stood at 41% of GDP at end 2008, well below the EU average of 61% of GDP. As a result, debt servicing costs reduced from 25% of tax revenue in 1991, to 3.8% in 2008.

However, in 2008, with the widening deficit, there has been a very sharp rise in the relative cost of Government debt issuance in recent times. In the past five months, the interest rate charged for Irish 5-year bonds has trebled, to 280bps (or 2.8%) higher than the rate for German Bunds of similar maturity. Similarly, the credit default swap (CDS) rate on Irish bonds - representing the cost of insuring against default - which had been similar to that of Germany for much of the decade to date, began to increase dramatically from the third quarter of 2008 and now exceeds that for Greece, previously the country with the highest CDS rate in the EU.

In part at least, the deterioration in Ireland's relative cost of funds is related to the contingent liabilities of €440Bn assumed by the Government in respect of banks and credit institutions deposit guarantees. These were taken on from 30 September, and it is from around that date that credit spreads have deteriorated most sharply.

In determining the price to charge for Irish Government borrowing, Capital markets are simply adding contingent liabilities assumed under the guarantee to the State's outstanding debt and its prospective debt as a result of the widening deficit. In effect the sovereign debt rating is being intertwined with the country's banking problems via the guarantee on bank liabilities.

Uncertainty has been created because of the contingent nature of the bank guarantee and it is evident to market participants that credit institutions' deposits have not been stable since the guarantee was put in place. Hence, the probability of the guarantee being called has been raised. At the same time the underlying cause of instability in banks' funding: the question of the capital adequacy of the credit institutions to meet prospective impairments, remains unresolved. In these circumstances the likelihood is that the uncertainty premium in yield being attached to government debt will continue and indeed may increase, as economic conditions deteriorate.

In this context, it is imperative that initiatives should be undertaken that will lead to stability in banks deposit and term debt liabilities and eliminate the need for a renewal of the guarantee. To achieve this requires removing all doubts about capital adequacy of the credit institutions and their capacity to deal with prospective loan impairments.

3. Dealing with Loan Losses:
The report considers three options for tackling the related market uncertainties around capital levels in the banks, and the extent of liability of the State.

A. Recapitalisation:
Building on the assessment above on likely impairment rates, future capital shortage is anticipated by testing the adequacy of current capital in stress scenarios. In current market conditions the only realistic source of capital for the banks is the State. The report notes that where Government is guaranteeing the liabilities of the banks and has injected capital to cover losses on loans, nationalisation may be the most effective means of protecting the interest of all stakeholders.

B. Asset Guarantee:
Under this option, the State guarantees the level of future losses on certain (risky) bank assets. The assets remain on the balance sheet of the bank and the banks commit to covering losses on these assets up to a certain 'first loss' amount. There is no upfront cost to the State and the banks pay a fee or premium for this cover.

C. Asset Purchase:
In this scenario, risky assets are transferred from the bank at an agreed price. The State would have to fund the asset purchase, via the issue of Government bonds to the banks, which would negatively affect the fiscal position. The bank takes a loss on the sale and recognises this up front in its profit and loss account. The bank is then effectively cleansed of these risky assets.

The report considers the merits of asset guarantee versus assets purchase:

	Pro	**Con**
Asset Guarantee	• No upfront cost to State • Earns premium • Risk sharing provides banks	• While risk is partially transferred, assets remain on the banks' balance sheets,

	with incentive to manage loans	creating continuing uncertainty for investors around the banks positions • Creates a further contingent liability for the State •
Asset Purchase	• Banks are cleansed of troubled assets • Earns net income after financing cost • Loss sharing, since the bank has to write off the difference between the book value and the purchase price • Position for investors in the banks is made clear • State gains control over asset management	• Large upfront cost, involving increase in national debt • Losses accruing to banks would result in requirement for a further recapitalisation to maintain CT1 levels above 7.5% • Downside risk on assets accrues to State

While the asset guarantee approach has the initial attraction of having no upfront cost to the State, the approach would be subject to the same issues already encountered with the guarantee of bank liabilities: Capital markets have not grappled well with the uncertainty involved with the contingent liabilities assumed by the State and have priced Irish sovereign debt unfavourably as a result.

A further guarantee approach, this time in respect of banks' property related loan assets, would create a further layer of uncertainty through the creation of another contingent liability on the Exchequer. This would further entwine the sovereign rating with Irish banks capital adequacy problems without actually providing any clarity as to how capital adequacy would be achieved, other than through a calling of the contingent liability. By contrast the asset sales approach, while involving the recognition of 'pain' at the outset has the merit of certainty and clarity, provided the projection of the extent of impairment is accurate.

Also, an Asset Management Agency (NAMA) would offer prospects for avoiding many of the shortcomings associated with a continuation of the existing bank-property developer relationship. Potential advantages include: (i) economies of scale in administering workouts (since workouts require specialized, and often scarce, skills) and in forming and selling portfolios of assets, (ii) benefits from the granting of special powers to the government agency to expedite loan resolution and (iii) the interposing of a disinterested third party between bankers and clients, which might break "crony capitalist" connections that otherwise impede efficient transfers of assets from powerful enterprises. The latter may seem particularly beneficial in circumstances markets, where ownership concentration and connections between borrower and banks are often very close.

The NAMA would have the potential to attract potential to attract long term capital to invest in the assets taken on to achieve higher values by working out the projects rather than disposing of the assets.

The up-front losses that would accrue to the banks under the proposed asset purchase approach (€158bn of assets purchased for €124bn) would require additional recapitalisation to maintain the banks'Core Tier 1 capital ratios at 7.5%, of:

Total	AIB	Anglo	BOI	INBS	ILP	EBS
16.25	5.0	8.5	0.75	1.5	0.0	0.5

To minimise the costs to the State, consolidation of rump of INBS and Anglo (after the asset purchase transaction) to be sold to highest bidder as a business franchise, or wound downs as liabilities mature is recommended. An additional capital injection of c.€2bn would be required from the State to stabilise the (combined) institutions and maintain a Core Tier 1 capital level of around 5%. This approach would leave a requirement for further State capital provision in the banking sector, of around €7.5bn.

The impact on AIB and BoI of a further re-capitalisation as proposed would (depending on the precise terms of the investment) raise the degree of State ownership in these institutions to 90% and 85% respectively. In consequence most of the pre-impairment earnings of these institutions would accrue to the State. However there is a distinction between this position and fully nationalised entities that - similar to the situation now applying to RBS in the UK - in that both banks would retain their stock exchange listings. Therefore as market conditions improve, there will be a natural exist mechanism available for the Government to divest itself of majority ownership should it wish to.

In all circumstances it is imperative that agreement of the ECB to funding a bond of face value of €124bn would be procured before any decision is taken by Government to proceed with the recommended approach.

4. Proposal for a National Asset Management Agency:

Functions to be carried out by a NAMA comprise:

- Management and control of the assets transferred to it;
- Employment/outsourcing whatever resources required to carry out its functions efficiently and professionally;
- As it will control a large segment of the market, it should be able to regulate against further market failure due to oversupply in the future;
- It will carry no previous baggage and will have a single objective - to maximise value over a given period;
- It will not have any other banking functions or aspirations;
- It will not favour any institution or client over another, but can make decisions with the advantage of an overview which individual banks cannot have;
- It will have well marked out procedures to prevent fraud but will encourage a suitable commercial posture;

It is proposed that the NAMA be constituted via an extension of the remit of the NTMA because of the Agency's international reputation, and core expertise and technical know how. The NAMA initiative would require new legislation to establish the NAMA and define its remit, including:

- Provision of powers to price and effect transfers of relevant assets
- Definition of assets eligible for transfer

- Obligation on the banks to co-operate in relevant aspects
- Provision for an Assessor to ensure the constitutionality of the transfers

The NAMA legislation should also provide for mandatory transfer of eligible assets from the banks because a voluntary approach would be slow, prone to breakdown, and would raise difficulties in terms of the pricing of assets. A failure to provide absolute clarity to markets in relation to the timing and terms of the asset transfer could prove fatal to the initiative, and mandatory transfer is therefore recommended.

In relation to valuation of assets, a first valuation would be done by the NAMA prior to transfer, following expedited due diligence. An assessor structure would subsequently follow at a suitable time to ensure that the amount paid was fair.

Income producing assets would have the prospect of being written down to a level where the income (in aggregate and with some headroom) would pay interest and yield a profit. Non-income producing assets could be transferred on the basis of current market value of the underlying security, a 'normalised' value of the security, or an across-the-board discount of the assets of x cents in the Euro. In the later case, the transferring institution could have equity (or other exposure) to the NAMA proportionate to the "value" of the assets transferred.

One way to overcome the difficulties of pricing assets would be for the transferring banks, to provide warrants for the purchase of shares in the bank which can be exercised by the Government in several years time at a price, which depend inversely on the value of the impaired debt at that future date. The future date would need to be set far enough into the future for the market in these kinds of assets to have settled down and their price less imponderable.

The NAMA could be capitalised by:
- Credit-enhanced Bond without a Government Guarantee:
Under this approach the NAMA would issue a bond to the six covered institutions in an amount sufficient to cover the value of the transferred assets. The credit quality of the bond would depend on the equity in the balance sheet of the NAMA. The greater the equity, the lower the exposure of the bondholders to the impaired loans. The principal disadvantage is that the transfer of risk from the banks is only partial, to the extent of equity in the balance sheet of the NAMA. As to the provision of equity, it is unlikely that private equity would participate without the presence of State equity, on say a 50:50 basis. However, there are indications that private equity would be interested to participate in acquisitions of bank property portfolios. The advantage of this approach is that it limits the Exchequer's exposure to funding the transfer of the loans to NAMA, to the extent required to adequately supplement private equity participation.

- Credit bond with a Government Guarantee:
The advantage of this approach is that the bond would be eligible collateral for the purpose of Repo agreements at the Euopean Central Bank and this could be used by the banks to replenish liquidity. The disadvantage is that it would add €123.9Bn to the national debt.

The impact of such an increase in the national debt is difficult to predict. A lot of negative news has already been priced in the State's relative cost of borrowing, so it could not be concluded that funding cost would deteriorate in line with the increase in indebtedness. A key question would be whether the overall NAMA initiative was considered by capital markets to resolve the banks' capital adequacy requirements, and the associated attrition in Irish banks' deposit funding. Another key factor relates to the underlying public finance position and current efforts towards stabilising the deficit. Also, the fact that the proposed debt issuance would only be undertaken with the support of the ECB, would tend to mitigate adverse speculative reaction. There remains the risk however, that the market may focus solely on the headline news, pushing cost of borrowing wider, unless the strategic plan is explained comprehensively and clearly.

In relation to the type of Government bond that could be supplied, while the initial attraction could be to supply an instrument with low Exchequer cash outlays (non-interest bearing bullet bond with long maturity), this would adversely affect income streams and profitability in the banks, and market perceptions around the intentions and capabilities of the State to honour the bond. It is concluded that the most effective approach is to inject a type of bond which is more in line with the sort of asset which a bank would voluntarily hold on its balance sheet: short-term, and with interest rate floating in line with the market. Such an instrument can more easily be made marketable, thereby freeing the bank to move forward with an asset-side strategy that is not dependent on its particular failure history.

The cost of servicing a marketable bond of c. €120bn would be c.€2.1bn per annum. It is calculated - on the basis of €100bn of investment property assets being transferred to the AMC - that even allowing for a high level of impairment of these assets, the cash flows generated would be sufficient to ensure no net burden in terms of additional service costs.

Business Model of the NAMA:
In relation to the various categories of assets taken on, NAMA will be charged with their management in terms of disposal, holding, consolidating and creation of joint ventures for maximising return on the assets. In order to discharge the functions, NAMA will need to establish or source functional competence in: Legal; Project Finance; Project management; Planning and Design (external); Sales & Marketing (external).

Review of the Guarantee Scheme:
It is recommended that the Guarantee of bank liabilities be restructured to:
- extend the Guarantee to cover future longer term bond issuance;
- remove dated subordinated debt (Lower Tier 2), asset covered securities, and senior unsecured debt maturing beyond the 29 Sep 2010, from coverage of the guarantee, because the covered institutions get no benefit from the guarantee of these types of liabilities;
- change some of the commercial conduct provisions to enhance supervisory powers;
- make technical amendments to clarify certain issues raised by the market.

Appendix 2 – Strategic Options

This appendix assesses the high level options available to the Government to address the current threat to the stability of the Irish banking system.

Take no further action

Banks are currently managing the loans as impaired or distressed assets. Banks are not currently enforcing on these loans due to concerns as to the level of losses, the value of underlying collateral and the impact on their capital of any write downs. If they could continue to fund themselves, the banks could continue to adopt this approach until such time as the market improves at which stage the borrowers may be able to repay the loans or the banks might be in a position to enforce the loans and sell the relevant properties.

Pros	Cons
• Less immediate Exchequer exposure. • Forces banking system to address its own issues.	• Ultimately will threaten the financial position of the banks • Delays market adjustment and prolongs serious economic distortions • Will not assist lending to real economy • Potential to cause serious damage to the real economy • Will not address liquidity risk • Will not be acceptable to the market • Heightens risk of sovereign default

Establish an insurance scheme

The State could establish an insurance scheme whereby, for example, it provides insurance to each of the Banks against the majority of the losses they incur on the relevant loans above a certain "first loss" position (for example, 20 per cent.). The loans would remain on the books of the Bank who would continue to manage them over time. It is also likely that the banks would be required to share a proportion of the losses above that first loss amount (perhaps another 10 per cent. of all amounts covered by the insurance) to incentivise them to achieve the best recovery for the loans. The banks will pay a fee to the State for providing the insurance (in cash or securities of the bank) and any insurance payments could be settled by means of the State delivering government bonds to the banks which they could use as collateral to obtain cash in the market or from the ECB.

Pros	Cons
• No initial cash outlay and no immediate impact on GGD • Banks continue to fund themselves • Banks remain responsible for managing the loans • Some precedent, similar to the UK scheme • State could earn a fee (subject to complicated State Aid issues and banks ability to pay)	• Loans remain on Bank's books. No finality, and no clean break • Banks continue to manage loans in their own interests, not in the interests of the State • The insurance is a large contingency, and its unknown what the final cost will be. Uncertainty will weigh on the State's finances • No "floor" on property values and limited control for the State • Large degree of complexity considering competing objectives • Significant issues in pricing the insurance and allocating the losses • Significant time to establish

Asset Management Agency

An Asset Management Agency ("AMA"), often termed a "bad-bank", would be established, probably as a non-deposit-taking, unregulated statutory body. It would purchase from certain eligible banks the non-performing loans, issuing government bonds as the purchase price.

There would be cap on the amount available to the AMA to purchase the loans. Eligibility criteria for banks able to make use of the AMA would have to be drawn up, e.g. based on systemic importance, access to similar schemes in other countries, etc. Banks would be subject to a time-limit within which they would have to make use of the AMA.

The AMA would then operate under a mandate provided to it in legislation to manage the loans or, in appropriate circumstances, enforce the loans, crystallise the defaults and hold the property on behalf of the State over time. When appropriate it would sell the properties back into the property market.

Pros	Cons
• Significantly cleanses the good banks, is a "clean break" • State has complete control over process • Allows good banks increase lending to the real economy • The company would have market power enabling it to prevent fire sales • Precedent: This is very similar to the successful Swedish model and the US RTC model used to deal with the S&L crisis • No ongoing regulation or need to maintain minimum capital, as not a bank • Complimentary to recapitalisation of AIB and Bank of Ireland • No legacy issues in institution, as brand new • Helps to put some "floor" on asset values • Upside (if any) belongs to the State • State owning the land may have other benefits, building schools hospitals etc • Is the most transparent option • Offers better potential for stimulating bank liquidity raising	• Significant impact on GGD and State credit rating • Initial high cost, as asset purchases are funded on day-one (although no need for cash, as government securities can be provided) • Transfer of loans will crystallise losses with corresponding capital impact • Establishment of a new structure to run the portfolio • Identification of appropriate experts, not connected with existing problem assets and banks to run AMC • Market acceptance of increased level of Irish government bond issuance is required • Political implications and conflicts of interests in managing the portfolio • Eligibility for scheme may potentially be broader than for bank guarantee scheme, i.e. could have to extend to non-covered institutions • Will need some continuing access to cash to assist in loan workouts • May not generate sufficient investor interest to meet the resultant additional debt and other costs.

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Appendix 3

The tables below highlight the impact of the financial transaction proposed in the Bacon report on the balance sheets of the banks (6 covered institutions), the AMC and the Government. (All figures in billions)

Aggregated Bank Balance Sheet- Before			
Assets		Liabilities	
L&D Loans	€64	Deposits	€240
Property Inv Loans	€95	CP & CDs	€40
Other Loans(mortgages etc)	€281	Interbank	€43
Treasury Assets	€75	Long Term Funding	€125
Other Assets	€45	ECB	€52
		Subordinated Debt	€20
		Equity	€40
TOTAL	€560		€560

Aggregated Bank Balance Sheet - After			
Assets		Liabilities	
~~L&D Loans~~	~~€64~~	Deposits	€240
~~Property Inv Loans~~	~~€95~~	CP & CDs	€40
Other Loans	€281	Interbank	€43
Treasury Assets	€75	Long Term Funding	€125
Other Assets	€45	ECB	€52
Gov Bond	€120	Subordinated Debt	€20
		~~Equity~~	~~€40~~
TOTAL	€520		€520

Asset Management Company Balance Sheet			
Assets		Liabilities	
Bank Loans	€120	Gov Debt	€120

Government Balance Sheet			
Assets		Liabilities	
Loan to AMC	€120	Increased Gov Debt	€120

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Appendix 4
Proposed Asset Management Bridge Scheme [formerly "CLS"]

It is expected that current extreme liquidity pressures on the Irish banking system will persist and may even intensify following any announcement of an Asset Protection Scheme for the banking sector (i.e. Asset Management Company and / or risk insurance).

The Central Bank and Financial Services Authority of Ireland (CBFSAI) currently has ECB approval for an Emergency Liquidity Assistance (ELA) facility of €15bn. for Anglo Irish Bank.

While it is legally feasible for an institution to decide not to disclose that it is drawing ELA, the longer the institution remains on ELA the stronger the legal onus may be to disclose it particularly when the institution's shares are traded. In addition the information published in the CBFSAI's monthly balance sheet will identify (but not in an obvious way) that substantial ELA is being provided in the Irish market which is likely to lead to the information coming out in the market in any event or unhelpful speculation as to who is accessing ELA.

Very careful consideration therefore needs to be given to whether any other large systemic publicly traded institution in Ireland should be permitted to access ELA. It is considered that the 'bad name' that any institution which is known to be drawing ELA will acquire will accelerate the pace of liquidity outflows and make it very difficult for that institution ever to be in a position to fund itself in the market again.

Consequently, it is proposed that as a short term alternative an asset swap arrangement is put in place for the covered institutions by the NTMA which if necessary will allow them to acquire ECB liquidity in respect of their non-ECB eligible collateral. This will be achieved by swapping this collateral (a substantial proportion of which is high quality) for Irish Government short dated Treasury Bills specifically issued for this purpose (under powers available under section 6(11) of the Credit Institutions Financial Support Act, 2008 (CIFS)). The bonds can then be repo-ed with the ECB.

This approach mirrors mechanisms that have been put in place in some other EU Member States. In order for the system to work, the ECB must be prepared to accept these Treasury Bills. The CBFSAI has consulted with the ECB and it has been indicated that the bills will be accepted. The current assessment is that this funding model could yield up €[60] bn. to the banking system in Ireland. At current rates of outflow this amount amounts to approximately [10] weeks liquidity. It, therefore, provides very valuable additional time for efforts to stabilise the Irish banking system to work. It also allows ELA to be provided only to certain institutions, thereby distinguishing the systemically viable ones. It would, if fully implemented, however, result in approximately a doubling in ECB liquidity provided to the Irish banking system from €60bn. to €120bn. – at which time Ireland would account for in excess of [15%] of total ECB liquidity. It should be noted that this level of ECB exposure to Ireland would be expected to generate very significant political pressures. It is also important to note that this Scheme could result in an increase in the Government's borrowing to € [135bn].

It is proposed in order to seek to accentuate the impact on market perceptions of an announcement of the establishment of an Asset Management Agency in Ireland to encourage positive liquidity inflows, that this asset swap arrangement would be termed the Asset Management Bridge Scheme to stress the extent that it is complementary and temporary for the purpose of underpinning the establishment of the Asset Management Agency.

Appendix 5: Guarantee Scheme Review

A review of the Guarantee is currently underway, as required by the European Commission and the terms of the Guarantee Scheme itself, with the purpose of establishing whether the Guarantee continues to assist in achieving the objectives of the Act of 2008 and whether there remains a continued justification for the provision of financial support under the Guarantee Scheme.

In summary, whilst the Guarantee had a successful short-term impact, the following long-term deficiencies have been identified which require the Guarantee to be restructured if its existence is to remain both effective and justified:

- There are market concerns regarding the credibility of the Guarantee given the scale of the guaranteed liabilities of €440bn.
- The Guarantee focuses solely on liquidity and does not address the issue of deteriorating asset quality and the consequent potential for significant write-downs and capital reductions as debts arise in the covered institutions.
- The liquidity position of the Irish banking system remains under extreme stress with the Guarantee not proving effective in preventing these outflows.
- Key to the covered institutions' long term sustainability is their ability to maintain deposits and their ability to obtain long-term funding from the markets. In practice, the majority of the liabilities covered by the guarantee are short/medium term bonds which were already in issue when the Guarantee was introduced – in this regard the Guarantee does not assist the covered institutions to obtain new long-term funding.
- Credit institutions in other EU Member States, e.g. the UK and France, have been able to make use of guarantees relating to long-term funding. In contrast, the covered institutions have not been able to raise longer term funding with a maturity post-29 September 2010. In fact, they have not had very much success raising even short-term funding (less than €7bn) that matures within the period of the Guarantee. As a result, the covered institutions remain very heavily reliant on ECB funding.
- By virtue of being the first guarantee of its kind and the urgency of its introduction, the Guarantee is generally out-of-step with the guarantee models used in other EU Member States.

There no intention to withdraw the Guarantee at this stage. Indeed, such a move could have an extremely negative impact on both the State (in terms of reputation and creditworthiness) and the covered institutions. Instead, it is proposed that the Guarantee Scheme be restructured as follows:

- An extension of the Guarantee Scheme to cover longer-term bond issuance by the covered institutions. This would be in line with both international and EU trends where the average term of State cover for bond issues extends beyond 2010.
- Changes to some of the commercial conduct provisions contained in paragraphs 36 to 49 of the Guarantee Scheme, in order to enhance the Minister of Finance, Central Bank and Financial Regulator's supervisory powers in relation to the covered institutions for the duration of the Guarantee.
- Purely technical amendments to the Guarantee Scheme to clarify certain matters which have given rise to queries from the market and interested parties.

A case could also be made that in order to enhance its credibility the scope for reducing the contingent liability under the Guarantee should be examined. In this context, it is argued that the covered institutions do not derive any benefit from the Guarantee from the inclusion of:-

(a) dated subordinated debt (Lower Tier 2);
(b) asset covered securities; and
(c) senior unsecured debt that matures or extends beyond the expiry of the Guarantee on 29 September 201

The migration of some or all of these liabilities from the Guarantee would lead to a very substantial reduction in the State's contingent liability under the Guarantee. The significant strengthening of the risk position of the covered institutions that would result from their participation in an asset protection scheme may, therefore, provide an opportunity for consideration of the removal of certain liabilities from the Guarantee. It is of course essential that any plans in this area are subject to comprehensive exploration so as to ensure that the market response will be positive and that there will be no negative impact on the State's creditworthiness.

Any restructuring of the Guarantee will require both legislative and State aid approval. An extension of the 'blanket' guarantee currently in place to encompass longer-term bond issuance may be difficult to secure from the European Commission on account of the further divergence it would represent from the common EU framework for bank guarantees currently in place.

Appendix 6: State aid aspects to the Bacon report

Background

The European Commission published a Communication on the Treatment of Impaired Assets in the Community Banking Sector on 27 February, 2009. The Communication provides guidance on how the Commission will review asset-relief measures under the Community rules on State aid. The following issues arise in the context of the Bacon Report, and the proposal to transfer all property related assets of the six covered institutions to an AMC, in light of the Communication.

Eligible Assets

First, in relation to the type of assets that might be covered by an asset-relief measure, such as an asset insurance scheme or, as proposed in the Bacon Report, an asset purchase scheme, the Commission states in its Communication that assets that cannot presently be considered impaired should not be covered by an asset-relief programme (para. 35). The Commission also states that asset relief should not provide an open-ended insurance against future consequences of recession (para. 35) and that it would not consider assets eligible for asset relief measures where they have entered the balance sheet of the beneficiary bank after a specified cut-off date prior to the announcement of the relief measure, say, end 2008 (para. 36).

The Bacon proposal would include, as part of an asset purchase programme, assets such as Building and Development Land loans which clearly constitute impaired assets but also commercial loans which may not constitute impaired assets. Consequently, the State would have to justify the inclusion of such assets in any scheme. It would be necessary to show that the extent of the scheme is necessary and justified in the circumstances if the proposal is to work. The Commission suggests in its Communication that it may be possible for banks to be released of impaired assets if the assets represent a maximum of 10-20% of the overall assets of the bank covered by the relief measure but again this appears subject to the premise that the assets involved are impaired.

Cost to the State

A second issue that arises in the context of the Bacon proposal is the cost involved to the State. In this regard, the Commission refers in its Communication to the impact which any proposal might have on the budgetary position of Member States. The Bacon proposal would add €124bn. to the national debt at end 2009-a total of €199bn (111% of GDP). Against that, and the upfront cost in general, it may be that some of the assets involved would prove profitable in the future which would reduce the overall cost involved to the State. This has been the case in some of the "Bad Bank" schemes in the past, for example, in Sweden.

Eligible institutions

Third, as with previous proposals discussed with the Commission, the Commission is likely to raise an issue with respect to the fact that the scheme would only apply to the six covered institutions. This point has been made by Commission officials in initial discussions. The State would argue that the extent of the problem is focussed on these six banks and, therefore, that should also be the focus of the proposal. It might also be pointed out that some other banks may receive similar support through their parent in other Member States.

Valuation process etc.

In addition to these considerations the Commission will want to ensure that the process it outlines in its Communication on the review of asset-relief measures is followed. This would relate to matters such as the valuation of the assets, enrolment in the scheme, reviews of the scheme, likely restructuring plans for the banks involved, appropriate remuneration for the State and behavioural commitments on the part of the banks.

Distribution of largest debtors

Distribution of largest debtors

Table 2 provides a breakdown of all debtor connections by size of nominal debt exposure. It should be noted that many of the debtors are also indebted to financial institutions which are not part of the NAMA scheme.

Nominal Debt	Number of debtor connections	Average nominal debt per connection €m	Total nominal debt in this category €m
In excess of €2000m	3	2,758	8,275
Between €1000m and €2000m	9	1,549	13,945
Between €500m and €999m	17	674	11,454
Between €250m and €499m	34	347	11,796
Between €100m and €249m	82	152	12,496
Between €50m and €99m	99	68	6,752
Between €20m and €49m	226	32	7,180
Less than €20m	302	7	2,117
Total	772	96	74,015

Table 2: Distribution of NAMA debtor connections by size of nominal debt

OIFIG AN AIRE AIRGEADAIS

Ref No: **1 April 2009**

SECRET

Memo for Government

Proposal for a National Asset Management Agency

1. Decision Sought

The Minister for Finance asks the Government to approve an announcement on Budget Day that he intends to set up a National Asset Management Agency (NAMA) under the auspices of the National Treasury Management Agency.

The NAMA will purchase the land and development books of the covered institutions and certain property investment loans associated with the largest 20 or so borrowers from these institutions.

This purchase, which will be funded by the issue of Government Bonds, will be at a discount to take account of the need for write downs by the banks. The total book value of the assets purchased will be likely to be of the order of €80bn.

2. Background

Concerns over asset quality in Irish banks relate to property based lending, generally land and development lending. The issue of how best to address this problem has been addressed in the context of the scheduled six month review of the Credit Institutions (Financial Support) Scheme, 2008.

The Minister for Finance appointed Mr Peter Bacon to work in conjunction with the NTMA to report and advise him on the best solutions in this area. His report assesses various options including risk insurance but recommends that an Asset Management Agency be established to purchase a portfolio of loans from the banks focusing on the riskiest loans. After the review of the various options in consultation with the NTMA, the Governor of the Central Bank, Financial Regulator, and taking account of the Bacon report the Minister has decided that a National Asset Management Agency to manage and work out these risky loans represents the best option.

3. Advantages of National Asset Management Agency

The aim of establishing an Asset Management Agency is to provide the banks with a clean bill of health, to strengthen their balance sheets, to considerably reduce uncertainty over bad debts and as a consequence ensure the flow of credit on a commercial basis to individuals and businesses in the real economy.

An asset management agency would

- Deal with the issue of impaired property loans more decisively and definitively, providing the banks with cleaner balance sheets and reducing the risk of further impact of impairments from property loans on the banks
- Improve the funding position of the banks by providing them with assets that can be used to access ECB funding
- Remove management of the problem loans from the banks, which should provide greater control of the work-out of the loans and deal with market concerns that the banks are not realistic about the extent of likely losses
- The asset manager should have limited regulatory capital requirements in respect of losses on impaired loans
- Should improve sentiment towards the banks and allow management time to be refocused on rebuilding strength particularly in core retail businesses and maintaining their deposit bases.

4. Assets to be included

The Minister has considered three possible approaches

i. Land and Development loans only, which is the riskiest part of the banks loan portfolio – these are currently valued at c€60bn

ii. Land and development loans plus the banks 20 or so largest commercial exposures– this portfolio would amount to circa €80bn.

iii. All land and development and property development loans, currently valued at c€160bn.

Taking account of the advice of the NTMA, the Central Bank, the Financial Regulator, the Department of Finance and legal and financial advisors the Minister has decided in favour of option ii, the land and development loans plus the banks 20 or so largest exposures (exact number to be decided based on assessment of exposures). In reaching this conclusion the Minister has taken account of the impact on the banks, on financial markets and on the national debt.

It is proposed that the assets would be purchased through the issue of government bonds to the banks. The Agency would then manage the loan assets over time to ensure the minimum loss for the State. The assets being considered for transfer currently have book value assessed at:

	Total €bn
Net Exposure to largest borrowers	17
Land & Development Book	64
Total exposure to top borrowers and L&D books	**81**

The Government should note that **this is not a final figure.** The loan books will have to be worked out and reviewed with each of the Banks to ensure that the appropriate loans are taken and that the banks are cleared of their identified riskiest loans. In view of the administration costs associated with management of small loans and the large number of such loans where the banks have very significant other relationships with

the customers special arrangements will be put in place for such customers. A number of options are being considered, but all involve transferring the economic value of the loans to the State. The Minister will revert to Government with proposals for the management of such small loans.

5. Cost to the State

To ensure best value for money for the taxpayer the loans will be transferred to the NAMA at an appropriate written down value. All loans transferred will be classified as high risk, medium risk or low risk and the write down the bank will take on these loans will depend on how risky each category of asset is perceived (see appendix 1). Most of the land and development books will be categorised as high risk and will attract a higher rate of discount. The rates of discount are subject to EU state aid approval.

The annual interest charged to the State for bonds of this size is likely to be of the order of €1.2bn. The income accruing to the underlying asset book is also estimated to be of the order of €1.2bn. However, there will also be administrative costs for the agency and the bond interest and agency income may not match exactly leading to a net cost to the State over the initial running period of the agency (until assets are sold).

The main disadvantage of an Asset Management Agency is the upfront impact this will have on the national debt. The impact could raise the ratio of debt to GDP from 52% to approximately 85% (compared to an EU average of 60%). It is not clear whether this agency's assets will be on the States balance sheet and we are in discussions with the CSO to try and ensure that the scheme is designed to keep them off the balance sheet. In this context we note that similar UK Treasury Bills are off balance sheet.

6. The National Asset Management Agency

It is proposed to establish the National Asset Management Agency on a statutory basis, under the aegis of the National Treasury Management Agency. A central feature of the arrangement is that the banks will have to play their part in a practical and demonstrable manner – they will probably be charged with contributing to the agency by providing highly skilled staff. All income from the purchased loans will accrue to the NAMA as will proceeds from the eventual sale of the underlying assets. The Government will on the winding up of NAMA determine if it has made a profit or a loss in its lifetime. Any profits accrue to the State but any losses incurred by NAMA will be clawed back from the participating institutions by means of a levy over a number of years.

7. Participation

This initiative arises from the compulsory review of the Bank Guarantee Scheme. In keeping with the terms of the Scheme participation in the Asset Management Agency will be offered to all the covered institutions. Optional participation is proposed, but any bank that opts in would have to agree that all loans in particular portfolios have to be sold to NAMA at the discounted rate determined for that category of risk.

The legislation will also provide for a mandatory power to acquire assets so as to ensure against any recalcitrance on the part of institutions, or to overcome legal difficulties with the assignment of assets.

8. Bank Guarantee Extension

In addition to pursuing the NAMA option the Minister for Finance is also in discussions with the EU Commission on the possible extension of the Bank Guarantee beyond September 2010 for a more limited range of instruments.

Appendix 1

Agency Structure	Commercial Semi State entity, ideally structured to be off Balance Sheet [requires agreement of Eurostat]. Should be carried out under the governance, direction and management of the NTMA and be designated as, for example, the National Asset Management Agency (NAMA).
Institutions Covered	Those covered by the Government guarantee who are regarded by the Government as appropriate for inclusion having regard to the structure of their loan book, their access to support, their ownership structure and their relative importance to the national economy.
Assets Covered	All loans in respect of the purchase of land for development and associated work in progress arrangements. In addition, certain property investment loans, especially where associated with the largest 20 or so borrowers. Exact assets to be considered further.
Size of NAMA	Potentially €80bn to €90bn in assets
Timeframe	Budget day announcement with legislation enacted soon thereafter. Preparation of legislation and preparation of the management structures would be initiated in parallel.
Legislation	The NAMA initiative would require new legislation (the "NAMA Act") which would create NAMA under the umbrella of the NTMA.
Pricing	Portfolio pricing depending on the category of underlying security. Appropriate percentage discounts would be paid for Land & Development Loans and for property investment loans depending on the assessment of risks involved. The objective should be to break the link between banks and the property assets, at least at the outset. EU requirements may require a more disaggregated valuation of assets.
Participation	Optional participation proposed, but banks would have to agree that all loans in particular portfolios have to be sold to NAMA. The legislation should also provide for a mandatory power to acquire assets so as to ensure against any recalcitrance on the part of institutions, or to overcome legal difficulties with the assignment of assets.
Payment	Property loans sold to NAMA will be paid either in Government Bonds or in Government guaranteed bonds issued by NAMA.
Clawback	The government will on the winding up of NAMA determine if it has made a profit or a loss in its lifetime. Any profits accrue to the State but any losses incurred by NAMA will be clawed back from the participating institutions by means of a levy over a number of years.

Special Purpose Vehicles (SPV's)	In order to achieve the optimal return some property loans sold to NAMA will be capable of being transferred into NAMA SPV's which will be capable of being worked out and disposed of in an orderly manner with private equity partners.
NAMA	The Government will capitalise NAMA with sufficient equity so as to undertake its business in an optimal manner.

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

deposits with a maturity of post-September 2010[10]. While the guarantees have provided some relief to banks, they have not allowed them to restore their access to term market funding. The ELG Scheme has been prolonged to 31 December 2011 for all liabilities under the Scheme, subject to continuing EU Commission state aid approval at six-monthly intervals.

14. **The government also took action to strengthen banks' capital.** Given banks' difficulties to find a private solution to their capital needs, the government provided additional capital in cash or through promissory notes[11] to five domestic institutions, Irish Life and Permanent being the exception. A second measure the government took with a view to providing impaired assets relief to banks was the establishment of the National Asset Management Agency (NAMA, see Box 1). In total, some €46 billion (29% of GDP) has been injected in domestic banks over the period 2009-2010 (see Table 2). This amount does not include additional recapitalisations which will be identified under the EU/ECB/IMF Programme and injected over its course.

Table 2: Capital injections into Irish banks during the crisis (as of 28 January 2011)

Bank	Capital injections
Anglo Irish Bank ***(Nationalised in January 2009)***	**Total**: **€29.3bn** (18 1/3 % of GDP), including o €4 bn (June 2009) o €8.3 bn in form of a promissory note (March 2010), increased to 10.3 bn (May 2010). o €8.6 bn through a promissory note (notified June 2010, approved by the Commission on 10 August). o €6.4bn (of which €1.5bn already approved in August 2010) through a promissory note (December 2010),
Allied Irish Bank (AIB)	**Total: €7.2bn** (4½% of GDP), including o €3.5 bn (2¼% of GDP) in preference shares, via the National Pension Reserve Fund (NPRF) (February 2009) (*As part of the capital injection approved by the Commission in December 2010, all preference shares were converted into ordinary shares to increase the equity in the bank*) o €3.7bn cash investment by the NPRF in equity (December 2010)
Bank of Ireland (BoI)	**Total: €3.5 bn** (2¼% of GDP) in preference shares, via the NPRF (February 2009) of which €1.7 billion were converted into equity as part of BoI's capital raise in April 2010
Irish Nationwide Building Society	**Total: €5.4bn** (3½% of GDP), including o €0.1bn through special investment shares (March 2010) o €2.6bn in form of a promissory note (March 2010) o €2.7bn in form of a promissory note (December 2010)
EBS Building Society	**Total: €0.9bn** (½% of GDP) o €0.1bn through special investment shares (March 2010) o €0.25bn in form of a promissory note (June 2010) o €0.525bn in form of special investment shares (December 2010)
TOTAL	**€46.3bn (29% of GDP)**

Note: In addition, covered institutions benefit from the *bank guarantees* granted by the Irish authorities and have *transferred impaired property-related assets* to the bad bank "NAMA".
Source: Commission services

[10] The liabilities covered include: all deposits (to the extent not covered by deposit guarantee schemes in the State (other than the Credit Institutions Financial Support Scheme) or any other jurisdiction); senior unsecured certificates of deposit; senior unsecured commercial paper; other senior unsecured bonds and notes. In addition, a blanket guarantee will apply to all relevant deposits incurred or rolled-over by a participating institution from the time such participating institution avails of a guarantee under the ELG Scheme for the first time, regardless of type, nature or the identity of the depositor.

[11] Debt securities issued by the Irish State which qualify as core Tier 1 capital for the purpose of the calculation of Irish banks' regulatory capital adequacy ratio. The nominal amount of these securities is not disbursed immediately but over a 14 year period. The holder of these securities is also entitled to receive a coupon from the Irish State.

INBS Re-structuring options

1. Trade Sale amalgamation of the institution with another institution

This option involves the sale or transfer of INBS in whole or substantial part to another credit institution. This would involve the assumption of the Society's asset and liabilities on a going concern basis.

- ✓ May provide assurance to the depositors, bondholders and many other creditors of the Society about the future, particularly if the receiving credit institution is of sound standing.
- ✓ Eliminates the institution – allows Government to focus on remaining institutions and if it removes "INBS brand" may help in securing a satisfactory Commission decision, particularly if it arises from an open market transaction
- ✓ Help in the restructuring of the Irish banking sector
- ✓ Cleansed of its bad assets and following the imposition of losses/haircuts on equity and subordinated debt interests in the Society, it may have an interest from possible bidders
- ✓ May help retain the employment of some of the employees
- ✓ Accepting institution may accept the value of the Promissory Notes and NAMA bonds and thereby avoid significant immediate liquidity and capital financing requirements for the State
- ✓ May secure some small economic return from the State's capital investment

- ✗ No obvious candidate for the assumption of the Society as a whole (or in substantive part)
- ✗ May not eliminate the State's liability (contingent or real) for the Society's liabilities as any accepting institution may require ongoing guarantees (over and above the existing formal ELG and Deposit Protection Guarantee Schemes) or other supports
- ✗ May, therefore, have a potential further capital and or liquidity costs for the Society
- ✗ Even after NAMA there may be a concern about the poor quality of the residual loan book
- ✗ The greatest attraction for a suitor is likely to arise in particular parts of the Society eg deposit book rather than in the Society as a whole
- ✗ May not be acceptable to the Commission, particularly if it does not arise from an open market sales process of if it involves the provision of State support (eg guarantees) to the receiving institution
- ✗ Ongoing legacy, subordinated debt issues may deter another interested parties
- ✗ Legislation will be required for a speedy sale of the Society following its conversion to a company (more problematic if it is to be transferred as a building society)
- ✗ Likely to remove the building sector presence from the Irish financial services market

2. Break-up and sale of the institution

This option involves the breaking up of INBS and the sale of the various parts of the Society to other institutions.

- ✓ Eliminates the institution may (depending on the details) be satisfactory to the Commission
- ✓ Parts of the Society may prove to be more attractive to a number of institutions than would be the case if sold as a whole (or substantially as a unit) e.g. synergies when it comes to retail branch network, mortgage book etc
- ✓ In particular, its deposit book may have attractions for certain other institutions
- ✓ May help retain the employment of some of the employees and value compared to a liquidation process
- ✓ Institution accepting the deposit book and other funding liabilities may accept the Promissory Notes and NAMA bonds as a consideration for those liabilities (and thereby avoid significant immediate liquidity/financing requirements for the State)
- ✓ May secure some small economic return from the State's capital investment
- ✓ May help in restructuring the Irish banking sector

- ✗ May give rise to immediate funding requirements to finance the transfer of the deposit book or other liabilities (the Promissory Note or NAMA bonds may not be acceptable to an accepting institution)
- ✗ The State may be left with a substantial rump of the Society (both from the asset and liability side of the balance sheet)
- ✗ May not eliminate the State's liability (contingent or real) for the Society's liabilities as any accepting institution may require ongoing guarantees (over and above the existing formal ELG and Deposit Protection Guarantee Schemes) or other supports
- ✗ May, therefore, have a potential further capital and or liquidity costs for the Society
- ✗ Even after NAMA there may be a concern about the poor quality of the residual loan book that may make this difficult to sell at a reasonable price
- ✗ May not be acceptable to the Commission, particularly if it does not arise from an open market sales process or if it involves State support for the receiving institution
- ✗ Ongoing legacy, subordinated debt issues may deter another interested parties
- ✗ Legislation will be required for a speedy sale of the Society following its conversion to a company (more problematic if it is to be transferred in various parts if it is done so as a building society)
- ✗ Likely to remove the building sector presence from the Irish financial services market
- ✗ Will likely result in the loss of the majority of jobs in the Society

3. Gradual wind down of the Society

Post NAMA, the Society will be too small to small to remain a viable independent organisation. If it is not possible to sell/transfer the Society in whole or in part, a wind down of the Society over time may have to be considered. This will involve the State in the work out of both the remaining non-NAMA assets and liabilities of the Society.

- ✓ Such an approach is likely to secure the maximum value from the remaining assets of the Society (particularly vis a vis a liquidation option)
- ✓ It will remove the institution for the sector over the medium term
- ✓ It will limit to a small extent the future capital needs of the domestic banking sector
- ✓ Avoids the need for a stronger institution to take on the INBS with consequent "contamination" risk
- ✓ Avoids immediate payment of Promissory Note which would arise on the liquidation of the Society

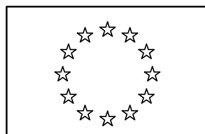
- ✗ May lead to further deposit erosion which the public system will have to fund
- ✗ Increase the risk that deposits will move from the domestic banking sector
- ✗ Ongoing running costs of the Society will have to be financed
- ✗ May not be to the satisfaction of the Commission as the Society will continue in being (may be addressed by a ban on new lending and a prohibition on paying premium deposit rates
- ✗ No attraction for obtaining new wholesale debt or deposits
- ✗ Will involve the State in funding the wind up of the Society and the work out of the remaining non-NAMA assets - this is likely to be a very protracted exercise
- ✗ Taxpayer will continue to have to meet liabilities as they arise on a going concern basis including liabilities that are not formally covered by a State guarantee - this will offset any gain on the asset side arising from a gradual wind down process (assumes subordinated debt bond holders will be addressed separately)
- ✗ Duplication of work will arise in the work out of the non-NAMA loan book unless there is some line with the Anglo asset recovery vehicle

4. Immediate liquidation of the Society

This process involves a petition to the High Court to secure a winding up of the Society. A liquidator would be appointed to realise the value of the Society's assets and to distribute those assets to meet the liabilities of the Society having regard to the order of preference.

- ✓ Likely to be acceptable to the Commission as it will immediately remove the very distressed Society from the banking sector
- ✓ Brings an end to the distressed institution and removes it from the banking landscape
- ✓ Terminates ongoing running costs of the Society
- ✓ It will limit to a small extent the future capital needs of the domestic banking sector
- ✓ Will cap the State's liability for the institution at the full extent of the guaranteed liabilities; therefore, unless a policy decision is made to the contrary, the (relatively small amount) of unguaranteed subordinated debt, senior debt and deposits will not fall on the State for payment following the liquidation and distribution of the assets

- ✗ Due to the guarantee and other State supports, likely to be a costly option for the State and will realise those costs in the near term
- ✗ The Promissory Note (currently €2.6bn with a proposed increase to €5.3bn) will fall for immediate payment from The Exchequer on wind up of the Society
- ✗ The marketable assets of the Society - eg its remaining non NAMA loanbook – will be put on the market at a time of depressed prices and accordingly are likely to secure a lower price that would be achieved over the medium term (ie will only achieve firesale prices)
- ✗ It is likely that further payments will also be required from the State as the realisation of the assets of the Society is unlikely to be at a level that will fully meet all of the State guaranteed liabilities of the Society
- ✗ May give rise to the payment of NAMA bonds



EUROPEAN COMMISSION

Brussels, 21.12.2010
C(2010) 9475 final

Subject: State aid N 553/2010 – Ireland
Second emergency recapitalisation in favour of Allied Irish Banks plc

Sir,

The Commission wishes to inform the Irish authorities that, having examined the information supplied by your authorities, it has decided to approve the measure referred to above for Allied Irish Banks plc ("AIB" or "the Bank").

1 PROCEDURE

(1) On 12 May 2009, the Commission approved a EUR 3.5 billion capital injection into the Bank in the form of Core Tier 1 New Preference Shares[1].

(2) Following this capital injection, the Bank submitted an initial restructuring plan on 13 November 2009 followed by a number of exchanges.

(3) On 30 March 2010, the results of the Prudential Capital Assessment Review (PCAR) were announced by the Irish financial regulator. These results highlighted the need for AIB to increase its capital, which led to changes to the restructuring plan.

(4) On 4 May 2010, AIB submitted a revised restructuring plan, which again was followed by a number of exchanges between the Commission and the Irish authorities.

(5) On 30 September 2010, the Irish Minister of Finance made a public statement on the situation of the Irish banking sector and announced that AIB needed additional capital of EUR 7.9 billion (taking into account the capital generated by the sale of its Polish subsidiary). The Minister also confirmed that in the current stressed market conditions, the Bank was unlikely to be able to conduct a traditional privately underwritten

1 Commission Decision in Case N 241/2009, *Capital injection into Allied Irish Bank,* OJ C 223, 16.09.2009, p. 2

Mr Micheál MARTIN,
Minister for Foreign Affairs,
Department of Foreign Affairs
80, St. Stephen's Green,
Dublin 2,
Ireland

transaction as was originally contemplated in July 2010, announcing at the same time that in these circumstances the Irish State would underwrite the capital raise, thus effectively committing to provide a further State-funded recapitalization of the Bank.

(6) On 28 November 2010, the Irish Government announced that a Programme for Support (the “Programme for Support”) has been agreed with the Commission and the International Monetary Fund (“IMF”), in liaison with the European Central Bank (“ECB”). As part of the Programme for Support, the Government has agreed to undertake certain bank recapitalisation and reorganisation measures under a Programme for the Recovery of the Banking System (the “Banking System Programme”). As part of the Banking System Programme, and building on the results of the Central Bank of Ireland’s (the “Central Bank”) PCAR carried out earlier in the year, the Central Bank has set new minimum and target capital requirements for AIB and other credit institutions in Ireland. The Central Bank publicly announced the new minimum and target capital requirements for Irish banks on 28 November 2010.

(7) On 2 December 2010, the Irish authorities notified to the Commission a second emergency recapitalisation in favour of AIB, for an additional net recapitalisation of up to EUR 9.8 billion, to be granted in 2 phases. In addition, all (minus one) the EUR 3.5 billion of Preference Shares will be converted into ordinary shares, as explained in paragraph (40).

2 DESCRIPTION OF THE MEASURE

2.1 The beneficiary

(8) A detailed description of AIB is provided in Section 2.1 of the Commission decision concerning the first recapitalisation of the Bank of 12 May 2009[2]. A short summary is provided below.

(9) AIB is with The Governor and Company of the Bank of Ireland (“Bank of Ireland") one of the two largest banks in Ireland. It is a diversified financial services group which offers a full range of personal and corporate banking services with an emphasis on the Irish retail banking market (in terms of market share in Ireland, the Bank has approximately: [30-40][*]% of personal current accounts, [10-20]% of mortgages, [30-40]% of savings and [40-50]% of SME current accounts). As of 8 December 2010, AIB remains a listed company and its shares are quoted on the Dublin, London and New York stock exchanges.

(10) Its main areas of operation outside Ireland are the UK, the US and Eastern Europe (Poland in particular), however the Bank has recently embarked on a far reaching divestment programme of its foreign operations.

(11) According to its annual report for the year ended 31 December 2009, AIB had total assets of EUR 174 billion and total deposits of approximately EUR 147.9 billion, which consisted of customer deposits (EUR 83.9 billion), deposits by banks (EUR 33.333 billion) and debt securities in issue (EUR 30.6 billion). As of the same date, AIB’s total loan book was approximately EUR 131.5 billion. The loan to deposit ratio was 146% (123% excluding loans held for sale to NAMA). The level of deposits has

[2] Commission Decision in Case N 241/2009, *Capital injection into Allied Irish Bank,*

[*] Confidential information

however been steadily decreasing from September 2010 and the amount of customer deposits is currently at EUR […] billion (as of 2 December 2010).

(12) AIB's current credit ratings are […] by Moody's, S&P and Fitch respectively (downgraded by S&P on 8 October 2010 and put on Credit Watch Negative by Moody's on 6 October 2010). The level of AIB's 5 year Senior CDS spread is approximately 1050 bps as of 8 December 2010. This compares to around 800 bps for Bank of Ireland and to approximately 150 bps for the 5 year senior financials ITRAXX index on the same day (vs. 244 bps 6 months ago on 10 May 2010). AIB's share price is EUR 0.51 at 8 December 2010 (vs. EUR 1.23 6 months ago on 18 May 2010).

(13) As of 12 November 2010, AIB had participated to the following sector wide State support measures:

(i) The Credit Institutions Financial support Scheme (CIFS) from 24 October 2008 to 29 September 2010[3];

(ii) The Eligible Liabilities Guarantee Scheme (ELG) from 21st January 2010. Amount of liabilities covered at 30 September 2010 is EUR […] billion[4];

(iii) An asset relief measure consisting of the transfer of commercial property and development loans to the National Asset Management Agency ("NAMA") from 12 February 2010[5]. As part of the first tranche of assets transferred to NAMA, AIB transferred bank assets with an aggregate loan balance of EUR 3.288 billion at an average discount of 42% (i.e. for a purchase price of EUR 1.905 billion). The second tranche of bank assets to NAMA contained assets with an aggregate loan balance of EUR 2.674 billion at an average discount of 48.5% (i.e. for a purchase price of EUR 1.403 billion). It is currently expected that the remaining AIB bank assets (EUR 13.5 billion) will begin to transfer to NAMA in November 2010 for completion by the end of the year at an average discount of 60%[6].

(14) In addition to the above, on 11 February 2009, the Government announced the decision to inject EUR 3.5 billion into AIB in the form of preference shares (the 2009 Preference Shares). The 2009 Preference Shares are Core Tier 1 non-cumulative perpetual preference shares in the Bank with a fixed annual dividend of 8% (or the right to shares in lieu) and with detachable warrants to acquire further ordinary shares in AIB (the "Warrants"). The 2009 State Investment was approved by the Commission under EU State aid rules on 12 May 2009[7].

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[3] See Commission Decision in Case NN48/2008, Guarantee Scheme for Banks in Ireland, OJ C 312, 06.12.2008, p. 2.

[4] See Commission Decision in Case N349/2009, Credit Institutions Eligible Liability Guarantee Scheme, OJ C 72, 20.3.2010, p. 6, subsequently prolonged until 30.6.2010 through the Commission's Decision in Case N198/2010, Prolongation of the Eligible Liabilities Guarantee Scheme, OJ C 191, 15.7.2010, p. 1 and again extended until 31.12.2010 through the Commission Decision in Case N254/2010, Second Prolongation of the Eligible Liabilities Guarantee Scheme, OJ C 238, 03.09.2010, p. 2.

[5] Commission Decision in Case N 725/2009, *Irish asset relief – NAMA*, OJ C 94, 14.4.2010, p. 10.

[6] Under the terms of the support programme announced on 28 November 2010, loans with a nominal value of between EUR 0 to 20 million will also be transferred, corresponding to an additional loan nominal value of EUR […] billion. .

[7] See Commission Decision in Case N241/2009, *Capital injection into Allied Irish Bank*, OJ C 223, 16.09.2009, p. 2.

(15) Following the Commission decision of May 2009, the Irish authorities submitted a restructuring plan for AIB on 13 November 2009. Central to this plan was AIB's intention to sell some its foreign subsidiaries. After a number of iterations and following the results of the PCAR exercise, AIB ultimately decided to engage in a more far-reaching divestment programme and to divest all its main foreign subsidiaries (Polish, UK and US). A revised restructuring plan was submitted on 4 May 2010.

(16) In the second half of 2010, AIB started the divestment programme. The sale of the Polish business to Santander was announced on 10 September 2010 for a total consideration of EUR 3.1 billion. The transaction will generate EUR 2.5 billion of equivalent equity tier 1 capital which is in line with July 2010 expectations (see Table 1). The divestment of the US business (M&T shares) was also completed on 4 November 2010, with a positive capital impact of EUR 900 million, slightly in excess of expectations. However, the sale of the UK business is proving more challenging. In November 2010, AIB announced its decision to halt the current sales process of AIB UK and to undertake instead a strategic review of its UK business. The above impacts of the Polish and the US divestments have been taken into account in the amount of recapitalisation necessary for AIB by the Irish financial regulator.

Table 1: Equity Tier 1 impact disposals AIB

Disposals	Equity Tier 1 Impact in EUR billion
BZWBK (Polish business)	+ 2.500
M&T (US business)	+ 0.900
Total capital impact from disposals	+ 3.400

2.2 The events triggering the measure

(17) AIB, like the main other Irish banks, was very exposed to its home market and in particular to the property market. From 2002 to 2008, AIB's exposure to the property market grew rapidly fuelled by the Bank's easy access to wholesale funding. This left the Bank in a very vulnerable position when the global financial crisis hit and the Irish real estate bubble burst.

(18) The subsequent material deterioration in the financial position of AIB led it to participate in all the sector-wide support measures put in place by the Irish State in order to safeguard the stability of the financial system in the State. […]

<u>The Central Bank's PCAR exercise</u>

(19) On 30 March 2010, the Irish Financial Regulator announced that it (together with the Central Bank) had carried out an exercise to determine the forward-looking prudential capital requirements of certain Irish credit institutions, covered by the CIFS Scheme and the ELG Scheme which included AIB ("the PCAR exercise"). The PCAR exercise was undertaken to determine the recapitalisation requirements (if any) of the participating credit institutions if they were to meet regulatory capital needs in both an expected (base case) and a stressed case scenario for the period 2010 to 2012.

(20) The PCAR was undertaken to determine the recapitalisation requirements of certain Irish credit institutions with reference to both a base case and a stressed case scenarios:

(i) Base case scenario: A target level of 8% Core Tier 1 Capital after taking account of the realisation of future expected losses and other financial developments under a base case scenario. As a further prudential requirement, the capital used to meet

the base case target must be principally in the form of equity, the highest quality form of capital, with 7% equity as the target level.

(ii) Stressed case scenario: A target level of 4% Core Tier 1 Capital that should be maintained to meet a stress scenario for loan losses and other financial developments.

(21) The Financial Regulator required the credit institutions that had completed the exercise, including AIB, to prepare recapitalisation plans to comply with the additional capital specified by the PCAR. The Financial Regulator required that the amount of capital set by the PCAR process was to be in place by the end of 2010[8].

(22) Under the PCAR, the Financial Regulator determined AIB's additional capital requirements as:

(i) An additional EUR 7.396 billion of equity capital to meet the base case target of 7% equity, before taking account of projected asset disposals, and

(ii) EUR 4.865 billion of Core Tier 1 capital, less any equity generated under paragraph (i) above, excluding conversion of preference shares held by the Government, to meet the base case target of 8% Core Tier 1. This additional Core Tier 1 capital also satisfied AIB's stress case target of 4% Core Tier 1.

The increase in the haircut for the transfer of loans to NAMA

(23) The capital increases resulting from the PCAR exercise announced on 30 March 2010 were based on (i) the Central Bank's own assumptions regarding expected losses for non NAMA loans (including a buffer) and on (ii) the haircuts applied for the transfer of the first tranche of assets for NAMA assets, which was 42%. However, it later appeared that the required haircut for the transfer of the third tranche of NAMA was in fact greater than for the first tranche, namely 60% (and as such greater than the assumption used in the PCAR exercise). At the request of the Minister, NAMA has now provided an estimate of the NAMA haircuts on all remaining tranches.

(24) Following the higher haircut for the second tranche of NAMA, the Central Bank advised AIB that it will be required to raise an additional EUR 3 billion by 31 December 2010, on top of the EUR 7.4 billion additional equity and EUR 4.9 billion additional Core Tier 1 already announced under PCAR requirements.

The Minister's 30 September 2010 announcement

(25) The additional capital requirement for AIB following the higher NAMA haircut was announced by the Irish Minister for Finance on 30 September 2010. According to the announcement, AIB's new total capital requirement amounted to EUR 7.9 billion after deducting the capital generated by the sale of its Polish subsidiary[9]. As for core tier 1

[8] However the Financial Regulator has taken a more flexible approach with regard to the capital increase resulting from the sale of the Polish subsidiary BZWBK. The net proceeds will only impact the balance sheet of AIB when the sale process is completed (early 2011).

[9] Subsequently reduced to EUR 7.0 billion following the sale of the US business.

capital (also taking into account the sale of the Polish and US businesses) this meant a new core tier one requirement of EUR 4.5 billion.

(26) In his statement, the Minister announced that the new Core Tier 1 capital requirement would be met through an open offer and placement of shares to existing and new shareholders of AIB for an amount of EUR 5.4 billion that the Government would ultimately fully underwrite. It has since been decided that such open offer and placement operation will not proceed at this time given the current stressed market circumstances and the Programme for Support, and that the State will inject the capital needed in full following the adoption of a Special Resolution Regime for banks.

Announcement of the Programme for Support

(27) On 28 November 2010, the Irish Government announced that a EUR 85 billion Programme for Support had been agreed with the Commission and the IMF, in liaison with the ECB. The Irish State will contribute EUR 17.5 billion to the facility, which will come from the National Pensions Reserve Fund[10] ("NPRFC") and other domestic cash resources. This reduces the extent of external assistance under the facility to EUR 67.5 billion. The external support will be broken down as follows: EUR 22.5 billion from the European Financial Stability Mechanism ("EFSM"); EUR 22.5 billion from the European Financial Stability Fund ("EFSF") and bilateral loans from the UK, Sweden and Denmark; and EUR 22.5 billion from the IMF's Extended Fund Facility ("EFF").

(28) The Programme for Support has two parts. The first part deals with bank restructuring and reorganisation under a Banking System Programme (EUR 35 billion) and the second part deals with fiscal policy and structural reform (EUR 50 billion). The Banking System Programme provides for a recapitalisation, fundamental downsizing, restructuring and reorganisation of the banking sector.

(29) The recapitalisation needs resulting from the Programme for Support will build on the results of the 30 March 2010 PCAR, and will factor in a new minimum capital requirement target of 10.50% core tier 1 for AIB, Bank of Ireland, Irish Life and Permanent ("ILP") and Educational Building Society ("EBS"). Further, the Central Bank is requiring AIB, Bank of Ireland and EBS to raise sufficient capital to achieve a capital ratio of at least 12% Core Tier 1 by 28 February 2011 (May 2011 for ILP). The Central Bank requires this additional capital to be in the form of equity. The target of 10.5% minimum Core Tier 1 capital will become the ongoing minimum capital requirement for AIB, Bank of Ireland, EBS and ILP going forward.

(30) This increase in the target requirement from 7% equity/8% core tier 1 to 12% core tier 1 will generate an additional core Tier 1 capital need of EUR […] billion for AIB.

(31) Immediate further deleveraging of the banks will be achieved by the extension of the NAMA programme to include approximately EUR […] billion of land and development loans in AIB, which had previously been excluded as they were below a value threshold of EUR 20 million. It is expected that all loans will be transferred by end-March 2011. The additional capital requirement will be met by the Programme for Support. This measure will be notified to the European Commission in accordance

[10] The NPRFC is a statutory body whose sole purpose is to manage the assets of the National Pension Reserve Fund on behalf of the Irish finance Minister. The NPRF is a fund established in 2001 with the objective of meeting as much as possible of the costs of social and public service pensions from 2025. The assets of NPRFC are owned y the Minister. The NPFRC already holds the 2009 Preference Shares.

with EU State aid rules (in particular with regard to the assessment of the discounts to be applied to loans).

(32) The transfer of these smaller loans to NAMA will lead to an estimated additional Core Tier 1 capital need of EUR […] billion for AIB.

(33) As a result of the new target capital ratio under the base case of 12% and of the further transfer of assets to NAMA, the Central Bank estimates that AIB requires additional Core Tier 1 capital of approximately EUR 5.3 billion[11]. The core tier 1 capital requirement announced in September 2010 (and still to be met) was EUR 4.5 billion. This means that AIB is required to raise approximately EUR 9.8 billion of additional Core Tier 1 capital by end-February 2011.

Announcement on Special Resolution Regime and Recapitalisation Measures

(34) In the week 13-19 December 2010, the Irish [Government] announced the passing of the Credit Institutions (Stabilisation) Bill 2010. This Bill puts in place a special resolution regime aimed at providing the State with the proper powers and legislative tools necessary to complete the recapitalisation and restructuring measures spelled out in the Banking System Programme.

2.3 The measure

(35) The notified measure concerns: (i) the recapitalisation of AIB; and (ii) the conversion of preference shares into ordinary shares.

(36) The State will recapitalise AIB up to EUR 10.2 billion to first reach the capital requirements of the Irish financial regulator following from the PCAR as updated on 30 September 2010 and secondly the Core Tier 1 capital levels agreed upon in the Banking Support Programme ("the Recapitalisation Measures").

(37) The Recapitalisation Measures will take place in two phases:

(i) The Capital Contribution: a capital contribution by the Irish State of EUR 3.9[12] billion into AIB for new ordinary shares and common non voting shares ("CNV Shares") to be completed prior to end December 2010;

(ii) The Further Capital Contribution: a capital contribution by the Irish State of up to EUR 6.3 billion[13] into AIB for new ordinary shares and / or CNV Shares prior to end of February 2011.

(38) The net capital injection by the Irish State will be EUR 9.8 billion. EUR […] of fees will be paid by AIB to the State in relation to the Capital Contribution, the Further Capital Contribution, and the conversion of preference shares.

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11 EUR […].

12 This amount covers the fees payable by AIB to the State in relation to the Capital Contribution, the conversion of Preference Shares and the cancellation of the warrants. The Capital Contribution will provide net proceeds to AIB of EUR 3.7 billion.

13 This amount covers the fees payable by AIB to the State in relation to the Further Capital Contribution. The Further Contribution will provide net proceeds to AIB of EUR 6.1 billion. AIB may generate additional core tier 1 capital through a liability management exercised and/or asset disposals prior to end of February 2011. The amount of Further Capital Contribution will be reduced accordingly.

(39) Both the Capital Contribution and the Further Capital Contribution will be in the form of a direct purchase by the State without offering an opportunity to participate in the capital injection to existing shareholders, as foreseen under the special resolution regime created by the Credit Institutions (Stabilisation) Bill. The Capital Contribution will be funded through existing cash reserves of the NPRFC. The Further Capital Contribution will be funded through the Programme for Support. The shares issued through both exercises will be held by the NPFRC on behalf of the Minister for Finance.

(40) The NPFRC also holds the existing EUR 3.5 billion of 2009 Preference Shares. To simplify the capital structure of AIB, and because investors have a lower perception of preference shares than ordinary shares when providing funding to banks, it is intended that the State will convert all the Preference Shares into ordinary shares […]. This conversion will have no impact on the core tier 1 ratio of the bank as the Preference Shares are already regarded as core tier 1 by the Financial Regulator. The NPFRC will keep one Preference Share to maintain certain specific rights attached to Preference Shares[14].

(41) The Capital Contribution and the conversion of Preference Shares will be done at a price set as the lower of (i) the closing price of AIB's ordinary stocks on 26 November 2010 (EUR 0.342 per share) which was the last trading day prior to the Central Bank of Ireland announcement on 28 November 2010; or (ii) the closing price of AIB's ordinary stocks on the last trading day prior to the Government's announcement of the AIB recapitalisation measures, which is anticipated to be made following the enactment of the legislation enabling the State to recapitalise the bank without market placement.

(42) The Further Capital Contribution will be done at a price that will be set at a later stage because the terms of the transaction are not exactly yet known. The price of AIB shares may further decline, and the size of the transaction may be affected by the success of potential liability management exercises. However the Irish authorities have committed that the Further Capital Contribution will be done at a price that will not exceed the price of the Capital Contribution.

(43) On this basis, NPFRC will hold on behalf of the Minister 95-[…] % of the entire issued ordinary share capital of AIB.

(44) Because of a technical regulatory issue arising from the change of control of AIB before the sale of the Polish subsidiary BZWBK to Santander is closed, the State intends to initially limit its voting rights and ordinary shareholding of AIB to a level below 50% for a period of time up to completion of the sale of BZW to Santander. This will be achieved by the NPFRC subscribing initially to ordinary shares for up to 49.9% of the bank ordinary shareholding and for the remainder of the recapitalisation in CNV Shares.

(45) The State will convert all the CNV shares into ordinary shares as soon as the sale of BZWBK has been completed if AIB is delisted. If AIB retains its existing listing, the State will convert a number of CNV shares so as its ordinary shareholding will remain below 75%.[15]

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[14] The specific rights attached to the preference shares are: (i) 25% of total ordinary share voting rights in respect of resolutions concerning change of control and board appointments; and (ii) the right to directly appoint up to 25% of the board of directors of AIB.

[15] […] If not, the Irish Listing Rules and the UK Listing Rules generally state that a listed company must maintain a minimum free float of 25% at all times.

(46) The CNV Shares are expected to be issued directly to and subscribed by the NPRFC at the same price as the ordinary shares. It is anticipated that the CNV Shares will have substantially the same features as ordinary shares except for the fact that they will not carry voting rights (in particular they will count as core tier 1 capital). They will be convertible into ordinary shares on a one for one basis at any time at the NPFRC's sole discretion.

(47) For the Capital Contribution, the NPRFC will receive a […]% fee on the gross proceeds of the transaction up to 49.9% NPFRC ownership and a […]% fee on the gross proceeds in excess of this amount (rounded upwards to the nearest EUR 100 million). For the Further Capital Contribution, the NPFRC will receive a […]% fee on the gross proceeds if CNV shares are issued, and […]% if only ordinary shares are issued. The total amount of fees to be received by the State is expected to be EUR […] million.

(48) The State's existing warrants (which were issued to the State in May 2009 with the issuance of the Preference Shares), will be repurchased by AIB for a fee of approximately EUR 50 million[16].

(49) […] [17]

(50) AIB will be subject to behavioural conditions under the terms and conditions of the Recapitalisation Measures in addition to those already included in the ELG Scheme and the 2009 State Investment. In particular AIB will need to implement measures to promote availability of credit, will not pay dividends unless agreed by the Irish authorities, will review its corporate governance along lines set by the Irish authorities, and will review its remuneration policy along lines set by the Irish authorities.

3 POSTION OF THE IRISH AUTHORITIES

(51) The Irish authorities accept that the measure constitutes State aid. They are of the view that the measure is compatible with the internal market on the basis of Article 107(3)(b) of the Treaty on the Functioning of the European Union (hereinafter "TFEU") as it is necessary to remedy a serious disturbance in the Irish economy. In particular the Irish authorities submit that the measure is (i) appropriate and well targeted; (ii) necessary and limited to the minimum amount necessary; and (iii) proportionate as designed to minimize negative spill-over effects on competitors.

(52) *Appropriate and well-targeted.* The Irish authorities submit that AIB is systemically important for the maintenance of stability of the financial system in Ireland. AIB is one of the largest financial institutions in the State with 182 main branches, 88 sub-offices, 15 business centres and approximately 7,284 staff. It has a balance sheet size of around EUR 174 billion and accounts for a material share of customer deposits and lending in the Irish economy. Further, the Central Bank recognises the systemic importance of AIB for the Irish financial system in a letter dated 3 December 2010.

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[16] On purchase of the 2009 Preference Shares, the State received detachable warrants for the equivalent of constituting 25% of the ordinary share capital of the Bank existing on the exercise date of the Warrants calculated on a post-dilution basis. The State may exercise this option from the fifth to the tenth anniversary of the purchase of the New Preference Shares. The warrants are divided into two equal tranches with different strike price. The strike price of the "Core Tranche" of the Warrants is EUR 0.975. The strike price of the balance of the Warrants granted to the State is EUR 0.375.

[17] […]

(53) The Irish Authorities also stress that the purpose of the Recapitalisation Measures is to ensure compliance by AIB with the new capital requirements announced by the Central Bank as part of the Banking System Programme. As such they view the injection of equity capital as a well targeted and appropriate measure to achieve this objective.

(54) *Necessary and limited to the minimum amount*. The Irish authorities submit that the measure is limited in size to what is necessary to ensure the compliance by AIB with the new target capital ratio announced by the Central Bank on 28 November 2010. In addition, they point out that AIB will attempt to raise additional core tier 1 equity prior to the completion of the Further Capital Contribution through a liability management exercise and/or assets disposals. Any amount of core tier 1 raised in such a way will reduce the amount of the Further Capital Contribution.

(55) The Irish Authorities also submit that the purchase price and the conversion price for the Capital Contribution (closing stock price on the last trading day prior to the announcement) will ensure an appropriate level of dilution of existing shareholders. They further recall that the State will receive a fee of between […]% of the gross proceeds as well as a cancellation payment for the warrants. They conclude that the Recapitalisation Measures for AIB are limited in scope and duration to what is strictly necessary to achieve their objective.

(56) *Proportionate*. The Irish authorities submit that the behavioural constraints imposed by the terms and conditions of the Recapitalisation Measures, together with the conditions imposed under the ELG scheme, contain an extensive range of safeguards against possible abuses and distortions of competition.

(57) The measure is subject to a remuneration (bank fees on […]% of the gross proceeds of the transaction). Overall however, the Irish authorities acknowledge that how and when the State may recoup its investment will be dependent on many factors[…]. Nevertheless, the Irish authorities have submitted that the proposed recapitalisation of AIB is consistent with the State commitments agreed under the Programme of Financial Support for Ireland. In particular they submit that it is essential that the State supports AIB as a systematically important bank, essential to maintenance of financial stability in the country. AIB is the biggest Irish clearing bank and accounts for a major share of customer deposits and lending in the domestic economy.

(58) Furthermore, the Memorandum of Understanding setting some of the conditions of the Programme for Support indicates that the Irish Authorities will provide an updated restructuring plan for AIB by the end of the first quarter 2011. For the purpose of this decision, and as indicated in Recital 44 of the Commission Communication on "The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortion of competition" (hereinafter "the Recapitalisation Communication")[18], the Irish Authorities commit to submit a restructuring plan within 6 months of this decision. This restructuring plan will take into consideration the Recapitalisation Measures, as well as reorganisation measures decided under the Banking System Programme.

[18] Commission Communication on "The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortion of competition", OJ C 10 of 15.01.2009, p. 2.

4 ASSESSMENT

4.1 Existence of State aid

(59) The Commission first has to assess whether the measure constitutes State aid within the meaning of Article 107(1) TFEU. According to this provision, State aid is any aid granted by a Member State or through State resources in any form whatsoever which distorts, or threatens to distort, competition by favouring certain undertakings, in so far as it affects trade between Member States. The Commission in this context observes that the Irish authorities do not dispute that the measure constitutes State aid.

(60) The Commission observes that in this case State resources are involved as the measure is entirely financed by the State (regardless of the origin of the funds).

(61) The Commission also has to assess whether the measure confers a selective advantage on the beneficiary of the aid. The Commission considers the measure to be selective as it solely benefits AIB.

(62) The measure furthermore confers an advantage on AIB as it allows AIB to absorb losses on the transfer of NAMA assets and future losses on other assets and as such potentially to avoid insolvency. Although several banks in Ireland and in the EU have benefited from State aid in the course of the ongoing financial crisis, most have received less support in proportion of their risk weighted assets. In addition many banks have not received aid.

(63) The Commission considers that the proposed recapitalisation would not have been provided by a market economy investor expecting a reasonable return on his investment. The measure foresees an upfront remuneration for the State under the form of an underwriting fee of […]% on the gross proceeds of the recapitalisation. However, the ordinary shares do not carry any fixed remuneration and the Irish authorities did not provide evidence that the State will be in a position to recoup its overall investment if and when it sells its participation in the bank.

(64) The Commission finds that the measure is also able to affect trade between Member States as AIB is competing on, amongst others, the Irish retail savings markets, the Irish mortgage lending markets and the Irish and UK commercial lending markets. In the Irish market, some of AIB' competitors are subsidiaries of foreign banks, while in the UK market AIB competes with both UK-based banks and the subsidiaries of foreign banks active on the UK market.

Conclusion

(65) Due to the above considerations, the Commission considers that the measure fulfils all conditions laid down in Article 107(1) TFEU and, therefore, those measures qualify as State aid to AIB.

4.2 Compatibility of the aid

(66) As regards compatibility of the aid provided to AIB with the internal market, the Commission first needs to determine whether the aid can be assessed under Article 107(3)(b) TFEU, i.e. whether the aid remedies a serious disturbance in the economy of Ireland. Subsequently, once the applicable legal basis has been determined, the Commission has to assess whether the measure at issue is compatible with the internal market.

4.2.1 Legal basis for the compatibility assessment

(67) Article 107(3)(b) TFEU provides for the possibility that aid falling within the scope of Article 107(1) TFEU can be regarded as compatible with the internal market where it "remedies a serious disturbance in the economy of a Member State".

(68) Given the present circumstances in the financial markets, the Commission considers that the measure may be examined under Article 107(3)(b) TFEU.

(69) The Commission considers that market conditions deteriorated all over the world since the last quarter of 2008. The Commission observes that Ireland in particular has been severely hit by the financial and economic crisis. The economic downturn combined with the fall in property prices and the exposure of the Irish banks to land and property development loans have led to significant impairments for Irish banks. Irish banks have furthermore been faced with difficulties in obtaining funding and capital from the markets due to the uncertainty associated with the property market in Ireland, the future economic development and the pressure on the sovereign.

(70) The Irish authorities have shown that without the capital injection […]. This position has been confirmed by the Irish Central Bank in a letter dated 3 December 2010. According to the Irish Central Bank, it is essential that AIB receives the recapitalisation in order to avoid severe financial difficulties, as it is a systemically important financial institution. As indicated by the Irish authorities, AIB has a significant number of depositors.

(71) For these reasons the Commission accepts that the EUR 9.8 billion additional net recapitalisation in favour of AIB and the conversion of preference shares into ordinary shares are necessary to avoid a serious disturbance in the economy of Ireland.

4.2.2 Compatibility assessment

(72) In line with point 15 of the Banking Communication[19], in order for an aid or aid scheme to be compatible under Article 107(3)(b) TFEU it must comply with the general criteria for compatibility[20]:

a. *Appropriateness*: The aid has to be well targeted in order to be able to effectively achieve the objective of remedying a serious disturbance in the economy. This would not be the case if the measure were not appropriate to remedy the disturbance.

b. Necessity: The aid measure must, in its amount and form, be necessary to achieve the objective. That implies that it must be of the minimum amount necessary to reach the objective, and take the form most appropriate to remedy the disturbance.

c. Proportionality: The positive effects of the measure must be properly balanced against the distortions of competition, in order for the distortions to be limited to the minimum necessary to reach the measure's objectives.

(73) The Recapitalisation Communication further elaborates on the three principles of the Banking Communication and states that recapitalisations can contribute to the restoration of financial stability. In particular the Recapitalisation Communication

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[19] *The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis*, OJ C 270, 25.10.2008, p.8.

[20] See paragraph 41 of Commission decision in Case NN 51/2008 *Guarantee scheme for banks in Denmark*, OJ C 273, 28.10.2008, p.2.

states that recapitalisations may be an appropriate response to the problems of financial institutions facing insolvency.[21]

4.2.2.1 Compatibility with the Banking and Recapitalisation Communications

a. Appropriateness of the measures

(74) This second recapitalisation measure of AIB directly results from the capital requirements imposed by the Irish financial regulator, and will allow the Bank to meet its new target regulatory capital requirements in two steps. The injection of equity capital is the single most efficient and straight forward measure to shore up one bank's capital.

(75) AIB is the second largest banking institution in Ireland with very material shares of Irish retail banking services. As such AIB is a systemically important bank for Ireland. Consequently, a default of AIB would create a serious disturbance in the Irish economy. This serious disturbance would even be aggravated under the current circumstances where all financial institutions in Ireland face severe limitations to access funding, and limit to a certain extent the provisions of loans to the Irish economy. The measure thereby ensures that financial stability in Ireland is maintained. For those reasons, the Commission finds that the measure is appropriate.

b. Necessity – limitation of the aid to the minimum

(76) According to the Banking Communication, the aid measure must, in its amount and form, be necessary to achieve the objective. That implies that the capital injection must be of the minimum amount necessary to reach the objective. In this context, the Commission observes that the amount of the measures will ensure that AIB will fulfil its regulatory capital requirements and will be in line with the terms agreed by Ireland and the Banking System Programme. The proposed amount of recapitalisation is then limited to the minimum necessary to meet such requirements.

(77) On the purchase price per ordinary share, the Commission notes that it is equal to the the lower of (i) the closing price of AIB's ordinary stocks on 26 November 2010 (EUR 0.342 per share) which was the last trading day prior to the Central Bank of Ireland announcement on 28 November 2010; or (ii) the closing price of AIB's ordinary stocks on the last trading day prior to the Government's announcement of the AIB Recapitalisation Measures, which is anticipated to be made following the enactment of the legislation enabling the State to recapitalise the bank without market placement. Both prices could be viewed as the market price, and the lowest of these prices will be chosen, thus maximising the dilution of existing private shareholders. The Commission observes that the level of dilution obtained with such price per share is already very significant: current shareholders will be diluted from approx. 81.4% shareholding of the Bank currently to a maximum of 5% and potentially less.

(78) The Further Capital Contribution will be done at a price that will not exceed the price of the Capital Contribution, and potentially lower if the price of shares declines. It is thus considered as appropriate as it will maximise the shareholding of the State.

(79) The Preference Shares will be converted into ordinary shares at the conversion price used for the Capital Contribution. The Preference Shares will not be converted at a price lower than the subscription price of the ordinary shares purchased with cash as, amongst other reasons, this would contradict the principle of equal treatment of

[21] Recapitalisation Communication, paragraph (6).

ordinary shareholders (i.e. the State as sole holder of the preference shares would be allowed to purchase the same ordinary shares to be issued in the same transaction at a lower price).

(80) The Irish Government will subscribe to CNV shares for a portion of the issue amount, in order to limit State shareholding below 50% in the short term. According to the Irish authorities, this construction is temporary and necessary for regulatory reasons to limit aid to the minimum. The State will convert all the CNV shares into ordinary shares as soon as the Polish regulatory issue is solved if AIB is delisted […]. If AIB retains its existing listing, the State will convert a number of CNV shares so as its ordinary shareholding will remain below 75%. This second option would be acceptable from a State aid perspective, because the CNV and ordinary shares carry the same economic rights, and the State can convert the CNV shares at will.

(81) In conclusion, the measure is necessary in both its amount and form to achieve the objectives of limiting the disturbance in the Irish banking system and economy as a whole.

Remuneration of the aid

(82) The aid granted by the Irish authorities to AIB is fully in the form of ordinary shares (after the conversion of Preference Shares into ordinary shares) . The Irish authorities have not indicated whether they consider it likely that they will recoup their investment in the medium or long term by selling their stake in AIB.

(83) The measure foresees an upfront remuneration for the State under the form of an underwriting fee of […]% on the gross proceeds of the recapitalisation. However, the ordinary shares do not carry any fixed remuneration […]. Overall the remuneration of the State aid is thus very limited.

(84) Paragraphs 15 and 44 of the Recapitalisation Communication explain that lower remuneration in duly justified cases can be accepted in the short-term for distressed banks on the condition that the lower remuneration will be reflected in the restructuring plan.

(85) It is therefore necessary for the Commission to verify whether AIB is fundamentally sound or distressed. The Recapitalisation Communication provides a number of indicators to assess the risk profile of a financial institution, and whether the bank is fundamentally sound or distressed: (i) capital adequacy and sustainability of the business model; (ii) size of the recapitalisation; (iii) current CDS spreads; and (iv) the current rating of the financial institution and its outlook.[22]

(i) *Capital adequacy and sustainability of the business model*. The Recapitalisation Measures account for [10-20]% of AIB Risk Weighted Assets (RWAs)[23]. They will be sufficient for AIB to reach a 12% core tier 1 ratio. Absent the Recapitalisation Measures, the bank could not respect the capital requirements imposed by the financial regulator (10.5% core tier 1) by a large margin. Although the bank has preserved its traditional bank activities, it excessively engaged in the area of land and development property in the past, which have largely contributed to the difficulties of the bank. This excessive exposure is reflected in the bank's contribution to NAMA.

(ii) *Size of the recapitalisation*. In total the Irish Government will have injected EUR 13.3 billion (including the first recapitalisation of AIB and the Recapitalisation

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[22] See the Annex to the Recapitalisation Communication.

[23] Recapitalisation measures: EUR 9.8 billion. RWAs 2011 (reference for PCAR 2010 exercise): EUR […]

Measures subject to the present decision), equivalent to [10-20]% of the banks' RWAs, largely in excess of the 2% threshold provided for in the Recapitalisation Communication

(iii) *Current rating of the financial institution and its outlook.* AIB's current credit ratings are […] by Moody's, S&P and Fitch respectively (downgraded by S&P on 8 October 2010 and put on Credit Watch Negative by Moody's on 6 October 2010).

(iv) *Current CDS spreads*. The level of AIB's 5 year Senior CDS spread is approximately 1050 bps as of 8 December 2010. This compares to around 800 bps for Bank of Ireland and to approximately 150 bps for the 5 year senior financials ITRAXX index on the same day (vs. 244 bps 6 months ago on 10 May 2010).

(86) Based on the forgoing indicators, the Commission has come to the conclusion that AIB is in a distressed financial situation according to the criteria laid down in the Annex to the Recapitalisation Communication, and therefore needs to submit a restructuring plan. In particular, AIB cannot meet its regulatory capital requirements without Government support, its ratings are significantly degraded, and the recapitalisation measures will account for more than [10-20]% of its RWAs.

(87) Having established that AIB is a financial institution in distress, which without the State intervention […] could endanger financial stability in Ireland, the Commission considers it justified that a very low remuneration is paid for the measure. That approach is in line also with the Commission's previous decisional practice[24]. AIB is currently not in a position to pay the remuneration required for distressed banks as indicated in the Restructuring Communication. The Recapitalisation Communication also states in paragraph 44 that the use of recapitalisation for a distressed bank can only be accepted on the condition of a far-reaching restructuring.

(88) In addition, under the current economic situation in Ireland combined with the high level of distress of the bank and the lack of perspectives of return to profitability for the bank, no private investor is likely to provide the necessary capital to AIB.

c. Proportionality – measures limiting negative spill-over effects

(89) In spite of the relatively narrow margin of manoeuvre of the Irish authorities ([…]situation of most of the other Irish credit institutions and of the sovereign itself), the transaction provides adequate burden sharing through several points:

(90) Dilution: the transaction will dilute existing shareholders from a current holding of 81.4.%to 0-5%. The Commission views this level of dilution as very material.

(91) Fees: the State will receive underwriting fees of […]% of the gross amount of ordinary shares (regardless of any amount taken by private investors or existing shareholders) plus […]% on the gross amount of CNV shares. The Commission views the fees as adequate with regards to financial difficulties of the bank. The fees will be funded through the recapitalisation and paid back to the State. Although it is neutral for the State, the payment of the fees contributes to further dilution of AIB's shareholders.

(92) Warrants: it is intended that the State will hand over its existing warrants for a price of EUR 50 million. The Commission considers that the assumptions used to price the warrants are conservative and that the price proposed is a fair amount. In particular at best only one third of this amount consists in the intrinsic value of the warrants (target price minus current price), whereas two third of the price consists in the time value

[24] The same approach was taken in point 64 of Commission decision in Case N 356/2009, Recapitalisation of Anglo Irish bank, OJ C 235, 30.9.2009.

(future gains due to increase in the share price). The time value assumptions appear relatively optimistic, which results in a higher price paid to the State.

(93) *Change in management:* following the announcement of this second recapitalisation, both the Executive Chairman and the Group Managing Director stepped down.

(94) *Higher underwriting fee for the CNV shares*: The CNV shares will be underwritten for a higher fee of […]% which compensates for the loss of voting rights, although the Irish government will exercise a de facto control of the bank and will convert the CNV shares in ordinary shares as soon as feasible.

(95) *Restructuring Plan:* AIB will provide an updated restructuring plan at the latest within 6 months of the date of this decision which will reflect the massive State aid injected in the bank, and the lack of appropriate remuneration for this aid.

(96) *Behavioural measures:* AIB had already proposed a number of behavioural measures as a result of its participation in the Irish guarantee schemes, to help tackle potential competition distortion effects. In light of the state of the Irish economy and banking system and of the systemic importance of AIB, the Commission is of the view that these measures are sufficient to justify the distortion of competition caused by the aid during the restructuring process. This is however without prejudice of additional measures to address distortion of competition that may be attached to the restructuring plan of the bank.

(97) The Commission thus considers the above elements to be sufficient to consider the measure as proportionate and to temporarily approve the measure as emergency aid.

Conclusion

(98) The Commission thus concludes that the measure is: (i) appropriate; (ii) necessary; (iii) that the fact that the capital injection is unlikely to be adequately remunerated by AIB is justified under the circumstances; (iv) AIB is under the obligation to submit a revised restructuring plan; and (v) there are sufficient measures limiting the negative spill-over effects for other competitors. The Commission can therefore approve the measure.

4.2.2.3 Viability review and restructuring plan

(99) The Recapitalisation Communication states in paragraph 44 that the use of recapitalisation for a distressed bank can only be accepted on the condition of a far-reaching restructuring. The Commission furthermore observes that the aid provided to AIB is a high multiple of the established threshold of 2% of its RWA ([10-20]%), which together with the rest of indicators of the Annex to the Recapitalisation Communication (as examined in paragraph (85)), confirms that in-depth restructuring is required.

(100) The Commission furthermore observes that the Banking System Programme stipulates that the Irish authorities will submit a revised restructuring plan for AIB before the end of the first quarter 2011. For the purpose of this decision, and as indicated in Recital 44 of the Recapitalisation Communication, the Irish Authorities commit to submit a restructuring plan within 6 months of this decision.

(101) In line with the provisions of the Memorandum of Understanding of the Banking System Programme, the Commission anticipates the restructuring plan to build on the already completed divestments (paragraph (16)) to include far reaching deleveraging measures to address the bank's funding and liquidity issues. The Commission anticipates the plan to focus on balance sheet reduction to reach the loan to deposits ratio targets to be set for end 2013 by the Irish Authorities consultation with the ECB, EC and the IMF by end Dec 2010. For these reasons, the Commission accepts the

commitment of the Irish authorities to submit a revised restructuring within six months of the present decision.

(102) The Commission therefore requires that the revised restructuring plan will (i) take into account all aid measures AIB has received; (ii) fulfil the requirements of the Restructuring Communication[25] as regards return to viability, burden-sharing and own contribution and measures limiting the distortion of competition and (iii) take into account reorganisation measures decided under the Banking System Programme. In any event, the restructuring plan should be submitted to the Commission within six months of the present decision.

CONCLUSION

- The Commission concludes that the net capital injection of EUR 9.8 billion by the State constitutes State aid pursuant to Article 107(1) TFEU.

- The Commission finds that the rescue measure in favour of Allied Irish Bank fulfils the requirements of Article 107(3)(b) TFEU and is temporarily compatible with the internal market for reasons of financial stability. The rescue measure in favour of Allied Irish Bank is accordingly approved for six months or, if the Irish authorities submit a restructuring plan within the period prescribed in the next point, until the Commission has adopted a final decision on the restructuring plan of the bank.

- The Commission requires the Irish authorities to submit a revised in-depth restructuring plan within six months of the present decision, which takes into account the further aid provided to Allied Irish Bank and the substantial size of the aid – in terms of % of RWA – granted to Allied Irish Bank.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

http://ec.europa.eu/community_law/state_aids/state_aids_texts_en.htm

Your request should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State Aid Greffe
Rue Joseph II 70
B-1049 Brussels
Fax No: (+32)-2-296.12.42

Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President

25 Communication from the Commission "The return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules", OJ C195, 19.8.2009, p. 9.

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.

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.

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

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

National Treasury Management Agency

30 November 2010

30th November 2010
you have full authority
in the matter

Brian Lenihan

Mr. Brian Lenihan T.D.
Minister for Finance
Government Buildings
Upper Merrion Street
Dublin 2

Strictly Price Sensitive

Dear Minister,

The NTMA has been approached by the Libyan Investment Authority (LIA) which is interested in acquiring a large portion of the directed investments held by the NPRF in Bank of Ireland. The NPRF holds a 36% interest in the ordinary shares of the bank with a current market value of €589m and preference shares with a par value of €1,837m. The LIA is interested in acquiring 24% of Bank of Ireland's ordinary shares from the NPRF (market value: €394m), representing some two thirds of the NPRF's directed investment in the bank's ordinary shares, and €1bn of the NPRF's holding of preference shares.

The LIA has outlined in an indicative proposal that it is prepared to pay par value of €1bn for the preference shares, excluding the €74m coupon due to the NPRF on those shares. It is unclear what price the LIA is prepared to pay for the 24% interest in the ordinary shares although they are fully aware of the NPRF's original purchase price and the obvious sensitivity attaching to that price. The LIA has also indicated that it would source debt funding of up to €2bn for the bank.

Like all quoted assets in the NPRF portfolio, the ordinary shares are marked to market value on a daily basis. On this basis a sale of the ordinary shares at a price of, say 50 cents per share, would represent a profit of €242m relative to the current mark to market value. The preference shares which, unlike the quoted equities, are not marked to market would be sold at the recorded value in the NPRF accounts, albeit at a premium to estimated market value, which is likely to be 73% of par (i.e. 73 cents) or lower based on the most recent analysis by Rothschild, and excluding the €74m accrued coupon. A sale of the 24% interest in the ordinary shares would raise €636m which, combined with the €491m warrant cancellation fee and €52m transaction fee accruing to the NPRF in the first half of this year, is €102m lower than the €1,281m average cost of acquiring the shares. Each 5c variation in the price obtained on a sale of the shares would vary the overall proceeds by €64m.

The sale of the majority of the NPRF stake in Bank of Ireland would have the following advantages:

- On a commercial basis a sale on the indicative terms above would represent a substantial premium to current market value and to the current valuation of the assets in the NPRF.

- The Central Bank has required Bank of Ireland to raise a further €2.2bn in core tier 1 capital before 28 February 2011. The bank's existing private sector shareholders are unlikely to recapitalise the bank ahead of that deadline, leaving the State as the only source of the capital. The LIA is fully aware of the bank's requirement to raise fresh capital before end February next and the possibility of

further capital requirements beyond that date on foot of a new PCAR review and possible balance sheet deleveraging. It has indicated that it would be prepared to follow its money in a new capital raising. If the ordinary shares are sold at 50c and the preference shares at par the cash proceeds obtained by the State would be €1,636m which, combined with the €528m that the LIA would be expected to contribute to the upcoming capital raise, would eliminate the need for any material net drawing on the State in the forthcoming recapitalisation.

- The sale of a 24% interest in the bank is likely to result in the State's interest being held below 50%, given that the LIA has indicated that it would take up its rights should the bank be required to raise further capital. Maintaining a majority private ownership would underpin the valuation of the remaining NPRF interest in the bank and increase the potential for that remaining stake to be sold at a later date.

- A reduction in the funds required by Bank of Ireland from the State would free up capital necessary to support the other Irish banks and the broader economy.

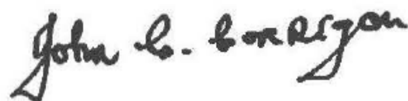
- A large investment by an outside strategic investor at this stage would likely build market confidence in the banking system generally and in the wider economy.

It should be noted, on the downside, that the transaction would represent a loss on the original invested amount (which nonetheless has been written down as indicated above) and that the transaction fee at 6% is high, reflecting the bilateral nature of the transaction.

On balance, the NTMA recommends that this sale be pursued. NTMA representatives have been invited to meet the LIA investment committee in Tripoli later this week to negotiate a sale of a portion of the NPRF stake as outlined above. In that regard, your authority is sought to negotiate a sale of the ordinary shares for a price of not less than 50c and the preference shares at par value. The NTMA will be supported by its legal and banking advisors.

Kind regards

Yours sincerely



John C. Corrigan
Chief Executive

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)

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.

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

31 January 2011

This document contains substantial amounts of confidential information.
No disclosure of any information contained in this document should be made without prior written consent.

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**

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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

Confidential work in progress. For discussion purposes only – not for distribution

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

THE HIGH COURT

2011 No. 29 MCA

FRIDAY THE 1ST DAY OF JULY 2011

BEFORE MR JUSTICE MCGOVERN

IN THE MATTER OF IRISH NATIONWIDE BUILDING SOCIETY

AND

IN THE MATTER OF THE CREDIT INSTITUTIONS (STABILISATION) ACT, 2010

AND

IN THE MATTER OF AN APPLICATION BY THE MINISTER FOR FINANCE FOR A TRANSFER ORDER IN RELATION TO IRISH NATIONWIDE BUILDING SOCIETY PURSUANT TO SECTION 34 OF THE CREDIT INSTITUTIONS (STABILISATION) ACT 2010 AND ANCILLARY ORDERS

The ex parte application of the Minister for Finance (the "Applicant") for a Transfer Order pursuant to Section 34 of the Credit Institutions (Stabilisation) Act 2010 (the "Act") along with related reliefs including an application under Section 60 of the Act for restrictions with regard to the disclosure in open Court publication or reporting of material which is commercially sensitive coming before this Honourable Court this day in the presence of Counsel for the Applicant.

And on the application by Counsel for the Applicant for an Order prohibiting publication of the fact of the within application pending the making of a Transfer Order pursuant to Section 34 of the Act

And on hearing said Counsel for the Applicant

The Court doth so Order

Whereas on reading the Affidavit of John Moran sworn the 29th day of June 2011 and the exhibits thereto and on hearing what was offered by Counsel for the Applicant

And whereas the transferee Anglo Irish Bank Corporation Limted ("Anglo") a credit institution licensed in Ireland and whose registered office is at Stephen Court 18/21 St Stephen's Green Dublin 2 has agreed to accept the Transfer on the terms set out in this Order

IT IS ORDERED that the Applicant be granted the following reliefs:

A. A Transfer Order pursuant to Section 34 of the Act in the terms provided hereinafter.

B. On the making of this Transfer Order (the "Transfer Time") all the assets and liabilities of INBS at the Transfer Time (other than the excluded assets and liabilities set out in Paragraphs 2.1 and 2.2 hereinafter) whether situated in or outside the State, whether governed by the laws of the State or any foreign law (and including, without limitation, foreign assets and foreign liabilities) and whether actual or contingent, including, without limiting the generality of the foregoing, all right, title, benefit and interest of INBS in and to and all obligations and liabilities of INBS in respect of those assets and liabilities set out in the Paragraphs 1.1 to 1.23 inclusive hereinafter (the "Assets and Liabilities") shall be transferred by INBS as beneficial owner to Anglo, being the transferee, immediately in accordance with sections 34(7)(a), 39 and 41 of the Act for the consideration and under the terms and conditions specified in this Transfer Order:

1.1 all property (real or personal) and whether registered or unregistered, freehold or leasehold including, without limiting the generality of the foregoing, the branch offices set out in Part 1, the development properties set out in Part 2 and the investment property set out in Part 3 of Schedule 1 to this Transfer Order;

1.2 all fixtures and fittings, plant, machinery, computer and IT equipment, all other equipment, furniture, chattels and other tangible assets (excluding any which are attached to a leasehold property and which are the property of the landlord) attached or not to any real property and owned or used by INBS;

1.3 all motor vehicles owned, leased or used by INBS;

1.4 the goodwill of INBS in connection with its business and the right to carry on the business in succession of INBS;

1.5 all causes of action, claims, entitlements and proceedings that relate to any period prior to the Transfer Time (whether arising from breach of law, regulation, contract, tortious actions or omissions, breach of duty or otherwise howsoever arising and whether actual, contingent or prospective) which INBS is or would at any time in the future (apart from the making of any transfer order) be entitled to take, make or claim against any person, company, body corporate, partnership, limited partnership or any other association or entity ("Person") and all remedies and recourse in respect thereof ("INBS Claims"), including, but without limitation to the generality of the foregoing, all INBS Claims against any director, officer or employee or former director, officer or employee of INBS in respect of any negligence, wrongdoing, default, breach of duty, breach of contract, breach of trust or on any other ground whatsoever;

1.6 all licences, contracts, agreements, deeds, protocols or arrangements (whether or not in writing) to which INBS is a party or to which it is otherwise entitled or by which it is otherwise bound;

1.7 all shares owned or held by INBS in all subsidiaries and subsidiary undertakings of INBS, including the companies and other entities listed in Schedule 3 to this Transfer Order;

1.8 all "available for sale debt securities", all "available for sale equity securities" and all other shares, securities, debentures, stock or other interests of any kind held by INBS in any company or any other Person;

1.9 all trade marks (registered and unregistered), service marks, logos, patents, copyrights (including copyright in computer programs), database rights, confidential information, business or trade names, set up, domain names, know how and all other intellectual property rights;

1.10 all contracts of employment and/or collective agreements in respect of INBS employees existing at the Transfer Time;

1.11 all rights, liabilities and obligations of INBS arising from the provisions of any occupational pension scheme (whether defined benefit, defined contribution or otherwise);

1.12 all:

(a) mandates, terms and conditions, instructions, applications, customer verification documents, directions, files, books, correspondence and other records of any kind of INBS in so far as they relate to the Assets and Liabilities held on whatever medium; and

(b) customer documentation relating to the provision of any banking or other service or facility (including, without limitation, solicitors' undertakings, certificates of title, architects' certificates of compliance, valuation reports, insurance and assurance (whether life and/or non-life) proposals, and declarations, authorisations, consents and application forms from applicants for loans) and all documents (whether for the purpose of disclosure, information, consents, declarations, authorisations or otherwise) received by INBS from its customers or potential customers, including all documents relating to the requirements of the Criminal Justice Act 1994, the Criminal Justice (Money-laundering and Terrorist Financing) Act 2010, the Data Protection Acts 1988 and 2003, the Consumer Credit Act 1995, the Family Home Protection Act

1976, the Family Law Act 1981, the Judicial Separation and Family Law Reform Act 1989, the Family Law Act 1995 and the Family Law (Divorce) Act 1996, the Consumer Protection Code (issued by the Central Bank of Ireland (the "CBI")) and any other enactment;

1.13 all debt securities, loan instruments, bonds, notes, promissory notes, debentures, loan stock, commercial paper, certificates of deposit and all other instruments of any kind constituting or evidencing indebtedness or otherwise involving the extension of credit by, and providing for payment of money to, the holder thereof (whether upon the occurrence of a contingency or otherwise), whether in bearer, registered or dematerialised form or otherwise, issued by INBS or in respect of which it is the debtor or obligor immediately before the Transfer Time, including all amounts outstanding under notes issued by INBS under its €10,000,000,000 Euro Medium Term Note Programme, and related documentation, including, without limitation, any contracts, agreements, instruments or deeds;

1.14 all amounts standing to the credit of any account representing or evidencing funding (whether by means of repurchase transactions, loans, deposits or otherwise) provided to INBS at the Transfer Time by the CBI, the European Central Bank (in each case whether under Eurosystem monetary policy operations or otherwise) or any other central bank or equivalent institution, and the related account;

1.15 all inter-bank deposits and all other accounts designated with holder type codes 04 (Financial Institutions), 20 (Central Government), 24 (General Government) or 99 (EMTN) in the accounting records of INBS;

1.16 all accounts (and any amount standing to the credit or, as applicable, debit thereof) identified in the accounting records of INBS by branch "91" including:

(a) all accounts in the name of or on behalf of any person or persons (including

any individual or body corporate) over which INBS has been granted by way of written agreement a lien or any other type of security;

(b) all internal administration accounts designated by the product code DRLFSQ in the accounting records of INBS;

(c) those accounts identified in the accounting records of INBS by reference to the customer sequence number 47973 (mortgage controlled accounts); and

(d) inter-company accounts relating to special purpose vehicle companies;

1.17 all currency, interest rate or other swap contracts or other derivatives of any kind whatsoever to which INBS is a party, including, without limitation, the master swap agreement listed in Schedule 2 to this Transfer Order, and all trades and transactions documented thereunder or entered into pursuant thereto and all confirmations, credit support annexes, credit support deeds and other collateral arrangements entered into in connection therewith and all cash or other assets of any kind provided by or to INBS as collateral in connection therewith;

1.18 the promissory note received by INBS from the Minister for Finance (the "Minister") on 22 December 2010;

1.19 all loan or other facilities made by INBS to any Person and all agreements, contracts, deeds or other instruments or documents relating thereto and all amounts owing to INBS by any Person on any account whatsoever and in any currency and to, in and under every mortgage, charge, pledge, guarantee, indemnity or any other form of security or other collateral (including without limitation to the generality of the foregoing, interests in insurances) (collectively, "Loans and Related Security") held by INBS or to which it is entitled in respect thereof, in each case at the Transfer Time, including, without limitation, (i) all loan accounts identified on the Society's loan

administration system (the "Summit" system) with a Global type "L" or "M" or "I" or "SU" and with a process status of either 1, 2, 3 or 4, in each case at the Transfer Time, and (ii) inter-company loans between the Society and subsidiary companies which are recorded on the Society's general ledger system with nominal account numbers 730200, 780500, 780610, 780620, 780630, 780640, 780650, 780700, 781000, 781050, 781280 and 781300;

1.20 all cash in any currency held by or on behalf of INBS at the Transfer Time, including all cash on hand as identified on the Society's general ledger system by nominal account numbers 700100, 700400, 700500, 700600 and 700100 and deposits with the CBI at the Transfer Time in the name of the Society;

1.21 all (i) guarantees, indemnities, bills of exchange, counter-indemnities, (ii) standby or documentary letters of credit and (iii) construction, performance or other bonds, in each case issued or granted by INBS or in respect of which it is the debtor or obligor; and

1.22 all claims, rights and entitlements to or for refunds or abatements of, and liabilities in respect of, taxes assessed against, paid by or collected from INBS by the Revenue Commissioners in Ireland, HM Revenue & Customs in the United Kingdom or the recognised tax authorities in any other jurisdiction in which the Society has undertaken any transactions of whatsoever nature ("Tax Claims") with full power and authority to Anglo (in its own name or in the name of INBS) to make all such claims, execute and file all such documents and do all such other acts and things as may be necessary to enforce or recover all such Tax Claims including authority to compromise and/or settle all such Tax Claims; and

1.23 the Loans and Related Security related to any loan account designated or recorded with or under pool code 'NAMA1' on the Society's loan administration system at

the Transfer Time.

but excluding

2.1 the liabilities and obligations of INBS to its members in respect of the Special Investment Shares in INBS held by the Minister together with any balances remaining on the general reserve and capital contribution accounts on INBS' balance sheet; and

2.2 all causes of action, claims, entitlements and proceedings that relate to any period prior to the Transfer Time (whether arising from breach of law, regulation, contract, tortious actions or omissions, breach of duty or otherwise howsoever arising and whether actual, contingent or prospective) which the CBI or any governmental, regulatory or prosecuting authority in any jurisdiction is or would at any time in the future (apart from the making of any transfer order) be entitled to take, make or claim against INBS and/or any Person and all remedies and recourse in respect thereof ("Regulatory Actions"), including, but without limitation to the generality of the foregoing, all Regulatory Actions involving any director, officer or employee or former director, officer or employee of INBS in respect of any negligence, wrongdoing, default, breach of duty, breach of contract or breach of trust or on any other ground whatsoever.

C. The consideration for the transfer of the assets is the assumption by Anglo of the liabilities, in each case, comprised in the Assets and Liabilities (the "Consideration").

D. It is a condition of this Transfer Order that this Transfer Order (including the consequences thereof provided for in the Act) and each and every part thereof is a reorganisation measure to which sections 61 and 62 of the Act apply.

E. The Court further notes that the Minister considers the incidental, consequential and sup-

plemental provisions set out below to be appropriate for implementing the transfer of the Assets and Liabilities and securing that it be fully and effectively carried out and the Court also considers those provisions to be appropriate for those purposes and accordingly orders, under section 37(9) of the Act, as follows:

1.1. INBS and Anglo shall each transfer or disclose to each other such information (including personal data within the meaning of the Data Protection Acts 1988 and 2003 or the Data Protection Act, 1998 (as amended) of the United Kingdom) as is required to enable the other to carry out or undertake any matter or thing provided for under this Transfer Order.

1.2. Any instruction, order, direction, confirmation, declaration, documentation, mandate or authority given to INBS in the course of or incidental to or relating to the Assets and Liabilities and subsisting immediately before the Transfer Time shall be treated for all purposes relating to the Assets and Liabilities as having been given to Anglo.

1.3. Any payment received on or after the Transfer Time by or in relation to INBS that relates to the Assets and Liabilities held by or with INBS immediately before the Transfer Time is to be treated as received by or in relation to Anglo.

1.4. Anything (i) that relates to some or all of the Assets and Liabilities immediately prior to the Transfer Time and (ii) which is in the process of being done in relation to the Assets and Liabilities by INBS immediately before the Transfer Time shall be continued by or in relation to Anglo on the same terms and subject to the same discretions save as otherwise necessitated, and only to the extent necessitated, by the transfer of the Assets and the Liabilities to Anglo.

1.5. Nothing in this Transfer Order shall prejudice or limit in any way the rights of INBS or Anglo (as the successor to INBS in respect of the Assets and Liabilities) to claim or recover from any director, officer or employee or former director, officer or em-

ployee or other Person in respect of any negligence, wrongdoing, default, breach of duty, breach of contract, breach of trust or on any other ground whatsoever that relates to any period prior to the Transfer Time.

1.6. Nothing in this Transfer Order shall prejudice or limit in any way the right of INBS or Anglo (as the successor to INBS in respect of INBS Claims and Tax Claims) to any existing privilege or to claim privilege in respect of any documentation or other information relating in any way whatsoever to any INBS Claim, Tax Claim or Regulatory Action.

1.7. Without prejudice to the generality of section 39 of the Act, the Guarantee in favour of the CBI, dated 18 February 2011, wherein the Minister guarantees all sums due to the CBI by INBS under the facility agreement between INBS and the CBI dated 18 February 2011, shall remain in place with full force and effect after the Transfer Time.

1.8. From the Transfer Time, and without prejudice to any authorisation of INBS under section 17 of the Building Societies Act 1989 after the Transfer Time, in any instruments or documents relating to the Assets and Liabilities, any reference to INBS holding or being required to hold an authorisation under section 17 of the Building Societies Act 1989 (or any similar former statutory provision) or INBS being authorised for the purposes of or under the Building Societies Acts 1989 to 2006 (or any similar former enactment), shall have effect as if such references were instead references to Anglo holding or being required to hold a licence from the CBI under section 9 of the Central Bank Act 1971 or any replacement thereof.

1.9. The reference in clause 5.1 of the transfer support agreement dated 23 February 2011 between INBS and Irish Life & Permanent PLC to the final transfer of loans and related assets from INBS to the National Asset Management Agency ("NAMA") shall

be read and construed after the Transfer Time as a reference to any transfer by Anglo to NAMA before 30 September 2011 of any such loans and related assets which are transferred by INBS to Anglo pursuant to this Transfer Order and the Act.

F. Declaring pursuant to Section 34(4) that this Transfer Order and each and every part of it is a reorganisation measure for the purposes of Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions (the "CIWUD Directive"), and the European Communities (Reorganisation and Winding-Up of Credit Institutions) Regulations 2011 (S.I. No. 48 of 2011) (the "2011 Regulations") and accordingly, it is intended that this transfer order should have full effect in all applicable jurisdictions (including, without limitation, the United Kingdom of Great Britain and Northern Ireland) in accordance with the CIWUD Directive, the 2011 Regulations and the Act, including, in particular, but not limited to section 61 of the Act.

G. An Order pursuant to Section 60 of the Act directing that there be no disclosure in open Court, publication or reporting of paragraphs 28.5, 30, 50, 53, 54, 64 and 100 of the Affidavit of John Moran sworn on 29th day of June 2011 which are highlighted in yellow in said Affidavit, or those documents contained in exhibits JM7, JM9, JM10, and the Report of the Central Bank at exhibit JM13.

H. An Order pursuant to Regulation 9 of the European Communities (Reorganisation and Winding-Up of Credit Institutions) Regulations 2011 directing that the Courts Service arrange for publication forthwith of an extract of this Order.

MARY KELLY
REGISTRAR
1ST JULY 2011

David J O'Hagan
Chief State Solicitor
Solicitor for the Applicant

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.

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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.

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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.

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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.

DRAFT

CREDIT INSTITUTIONS (STABILISATION) ACT 2010

Proposed Transfer Order

Purposes and Intention

1. This Proposed Transfer Order is made on February 2011 in relation to Irish Nationwide Building Society ("**INBS**") pursuant to the provisions of section 33 of the Credit Institutions (Stabilisation) Act 2010 (the "**Act**").

2. This Proposed Transfer Order is made because, having consulted the Governor of the Central Bank of Ireland, I am of the opinion that a Transfer Order in the terms of this Proposed Transfer Order is necessary to secure the achievement of a purpose or purposes of the Act, namely:

   2.1 to address the serious and continuing disruption to the economy and the financial system and the continuing serious threat to the stability of certain credit institutions in the State and the financial system generally (section 4(a) of the Act);

   2.2 to implement the reorganisation of INBS, a credit institution in the State, to achieve the financial stabilisation of INBS and its restructuring (consistent with the State aid rules of the European Union) in the context of the National Recovery Plan 2011-2014 and the European Union/International Monetary Fund Programme of Financial Support for Ireland (section 4(b) of the Act);

   2.3 to continue the process of preservation and restoration of the financial position of INBS through the issue of special investment shares under section 18(1A) of the Building Societies Act 1989 (section 4(d) of the Act);

   2.4 to protect the interests of depositors in credit institutions, (section 4(e) of the Act);

   2.5 to address the compelling need:

      (a) to facilitate the availability of credit in the economy of the State,

      (b) to protect the State's interests in respect of the guarantees given by the State under the Credit Institutions (Financial Support) Act 2008 and to support the steps taken by the Government in that regard,

      (c) to protect the interests of taxpayers,

      (d) to restore confidence in the banking sector and to underpin Government support measures in relation to that sector, and

      (e) to align the activities of the relevant institutions and the duties and responsibilities of their officers and employees with the public interests and the other purposes of the Act (section 4(f) of the Act);

   2.6 to preserve and restore the financial position of INBS (section 4(g) of the Act); and

   2.7 to empower the Court to impose reorganisation measures on INBS through orders made in reliance on Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding-up of credit institutions (the "**CIWUD Directive**"), (section 4(h) of the Act).

3. The intention of this Proposed Transfer Order and of each part of it is the preservation or

restoration of the financial position of INBS which is a credit institution under the Act and I so declare for the purposes of section 33(3) of the Act.

4. This Proposed Transfer Order and each part of it is a reorganisation measure for the purposes of the CIWUD Directive and the European Communities (Reorganisation and Winding-Up of Credit Institutions) Regulations 2011 (S.I. No. 48 of 2011) (the "**2011 Regulations**") and, accordingly, it is intended that this Proposed Transfer Order and any transfer order in the terms of this Proposed Transfer Order made by the High Court pursuant to section 34 of the Act should have full effect in accordance with the CIWUD Directive, the 2011 Regulations and the Act, including, in particular, but not limited to, section 61 of the Act.

5. INBS is a "relevant institution" and a "credit institution" as those terms are defined in section 2(1) of the Act.

6. The transferee is Irish Life & Permanent plc, a credit institution licensed in Ireland and whose registered office is at Irish Life Centre, Lower Abbey Street, Dublin 1 ("**ILP**").

Transfer of Assets and Liabilities

7. On the making of a transfer order under section 34 of the Act (the "**Transfer Time**") the following assets and liabilities of INBS set out in this paragraph 7 (other than the Excluded Liabilities as defined in paragraph 7.1 below) (the "**Assets and Liabilities**") shall be transferred by INBS as beneficial owner to ILP immediately in accordance with sections 34(7)(a), 39 and 41 of the Act for the consideration and under the terms and conditions specified in this Proposed Transfer Order:

 7.1 the "**Deposits**" being each deposit or other account (including each share account) in any currency (including all amounts standing to the credit of each such account) held at the Transfer Time with INBS in the name of or on behalf of any person or persons (including any individual or body corporate), including all demand accounts (investment share accounts, Money Maker accounts, deposit accounts, instant access deposit accounts and regular savings accounts), notice accounts (Goldsaver 50/90 day notice accounts, Select 30 Deposit accounts, Advantage 30 accounts, Flexisaver 21 day notice accounts, Freedom accounts), term accounts (Fixed Rate Bonds, Fixed Rate Income Bonds, Fixed Term Accounts), Euro Equity Linked Nokia Bond and all deposits by Irish Nationwide (I.O.M.) Limited, but excluding the following (the "**Excluded Liabilities**"):

  (a) all amounts outstanding under notes (including dated subordinated notes) issued by INBS under its €10,000,000,000 Euro Medium Term Note Programme;

  (b) any amount standing to the credit of any account representing or evidencing funding (whether by means of repurchase transactions, loan, deposits or otherwise) provided to INBS at the Transfer Time by the Central Bank of Ireland, or the European Central Bank (whether under Eurosystem monetary policy operations or otherwise) or any other central bank or equivalent institution, and the related account;

  (c) all inter-bank deposits and all other accounts designated with holder type codes 04 (Financial Institutions) (other than any deposits made by Irish Nationwide (I.O.M.) Limited), 20 (Central Government), 24 (General Government) or 99 (EMTN) in the accounting records of INBS;

  (d) all accounts identified in the accounting records of INBS by branch "91" including:

(i) all accounts in the name of or on behalf of any person or persons (including any individual or body corporate) over which INBS has been granted by way of written agreement a lien or other form of security (the "**Collateralised Accounts**");

(ii) all internal administration accounts designated by the product code DRLFSQ in the accounting records of INBS;

(iii) those accounts identified in the accounting records of INBS by reference to the customer sequence number 47973 (mortgage controlled accounts); and

(iv) inter-company accounts relating to special purpose vehicle companies;

(e) the Special Investment Shares in INBS held by the Minister;

7.2 the "**Financial Assets**" being:

(a) €2,891,000,000 nominal amount of Irish Government Guaranteed Floating Rate Notes issued by National Asset Management Limited (as more particularly described under the heading 'Senior NAMA Notes' in Table 1.1 of Schedule 1) (the "**Senior NAMA Bonds**"); and

(b) €790,320,000 nominal amount of Irish Government and Financial Institution bonds (as more particularly described in Table 1.1 of Schedule 1) (the "**Other Bonds**").

7.3 the "**ELG Scheme Agreement**" being the rights and obligations of INBS under the eligible liabilities guarantee scheme agreement dated 2 February 2010 between Irish Nationwide (I.O.M.) Limited (as participating institution), INBS (as related party) and the Minister;

7.4 the "**Business Agreements**" being:

(a) the swap arrangements entered into by INBS in connection with the Euro Equity Linked Nokia Bond forming part of the Deposits; and

(b) the secure transport services agreement entered into by INBS,

as listed in Schedule 3 of the transfer support agreement entered into by INBS and ILP on 23 February 2011, a copy of which is set out in Schedule 2 (the "**Transfer Support Agreement**");

7.5 the "**Employees**" being the rights and obligations of INBS arising from contracts of employment existing at the Transfer Time or from collective agreements and in either case in respect of those employees of INBS wholly or mainly assigned to INBS's Deposit business as listed in the Transfer Support Agreement;

7.6 the "**Isle of Man Shares**" being the entire issued share capital of Irish Nationwide (I.O.M.) Limited ("**IOMCo**") at the Transfer Time and whether in certificated, de-materialised or uncertificated form;

7.7 the "**Records**" being all mandates, terms and conditions, instructions, applications, customer verification documents, directions, files, books, correspondence and other records of INBS in so far as they relate to the assets and liabilities of INBS (other than the Excluded Liabilities) referred to at paragraphs 7.1 to 7.6 above (both

inclusive), held on whatever medium.

8. The consideration for the transfer of the assets is the assumption by ILP of the liabilities, in each case, comprised in the Assets and Liabilities, together with the payment in cash by ILP to INBS of the sum of €2,311,097 (the "**Consideration**"). INBS and ILP will make such additional payments to each other as may be determined in accordance with the adjustment provisions in Schedule 3 to this Proposed Transfer Order.

9. It is a condition of this Proposed Transfer Order that this Proposed Transfer Order (including the consequences thereof provided for in the Act) is a reorganisation measure to which sections 61 and 62 of the Act apply.

10. The Minister considers the incidental, consequential and supplemental provisions set out below to be appropriate for implementing the transfer of the Assets and Liabilities and securing that it be fully and effectively carried out and accordingly provides, under section 33(6)(b) and section 37(9) of the Act, as follows:

    10.1 INBS and ILP shall each transfer or disclose to each other such information (including personal data within the meaning of the Data Protection Acts 1988 and 2003 or the Data Protection Act, 1998 (as amended) of the United Kingdom) as is required to enable the other to carry out or undertake any matter or thing provided for under this Proposed Transfer Order, including the provision of services to the other as provided for in the Transfer Support Agreement.

    10.2 Any instruction, order, direction, confirmation, declaration, documentation, mandate or authority given to INBS in the course of or incidental to or relating to the Assets and Liabilities and subsisting immediately before the Transfer Time shall be treated for all purposes relating to the Assets and Liabilities as having been given to ILP.

    10.3 Save for payments to be made by ILP to INBS pursuant to the provisions of this Proposed Transfer Order or of the Transfer Support Agreement, any payment received on or after the Transfer Time by or in relation to INBS that relates to the Assets and Liabilities held by or with INBS immediately before the Transfer Time is to be treated as received by or in relation to ILP.

    10.4 Anything:

        (a) that relates to some or all of the Assets and Liabilities immediately prior to the Transfer Time; and

        (b) which is in the process of being done in relation to the Assets and Liabilities by INBS immediately before the Transfer Time,

    shall be continued by or in relation to ILP on the same terms and subject to the same discretions, subject as provided for in the Transfer Support Agreement or as otherwise necessitated by the transfer of the Assets and the Liabilities to ILP.

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Brian Lenihan,
Minister for Finance

February 2011

Schedule 1

Table 1.1: Financial Assets

Financial Assets	ISIN	Maturity Date	Nominal Value (€'000s)	Value as % of Nominal Value Prescribed by ILP	Value Prescribed by ILP (€'000s)
Senior NAMA Notes					
Senior NAMA Notes	XS0548495919	01-Mar-2011	€451,000	98.50%	€444,235
Senior NAMA Notes	XS0548498699	01-Mar-2011	€334,000	98.50%	€328,990
Senior NAMA Notes	XS0496223768	01-Mar-2011	€421,000	98.50%	€414,685
Senior NAMA Notes	XS0566369434	01-Mar-2011	€1,413,000	98.50%	€1,391,805
Senior NAMA Notes	XS0568464258	01-Mar-2011	€272,000	98.50%	€267,920
Senior NAMA Bonds			**€2,891,000**		**€2,847,635**
Irish Government and Financial Institution Bonds					
Gov-Irl	IE00B6089D15	18-Oct-2019	€45,000	79.18%	€35,631
Gov-Irl	IE00B3KWYS29	15-Jan-2014	€15,000	86.09%	€12,914
Gov-Irl	IE00B60Z6194	18-Oct-2020	€150,000	70.65%	€105,975
Gov-Irl	IE0006857530	18-Apr-2016	€277,000	80.20%	€222,154
AIB	XS0484576813	04-Feb-2013	€5,000	82.91%	€4,146
AIB	XS0496222877	19-Mar-2015	€28,000	70.41%	€19,715
Anglo	XS0502258790	15-Apr-2015	€50,000	70.10%	€35,050
BOI	XS0482810958	28-Jan-2015	€53,350	72.56%	€38,711
BOI	XS0456135184	08-Apr-2013	€21,000	76.10%	€15,981
BOI	XS0555679728	05-Mar-2013	€31,000	87.89%	€27,246
EBS	XS0490069266	25-Feb-2015	€25,000	71.74%	€17,935
IL&P	XS0504108118	22-Apr-2013	€17,600	81.16%	€14,284
IL&P	XS0493444060	10-Mar-2015	€72,370	70.74%	€51,195
Total Other Bonds			**€790,320**		**€600,935**

Table 1.2: Transaction Elements as of Close of Business on 17 February 2011

Total Liabilities	€'000s
Reference Date Retail Deposit Amount	2,717,615
Reference Date Corporate Deposit Amount	475,286
Reference Date IOM Deposit Amount	444,936
Target Net Assets (IOMCo Equity)	110,332
IOMCo Other Liabilities	2,743
Total Liabilities	**3,750,912**

Total Assets Available to Match Liabilities	€'000s
Senior NAMA Bonds	2,847,635
Irish Government Bonds	600,935
Total Assets - Sub Total	**3,448,570**
Residual Requirement	**302,342**
Loans and Advances to Customers in IOMCo	1,500
Tangible Fixed Assets in IOMCo	530
Other Assets in IOMCo	81
Residual Cash Requirement	**300,231**
of which Cash Already in IOMCo	135,006
Deficit of Assets Versus Liabilities	**165,225**

Consideration Paid for Each Deposit Book	% of Deposit Book	€'000s
Irish Retail Deposit Book	2.0%	54,352
Corporate Deposit Book	0.6%	2,852
IOM Deposit Book	0.0%	-
Element of Consideration Relating to Deposit Book (A)		**57,204**

Consideration Paid for IOM Equity	€'000s
Current Estimated IOM Book Value	110,332
Element of Consideration Relating to IOM Equity (B)	**110,332**
Deficit of Assets Versus Liabilities (C)	**(165,225)**
Net Consideration (= A + B + C)	**2,311**

The following definitions shall apply for the purposes of the calculations in Schedule 3:

"**Corporate Deposit Valuation Factor**" means 0.6 per cent.;

"**IOM Deposit Valuation Factor**" means 0.0 per cent.; and

"**Retail Deposit Valuation Factor**" means two per cent..

Schedule 2

Transfer Support Agreement

Schedule 3

Adjustments to Transaction Elements

1. Within five (5) days of the Transfer Date, INBS shall prepare and deliver to ILP the Certificate confirming the following:

   (i) the Calculation Time Retail Deposit Amount;

   (ii) the Calculation Time Corporate Deposit Amount;

   (iii) the Calculation Time IOM Deposit Amount;

   (iv) the IOMCo Net Assets;

   (v) the Asset Package Interest;

   (vi) the Adjustment to Transaction Elements; and

   (vii) the Total Adjustment.

2. If the Total Adjustment is positive, ILP shall pay to INBS an amount equal to the Total Adjustment, which amount shall be settled by ILP transferring to INBS Irish Government Bonds (as selected by INBS from the Irish Government Bonds set out in Table 1.1 of Schedule 1), valued at their Prescribed Value, with the remaining balance of the Total Adjustment (if any) to be paid by ILP in cash provided always that the maximum possible amount of Irish Government Bonds shall be selected by INBS so as to minimise the amount of any cash payment required under this paragraph 2. If the Total Adjustment is negative, INBS shall pay to ILP an amount equal to the Total Adjustment (taking the absolute number and disregarding that it is negative), which amount shall be settled by INBS transferring to ILP Selected Irish Government Bonds (the "**Selected Irish Government Bonds**") with ISIN: IE0034074488 valued at 68.91% of nominal value plus accrued interest with the remaining balance of the Total Adjustment (if any) to be paid by INBS in cash provided always that the maximum possible amount of Irish Government Bonds shall be selected by INBS so as to minimise the amount of any cash payment required under this paragraph 2. The "**Prescribed Value**" of an Irish Government Bond for the purposes of this paragraph 2 means the aggregate of: (a) the value of that bond determined by applying the Relevant Percentage applicable to it to the aggregate nominal amount of the bond to be transferred; and (b) the accrued interest on that aggregate nominal amount. The "**Relevant Percentage**" applicable to an Irish Government Bond for the purposes of this paragraph 2 is the percentage set out opposite that bond under the heading 'Value as % of Nominal Value Prescribed by ILP' in Table 1.1 of Schedule 1.

3. All payments and/or transfers required to be made under this Schedule 3 shall be made by INBS or (as the case may be) ILP within five (5) days of the delivery of the Certificate to ILP, such delivery to be effected in accordance with the Transfer Support Agreement.

4. All transfers by ILP of Irish Government Bonds or by INBS of Selected Irish Government Bonds with ISIN: IE0034074488 shall be effected as beneficial owner and free from all Encumbrances.

5. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the Calculation Time Retail Deposit Amount exceeds the Reference Date Retail Deposit Amount, ILP shall pay to INBS an amount equal to the excess amount multiplied by the Retail Deposit Valuation Factor and INBS shall pay to ILP an amount equal to the excess amount.

6. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the Reference Date Retail Deposit Amount exceeds the Calculation Time Retail Deposit Amount, INBS shall pay to ILP an amount equal to the excess amount multiplied by the Retail Deposit Valuation Factor and ILP shall pay to INBS an amount equal to the excess amount.

7. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the Calculation Time Corporate Deposit Amount exceeds the Reference Date Corporate Deposit Amount, ILP shall pay to INBS an amount equal to the excess amount multiplied by the Corporate Deposit Valuation Factor and INBS shall pay to ILP an amount equal to the excess amount.

8. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the Reference Date Corporate Deposit Amount exceeds the Calculation Time Corporate Deposit Amount, INBS shall pay to ILP an amount equal to the excess amount multiplied by the Corporate Deposit Valuation Factor and ILP shall pay to INBS an amount equal to the excess amount.

9. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the Calculation Time IOM Deposit Amount exceeds the Reference Date IOM Deposit Amount, ILP shall pay to INBS an amount equal to the excess amount multiplied by the IOM Deposit Valuation Factor.

10. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the Reference Date IOM Deposit Amount exceeds the Calculation Time IOM Deposit Amount, INBS shall pay to ILP an amount equal to the excess amount multiplied by the IOM Deposit Valuation Factor.

11. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the IOMCo Net Assets exceed the Target Net Assets, ILP shall pay to INBS an amount equal to EUR1 for each EUR1 of the excess.

12. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, if the Target Net Assets exceed the IOMCo Net Assets, INBS shall pay to ILP an amount equal to EUR1 for each EUR1 of the excess.

13. Subject to and in accordance with paragraphs 2 and 3 of this Schedule 3, ILP shall pay to INBS the Asset Package Interest.

14. For the purposes of determining the adjustments in paragraphs 11 and 12 of this Schedule 3, all Sterling amounts will be translated from Sterling to EUR at the Relevant Exchange Rate.

15. ILP shall permit INBS full access to the Records in order to allow INBS to prepare the Certificate in accordance with this Schedule 3.

16. For the purposes of this Schedule 3 the following terms shall have the meanings given to them below:

   "**Adjustment to Transaction Elements**" means any amount determined for the purposes of paragraphs 5 to 13 (both inclusive);

   "**Asset Package**" means the Financial Assets;

   "**Asset Package Interest**" means the aggregate amount of interest accrued on the Senior NAMA Bonds and the Other Bonds included in the Financial Assets at a time that is as close as is practicable to the Calculation Time;

   "**Calculation Time**" means 00.01 hours on the day immediately following the Transfer Date;

   "**Calculation Time Retail Deposit Amount**" means the total nominal amount of all Retail