

The German Bad Bank Legislation

July 2009

Speed read

- The German parliament has adopted "bad banks" legislation, which is expected to take effect shortly.
- The German bad bank concept comprises two principal schemes. The first is a scheme (**SPV Scheme**) involving a transfer of impaired structured securities from a financial institution to an institute-specific special purpose vehicle (**SPV**) in exchange for a bond guaranteed by the governmental rescue fund (**SoFFin**). The second is a scheme (**Consolidation Scheme**) under which risk positions or non-strategic business divisions of a financial institution may be transferred with legal or economic effect to a public law liquidation sub-agency (*Anstalt in der Anstalt - AidA*) formed on an institute-specific basis by and under the umbrella of the governmental Financial Market Stabilisation Agency (**FMSA**).
- While the SPV Scheme is particularly, but not exclusively, designed for private sector financial institutions, the Consolidation Scheme is expected to be used primarily by public sector banks (*Landesbanken* and *Sparkassen*).
- In addition, the deadline for SoFFin to make available the majority of the other existing financial market stabilisation measures, including the popular guarantee for new bank debt, has been extended by one year to 31 December 2010.
- Participation in the schemes is voluntary.
- As an additional measure to strengthen the regulatory capital base of German banks, the Ministry of Finance is proposing to eliminate the requirement to deduct losses on certain financial assets from the regulatory capital.

I. Introduction

On 13 May 2009, the German Federal Government adopted the first draft "bad bank" bill introducing the SPV Scheme (see our Client Bulletin of May 2009). On 10 June 2009, it adopted a second draft "bad bank" bill introducing the Consolidation Scheme. Both draft bills were introduced into, debated and amended during the parliamentary approval process.

On 3 July 2009, the German Parliament (*Deutscher Bundestag*) adopted the consolidated "bad bank" bill to implement both the SPV Scheme and the Consolidation Scheme. The Second Chamber (*Bundesrat*) approved the bill on 10 July 2010. It is expected that the legislation will take effect in the very near future.

The German "bad bank" legislation now comprises two principal schemes:

(i) first, the SPV Scheme which enables Germany's institutions to divest their impaired structured securities; and

(ii) second, the Consolidation Scheme under which risk positions or even non-strategic business divisions of an institution may be transferred with legal or economic effect to a public law liquidation sub-agency (AidA). For that purpose, the FMSA will become a federal public agency with full legal capacity.

The SPV Scheme is primarily, but not exclusively, designed for private sector financial institutions, whereas the Consolidation Scheme is expected to be used mainly by public sector banks. Participation in both schemes is voluntary. The deadline for SoFFin and FMSA to make available both schemes is 31 December 2010.

At the same time, the legislator has extended the deadline for SoFFin to make available the majority of the other financial market stabilisation measures to 31 December 2010.

As an additional step to strengthen the regulatory capital base of German banks, the Ministry of Finance is currently proposing to eliminate the requirement to deduct from core capital negative revaluation reserves in accordance with IAS 39. The Ministry proposes that unrealised losses on certain financial instruments, including loans, other receivables and bonds, categorised as available for sale financial assets, need no longer be deducted. The new rule which follows similar regulations in the United Kingdom and France would only have an effect on those banks that prepare that report to the Federal Financial Services Supervisory Authority (**BaFin**) on the basis of consolidated accounts in accordance with IFRS, which will exclude many of the German savings banks (*Sparkassen*) and German State Banks (*Landesbanken*). Banking representatives have proposed an extension to this amendment to include all banks, including banks which report to BaFin on the basis of German GAAP. The proposed amendment does not require parliamentary approval and would have an immediate effect on the core capital of banks.

II. The SPV Scheme

The SPV Scheme works as follows:

1. Transferor Entity

- Both private and public sector banks and financial holding companies domiciled in Germany on or before 31 December 2008, and their German and foreign subsidiaries (each a **Transferor Institution**), may participate in the SPV Scheme.

2. Transferee Entity

- A Transferor Institution may set up an institute-specific SPV to which eligible assets may be transferred.
- The SPV must be incorporated in Germany.
- The SPV will not be a regulated entity. It is expected that the SPV will not engage in licensable activities and will therefore not require a banking license.

3. Transferable Assets and Transfer Procedures

- Only structured securities (**Structured Securities**) and related hedges held at 31 December 2008 are eligible for transfer under the SPV Scheme.

- Structured Securities are defined generally as being characterised by high complexity and issued typically to securitise a portfolio of receivables, including ABS, CDO, CDOs of ABS, CLO, RMBS and CMBS. There are no restrictions on the maximum term to maturity of the Structured Securities.
- The Transferor Institution will transfer the impaired Structured Securities to the SPV in exchange for new debt securities issued by the SPV and guaranteed by SoFFin (the **Guaranteed Securities**). The transfer price of the Structured Securities will be equal to the issue price of the Guaranteed Securities.
- During the legislative process, the provisions on the transfer price of the Structured Securities have improved significantly in favour of Transferor Institutions. The specific transfer price of the Structured Securities will be the higher of (a) 90 % of their book value as of 30 June 2008, (b) 90 % of their book value as of 31 March 2009, and (c) their real economic value, provided that in all these cases the transfer price must not exceed the book value as of 31 March 2009. The recognition of 30 June 2008 as a reference date was introduced in the legislative process and to enable Transferor Institutions to transfer Structured Securities at 90 % of their book value as of that date (i.e. pre Lehman insolvency) if higher than their current book value, provided however that the transfer price is capped at 100 % of their book value as of 31 March 2009. The 10 % discount to book value will be applied only to the extent that the Transferor Institution would maintain a core capital ratio of at least 7 % after taking into account the write-down resulting from the reduced transfer price.
- Before Structured Securities can be transferred to the SPV, their real economic value must be determined by the Transferor Institution, analysed by a recognized independent expert nominated by SoFFin and confirmed by BaFin.

4. Application and Decision Making Process

- The Transferor Institution must apply for the SoFFin guarantee for the securities issued by the SPV within six months after publication of the law in the Federal Legal Gazette (*Bundesanzeiger*).
- The application must contain the incorporating documents of the SPV.
- The Transferor Institution must make full disclosure to SoFFin, the recognized independent ex-

pert and BaFin of the risks of the Structured Securities.

- The SoFFin guarantee will be issued only if the Transferor Institution demonstrates a viable business model and adequate capitalisation.
- The Transferor Institution or, if it is a subsidiary, its parent company must undertake stress tests. The results of the stress tests will not be published.
- SoFFin may impose substantially the same conditions as those applicable to recapitalisation measures, such as restrictions on executive compensation and obligations to restrict or dispose of certain business activities.
- SoFFin may require that the impaired Structured Securities be administered by a third party rather than the Transferor Institution. In any event, SoFFin is entitled to instruct the entity administering the assets. The law does not prescribe how the Structured Securities should be managed or which interests SoFFin should consider before giving instructions.
- The FMSA has discretion to decide whether or not a SoFFin guarantee will be granted, taking into account the relevance of the Transferor Institution to the stability of the financial market, the urgency of the matter, and ensuring the most efficient use of public funds. Applicants have no right to be supported by SoFFin.

5. Accounting

- Following the exchange of Structured Securities against Guaranteed Securities, the Structured Securities will be derecognised from the balance sheet of the Transferor Institution. Concerns potentially inhibiting a derecognition of those assets from the Transferor Institution's balance sheet were addressed and clarified during the legislative process. Any further depreciation in the value of the Structured Securities will therefore not lead to further write-downs of the value of the impaired assets on the Transferor Institution's balance sheet, thus also eliminating the need for the Transferor Institution to raise additional capital to make up for such write-downs.

6. Liability and Costs

- The legislation contains a multi-step process to cover losses on the Structured Securities following their transfer to the SPV.
- The Transferor Institution (or, if its is a subsidiary, its parent company) will be required to pay

the difference between the transfer price and the Fundamental Value (as defined below) out of its future distributable profits. The difference is payable in equal annual instalments, calculated on the basis of the duration of the guarantee, with a maximum of 20 equal annual instalments. If, in a given year, the Transferor Institution is not profitable enough to pay an annual instalment in full or in part, the amount of future instalments will increase accordingly.

- The **Fundamental Value** of the Structured Securities will be determined prior to a transfer of the Structured Securities on the basis of the real economic value of the Structured Securities minus an additional reasonable discount to reflect further risks in connection with the Structured Securities as determined by SoFFin.
- If, after all of the Structured Securities have matured or have been sold, the receipts from the Structured Securities are lower than the Fundamental Value, the holders of the Guaranteed Securities may call upon the SoFFin guarantee in the amount of such shortfall. The Transferor Institution will have to use any future annual surplus to make payments to SoFFin in order to compensate SoFFin for the payments under the guarantee. Until SoFFin has been fully compensated, distributions to shareholders will be prohibited.
- When all Structured Securities have matured or have been sold, the Guaranteed Securities may be redeemed and the SPV can be liquidated. Any liquidation surplus must be paid to the Transferor Institution for distribution to its shareholders.
- The guarantee is available only for a fee at market terms. In principle this is an individual percentage of the maximum amount of the guarantee, calculated on the basis of the risk of loss arising out of utilisation of the guarantee, and a margin. The time value of the Transferor Institution paying instalments must also be taken account. The fee can be paid in shares of the Transferor Institution.

7. Tax Treatment

- The legislation contains special tax provisions to support the intended relief of a Transferor Institution participating in the SPV Scheme.
- The transfer of the Structured Securities can be effected in a tax neutral manner since the book value will be the relevant criterion.

III. The Consolidation Scheme

The Consolidation Scheme works as follows:

1. Transferor Entity

- Private and public sector banks, financial holding companies, their subsidiaries and special purpose vehicles to which such institutions have transferred risk positions (each a **Transferor Entity**) may participate in the Consolidation Scheme.
- Banks and financial holding companies must have been domiciled in Germany on or before 31 December 2008, while subsidiaries and special purpose vehicles can also be domiciled outside Germany.

2. Transferee Entity (AidA)

- Upon request of an eligible institution, the FMSA may in its discretion establish an AidA (*bundesrechtliche Abwicklungsanstalt*) which is partly vested with legal capacity and organised as a federal public sub-agency within the FMSA.
- An AidA may enter into contracts in its own name and may be a party in legal proceedings. Each AidA will have its own accounts and must be registered in the commercial register. The assets of an AidA are separate and ring-fenced from the assets of the FMSA and any other AidA.
- As a rule, neither the FMSA, the SoFFin nor the government are responsible for any liabilities incurred by an AidA (see exceptions under section 6., fourth, sixth and tenth bullet point).
- The FMSA will supervise each AidA and may impose regulations addressing the duties, organisation, liquidation, minimum capital requirements and the supervision of an AidA. Such regulations will be published in the Federal Legal Gazette (*Bundesanzeiger*).
- Neither the FMSA nor any AidA may conduct business that requires a license under the European Banking Directive (2006/48/EC) or the Markets in Financial Instruments Directive (2004/39/EC). This restriction does not, however, prevent the transfer of risk positions or non-strategic business divisions that do not involve public deposit taking.
- Under the new law, an AidA is not considered a credit institution, a financial services institution, a securities services firm or an insurance undertaking. Thus, an AidA is not subject to banking license or minimum regulatory capital require-

ments which otherwise would have applied in the case of a transfer of a financial institution's business division to another entity. However, certain other (non-capital related) regulatory provisions of the Banking Act and the Securities Trading Act apply and the AidAs are subject to the supervision of BaFin in this regard.

- AidAs may not engage in any business activities other than the liquidation of the assets transferred to them.
- The establishment of management bodies and the appointment of managers of an AidA are subject to the FMSA's consent.

3. Transferable Assets and Transfer Procedures

- Under the Consolidation Scheme, a Transferor Entity may transfer to an AidA risk positions and business divisions that are not vital for the Transferor Entity's business strategy (collectively, the **Assets**).
- Risk positions are not limited to structured securities (as in case of the SPV Scheme) but include, in particular, receivables, securities, derivative financial instruments, rights and obligations under loans or guarantees and equity participations. There are no restrictions on the maximum term to maturity of the relevant Assets.
- Risk positions are eligible for transfer only if they had been acquired by a Transferor Entity on or before 31 December 2008.
- The transfer of the Assets can be effected either by way of universal succession in case of a transformation (*Umwandlung*) for liquidation purposes or by way of transfer of individual assets ("asset deal").
- A universal succession can take the form of a split-off (*Abspaltung*) or a spin-off (*Ausgliederung*) under the Transformation Act (*Umwandlungsgesetz*), which will apply in modified form.
- As consideration for the transfer of the Assets to an AidA, an interest in the AidA itself or a compensation payment can be granted to the direct or indirect shareholders or members (**owners**) of the Transferor Entity (in case of a split-off) or the Transferor Entity itself (in case of a spin-off).
- The legal reasoning describes the basic concept that the transfer shall take place at the current book value of the assets.
- A transfer of the Assets to an AidA by way of universal succession requires at least majority

owners' consent. However, if the universal succession will result in the direct or indirect owners assuming a loss compensation obligation or other personal liability for the Assets transferred, the consent of all affected owners is required.

- In order to facilitate and support the transfer of Assets by way of transformations, the bill provides that certain provisions of the Transformation Act, in particular those stipulating the joint and several liability of the transferor and transferee entities and the creditors' right to demand collateral to be provided, will not apply.
- In addition to a transfer of the Assets by universal succession or true sale, an AidA may also assume risk or provide risk protection in favour of the Transferor Entity by way of trust arrangements, guarantees, sub-participations or otherwise, thus becoming the economic owner of the Assets ("synthetic risk transfer").

4. Application and Decision Making Process

- The Transferor Entity must apply for the transfer of the Assets to an AidA. Different from the SPV Scheme, there is no separate deadline for applications for participation in the Consolidation Scheme (notwithstanding 31 December 2010 as general deadline).
- The Transferor Entity must make full disclosure of the risks of the Assets towards FMSA.
- A transfer of Assets under the Consolidation Scheme will only be possible if (i) the Transferor Entity, or in case of a transfer by a special purpose vehicle, the financial institution, demonstrates a viable business model and adequate capitalisation, (ii) a liquidation plan for the AidA in relation to the liquidation of the transferred Assets has been implemented, (iii) the Transferor Entity or, in case of a subsidiary, its parent company, has conducted stress tests in relation to the risks associated with the Assets, and (iv) it is ensured that the Transferor Entity or its direct or indirect owners remain fully liable in relation to the Transferor Entity's employees and the related pension and other employment related obligations.
- The FMSA may impose substantially the same conditions as those that apply to recapitalisation measures, such as restrictions on executive compensation and obligations to restrict or dispose of certain business activities.
- Further, the FMSA may impose principles as to the risk assessment, the refinancing and the sale

(without raising any undue market price influence) of the Assets. Notwithstanding the foregoing, an AidA is responsible for administering the transferred Assets.

- The FMSA has discretion to determine whether or not an AidA will be established and which Assets will be transferred, taking into account the relevance of the Transferor Entity for stability in the financial market, the urgency of the matter, and the objective of the most efficient use of public funds. Applicants have no right to be supported by the FMSA.

5. Accounting

- For AidAs the German generally accepted accounting standards (German GAAP) shall apply. As a consequence, AidAs are not subject to the market value depreciation provisions under IFRS. Each AidA will keep its own accounts, and there will be no group-wide accounting at the level of the FMSA.
- Whether balance sheet relief for regulatory capital purposes can be achieved must be assessed on a case-by-case basis depending on the individual transaction structure.

6. Liability and Costs

- In most cases, a transfer of Assets to an AidA will be permissible only if the direct or indirect owners of the Transferor Entity or, in case of a transfer by a special purpose vehicle, the direct or indirect owners of the financial institution having transferred the risk positions, assume the joint and several liability to compensate the relevant AidA for any losses incurred by it. Further, the direct or indirect owners may agree to assume personal liability regarding the Assets transferred.
- As between the owners, the internal loss sharing quota will be determined pro rata to their participation in the Transferor Entity. The owners may agree a disproportionate loss share quota, subject to compliance with EU state aid requirements.
- Any losses not recoverable from the owners must be compensated by the Transferor Entity out of distributable profits.
- In addition, it may be agreed that the FMSA will initially compensate an AidA for any losses incurred (and not recovered), and then take recourse against the Transferor Entity and/or its direct or indirect owners.

- Special liability provisions apply if one of the direct or indirect owners of a Transfer Entity is a German Federal State (*Bundesland*), as is the case for the German State Banks (*Landesbanken*). In such cases, the direct or indirect owners shall be obliged to compensate the relevant AidA for losses, pro rata to their ownership interest in the Transferor Entity, but no joint and several liability shall be imposed in this regard.
- Moreover, special liability provisions apply in relation to organisations of public savings banks or their holding companies (**Sparkassen**) as direct or indirect owners of a Transferor Entity. In such cases, any losses incurred by the relevant AidA shall be compensated in the following order: (i) first, by the Transferor Entity out of distributable profits (step 1); (ii) second, if the step 1 compensation is not sufficient to cover the losses incurred, the remaining losses shall be compensated by the Sparkassen (step 2), provided that the aggregate loss compensation liability of the Sparkassen shall be capped at an amount corresponding to their public law loss compensation obligation (*Gewährträgerhaftung*) for the relevant Transferor Entity as of 30 June 2008; (iii) third, the losses not covered by step 1 and step 2 shall be initially financed by the FMSA and then be refinanced in subsequent years out of the distributable profits otherwise payable to the Sparkassen (step 3); and (iv) finally, any remaining financial burdens shall be borne by the Federal Republic of Germany and the relevant Federal State in the ratio of 65:35.
- If, due to the fact that a Transferor Entity is widely held (e.g. in case of listed companies), it is not practicable for its owners to assume a loss compensation obligation, then the Transferor Entity itself, or in case of a transfer by a special purpose vehicle or a subsidiary, the financial institution, shall be obliged to assume the obligation to compensate any losses incurred by the relevant AidA, provided, however, that such loss compensation shall be exclusively paid out of distributable profits.
- The Transferor Entity's owners are entitled to any profit after the completion of the liquidation of the transferred Assets.
- Irrespective of the above loss compensation obligations, the FMSA may determine the amount and type of consideration payable for the transfer of the Assets or the risk protection provided in relation to the Assets.
- SoFFin may guarantee (non-tradable) bonds and other obligations incurred by an AidA solely for the purpose of refinancing the acquisition of structured securities. No such guarantee will be available in relation to the refinancing of other Assets. Further, as direct or indirect owner of a Transferor Entity, SoFFin may assume loss compensation obligations towards an AidA or personal liability regarding transferred Assets.
- The cost for the set-up and the on-going management of an AidA will be payable out of the assets of such AidA. Since the Transferor Entity or its owners remain liable for losses of their AidA, they will also be ultimately liable for these costs. In addition, AidAs are required to pay contribution fees to BaFin pursuant to the Financial Services Supervision Act.

7. AidAs established under Federal State Law

- The Federal States may establish their own AidAs under their federal state law (*landesrechtliche Abwicklungsanstalten*) to which risk positions acquired on or before 31 December 2008 and non-strategic business divisions of a Transferor Entity may be transferred, subject to full risk disclosure, a viable business model and adequate capitalisation. Except for the above requirements and the fact that federal state AidAs must not conduct business that requires a financial services license under European law, the Federal States have broad discretion how to set up a federal state AidA. In particular, the provisions regarding liability (see section 6 above) do not apply for AidAs established under the laws of a Federal State. No SoFFin guarantee (see before, section 6, tenth bullet point) is available to secure obligations incurred by a federal state AidA.

8. Tax Treatment

- The legislation contains special tax provisions to support the intended relief of a Transferor Entity participating in the Consolidation Scheme.
- The transfer of risk positions and non-strategic business divisions can be effected in a tax neutral manner since the book value will be the relevant criterion.

IV. Comparison of Both Schemes

The following comparison is meant as an overview only. For further details please see sections II. and III. above.

	SPV Scheme	Consolidation Scheme
Who is entitled to participate in the schemes as transferor ?	German banks, financial holding companies domiciled in Germany on or before 31 December 2008 and their German and foreign subsidiaries.	Idem, even if an institution has acquired risk positions from a (German or foreign) subsidiary or special purpose vehicle in order to participate in the Consolidation Scheme. In addition, special purpose vehicles to which such institutions have transferred risk positions.
Which assets are eligible?	Only structured securities (such as ABS, CDO, CDOs of ABS, CLO, RMBS and CMBS) and related hedges held by the transferor at 31 December 2008. No restrictions on the maximum term to maturity of the structured securities.	Individual risk positions (such as receivables, securities, derivative financial instruments, rights and obligations under loan or guarantee commitments and equity participations) acquired by the transferor on or before 31 December 2008 and non strategic business divisions. No restrictions on the maximum term to maturity of the relevant assets.
What type of entity may act as transferee ?	A newly founded, institute-specific special purpose vehicle (SPV) located in Germany.	The Financial Markets Stabilisation Agency (FMSA) will form an institute-specific liquidation sub-agency (AidA) under public law which is partly vested with legal capacity.
Are these entities supervised ?	SPVs will not be regulated and will not require a banking license.	AidAs are supervised by the FMSA to ensure compliance with law and statutes. No banking license is required and no minimum regulatory capital requirements are applicable, while certain (non capital related) regulatory rules apply (insofar subject to BaFin supervision). AidAs are not allowed to engage in deposit taking or the issuance of <i>Pfandbriefe</i> .
What transfer procedures apply?	Transfer of impaired structured securities to an SPV in exchange for new debt securities issued by the SPV and guaranteed by SoF-Fin.	Transfer of assets can be effected either by way of universal succession in the case of a transformation (<i>Umwandlung</i>) for liquidation purposes or by way of transfer of individual assets (asset deal). Transformation can take the form of a split-off (<i>Abspaltung</i>) or a spin-off (<i>Ausgliederung</i>). Furthermore, synthetic risk transfers are possible, e.g. by way of trust arrangements, guarantees, or sub-participations.
What consideration will the transferor receive in exchange for the transferred assets?	Structured Securities shall be transferred to the SPV at the higher of (a) 90 % of their book value as of 30 June 2008, (b) 90 % of their book value as of 31 March 2009, and (c) their real economic value, provided that in all these cases the transfer price must not exceed the book value as of 31 March 2009. No 10 % discount to book value will be made to the extent otherwise resulting in a decrease of transferor's core capital ratio below 7 %.	As consideration for the transfer of assets by way of transformation, an interest in the AidA or a compensation payment can be granted to the direct or indirect owners of the transferor or the transferor itself. In addition, FMSA may determine appropriate consideration.

Who will be liable for losses on the transferred assets?	The transferor or its shareholders, respectively, shall be liable for losses in two steps: First, anticipated losses (due to future depreciations) shall be compensated by way of annual payments out of distributable profits. Secondly, further losses incurred at maturity will have to be compensated out of future distributable profits; in this period of time distributions to shareholders will be prohibited.	As a rule, the direct or indirect owners of the transferor institution will be required to assume the joint and several liability to compensate for any losses incurred by the relevant AidA; the internal loss sharing quota is to be determined pro rata to their participation in transferor. If, due to the transferor entity being widely held, loss compensation by owners is not practicable, then the transferor itself shall be obliged to compensate for any losses, payable out of distributable profits only.
How will the capital relief for the institutions be achieved?	Following the exchange of the impaired structured securities against SoFFin guaranteed securities, the structured securities are derecognised from the balance sheet of the transferor. Therefore, any further depreciation of their value will not lead to further write-downs, thus also eliminating the need to raise additional capital to make up for such write downs.	Due to the variety of structuring alternatives no uniform approach to regulatory capital relief will be used in the consolidation scheme. In general, it is expected that the assets will be transferred to an AidA at the current book value of the assets and that the transfer will be structured in a way to allow for a derecognition of those assets from the balance sheet, thus eliminating the need for the transferor to raise additional capital in case of further depreciation of the value of the transferred assets. Since AidA shall use the German generally accepted accounting standards (German GAAP), there will be no need to adjust the value of the transferred assets as a result of temporary market fluctuations.
Who will profit from any gains of the impaired assets?	When all structured securities have matured or have been sold, the SoFFin guaranteed securities may be redeemed and the SPV can be liquidated. Any liquidation surplus must be paid to the transferor for distribution to its shareholders.	Any profit after the completion of the liquidation of the transferred assets shall be distributed to the transferor or its owners.
Is participation in the schemes compulsory ?	No. Participation is voluntary.	No. Participation is voluntary.
Is there a deadline for applications?	Yes. Application must be filed within six months after publication of the law the Federal Legal Gazette.	No, except for general deadline that FMSA may only make available stabilisation measures prior to 31 December 2010.
Which requirements must be met before a stabilisation measure may be used?	The application for the SoFFin guarantee must contain the formation documentation of the SPV. Full disclosure of the risks of the transferred securities towards SoFFin, the recognized independent expert and BaFin is required. The SoFFin guarantee will be issued only if the transferor demonstrates a viable business model and adequate capitalisation. Applicants have no right to be supported by SoFFin.	The establishment of an AidA must be applied for by the transferor. The transferor must make full disclosure of the risks of the transferred assets and business divisions towards the FMSA. An AidA will only be established if the transferor demonstrates a viable business model and adequate capitalisation and provide a detailed plan for the liquidation of the transferred assets and business divisions. The transferor or its owners remain responsible for the employees as well as for pension and other employment related liabilities. Applicants have no right to be supported by FMSA.

Is there a need to pass a stress test prior to using the stabilisation measure?	Yes. The transferor or, if it is a subsidiary, its parent company, will be required to undertake stress tests in relation to material risks. The results will not be published.	Idem.
What other conditions needs the transferor to comply with?	Restrictions under financial markets stabilisation legislation, e.g. regarding executive compensation, may be imposed.	Idem. In addition, <i>Landesbanken</i> shall only be allowed to use the Consolidation Scheme if the German Federal States (<i>Bundesländer</i>) holding participations therein have confirmed their intention to revise the <i>Landesbanken</i> structure and first steps of consolidation are emerging, leading to a significant reduction in total assets of the participating banks. The same rules shall apply in relation to other banks where overcapacity exists.
Is there a distinction between public sector banks and private banks?	The SPV Scheme is primarily designed for private sector financial institutions although the law is flexible enough as to allow other banks to use this scheme as well.	The Consolidation Scheme is expected to be used primarily by public sector banks although it is also available for private sector banks.
How will the transferred assets be managed ?	SoFFin may require that the impaired structured securities be administered by a third party rather than the transferor. SoFFin is entitled to give instructions to the entity administering the assets.	In principle, each AidA is responsible for the management of its own assets. In addition, the FMSA may impose principles as to the risk assessment, the refinancing and the sale (without causing any undue market price influence) of the acquired assets.
Are these schemes available free of charge ? Who will bear the costs of the transfer and the on-going costs of the transferee?	No. The guarantee is available only for a fee at market terms. The fee can be paid in shares of the transferor.	No. The cost for the set-up and the on-going management of an AidA will be payable out of the assets of such AidA. Since the transferor or its owners remain liable for an AidA's losses, they will also be ultimately liable for these costs. AidAs are required to pay contribution fees to BaFin pursuant to the Financial Services Supervision Act.

<p>Key contacts</p> <p>If you require advice on any of the matters raised in this document, please call any of our partners or your usual contact at Allen & Overy LLP.</p>	<p>Dr. Hartmut Krause Partner Tel. +49 (0)69 2648 5782 hartmut.krause @allenoverly.com</p> <p>Dr. Stefan Henkelmann Associate Tel. +49 (0)69 2648 5997 stefan.henkelmann @allenoverly.com</p>	<p>Peter H. Hoegen Partner Tel. +49 (0)69 2648 5905 peter.hoegen @allenoverly.com</p> <p>Martin Scharnke Associate Tel. +49 (0)69 2648 5835 martin.scharnke @allenoverly.com</p>	<p>Okko Hendrik Behrends Partner Tel. +49 (0)69 2648 5947 okko.behrends @allenoverly.com</p>
----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------	---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------	--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------	---------------------------------------------------------------------------------------------------------------------

Allen & Overy LLP

Breite Straße 27 40213 Düsseldorf Tel. +49 (0)211 2806 7000 www.allenoverly.com
 Taunustor 2 60311 Frankfurt am Main Tel. +49 (0)69 2648 5000 www.allenoverly.com
 Kehrwieder 12 20457 Hamburg Tel. +49 (0)40 82 221 20 www.allenoverly.com
 Erzbergerstraße 5 68165 Mannheim Tel. +49 (0)621 3285 631 www.allenoverly.com
 Maximilianstraße 35 80539 München Tel. +49 (0)89 71043 3000 www.allenoverly.com

Allen & Overy maintains a database of business contact details in order to develop and improve its services to its clients. The information is not traded with any external bodies or organisations. If any of your details are incorrect or you no longer wish to receive publications from Allen & Overy, please contact hartmut.krause@allenoverly.com.

In this document **Allen & Overy** means Allen & Overy LLP and/or its affiliated undertakings. The term **partner** is used to refer to a member of Allen & Overy LLP or an employee or consultant with equivalent standing and qualifications, or an individual with equivalent status in one of Allen & Overy LLP's affiliated undertakings.

Allen & Overy LLP or an affiliated undertaking has an office in each of: Abu Dhabi, Amsterdam, Antwerp, Bangkok, Beijing, Bratislava, Brussels, Bucharest (associated office), Budapest, Dubai, Düsseldorf, Frankfurt, Hamburg, Hong Kong, London, Luxembourg, Madrid, Mannheim, Milan, Moscow, Munich, New York, Paris, Prague, Riyadh (associated office), Rome, São Paulo, Shanghai, Singapore, Tokyo, Warsaw.

© Allen & Overy LLP 2009. This document is for general guidance only and does not constitute definitive advice. | FR:4998672.3