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# Handling Distressed Banks in Denmark

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## INTRODUCTION AND SUMMARY

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The Danish resolution scheme for handling distressed banks has attracted much attention, both in Denmark and abroad. The scheme came into force on 1 October 2010, at which date the general government guarantee expired. The scheme has been applied twice. Both cases related to banks which had granted a large number of risky credits ahead of the financial crisis. This was the reason that they were no longer able to meet the capital requirements.

The resolution scheme implies that ordinary customers will not notice any difference in the practical side of their day-to-day banking business, even if their bank becomes distressed. The scheme constitutes a controlled winding-up of a distressed bank, taking sufficient time to end activities in an orderly manner with the lowest possible losses for its creditors. It is not desirable to wind up a bank via compulsory liquidation, as this would mean that the depositors would have their payment cards cancelled and that borrowers' loans would be called. Moreover, compulsory liquidation proceedings take many years, during which creditors have no access to their funds.

The resolution scheme offers an alternative to compulsory liquidation and addresses a number of the practical challenges involved. However, creditors still have a risk of loss if a bank becomes distressed. This means that they have to take into account the risk profile of the individual bank, when they consider depositing sizeable amounts and purchasing bank bonds etc. Accordingly, the banks are motivated to limit their risks to obtain access to cheaper funding. Over time, the scheme will contribute to a healthier and stronger banking sector, which can stand on its own feet.

A transfer of a distressed bank to another bank is usually to be preferred, but uncertainty about the quality of the credits granted may be so significant that it is not possible to find a buyer. Therefore, the resolution scheme is only relevant if a market solution cannot be found.

With the resolution scheme, a distressed bank will be wound up without any financial risk for the Danish government. However, for the banks that have bought individual government guarantees under Bank

Rescue Package 2, the government could suffer a loss on equal terms with other non-subordinated creditors.

In principle, all Danish banks can decide to make use of the scheme if they become distressed. However, some banks are so important to the overall economy that neither the resolution scheme nor compulsory liquidation would be considered desirable.

In August 2011, a broad majority in the Folketing (Danish parliament) agreed to set up a committee to prepare the future rules on systemically important banks in Denmark. The committee will e.g. look into the criteria to be met for a bank to be systemic in Denmark, and the instruments that may be applied to systemically important banks facing difficulties.

## **BACKGROUND**

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The international financial crisis began in the summer of 2007 and was triggered by losses in the US subprime mortgage market. The crisis escalated in the autumn of 2008 when Lehman Brothers had to file for Chapter 11 bankruptcy. The collapse of Lehman Brothers shook the financial markets, which had expected the US authorities to save the investment bank, as had been the case with Bear Stearns earlier that year. This reinforced the reluctance between banks to lend to each other, and global money markets froze completely. In many countries, governments and central banks launched various crisis measures.

The lack of confidence in the interbank market also hit Denmark, and it became difficult for Danish banks to obtain funding abroad. During the years up to the financial crisis, when interest rates were low amid ample liquidity, several Danish banks had increased their lending much more than their deposits. These banks had become dependent on funding in the financial markets and had thus become vulnerable.

### **General government guarantee (Bank Rescue Package 1)**

In the autumn of 2008, the situation had become so critical that even sound banks had difficulty obtaining liquidity. Against this backdrop, a broad political majority entered into an agreement with the financial sector on a 2-year government guarantee in October 2008. The guarantee covered all depositors and other non-subordinated creditors in Danish banks as well as depositors in foreign banks' branches in Denmark until 30 September 2010. If a bank did not meet the capital requirements, it had to transfer all of its assets and non-subordinated liabilities to the state-owned winding-up company, the Financial Stability Company. Equity and subordinated capital, including Additional Tier 1 cap-

ital, would not be transferred, but would remain in the distressed bank. In return for the guarantee, the financial sector had to contribute up to kr. 35 billion. A potential profit in the Financial Stability Company would be reverted to the government. A total of eight Danish banks were taken over by the Financial Stability Company during the guarantee period.<sup>1</sup>

### **Government capital injections and individual guarantees (Bank Rescue Package 2)**

In February 2009, the Folketing adopted a new bank rescue package, under which Danish credit institutions could obtain government capital injections in the form of Additional Tier 1 capital. The background was deterioration of the economic conditions, which led to mounting pressure on the institutions' solvency. Due to the financial crisis, it was difficult to raise further capital in the international capital markets, and therefore the institutions could be forced to reduce their loans with a resultant risk of a credit crunch. When the scheme expired, capital injections had run into approximately kr. 46 billion, distributed among 43 institutions.

At the same time, a scheme was established, allowing Danish credit institutions to apply for individual government guarantees until 31 December 2010 for specific issuances with maturities of up to three years. The intention was to ensure that Danish credit institutions could raise liquidity, also after the expiry of the general guarantee. The scheme was intended to facilitate the transition to funding on normal market terms. As at 31 December 2010, 50 institutions had issued debt totalling kr. 193 billion with individual government guarantees. As at 30 June 2011, outstanding guarantees had been reduced to kr. 172 billion, primarily due to early redemptions.

### **The resolution scheme (Bank Rescue Package 3)**

The expiry of the general government guarantee on 30 September 2010 created a need to find a new model for winding up distressed banks. On the one hand, there was political consensus not to extend the general guarantee and that banks had to stand on their own feet again. The government guarantee was inevitable during the financial crisis, but would give rise to an inappropriate incentive structure in the sector in the long term. On the other hand, it would not be desirable to wind up

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<sup>1</sup> Capinordic Bank, EBH Bank, EIK Bank Danmark, EIK Banki Føroya P/F, Fionia Bank, Gudme Raaschou Bank, Løkken Sparekasse and Straumur Burdaras Investment Bank hf.

a distressed bank according to the rules laid down in the Danish Insolvency Act.

In June 2010, the Folketing therefore adopted a new scheme for handling distressed banks in an orderly manner. The scheme offers a clear alternative to compulsory liquidation in the form of controlled winding-up via the state-owned winding-up company, the Financial Stability Company.

## **ADVANTAGES OF THE RESOLUTION SCHEME**

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It is not desirable to wind up a bank via compulsory liquidation, as this would mean that the depositors would have their payment cards cancelled and that borrowers' loans would be called. Moreover, compulsory liquidation proceedings take many years, during which creditors have no access to their funds.

To avoid compulsory liquidation, distressed banks have previously been handled through ad hoc solutions with the government and Danmarks Nationalbank as active participants. To ensure sufficient time for an orderly winding-up, it has been necessary – unlike what applies to other private companies – to shield non-subordinated creditors from losses. The government and hence the taxpayers have instead covered the losses. The most recent example was in 2008 when Danmarks Nationalbank and the financial sector had to take over all assets and liabilities of Roskilde Bank except for Additional Tier 1 capital and Tier 2 capital.

Add to this the risk that the market perception will be that the government will always step in if a bank becomes distressed. This reduces the creditors' incentive to be aware of the risk assumed by the individual bank. Banks with high risk appetite would therefore be able to obtain funding on largely the same conditions as more conservative banks.

The absence of market discipline could cause the individual bank and the sector overall to assume inappropriately high risks. During periods of economic boom, the banks most willing to assume risk will tend to generate high returns. This puts pressure on more risk-averse banks to obtain the same return in the short term, thus pushing them to assume high risk. As a result, risk appetite in the sector may generally become too high.

Under the resolution scheme, a distressed bank can be wound up in a controlled and predictable manner without government involvement. The government can therefore only suffer a loss if it has assumed credit risk on a distressed bank, e.g. by issuance of an individual government guarantee. Basically, the risk of loss lies with the shareholders and the creditors. Consequently, each bank is motivated to limit its risks and

maintain an adequate capital buffer to obtain access to cheaper funding.

It has been said to pose a challenge that Denmark is the first European country to introduce a scheme involving a risk of loss for non-subordinated creditors. It is, however, worth noting that a uniform limit of 100,000 euro applies to coverage by the guarantee funds in all EU member states.

Danmarks Nationalbank attaches great importance to the European Commission's work to establish a common framework for crisis management. Overall, the future regulation is expected to pave the way for a system in which the use of public funds for the rescue of distressed banks is reduced. This could imply that non-subordinated creditors will contribute to bearing the losses when a bank becomes distressed, as is the case in Denmark today.

## THE RESOLUTION SCHEME IN GENERAL

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The resolution scheme will only be applied if it is not possible to find a market solution, cf. Box 1. In principle, market solutions and private transfers take precedence over using the resolution scheme, but uncertainty over the credits granted may be so substantial that it is not possible to find a buyer.

Winding-up under the resolution scheme presupposes that the bank no longer meets the regulatory capital requirements and that the Danish Financial Supervisory Authority has set a deadline for the bank's restoration of the capital. Therefore, the resolution scheme cannot be applied until the failure of the bank is imminent and inevitable.

The resolution scheme ensures that the distressed bank can transfer its activities to the Financial Stability Company during a weekend. In practice, the Danish Financial Supervisory Authority will, in so far as this is possible, announce a deadline for the distressed bank on a Friday afternoon, expiring on the forthcoming Sunday, cf. Box 2. A fast transfer of assets reduces the risk of a run on the bank.

No later than six hours after the bank has been notified of the deadline, the board of directors must decide whether the bank is to be wound up under the resolution scheme if the capital cannot be re-established before the deadline set. Otherwise, the bank must be wound up according to the rules laid down in the Danish Insolvency Act.<sup>1</sup> In the following, the bank is assumed to opt for the resolution scheme.

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<sup>1</sup> It may be decided at the general assembly meeting of the bank whether the resolution scheme is to be used in such a situation. If so, the board of directors must respect the decision made at the general assembly meeting.

## MARKET SOLUTIONS

Box 1

In most cases, the transfer of a distressed bank to another bank would be preferable to winding it up under the resolution scheme. Therefore, the intention behind the resolution scheme is that the possibilities of market solutions and private transfers are explored before the resolution scheme is applied. If a bank is in a situation of insolvency or is presumed to become insolvent, the board of directors can transfer the activities of the bank, in part or in full, to another bank without convening an extraordinary general assembly meeting.<sup>1</sup> This option is available until the time at which the board of directors of a distressed bank enters into a transfer agreement with the Financial Stability Company.

An amendment from June 2011 gave the Guarantee Fund for Depositors and Investors the possibility of providing a dowry or a guarantee for the coverage of a distressed bank's non-subordinated creditors if the distressed bank is transferred to another bank. Such dowry presupposes complete transfer of the distressed bank's non-subordinated claims to another bank, which is capable of continuing all activities under a viable business model. Thus, non-subordinated creditors, including depositors, will not suffer a loss, but shareholders and owners of subordinated capital will have lost their investment. The Guarantee Fund can only provide a dowry if this is a financially more favourable solution for the Guarantee Fund than to pay coverage to the depositors.

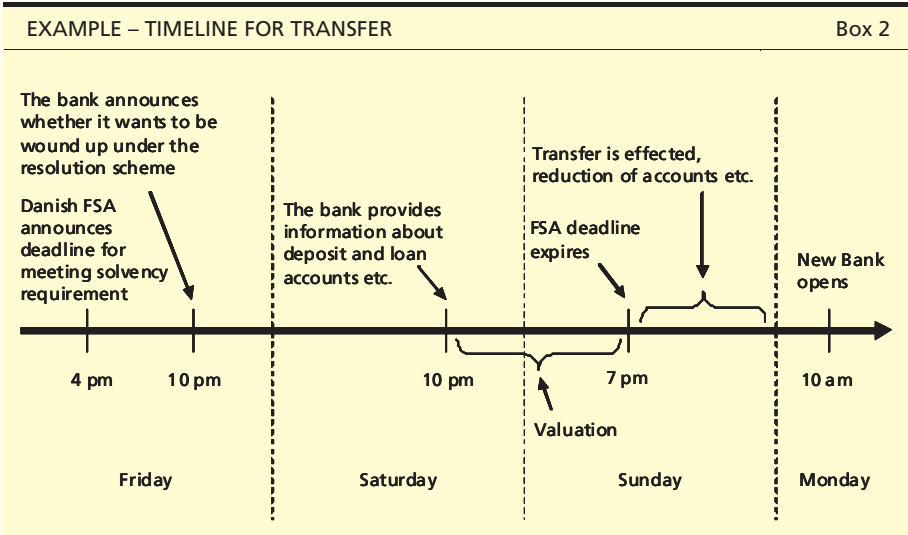
In August 2011, a majority of the Folketing agreed on a number of initiatives to strengthen the sector's scope for consolidation. In future, the Financial Stability Company will have the option of providing a supplementary dowry – in addition to a dowry from the Guarantee Fund – if this is necessary for a private transfer of a distressed bank. The Financial Stability Company can contribute an amount corresponding to the government's expected loss on individual government guarantees if the bank were to be wound up under the resolution scheme.

<sup>1</sup> Cf. Section 247 of the Danish Financial Business Act.

Over the next 24 hours, the distressed bank must provide certain information to the Financial Stability Company. This information will form the basis for a preliminary valuation of the bank's assets. Moreover, the bank must prepare an overview of deposits covered by the Guarantee Fund for Depositors and Investors. All banks are required to have efficient business procedures and systems that make it possible to provide such information within 24 hours. This is to ensure that the activities of the bank can always be transferred swiftly and efficiently.<sup>1</sup>

If the distressed bank cannot raise the required capital by the expiry of the deadline, it is obliged to conclude an agreement with the Financial Stability Company for transferring the bank's assets to a subsidiary of the Financial Stability Company (New Bank). In principle, the transfer

<sup>1</sup> The Danish Financial Supervisory Authority's Executive Order on readiness for winding-up stipulates the detailed requirements for the necessary business procedures and systems.



will comprise all the bank's assets. Moreover, New Bank must take over all employees, employee obligations and, if possible, other bilateral agreements. Such agreements, including netting agreements concerning trade in foreign exchange and derivatives contracts, can only be taken over in accordance with the conditions laid down in the specific agreements.

The Financial Stability Company and the board of directors of the distressed bank must agree on a preliminary transfer sum for the assets. New Bank pays the transfer sum by taking over a proportionate share of the distressed bank's non-subordinated liabilities. If the assets turn out to have a higher value, New Bank will take over additional liabilities.

The preliminary transfer sum will not be paid in full at the time of the transfer. Part of the transfer sum is retained in the form of an intermediate account to meet a situation in which the final valuation turns out to be lower than the preliminary valuation. The example in Box 3 illustrates the correlation between the transfer sum, the intermediate account and the proportionate share of non-subordinated liabilities taken over by New Bank.

In order for New Bank to carry on operation of the distressed bank's activities, the Financial Stability Company injects capital and liquidity into New Bank on the Sunday, so that it meets the regulatory capital and liquidity requirements. The Financial Stability Company can obtain the necessary funding via the Danish government's re-lending facility. Sunday evening, the Financial Stability Company issues a press release on the transfer, and Monday morning, New Bank opens as usual at the distressed bank's premises.

**CORRELATION BETWEEN TRANSFER SUM, OUTSTANDING BALANCE AND LIABILITIES TAKEN OVER BY NEW BANK**

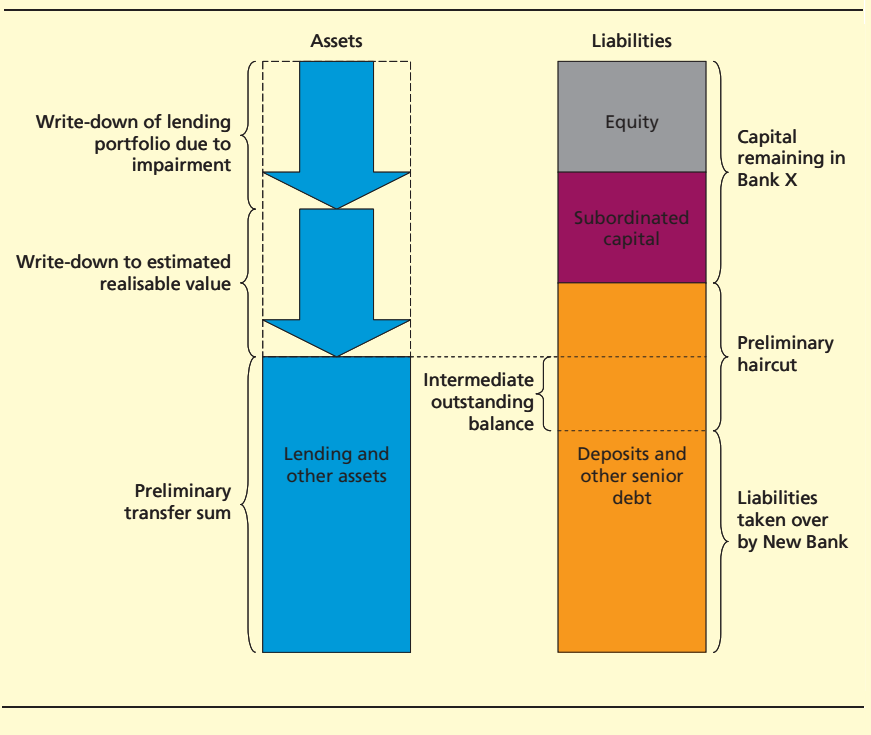
Box 3

A review of Bank X's exposures shows that a large share of its lending portfolio is impaired and therefore has to be written down, which means that the equity of Bank X is lost.

Bank X cannot meet the capital requirements and decides to apply the resolution scheme. The bank's assets are written down to estimated realisable values in the case of immediate transfer to an independent party. The sum of the estimated realisable values is identical to the preliminary transfer sum.

New Bank executes payment by taking over a proportionate share of non-subordinated claims against Bank X. Part of the transfer sum is retained in the form of an intermediate outstanding balance (meaning that Bank X will have a claim on New Bank). The outstanding balance is settled when the auditors' valuation is available.

**ASSETS AND LIABILITIES OF BANK X**



Danmarks Nationalbank's tasks in connection with the transfer of a distressed bank are described in Box 4.

**Deposits covered by the Guarantee Fund for Depositors and Investors**

Ordinary deposits are covered by the Guarantee Fund for Depositors and Investors up to an amount equivalent to 100,000 euro. The depositors' net claims are covered, implying that the calculation of the individual

DANMARKS NATIONALBANK'S OPERATIONAL TASKS	Box 4
<p>Danmarks Nationalbank primarily has two operational tasks when a distressed bank is wound up under the resolution scheme. The tasks are based on Danmarks Nationalbank's role in the Danish payment systems and as bank to the Financial Stability Company.</p> <p>Banks in Denmark hold accounts with Danmarks Nationalbank. Their primary account is the current account, but they also hold accounts used for various payment and settlement systems. These accounts are crucial for e.g. the bank's securities trading and settlement of retail payments, such as debit card payments.</p> <p>Customers of a distressed bank whose activities will be continued in a subsidiary of the Financial Stability Company (New Bank) must still be able to carry out daily banking transactions, including online banking transfers, debit card payments and securities trading via the bank. Therefore, Danmarks Nationalbank, the Financial Stability Company and the payment settlement companies VP Securities and Nets have agreed on a road map, under which New Bank takes over the distressed bank's accounts with and exposures to Danmarks Nationalbank. New Bank also takes over the distressed bank's participation in the Kronos and Target2 payment systems.</p> <p>Danmarks Nationalbank also has an operational role, as the Financial Stability Company holds an account with Danmarks Nationalbank. When the Financial Stability Company establishes New Bank, the Financial Stability Company may need capital and liquidity to comply with the regulatory requirements and meet New Bank's obligations. The Financial Stability Company can obtain the necessary funding by raising loans via the government's re-lending facility. Such re-lending will be paid out of the government's account with Danmarks Nationalbank.</p>	

depositor's claim must exclude any obligations of the depositor towards the bank in question, such as loans. Some special deposits are fully covered by the Guarantee Fund regardless of the size of the amount. These are e.g. certain pension-savings accounts, children's savings accounts, lawyers' client accounts and certain accounts stemming from property transactions and mortgaging.

At the time of the transfer of the distressed bank's assets, New Bank must assess the individual depositors' claims against the Guarantee Fund. Basically, New Bank takes over a proportionate share of the deposits covered, corresponding to the handling of other non-subordinated claims. If New Bank has to take over 75 per cent of non-subordinated claims according to the transfer agreement, this will also include 75 per cent of (net) deposits covered.

Furthermore, New Bank must credit an amount to the depositors' accounts, equivalent to the expected coverage from the Guarantee Fund. This ensures that the entire claim will be available to depositors on the Monday, presuming that the full amount is covered by the Guarantee Fund. Depositors with ordinary deposits that exceed the coverage from the Guarantee Fund will have an amount available corresponding to 100,000 euro plus a proportionate share of the remaining amount, cf. Box 5.

**EXAMPLE – DEPOSITS EXCEEDING KR. 750,000**

Box 5

According to the transfer agreement, New Bank takes over 75 per cent of Bank X's non-subordinated claims. A depositor has a deposit of kr. 2,000,000 and a loan of kr. 750,000. The depositor's deposit in New Bank at the opening on Monday morning can be calculated as follows:

- The depositor's net claim totals kr. 1,250,000, as the loan is offset against the deposit.
- Around kr. 750,000 (equivalent to 100,000 euro) is covered by the Guarantee Fund for Depositors and Investors. This amount is transferred in full, as New Bank must make an amount available in the customer's account corresponding to the expected coverage from the Guarantee Fund.
- Of the part of the net claim exceeding the coverage by the Guarantee Fund, namely around kr. 500,000, 75 per cent is transferred. Hence, additional kr. 375,000 will be made available to the depositor. A deposit totalling kr. 1,125,000 will be transferred.
- The depositor has a residual claim of around kr. 125,000 against Bank X. This amount is an unsecured claim against Bank X, and is at risk of being fully or partly lost.

The amounts on account may subsequently be adjusted. In connection with the deposits, New Bank is subrogated to the depositor's claims against the Guarantee Fund. Until New Bank receives payment from the Guarantee Fund, it can fund the amounts on account via liquidity from the Financial Stability Company, cf. Box 4.

### **Valuation and subsequent adjustment**

Valuation of the distressed bank's assets takes place in several steps. In connection with the transfer to New Bank, a preliminary valuation is made, which can subsequently be increased when two independent auditors have prepared a valuation report. If it turns out that there is a net profit in New Bank when all activities have been transferred to another party or liquidated, the transfer sum must be adjusted by this net profit.

Before the conclusion of the transfer agreement, the Financial Stability Company prepares a preliminary valuation of the distressed bank's assets. This valuation determines the size of the dividend on account. The dividend can subsequently be increased, but not reduced.

The assets are valued at estimated realisation values, meaning the value that the assets are expected to bring in at the time of acquisition in the case of immediate transfer between independent parties, less expected costs of sale. The valuation may not include goodwill and other intangible assets.

Part of the transfer sum is retained in an intermediate outstanding balance. The outstanding balance functions as a buffer in case the auditors' valuation is lower than the preliminary valuation. The size of the out-

## EXAMPLE – SUBSEQUENT ADJUSTMENT OF THE TRANSFER SUM

Box 6

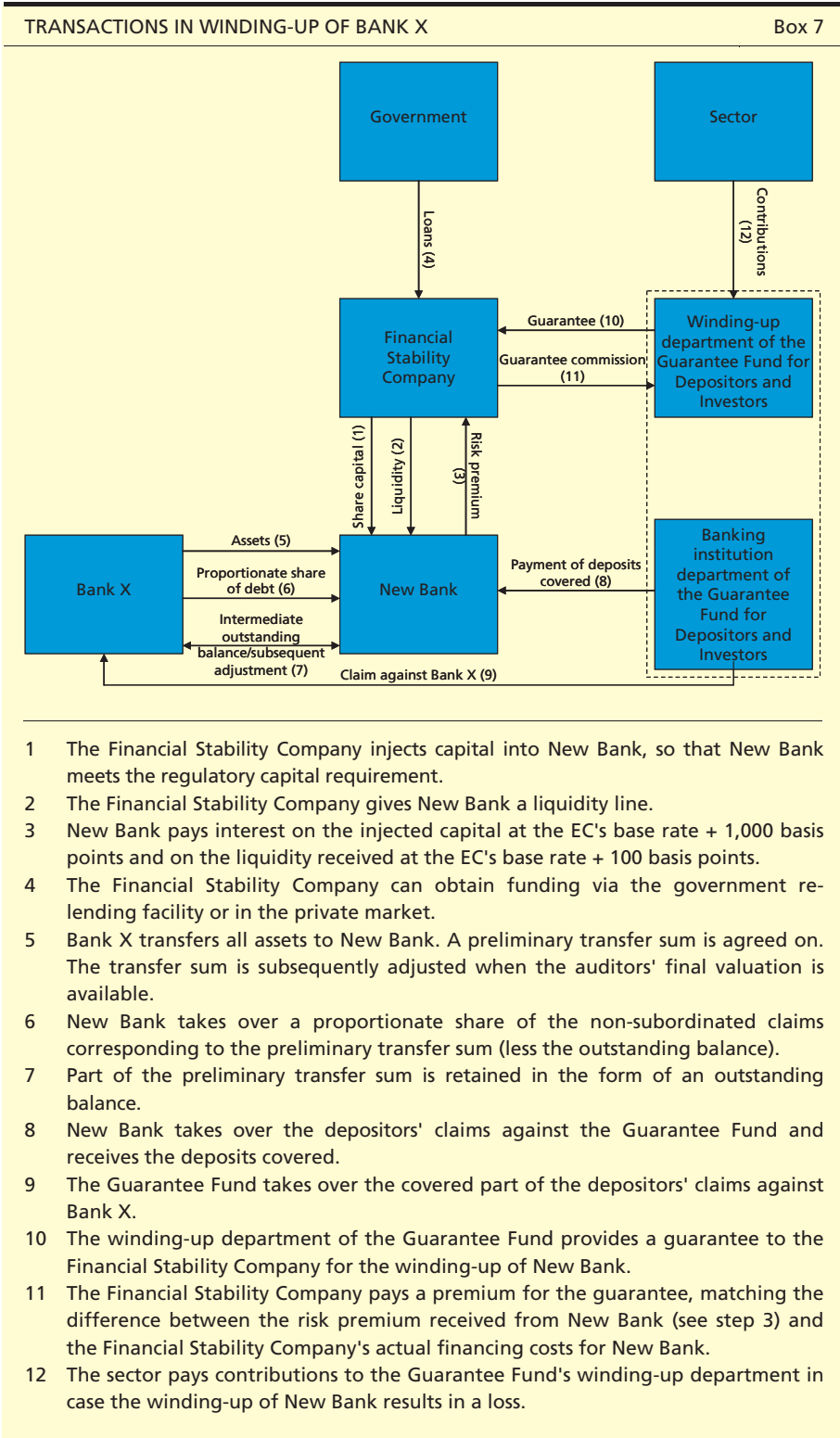
Bank X cannot meet the capital requirement and therefore transfers its assets to New Bank. Bank X and the Financial Stability Company agree on a preliminary transfer sum of kr. 1 billion. The valuation council of the Guarantee Fund for Depositors and Investors sets the intermediate outstanding balance at kr. 150 million. New Bank must therefore initially take over a proportionate share of non-subordinated claims worth kr. 850 million. The subsequent valuation – by two independent auditors – has the following consequences:

- If the auditors estimate the value of the assets at kr. 900 million, New Bank will have to take over an additional proportionate share of the claims, equivalent to kr. 50 million. This means that the dividend on account for non-subordinated creditors is increased. The outstanding balance is written down to 0.
- If the auditors estimate the value of the assets at kr. 700 million, New Bank has actually taken over claims of an excessive kr. 150 million. The outstanding balance cannot be negative, but is written down to kr. 0. New Bank's loss of kr. 150 million is covered by a guarantee provided by the Guarantee Fund.
- If the auditors estimate the value of the assets at kr. 1.2 billion, New Bank will have to take over an additional proportionate share of the claims, equivalent to kr. 350 million. This means that the dividend on account for non-subordinated creditors is increased. The intermediate account is written down to 0. If New Bank has taken over all non-subordinated claims, any residual amount is paid in cash to the estate of the distressed bank.

standing balance is fixed by the valuation council of the Guarantee Fund, taking into account uncertainty over the size, scope and value of the obligations. The outstanding balance is recognised in the distressed bank's balance sheet as a claim on New Bank.

Immediately after the transfer, the Financial Stability Company must advertise for creditors barring claims not lodged within three months, meaning that creditors are encouraged to report any claims on the distressed bank to New Bank. Two auditors appointed by the Institute of State Authorised Public Accountants in Denmark must as soon as possible after the expiry of the deadline prepare a valuation report with an independent assessment of the estimated realisable value at the time of transfer.

If the auditors find that the preliminary transfer sum is too high, the valuation of the assets must be adjusted via the outstanding balance. If the auditors find that the preliminary transfer sum is too low, however, New Bank has to take over an additional proportionate share of the distressed bank's liabilities. Consequently, the dividend on account for non-subordinated creditors will be increased. On the other hand, the dividend can never be reduced, not even if the outstanding balance unexpectedly turns out to be inadequate. If so, the Guarantee Fund will have to cover any losses, cf. Box 6. So there is no risk that the creditors will incur additional losses as a result of a changed valuation.



To ensure that the distressed bank (and its creditors) obtains payment for the full value of the assets, the transfer agreement must include a provision that the transfer sum will be adjusted subsequently by the net profit, if any, at New Bank after transfer to another party or liquidation of New Bank. A net profit means a profit after return at market rate on the equity made available by the Financial Stability Company. Hence, it is possible that the distressed bank's creditors may obtain further payment, also after the auditors' valuation.

Box 7 illustrates the payment transactions in the winding-up of a distressed bank.

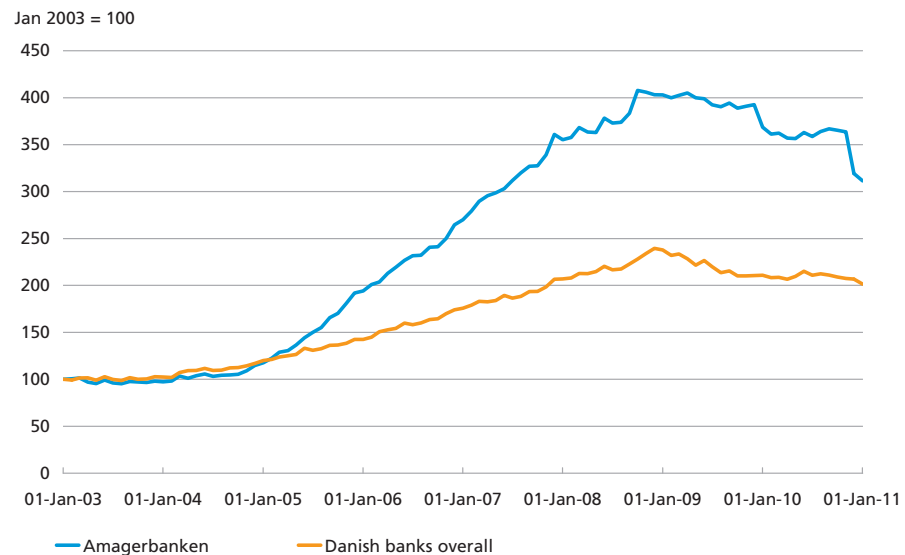
### CASE STUDY: AMAGERBANKEN

Amagerbanken was the first bank to be wound up under the resolution scheme. During the years ahead of the financial crisis, the bank reported strong lending growth, cf. Chart 1, particularly within property financing. At end-2010, Amagerbanken held a 1.6 per cent market share of total bank lending in Denmark, ranking ninth among banks in terms of lending.

The process leading up to the winding-up of Amagerbanken in February 2011 is described in the speech manuscript of the Minister for Economic and Business Affairs from the open consultation in the Trade and Industry Committee of the Folketing on 22 March 2011. The speech

LENDING GROWTH IN 2003-11

Chart 1



Note: Lending from Danish banks overall comprises loans from Danish branches only.  
 Source: Danmarks Nationalbank.

manuscript provides the basis for the description in this article of the sequence of events at the bank.

Attention was already focused on Amagerbanken when the financial crisis escalated in the autumn of 2008. Shortly before the adoption of Bank Rescue Package 1, the bank had been allowed to withdraw liquidity from Danmarks Nationalbank for a limited period. When Amagerbanken was included in the general government guarantee under Bank Rescue Package 1, the bank repaid the liquidity to Danmarks Nationalbank.

Amagerbanken was among the banks that made use of Bank Rescue Package 2 and applied for a government capital injection. The Danish Financial Supervisory Authority carried out an inspection of the bank, showing that the need for solvency reservations and write-downs was so pronounced that the bank had to raise new capital. Amagerbanken raised just under kr. 1 billion in capital, after which it once again met the solvency requirement. Against this backdrop, it obtained an agreement for a government capital injection of kr. 1.1 billion in December 2009.

Amagerbanken also decided to apply for an individual government guarantee. It applied for an individual government guarantee totalling kr. 13.5 billion from the Financial Stability Company, which entered into negotiations with Amagerbanken about the conditions for such a guarantee. The Financial Stability Company assessed that there was a not insignificant risk associated with granting the bank an individual government guarantee. Therefore, the Financial Stability Company found that the bank had to fulfil certain requirements to justify the guarantee.

In June 2010, Amagerbanken entered into an agreement with the Financial Stability Company on an individual government guarantee totalling kr. 13.5 billion. According to the agreement, the bank had to register a kr. 750 million increase of its capital base by 15 September 2010. Moreover, two members with special powers and appointed by the Financial Stability Company were to be elected to the Board of Directors.

The conditions stipulated by the Financial Stability Company were met by Amagerbanken's capital increase in September 2010 when the bank announced that it had raised almost kr. 900 million in capital. At an extraordinary general assembly meeting in November 2010, the bank's shareholders elected a new Board of Directors. In the same month, a new CEO was appointed.

The new management immediately instigated a detailed review of the bank's exposures. The review unveiled a need for further write-downs, which meant that Amagerbanken no longer met the solvency require-

ment. As a consequence, the bank agreed with the Financial Stability Company to transfer its activities to a new bank set up by the Financial Stability Company (Amagerbanken af 2011) on 6 February 2011.

Before the transfer to Amagerbanken af 2011, potential private solutions were discussed with various banks with a view to continuing Amagerbanken's activities in the private sector. However, no bank was willing to buy the bank in its entirety; not even in a structure in which the government participated via the Financial Stability Company.

### **The practical execution**

The purchase sum for Amagerbanken's assets was preliminarily set at kr. 18.5 billion. Amagerbanken af 2011 paid for the assets by taking over exposures of Amagerbanken worth kr. 15.2 billion. At the same time, an intermediate outstanding balance of kr. 3.3 billion was established. The transfer was effected between 8:00 pm and midnight on Sunday 6 February, during which interval no entries could be made in the online banking service due to technical changes.

Amagerbanken af 2011 took over liabilities equivalent to 58.8 per cent of the non-subordinated claims of Amagerbanken. This meant that non-subordinated creditors had their claims reduced by 41.2 per cent in so far as they were not covered by the Guarantee Fund for Depositors and Investors. More than 99 per cent of all depositors had their bank deposits covered. The shareholders and the owners of subordinated capital lost their entire investment.

Amagerbanken af 2011 opened on Monday 7 February 2011. The vast majority of customers were not affected by the transfer and could continue to use their payment cards and the online banking service as usual. Both domestic and foreign counterparties could execute payments to Amagerbanken af 2011 without any risk that the money would end up in Amagerbanken's bankruptcy estate. This was the first time that the scheme was applied, and a few of Amagerbanken's foreign counterparties were therefore insecure and dared not execute payments to Amagerbanken af 2011. This meant that Amagerbanken af 2011 was briefly cut off from executing other than purely domestic payments.

### **Status of the winding-up of Amagerbanken**

In May 2011, Amagerbanken af 2011 sold all retail customers and minor corporate customers to the Faroese bank P/F BankNordik for a total of kr. 235 million. Subsequently, the remaining gross lending of Amagerbanken af 2011 amounted to kr. 13 billion distributed on around 200 large exposures. The settlement of these exposures will continue in the coming period.

## INVESTIGATIONS INTO AMAGERBANKEN

Box 8

In August 2011, the Danish Financial Supervisory Authority published a report on the supervision of Amagerbanken. According to this report, further considerable deterioration in a number of the bank's large exposures was the key reason that it could no longer meet the regulatory solvency requirement and had to be wound up via the Financial Stability Company. It is also revealed that the Danish Financial Supervisory Authority intends to report the former daily management of Amagerbanken to the police for having misinformed the Financial Supervisory Authority or not having complied with the Financial Supervisory Authority's instructions on a number of occasions.

In addition to the Financial Supervisory Authority's report, there will be an independent legal enquiry into Amagerbanken. The enquiry will look into the reasons behind the bank's financial collapse. At the same time, it will be disclosed whether there is basis for claims for liability in damages and/or criminal liability against members of the bank's management. The Financial Stability Company's involvement in the management will be included in the investigation.

Moreover, Rigsrevisionen (the national audit office of Denmark) has launched an independent investigation of Amagerbanken's individual government guarantee and the relevant authorities' roles in this connection.

The results of the independent investigations are not available yet.

In June 2011, the Financial Stability Company announced the auditors' valuation of Amagerbanken. Their valuation initially provided the basis for increasing the preliminary dividend payout rate from 58.8 to 84.4 per cent. The Guarantee Fund for Depositors and Investors has decided to contest the auditors' valuation in court, claiming that it should be reduced by a maximum of kr. 4.5 billion. In this context, it should be noted that the Guarantee Fund is liable for any losses of Amagerbanken af 2011 if the assets turn out to have a lower value than assumed by the auditors.

As the Guarantee Fund has set a ceiling for the required reduction in the valuation, the Financial Stability Company has been able to calculate a higher dividend on account for Amagerbanken's creditors. The preliminary higher dividend was set at 66.1 per cent, corresponding to an increase of the dividend payout rate by 7.3 percentage points.

Box 8 describes the investigations launched after the winding-up of Amagerbanken in February 2011.