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UPDATE ON HETA ASSET RESOLUTION AG

The Austrian "Bundesgesetz über Sanierungsmaßnahmen für die HYPO ALPE-ADRIA-BANK INTERNATIONAL AG" (HaaSanG), published on 31 July 2014 in the Austrian Federal Law Gazette and implemented in August 2014 by the Austrian government, paved the way for the establishment of Heta Asset Resolution AG (Heta) as a wind-down vehicle to assume and manage large parts of the assets of the failed Austrian bank, Hypo Alpe-Adria Bank international AG (HAA). The idea was to wind down the HAA by 2020.

In addition, the Austrian "Act on the Recovery and Resolution of Banks" (BaSAG), as published in the Austrian Federal Law Gazette I No. 98/2014, was passed in January 2015. It transposed the EU Directive on the Recovery and Resolution of Credit Institutions and Investment Firms (BRRD) in Austria. Accordingly, Heta is not a bank as defined by the EU's Capital Requirements Regulation, but the application of the BRRD to Heta has been achieved as a result of a discretionary additional article included during the transposition of BRRD into Austrian law. In accordance with BaSAG, the Austrian Financial Market Authority (FMA) assumed the function of the national resolution authority on 1 January 2015. The FMA has received far-reaching powers conveyed upon its activities as the resolution authority, in order to be able to execute an orderly resolution in the event of the failure or threat of failure of an institution, and to ensure that financial market stability is maintained in Austria. The bail-in tool forms the core element of the BRRD. It permits the resolution authority to write down the eligible liabilities in a cascading contribution to loss absorption of an institution, or to convert them into equity capital. Furthermore, the FMA may also take measures for ensuring the continuity of services and avoiding adverse effects on financial stability by separating performing assets from impaired or under-performing assets.

Accordingly, the FMA issued an administrative ruling deferring the maturities of all debt securities issued by Heta and all other liabilities – including interest due dates – until 31 May 2016, provided that the liabilities do not qualify as non-eligible liabilities pursuant to Section 86(2) of the BaSAG (materially corresponding to Article 44(2) of the BRRD). Liabilities affected by the moratorium include also bonds and all repayment claims arising out of Austria against Carinthia and Kärtner Landesholding in relation to security granted for HETA liabilities. The accompanying edict in accordance with BaSAG was published on the FMA website, in the FMA's capacity as the designated resolution authority. You can read the accompanying edict on the FMA website (in German).

In the meantime a German bank, Bayerische Landesbank, has initiated legal proceedings in Germany against Heta whereby one of the legal issues before the Munich local court was whether the BRRD contemplates the application of its tools and powers to wind-down vehicles such as Heta.

The uncertainty stemmed from the fact that the BRRD only applies to MiFID firms and credit institutions within the meaning of the Capital Requirements Regulation – in other words, to financial institution and banks. Heta, as a wind down vehicle, does not have such license. In order to ensure that the BRRD would apply to Heta nonetheless, the Austrian legislature explicitly made Heta subject to the BaSAG. On 8 May 2015, the Munich court of first instance refused to recognize the moratorium on the basis that the application of BaSAG to Heta goes beyond the scope of the BRRD and, therefore, fell outside of Germany's obligation under the BRRD to give effect to measures taken by other resolution authorities. In doing so, the Munich court ordered Heta to pay Bayern LB approximately €2.3 billion. This decision is now subject to an appeal by Heta.

Furthermore, by its 28 July 2015 decision, the Austrian Verfassungsgerichtshof (VGH -Constitutional Court) annulled the HaaSanG, allowing the government to (1) bail-in Heta's subordinated debt holders, and (2) declare void the State of Carinthia's deficiency guarantees on that portion of Heta's subordinated debt in the amount of around €800 million. The VGH has repealed this legislation in its entirety and declared the unequal treatment of junior creditors by a set cut-off date of 30 June 2019 unconstitutional and a violation of property rights. The Court's decision lead to a booking in Heta's half-year statements of additional €800 million and thus increased its negative equity (local GAAP accounting). Consequently, unsecured creditors may ask Carinthia as the guarantor of the deficiency guarantee to compensate them for the difference based on the wind down of HAA. The ruling sends a strong signal that the value of the deficiency guarantee cannot be fully eliminated by law in hindsight by isolated measure.

In its ruling, the VGH did not address the payment moratorium introduced on 1 March 2015 by FMA on Heta's unsecured obligations. This moratorium remains in place until May 2016. Further, the HaaSanG was not repealed by the constitutional court.

Thereafter, in particular, German and European credit institutions and asset management companies have filed several legal claims against Heta. The main reason for such legal actions has been that several bonds and Schuldscheine of HAA/HETA have been issued under deficiency guarantees of the state of Carinthia and Kärtner Landesholding. Under such deficiency guarantees, a secured party may make a direct claim against the guarantor where the debtor is insolvent or where enforcement measures have failed or will likely fail. In these cases – and provided that the secured liabilities are due – a deficiency guarantor will be liable for payment.

Finally, the aforesaid legal actions have been filed with the Frankfurt/Main Regional Court which has jurisdiction to hear the action on the basis of effective choice of law clauses in most bond and the Schuldschein loans terms, since the finance instruments issued by HETA and its legal predecessor are governed by German law.

Contact

Dr. Andreas Fillmann
Partner
T +49 69 1739 2423
E andreas.fillmann@squirepb.com