Erste Bank: Relaxed attitude towards the cross guaranty system accusations

According to Erste Bank, the objections raised by BA-CA against the Group of credit institutions established by Erste Bank and the savings banks in Austria and against the full consolidation of the Austrian savings banks which participate in the cross guarantee system are nothing but a tactical ploy of its competitor.

Erste Bank regards the accusations as unfounded in fact and in law. The Group of credit institutions and the cross guarantee system are in compliance with both Austrian law and EU regulations as well as the International Financial Reporting Standards (IFRS). This is proved by two reputable expert opinions (a German summary is enclosed).

This is the English translation of an excerpt (summary) from the expert opinion of Eidos Wirtschaftsberatung GmbH. Please note that the expert opinion, a summary of which is set out above, was issued solely for the benefit of Erste Bank der oesterreichischen Sparkassen AG. It may not provide the basis for any liability of Eidos Wirtschaftsberatung GmbH towards any other person, including but not limited to potential.

Summary

In summary, we have come to the conclusion that the consolidation of Erste Bank (including the members of the S Group) as per IAS is necessary. The reasons for this conclusion is that in particular it would present the Erste Bank with the possibility to govern the strategic financial and business policy of a member of the S Group. Moreover, there is de facto the possibility to remove or appoint the majority of the members of the management body and/or the supervisory body – in the event of significant deviation from the jointly defined financial and business policy, in any case.

However, the regulations on the financial and business policy in the agreements conflict with the regulations relating to dismissal due to gross violation of professional ethics and takeover of the voting majority.
On the basis of Austrian Commercial Code (HGB)/the Austrian Banking Act (BWG), Erste Bank does not need to hold a stake in any respective Sparkasse institution for the purposes of IAS consolidation.

Sparkassen-Prüfungsverband Auditing agency		Eidos Wirtschaftsberatung GmbH Auditing and tax consulting company	
Mag. Wolfgang Riedl (Auditor)	Dr. Klaus Goschler (Auditing Director)	Mag. Erich Kandler (Auditor)	ppa/Mag. Kurt Schweighart (Auditor)

Enclosed

1. Agreement in principle from 26th September 2001
2. Partnership agreement of the S Haftungs- und Kundenabsicherungs GmbH (from 16th November 2001)
3. General Terms and Conditions for Auditors (Allgemeine Auftragsbedingungen für Wirtschaftstreuhandberufe – ABB)

Sparkassen-Prüfungsverband
Prüfungsstelle
Grimmelshausengasse 1
Postfach 157
1037 Vienna
Phone: +43-1-714 56 21-0
Fax: +43-1-714 56 21-33

Eidos Wirtschaftsberatung GmbH
Wirtschaftsprüfungs- und Steuerberatungsgesellschaft
Akademiehof
Friedrichstrasse 10
1015 Vienna
Phone: +43-1-588 54-4500
Fax: +43-1-588 54-4599

Statement on the IAS rendering of accounts for the intended S Group (cross-guarantee system)

21st March 2002

This is the English translation of an excerpt (summary) from the expert opinion of Schönherr Rechtsanwälte. Please note that the expert opinion, a summary of which is set out above, was issued solely for the benefit of Erste Bank der oesterreichischen Sparkassen AG. It may not provide the basis for any liability of Schönherr Rechtsanwälte towards any other person, including but not limited to potential investors.

1. Summary

1.1. General

Upon the entry into force of Federal Law Gazette 131/2002 on 1 September 2002, a new paragraph (2a) was added to Section 30 Austrian Banking Act (*BWG*) which extends the definition of "group of credit institutions" and thus indirectly also amends accounting provisions and bank supervision provisions as regards the consolidation of groups of credit institutions. It must be verified whether Section 30 (2a) BWG is consistent with the Directives both as regards the Directive relating to the taking up and pursuit of the business of credit institutions (hereinafter: Codified Directive) (2000/12/EC) referred to in the explanatory notes to the government bill and as regards the Directive on consolidated accounts (hereinafter: Consolidated Accounts Directive) (83/349/EEC) and the Directive on the annual accounts and consolidated accounts of banks and other financial institutions (Bank Accounts Directive) (86/635/EEC) harmonizing accounting of credit institutions.

All of the three mentioned Directives restrict to a few case groups referred to exhaustively the scope within which the Member States may prescribe consolidation; except for these cases, no consolidation may be prescribed. It is therefore doubtful whether Section 30 (2a) BWG can be subsumed both under an element of the Directives as regards accounting (Consolidated and Bank Accounts Directives) and as regards bank supervision (Codified Directive).

1.2. Compatibility with the Consolidated and Bank Accounts Directives

As regards the laws governing consolidated accounts, we believe Section 30 (2a) BWG can be subsumed under Art 1 (1) (c) of the Consolidated Accounts Directive, according to which a Member State shall require any undertaking governed by its national law to draw up consolidated accounts if that undertaking has a right to exercise a "dominant influence" over another undertaking.

The term "dominant influence" has been defined neither by EC secondary law nor by ECJ case law. If the term is interpreted as it is generally used in accounting law, "dominant influence" can be defined as "directly or indirectly consistent and comprehensive influence on material issues of the sub-undertaking's business policy". Section 30 (2a) BWG shows several elements which are consistent with this general

meaning of the term "dominant influence" as used in accounting. Section 30 (2a) BWG implies a dominant influence due to the fact that the central institution is able to "materially" influence the liable undertaking. By exercising such influence, the central institution can influence the subordinated credit institutions. This influence is "dominant" because the credit institutions can expect to be supported by the joint liability scheme only if they pursue their business policy "in good times" as requested by the liable undertaking. Even if Section 30 (2a) BWG does therefore not expressly refer to a right of the central institution to issue instructions, it is clear that the central institution can control the subordinated credit institutions' business and market policy because it holds a majority interest in the liable undertaking.

According to a proposal of the Commission to amend the accounting provisions, Art 1 (2) of the Consolidated Accounts Directive shall be adjusted to IAS so that in the future consolidation does no longer require the capital of the parent undertaking and the subsidiary undertakings to be connected, and a consolidation is already permitted if the parent undertaking "can" assert a dominant influence on the subsidiary undertaking, but does not actually do so. In the future, Section 30 (2a) BWG will therefore not only implement Article 1 (1) (c) but also Article 1 (2) of the Consolidated Accounts Directive.

As regards the laws governing bank accounts, Section 30 (2a) BWG cannot be subsumed under a relevant element, in particular not under Art 43 (2) (e), because the central institution's influence is not sufficient to refer to a "uniform management" as defined by accounting law. However, the Bank Accounts Directive expressly provides that all consolidation events of the Consolidated Accounts Directive apply also to credit institutions, so that Section 30 (2a) BWG is also compatible with the Bank Accounts Directive.

1.3. Compatibility with the Codified Directive

As regards the laws governing bank supervision, Section 30 (2a) BWG can be subsumed under Art 54 (4) first indent of the Codified Directive. This provision stipulates that the competent authorities shall determine whether and how consolidation is to be carried out for purposes of bank supervision if a credit institution can exercise "significant influence" over one or more other credit institutions. Two questions arise: on the one part, whether Section 30 (2a) BWG defines an event of "significant influence" and, on the other part, whether the Austrian legislator would have been obliged to grant the Financial Market Supervision Authority (*FMA*) discretion in Section 30 (2a) BWG to prescribe consolidation.

The first question of interpreting the term "significant influence" (just like the term "dominant influence" set forth in the Consolidated Accounts Directive) is not easy to answer, because neither relevant secondary law nor ECJ case law provide a definition. It is even more difficult to interpret the term because the same term was replaced by "material influence" elsewhere in the Directive. However, this question of interpretation need not be answered: If Section 30 (2a) BWG already qualifies as an event of

"dominant influence", it follows that the central institution's influence defined in Section 30 (2a) BWG is also "significant".

As regards the second question of interpretation concerning the lack of discretion of the FMA, the Austrian legislator, based on Community law and based on the Austrian Constitution, is not only entitled but even obliged to restrict the FMA's discretion and to precisely determine when "significant influence" as set forth in Art 54 (4), first sentence of the Codified Directive is satisfied for purposes of consolidation of groups of credit institutions. Had the legislator taken over the term "significant influence" from the Directive without further specification and left it to the FMA to determine when influence is sufficient for the purposes of consolidation of groups of credit institutions, the FMA would have been granted unrestricted discretion because the Directive insufficiently defines the term "significant influence", which is contrary both to the Austrian Constitution and to Community Law.

We believe that the question whether the full consolidation resulting from the new definition of a group of credit institutions in Section 30 (2a) BWG is proportional must be answered as follows. One of the purposes of the Codified Directive is to increase the protection of depositors. Full consolidation provides better transparency for depositors and therefore increased protection than does partial consolidation. This was why the EC legislators designed full consolidation as the standard and partial consolidation as the exception. Relevant scholarly writing accordingly demands that those Codified Directive provisions that require a partial consolidation be interpreted narrowly. The Austrian legislators' decision to use the choice they are given under Art 54 (4) of the Codified Directive in favour of a full consolidation both corresponds to the restrictive interpretation of partial consolidations advocated by legal scholars and to the Directive's purpose of promoting the protection of depositors to the greatest extent possible. This is also the reason why we believe that ordering a full consolidation is not an "arbitrary" exercise of this choice. As regards the objection that a full consolidation runs contrary to the "the principle of proportionality that derives from primary Community law", it is not clear why a full consolidation would impede the freedom of establishment of foreign banks more than a partial consolidation.

This is the English translation of an excerpt (summary) from the expert opinion of Eidos Wirtschaftsberatung GmbH. Please note that the expert opinion, a summary of which is set out above, was issued solely for the benefit of Erste Bank der oesterreichischen Sparkassen AG. It may not provide the basis for any liability of Eidos Wirtschaftsberatung GmbH towards any other person, including but not limited to potential.

Summary

In summary, we have come to the conclusion that the consolidation of Erste Bank (including the members of the S Group) as per IAS is necessary. The reasons for this conclusion is that in particular it would present the Erste Bank with the possibility to govern the strategic financial and business policy of a member of the S Group. Moreover, there is de facto the possibility to remove or appoint the majority of the members of the management body and/or the supervisory body – in the event of significant deviation from the jointly defined financial and business policy, in any case.

However, the regulations on the financial and business policy in the agreements conflict with the regulations relating to dismissal due to gross violation of professional ethics and takeover of the voting majority.
On the basis of Austrian Commercial Code (HGB)/the Austrian Banking Act (BWG), Erste Bank does not need to hold a stake in any respective Sparkasse institution for the purposes of IAS consolidation.

Sparkassen-Prüfungsverband Auditing agency		Eidos Wirtschaftsberatung GmbH Auditing and tax consulting company	
Mag. Wolfgang Riedl (Auditor)	Dr. Klaus Goschler (Auditing Director)	Mag. Erich Kandler (Auditor)	ppa/Mag. Kurt Schweighart (Auditor)

Enclosed

1. Agreement in principle from 26th September 2001
2. Partnership agreement of the S Haftungs- und Kundenabsicherungs GmbH (from 16th November 2001)
3. General Terms and Conditions for Auditors (Allgemeine Auftragsbedingungen für Wirtschaftstreuhandberufe – ABB)

Sparkassen-Prüfungsverband
Prüfungsstelle
Grimmelshausengasse 1
Postfach 157
1037 Vienna
Phone: +43-1-714 56 21-0
Fax: +43-1-714 56 21-33

Eidos Wirtschaftsberatung GmbH
Wirtschaftsprüfungs- und Steuerberatungsgesellschaft
Akademiehof
Friedrichstrasse 10
1015 Vienna
Phone: +43-1-588 54-4500
Fax: +43-1-588 54-4599

Statement on the IAS rendering of accounts for the intended S Group (cross-guarantee system)

21st March 2002

This is the English translation of an excerpt (summary) from the expert opinion of Schönherr Rechtsanwälte. Please note that the expert opinion, a summary of which is set out above, was issued solely for the benefit of Erste Bank der oesterreichischen Sparkassen AG. It may not provide the basis for any liability of Schönherr Rechtsanwälte towards any other person, including but not limited to potential investors.

1. Summary

1.1. General

Upon the entry into force of Federal Law Gazette 131/2002 on 1 September 2002, a new paragraph (2a) was added to Section 30 Austrian Banking Act (*BWG*) which extends the definition of "group of credit institutions" and thus indirectly also amends accounting provisions and bank supervision provisions as regards the consolidation of groups of credit institutions. It must be verified whether Section 30 (2a) BWG is consistent with the Directives both as regards the Directive relating to the taking up and pursuit of the business of credit institutions (hereinafter: Codified Directive) (2000/12/EC) referred to in the explanatory notes to the government bill and as regards the Directive on consolidated accounts (hereinafter: Consolidated Accounts Directive) (83/349/EEC) and the Directive on the annual accounts and consolidated accounts of banks and other financial institutions (Bank Accounts Directive) (86/635/EEC) harmonizing accounting of credit institutions.

All of the three mentioned Directives restrict to a few case groups referred to exhaustively the scope within which the Member States may prescribe consolidation; except for these cases, no consolidation may be prescribed. It is therefore doubtful whether Section 30 (2a) BWG can be subsumed both under an element of the Directives as regards accounting (Consolidated and Bank Accounts Directives) and as regards bank supervision (Codified Directive).

1.2. Compatibility with the Consolidated and Bank Accounts Directives

As regards the laws governing consolidated accounts, we believe Section 30 (2a) BWG can be subsumed under Art 1 (1) (c) of the Consolidated Accounts Directive, according to which a Member State shall require any undertaking governed by its national law to draw up consolidated accounts if that undertaking has a right to exercise a "dominant influence" over another undertaking.

The term "dominant influence" has been defined neither by EC secondary law nor by ECJ case law. If the term is interpreted as it is generally used in accounting law, "dominant influence" can be defined as "directly or indirectly consistent and comprehensive influence on material issues of the sub-undertaking's business policy". Section 30 (2a) BWG shows several elements which are consistent with this general

meaning of the term "dominant influence" as used in accounting. Section 30 (2a) BWG implies a dominant influence due to the fact that the central institution is able to "materially" influence the liable undertaking. By exercising such influence, the central institution can influence the subordinated credit institutions. This influence is "dominant" because the credit institutions can expect to be supported by the joint liability scheme only if they pursue their business policy "in good times" as requested by the liable undertaking. Even if Section 30 (2a) BWG does therefore not expressly refer to a right of the central institution to issue instructions, it is clear that the central institution can control the subordinated credit institutions' business and market policy because it holds a majority interest in the liable undertaking.

According to a proposal of the Commission to amend the accounting provisions, Art 1 (2) of the Consolidated Accounts Directive shall be adjusted to IAS so that in the future consolidation does no longer require the capital of the parent undertaking and the subsidiary undertakings to be connected, and a consolidation is already permitted if the parent undertaking "can" assert a dominant influence on the subsidiary undertaking, but does not actually do so. In the future, Section 30 (2a) BWG will therefore not only implement Article 1 (1) (c) but also Article 1 (2) of the Consolidated Accounts Directive.

As regards the laws governing bank accounts, Section 30 (2a) BWG cannot be subsumed under a relevant element, in particular not under Art 43 (2) (e), because the central institution's influence is not sufficient to refer to a "uniform management" as defined by accounting law. However, the Bank Accounts Directive expressly provides that all consolidation events of the Consolidated Accounts Directive apply also to credit institutions, so that Section 30 (2a) BWG is also compatible with the Bank Accounts Directive.

1.3. Compatibility with the Codified Directive

As regards the laws governing bank supervision, Section 30 (2a) BWG can be subsumed under Art 54 (4) first indent of the Codified Directive. This provision stipulates that the competent authorities shall determine whether and how consolidation is to be carried out for purposes of bank supervision if a credit institution can exercise "significant influence" over one or more other credit institutions. Two questions arise: on the one part, whether Section 30 (2a) BWG defines an event of "significant influence" and, on the other part, whether the Austrian legislator would have been obliged to grant the Financial Market Supervision Authority (*FMA*) discretion in Section 30 (2a) BWG to prescribe consolidation.

The first question of interpreting the term "significant influence" (just like the term "dominant influence" set forth in the Consolidated Accounts Directive) is not easy to answer, because neither relevant secondary law nor ECJ case law provide a definition. It is even more difficult to interpret the term because the same term was replaced by "material influence" elsewhere in the Directive. However, this question of interpretation need not be answered: If Section 30 (2a) BWG already qualifies as an event of

"dominant influence", it follows that the central institution's influence defined in Section 30 (2a) BWG is also "significant".

As regards the second question of interpretation concerning the lack of discretion of the FMA, the Austrian legislator, based on Community law and based on the Austrian Constitution, is not only entitled but even obliged to restrict the FMA's discretion and to precisely determine when "significant influence" as set forth in Art 54 (4), first sentence of the Codified Directive is satisfied for purposes of consolidation of groups of credit institutions. Had the legislator taken over the term "significant influence" from the Directive without further specification and left it to the FMA to determine when influence is sufficient for the purposes of consolidation of groups of credit institutions, the FMA would have been granted unrestricted discretion because the Directive insufficiently defines the term "significant influence", which is contrary both to the Austrian Constitution and to Community Law.

We believe that the question whether the full consolidation resulting from the new definition of a group of credit institutions in Section 30 (2a) BWG is proportional must be answered as follows. One of the purposes of the Codified Directive is to increase the protection of depositors. Full consolidation provides better transparency for depositors and therefore increased protection than does partial consolidation. This was why the EC legislators designed full consolidation as the standard and partial consolidation as the exception. Relevant scholarly writing accordingly demands that those Codified Directive provisions that require a partial consolidation be interpreted narrowly. The Austrian legislators' decision to use the choice they are given under Art 54 (4) of the Codified Directive in favour of a full consolidation both corresponds to the restrictive interpretation of partial consolidations advocated by legal scholars and to the Directive's purpose of promoting the protection of depositors to the greatest extent possible. This is also the reason why we believe that ordering a full consolidation is not an "arbitrary" exercise of this choice. As regards the objection that a full consolidation runs contrary to the "the principle of proportionality that derives from primary Community law", it is not clear why a full consolidation would impede the freedom of establishment of foreign banks more than a partial consolidation.