MARKET NOTICE: OUTLINE OF THE UK GOVERNMENT'S NATIONAL LOAN GUARANTEE SCHEME

1. The UK Government's National Loan Guarantee Scheme (NLGS), which provides financial support to small businesses by reducing the cost of borrowing from participating institutions, will operate as set out below.

Purpose of the scheme

2. The scheme was announced on 29 November 2011. It is intended to reduce the cost of borrowing for small businesses that do not have direct access to capital markets.

State Aid approval

3. The scheme received State Aid approval on 14 March 2012. State Aid approval is reviewed twice a year, in June and December. The first approval from the European Commission (EC) is valid until 30 June 2012. Subsequent extensions will be published on the DMO website at: www.dmo.gov.uk/nlgs.

4. There are two aspects of the scheme that are subject to the EC's approval: the provision of government guarantees to participating institutions; and the level of aid provided to small businesses through discounts on loan rates. Information on the decision related to State Aid Approval can be found on the EC's website.[1]

Access to the NLGS

5. In order to be eligible to participate in the scheme an institution must:

- be UK incorporated (or a UK subsidiary of a foreign institutions);
- have a significant role in the UK banking system and overall economy;[2]
- be regulated by the Financial Services Authority (FSA); and,
- have a track record of lending to small businesses for 6 months prior to joining the scheme.

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[1] http://europa.eu/rapid/pressReleasesAction.do?reference=IP/12/244&format=HTML&aged=0&language=EN&guiLanguage=en

[2] In addition to lending to small businesses, in assessing the role of an institution HM Treasury will take account of the size of an institution's sterling Eligible Liabilities as calculated by the Bank of England. For further details on the definition of Eligible Liabilities, please follow this link to the Bank of England website: http://www.bankofengland.co.uk/statistics/Pages/faq/faq_crds.aspx.

6. Please refer to the scheme rules available at: www.dmo.gov.uk/nlgs for the full requirements that need to be met before an institution can be considered to be eligible.

Allocation of guarantees to institutions

7. The size of allocation for each participating institution will be based, at the discretion of the HM Treasury, on a number of factors including the institution's:

- market share of lending to small businesses, gross and net lending to small businesses
- track record of lending to small businesses
- their capacity to lend under the scheme

8. The minimum allocation is £100 million.

Guarantee

9. The guarantee will be provided by HM Treasury in relation to eligible instruments issued by the participating institution or a member of its group. The guarantee is unconditional, irrevocable and ensures timely payment. The Deed of Guarantee is available to be viewed at: www.dmo.gov.uk/nlgs.

Period during which guarantees will be issued

10. It is intended that the Government will guarantee specified bank and building society debt instruments issued during a period not greater than 24 months from 20 March 2012, subject to State Aid approval.

Fees

11. The fee rate payable to HM Treasury on guaranteed issues will be based on an institution's cost of unsecured debt issuance and is subject to a minimum fee set by the EC's methodology, which can be found on the EC's website.[3] The cost of unsecured unguaranteed debt is estimated by using the institution's 5-year Credit Default Swap (CDS) spreads. HM Treasury may apply its own estimate of an appropriate CDS spread if public data is unavailable. This fee will be applied to the principal amount of the debt instrument. In addition, HM Treasury will charge an additional fee where it guarantees non-sterling denominated issuance.

[3] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2011:356:0007:0010:EN:PDF.

12. This fee is payable three-monthly in arrear commencing on the earlier of the third business day after the date of the guarantee certificate and the date of the guaranteed debt issuance and ending on (but excluding) the scheduled maturity date of the Guaranteed Liabilities.

Instruments guaranteed

13. Instruments eligible to be guaranteed are certificates of deposit (CDs) and senior unsecured bonds and notes. The guarantee may be applied to stand-alone debt securities or to instruments issued by way of programmes, and to plain vanilla, non-complex instruments only, in each case approved by HM Treasury at its sole discretion.

14. Instruments must be denominated in sterling, euro, US dollars or Yen.

Terms of guaranteed instruments

15. Instruments guaranteed under the scheme must have a maturity of at least one year and a maximum of five years. The Commission also requires that of the £20bn of government-guaranteed debt, a maximum of one third can have a maturity of between three and five years.

16. The issuer may not exercise early redemption clauses, either in full or in part, ahead of the scheduled maturity date of the instrument guaranteed under the scheme unless agreed with HM Treasury.

Eligibility of guaranteed instruments as collateral in the Bank of England's Sterling Monetary Framework

17. The Bank of England is announcing that it will accept as collateral instruments issued under this Scheme. So long as the guarantee applies, these instruments will form part of the wider collateral and Discount Window Facility securities sets and be eligible for operations where collateral from these sets is accepted. Further details of collateral eligible for the Bank's operations, including the haircuts that are applied, can be found on its website at: http://www.bankofengland.co.uk/markets/Pages/money/eligiblecollateral.aspx.

Risk weighting in FSA regulatory capital requirements

18. The Financial Services Authority (FSA) has deemed that under the Standardised Approach guaranteed securities will qualify for zero risk-weighting for capital adequacy purposes where both the Government guarantee and the exposure are denominated in sterling (under BIPRU 5.7.25). A guaranteed non-sterling exposure can also be zero weighted under the standardised approach, although under a different set of rules which depend upon the creditworthiness of the guarantor (BIPRU 3.4.1-3.4.3).

Eligible businesses

19. All UK businesses with a group annual turnover of not more than £50 million, including UK incorporated companies and branches of foreign incorporated parents with a legitimate business in the UK, may apply at participating institutions. [4]

20. The assessment and decision for granting a loan under the scheme rests with participating institutions. Participating institutions will operate the scheme in a fair and non-discriminatory way, without distorting their normal distribution of lending to businesses.

Passing through the benefit to businesses

21. Within three months of issuance of instruments guaranteed under the scheme, participating institutions are required to offer or otherwise commit to credit facilities to eligible businesses to pass through the benefit they receive from the issuance, and within a further three months period the relevant facilities must be drawn down. If participating institutions do not pass through the benefit in this way, they must repay the benefit to HM Treasury with interest.

22. At the end of the scheme the total present value of benefit that has been passed through to small businesses together with any amount returned to the HM Treasury has to match the aggregate present value benefit amount derived from government guaranteed issuance.

23. Participating institutions need to demonstrate they have successfully passed through at least 70% of the derived benefit associated with issuance under their current allocation and 100% of any prior allocation before they are entitled to apply for an additional allocation of guarantees.

Support to small businesses

24. Participating institutions are required to provide a discount of 100 basis points relative to their standard interest rates for loans under the National Loan Guarantee Scheme.

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[4] Please follow this HM Treasury web link for general information on the scheme: http://www.hm-treasury.gov.uk/nlgs.

Monitoring and reporting

25. Participating institutions are required to provide regular information to HM Treasury on their use of the National Loan Guarantee Scheme. The information will be used to inform HM Treasury of their performance under the scheme and compliance with the Scheme Rules and will inform future allocations of guarantees.

Reimbursing participating institutions for expenses incurred in operating the scheme

26. HM Treasury may reimburse participating institutions the additional administration and monitoring expenses associated with the NLGS.

Application process

27. Participating institutions that wish to apply for a government guarantee in respect of any issuance are required to use the proforma application form available on the UK Debt Management Office (DMO) website. This will need to be completed, signed and returned to the DMO.

28. Applicants will be encouraged to keep the DMO informed of any plans to utilise the Scheme in a timely manner. Typically, applications received by the DMO before 10:00am on any UK business day will, providing that they are complete and meet the necessary criteria, be approved on the same day. Those received after 10:00am will typically be approved on the following business day.

Published information

29. HM Treasury's Deed of Guarantee and the Rules of the Scheme are available at: www.dmo.gov.uk/nlgs.

30. General enquires related to the scheme, should be addressed to HM Treasury at: public.enquiries@hm-treasury.gov.uk.