

PROCEDURY ZWIĄZANE Z REALIZACJĄ POLITYKI KONKURENCJI

KOMISJA

POMOC PAŃSTWA – BELGIA

Pomoc państwa C 18/09 (ex N 360/09) – Dokapitalizowanie i pomoc związana z aktywami dla grupy KBC

Zaproszenie do zgłaszania uwag zgodnie z art. 88 ust. 2 Traktatu WE

(Tekst mający znaczenie dla EOG)

(2009/C 216/08)

Pismem z dnia 30 czerwca 2009 r., zamieszczonym w autentycznej wersji językowej na stronach następujących po niniejszym streszczeniu, Komisja powiadomiła władze belgijskie o swojej decyzji w sprawie wszczęcia postępowania określonego w art. 88 ust. 2 Traktatu WE dotyczącego wyżej wspomnianego środka pomocy.

Zainteresowane strony mogą zgłaszać uwagi na temat środka pomocy, w odniesieniu do którego Komisja wszczyna postępowanie, w terminie jednego miesiąca od daty publikacji niniejszego streszczenia i następującego po nim pisma. Uwagi należy kierować do Kancelarii ds. Pomocy Państwa w Dyrekcji Generalnej ds. Konkurencji Komisji Europejskiej na następujący adres lub numer faksu:

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Otrzymane uwagi zostaną przekazane władzom belgijskim. Zainteresowane strony zgłaszające uwagi mogą wystąpić z odpowiednio uzasadnionym pisemnym wnioskiem o objęcie ich tożsamości klauzulą poufności.

STRESZCZENIE

I. PROCEDURA

(1) Grupa KBC otrzymała wkład kapitałowy w wysokości 3,5 mld EUR (środek 1) od federalnych władz belgijskich, co Komisja zaakceptowała w dniu 18 grudnia 2008 r.⁽¹⁾ W dniu 18 czerwca 2009 r. grupa KBC przedstawiła plan restrukturyzacyjny w związku z pierwszym dokapitalizowaniem. W dniu 6 lutego 2009 r. region Flandrii przedstawił projekt zgłoszenia kolejnego wkładu kapitałowego dla grupy KBC w wysokości 3,5 mld EUR (środek 2). Kolejne informacje otrzymano w dniu 27 lutego i podczas spotkania w dniu 9 marca. Komisja otrzymała dodatkowe informacje w dniu 10 czerwca 2009 r. W dniu 14 maja 2009 r. ogłoszono działania na rzecz uwolnienia grupy KBC od kłopotliwych aktywów (środek 3). Komisja otrzymała informacje o tym działaniu w dniach 19 maja 2009 r. i

10 czerwca 2009 r. Zarówno środek 2 i 3 zostały oficjalnie zgłoszone Komisji w dniu 18 czerwca 2009 r.

II. STAN FAKTYCZNY

(2) Beneficjentem pomocy jest KBC, zintegrowana grupa bankowo-ubezpieczeniowa, obsługująca głównie klientów detalicznych, małe i średnie przedsiębiorstwa oraz klientów z zakresu bankowości prywatnej. Grupa KBC jest trzecią pod względem wielkości instytucją finansową w Belgii, ale ma też silną pozycję w państwach Europy Środkowej i Wschodniej. Grupa KBC jest także obecna w Rosji, Rumunii, Serbii, kilku krajach Europy Zachodniej oraz w mniejszym stopniu w Stanach Zjednoczonych i Azji Południowo-Wschodniej.

(3) Głównym powodem problemów grupy KBC jest pogorszenie ratingu kredytowego portfela dodatkowo zabezpieczonych papierów dłużnych (CDO). Grupa KBC wytworzyła syntetyczne CDO o wartości 27 mld EUR. Zawierania

⁽¹⁾ N 602/08, Dokapitalizowanie KBC, Dz.U. C 109 z 13.5.2009, s. 4.

utrzymujące się na rynkach finansowych od 2007 r. negatywnie wpłynęły na wartość portfela CDO należącego do grupy KBC. Agencje ratingowe znacząco zwiększyły szacowane ryzyko kredytowe, co zmusiło grupę KBC do znacznych odpisów na wspomnianych CDO. Odpisy te negatywnie wpłynęły na strukturę kapitałową grupy KBC. Narażenie grupy KBC na straty z tytułu portfela CDO było jeszcze większe, gdy MBIA, prywatny ubezpieczyciel zabezpieczający ryzyko związane z CDO o wartości 14,4 mld EUR, został zrestrukturyzowany, w wyniku czego agencje ratingowe gorzej oceniły to przedsiębiorstwo, co wywołało poważne wątpliwości dotyczące wartości ubezpieczenia i w konsekwencji części grupy KBC zajmującej się finansami strukturyzowanymi.

(4) W zaistniałej sytuacji władze belgijskie zdecydowały się na interwencję w postaci dokapitalizowania banku oraz uwolnienia go od aktywów o obniżonej jakości. Do inicjatyw tych należą:

(i) Drugie dokapitalizowanie w wysokości 3,5 mld EUR kapitału podstawowego warstwy 1 przez władze flamandzkie w formie bezterminowych papierów wartościowych typu mieszanego bez prawa głosu (środek 2) porównywalne do dokapitalizowania zaakceptowanego wcześniej przez Komisję w odniesieniu do grupy KBC (środek 1). Dokapitalizowanie to przybierze formę wkładu kapitału hybrydowego, który kwalifikuje się jako kapitał podstawowy warstwy 1. Wyemitowane papiery wartościowe nie podlegają zamianie na zwykłe akcje i można je wykupić tylko, gdy osiągną wartość 150 % ceny emisyjnej. Posiadaczom tych papierów wartościowych nie przysługuje prawo głosu. Dochody uzyskane z wkładu kapitałowego w wysokości 3,5 mld EUR zostaną podzielone pomiędzy KBC Bank i KBC Insurance w taki sposób, że [0–1] mld EUR zostanie dodane do kapitału KBC Insurance zwiększając wskaźnik wypłacalności z [...] ⁽²⁾ % do [...] %. Pozostała część dochodów ([2,5–3,5] mld EUR) zasili kapitał podstawowy pierwszej kategorii KBC Bank. Gwarancja federalnych władz belgijskich na 15 CDO o nominalnej wartości 20 mld EUR (środek 3). Gwarancją objęte jest zarówno ryzyko zabezpieczane przez MBIA (14,4 mld EUR), jak i papierami dłużnymi zatrzymanymi przez grupę KBC (łącznie 5,5 mld EUR).

(ii) Środek 3 składa się z trzech transz. Pierwsza transza strat w kwocie 3,2 mld EUR zostanie poniesiona w całości przez grupę KBC („pierwsza strata”). Straty poniesione w drugiej warstwie w kwocie 2 mld EUR powyżej „pierwszej straty” będą pokryte, na prośbę grupy KBC, przez państwo w 90 % (1,8 mld EUR), podczas gdy pozostałe 10 % ryzyka obarcza grupę KBC, poprzez subskrypcję nowych zwykłych akcji grupy KBC i papierów wartościowych typu mieszanego po cenie rynkowej („zakres dotyczący akcji”). Wszystkie straty powyżej „wysokości kapitału własnego” (do 14,8 mld EUR) zostaną pokryte w gotówce przez państwo do wysokości 90 %, podczas gdy 10 % ryzyka poniesie grupa KBC („zakres dotyczący gotówki”). Pierwsza strata, wysokość kapitału własnego i wysokość gotówki jak i czas gwarancji zostaną określone osobno dla każdego instrumentu. Jeśli chodzi

o „zakres dotyczący akcji”, grupa KBC uiszcza opłatę z tytułu gwarantowania emisji w wysokości 650 pb rocznie (tj. 120 milionów EUR rocznie). Jeśli chodzi o „zakres dotyczący gotówki”, grupa KBC uiszcza opłatę gwarancyjną, która wyrówna oczekiwane straty w portfelu CDO (1,13 mld EUR).

(5) Połączenie środka 2 i 3 doprowadzi do uzyskania wartości 11 % dla wskaźnika warstwy pierwszej i [...] % wskaźnika podstawowego warstwy pierwszej. Gwarancja zmniejszy też aktywa ważne ryzykiem o 6,3 mld EUR.

III. OCENA

(6) Komisja zdecydowała się tymczasowo zaakceptować środek 2 i 3 na okres 6 miesięcy pod warunkiem, że władze belgijskie przedłożą szczegółowy plan restrukturyzacyjny, jednocześnie otwierający formalne postępowanie wyjaśniające dotyczące pewnych aspektów środka 3.

(7) Jeśli chodzi o środek 3, Komisja uważa, że jest on zgodny z pewnymi aspektami komunikatu w sprawie aktywów o obniżonej jakości ⁽³⁾, mianowicie kwalifikowalnością aktywów [...]. Z drugiej strony, na podstawie dostępnych informacji Komisja powzięła wątpliwość, czy wycena i określenie rzeczywistej wartości ekonomicznej portfela CDO, które według władz belgijskich wynosi [...] mld, jest odpowiednia. Precyzyjniej rzecz ujmując, Komisja ma wątpliwości dotyczące dokładności założeń oraz metodologii, w tym założeń w sprawie korelacji dotyczących papierów komercyjnych i papierów wartościowych zabezpieczonych aktywami stanowiących aktywa bazowe portfela, założeń dotyczących cen nieruchomości oraz założeń dotyczących poziomu zaległości przedsiębiorstw wykorzystanych w modelu. Ponieważ wątpliwości dotyczące wyceny mają wpływ na ocenę Komisji odnośnie do podziału obciążeń i wynagrodzeń, Komisja nie jest w stanie podjąć decyzji w sprawie proponowanych zasad. Poza tym, Komisja otrzymała niewystarczające informacje, potrzebne do oceny czy zasada przejrzystości i przekazania odpowiednich danych zostały zachowane.

(8) Grupa KBC już przedłożyła, w związku z otrzymaniem pierwszego wkładu kapitałowego, plan restrukturyzacyjny w dniu 18 czerwca 2009 r. Jednakże, wzięwszy pod uwagę skalę i powtarzalność tych środków, Komisja uważa, że potrzebny jest głęboki plan restrukturyzacyjny. Dlatego Komisja zwraca się do władz belgijskich o przedłożenie w ciągu trzech miesięcy szczegółowego planu restrukturyzacyjnego, uwzględniającego pomoc przyznaną grupie KBC drugim i trzecim środkiem.

TEKST PISMA

„The Commission wishes to inform the Belgian authorities that, having examined the information supplied by your authorities on the measures referred to above, it has decided to raise no objections to both measures and temporarily approves them for six months. However, at the same time it will initiate the procedure laid down in Article 88(2) of the EC Treaty with regard to the asset relief measure since the Commission has doubts as to the compatibility of certain aspects of the measure when assessed in the light of the Commission's Communication on the treatment of impaired assets.

⁽²⁾ Tajemnice przedsiębiorstwa Informacja poufna; dane liczbowe zostały w miarę możliwości zastąpione odpowiednimi zakresami podanymi w nawiasach kwadratowych.

⁽³⁾ Komunikat Komisji w sprawie postępowania z aktywami o obniżonej wartości we wspólnotowym sektorze bankowym, przyjęty dnia 25.2.2009 r.

1. PROCEDURE

- (1) In December 2008, KBC received a capital injection by the Belgian authorities of EUR 3,5 billion (hereafter “measure 1”), which was approved by the Commission on 18 December 2008 for a period of six months ⁽⁴⁾. On 6 February 2009, the Belgian authorities submitted a draft notification of its intention to inject another EUR 3,5 billion of capital into KBC in two tranches of EUR 2 billion and EUR 1,5 billion (“measure 2”). The Commission received further information regarding this measure on 27 February and met with the Belgian authorities on 9 March. The Commission received additional information on 10 June 2009.
- (2) On 14 May 2009, KBC announced that it had reached an agreement with the Belgian authorities on an asset relief measure (“measure 3”). The Commission received further information on this measure on 19 May 2009 and 10 June 2009. Measures 2 and 3 were notified to the Commission on 18 June 2009. Both measures will be implemented upon Commission approval.
- (3) In conformity with the Commission's decision in Case N 602/08 regarding measure 1 the Belgian authorities submitted a plan for KBC on 18 June 2009.

2. DESCRIPTION OF THE MEASURES

2.1. The beneficiary

- (4) The KBC Group NV is the holding company of KBC Bank, KBC Insurance and KBL European Private Bankers (i.e. KBL EPB). KBC is an integrated bank insurance group, catering mainly for retail customers, small and medium enterprises (SMEs) and private banking clientele. KBC is one of the main financial institutions in Belgium. Besides its activities in Belgium, central and eastern Europe, KBC is present in Russia, Romania, Serbia, several Western European countries and to a lesser extent in the US and Southeast Asia.
- (5) KBC is publicly quoted. As of 31 December 2008, the majority of the shares (54,3 %) were held by a number of large shareholders: KBC Ancora (23 % of the ordinary shares), Cera (7 %), MRBB (12 %), and other core shareholders (11 %). KBC group companies hold 5 % of the ordinary shares and the free float constitutes 42 %.
- (6) For 2008, total assets on the balance sheet of KBC amounted to (non-audited) EUR 355,596 billion. The market value of KBC has fallen significantly, from EUR 23 billion on 1 August 2008 to EUR 5 billion on 15 June 2009. KBC employs 56 716 people worldwide, 19 196 of whom are in Belgium and 31 947 of whom are in Central and Eastern Europe and Russia. KBC has 8,2 million customers in Central and Eastern Europe and Russia (estimates 2007).
- (7) KBC's management structure consists of the following five main business units:

- (i) Belgium Business Unit: it groups all the banking and insurance activities in Belgium. This includes the retail and private banking activities of the KBC Bank in Belgium, the activities of KBC Insurance in Belgium and a number of Belgian subsidiaries.
- (ii) The Central & Eastern Europe and Russia (CEER) Business Unit: it comprises all group banking and insurance activities (i.e. retail bancassurance and merchant banking) pursued in Central and Eastern Europe and in Russia.
- (iii) Merchant Banking Business Unit: it groups the services provided to bigger SMEs and corporate customers, and all market activities worldwide (including Belgium, but not Central and Eastern Europe and Russia).
- (iv) European Private Banking Business Unit: it comprises the activities of both the KBL European Private Bankers group (KBL EPB) and the insurance company, VITIS Life.
- (v) Shared Services & Operation Business Unit: it provides support to and serves as a product factory for the other business units. It encompasses a number of divisions that deliver products to the group's other business units.

- (8) Profit contribution of the five business units is as follows (1H2008): Belgium Business Unit: 52 %, CEER Business Unit: 32 %, Merchant Banking Business Unit: 14 %, European Private Banking Business Unit: 8 %, Shared Service & Operations Business Unit: 6 %.
- (9) KBC has a strong position in the Belgium financial sector, more specifically on the following submarkets (market shares 2007): funds [...] ⁽⁵⁾, home loans [...], commercial credit to companies [...], commercial credit to natural persons [...], credit cards [...], current accounts [...], deposit accounts [...], bank cards [...], Branch (Tak) 23 [...] and damage insurance [...].

2.2. Events triggering the measures

- (10) In December 2008, KBC benefited from a capital injection of EUR 3,5 billion into the Group (measure 1). At the time, the intervention was needed as KBC had announced 3rd quarter losses of EUR 906 million, which were a consequence of provisions it was forced to make because of the downward revaluation of its Collateralized Debt Obligations (“CDOs”). The revaluation led to a loss in confidence on the market as regards KBC that was reflected in the share price and CDS spreads. Also, in view of the financial crisis, markets started to expect higher capital ratios for banks. As a result of the Belgian State's intervention as approved by the Commission ⁽⁶⁾, KBC's ratios were restored in line with market requirements.

⁽⁴⁾ See footnote 1.

⁽⁵⁾ See footnote 2.

⁽⁶⁾ See footnote 1.

Measure 2 — The capital injection by the Flemish authorities

- (11) In January 2009, Moody's announced that it was going to change the models used to value CDOs. This had the effect of further lowering the ratings of a large majority of corporate synthetic CDOs⁽⁷⁾. Reason for this was a strong increase in the likelihood of default for all corporate credits in synthetic CDOs as well as an increase in the default correlation Moody's applies to corporate portfolios. As a consequence, investors in KBC were uncertain as to the consequences of this announcement for the value of KBC's CDO portfolio, causing its share price to drop by more than 20 % in a day.
- (12) Upon Moody's announcement, KBC took a number of measures, the most important of which is the write-down of all non-super senior CDO notes in its portfolio to zero, resulting in markdowns of EUR 2,6 billion in the fourth quarter of 2008. These write-downs negatively affected KBC's capital ratios. The core Tier-1 ratio dropped to 7,2 % and the Tier 1 ratio to 9,7 %. [...]
- (13) Because of the decrease of its capital ratios, KBC needed strengthening of its capital base. Against this background, on 22 January 2009, the Flemish government announced that it was prepared to strengthen the capital base of KBC by up to EUR 3,5 billion.

Measure 3 — The asset relief measures by the Federal government

- (14) On 18 February 2009, MBIA Inc., headquartered in Armonk, New York, a private insurer hedging EUR 14,4 billion of KBC's CDO exposures, announced its decision to split its operating business into two sister companies. One would continue the municipal bond insurance business of MBIA, and the other would be structured as an entity for the run-off of the CDO/RMBS and structured finance business. Following this restructuring, the entity containing MBIA's obligation concerning CDO/RMBS and structured products was downgraded by Moody's from Baa1 to B3. This led to a considerable decrease in the value of the insurance KBC had bought from MBIA to absorb losses on its CDO portfolio. The deterioration of KBC's credit profile of corporate CDOs made it necessary for KBC to increase the counterparty risk associated with MBIA through a provision increase booked as a Credit Value Adjustment ("CVA")⁽⁸⁾. KBC's CVA on MBIA was increased from 40 % at the end of 2008 to 60 % in May 2009. Total provisions taken by KBC for counterparty risk associated with MBIA amount to EUR 2,5 billion.
- (15) Apart from the adverse changes in the CDO portfolio resulting from MBIA's restructuring, KBC was also experi-

encing increased volatility in its P&L account due to the volatility in credit spreads that were directly impacting the market valuation of KBC's CDO portfolio. The widening of the credit spreads and the worsening economic conditions resulted in a negative mark-to-market value adjustment of KBC's super senior holding of EUR 1,3 billion.

- (16) Combined, the evolution of the credit spreads and the restructuring of MBIA's business resulted in a negative value adjustment of EUR 3,8 billion at the end of the first quarter of 2009. This also negatively influenced KBC's capital ratios, which dropped to 5,3 % core Tier-1 and 7,1 % Tier-1, while the solvency ratio for the insurance business was reduced to 93 %. Following these events, KBC reached an agreement with the Belgian authorities on an asset relief measures.

2.3. The measures*Measure 2 — The capital injection by the Flemish authorities*

- (17) The recapitalisation will take the form of an injection of hybrid capital which qualifies as core Tier 1 capital. The terms of the deal are practically identical to the previous capital injection approved by the Commission on 18 December 2008 for a period of six months, except that the securities are not convertible into ordinary shares, and are only redeemable at 150 % of the issue price.
- (18) According to KBC's initial plan, the capital injection measure would consist of two tranches. Tranche 1 was to be issued, subscribed to, and paid in full on the issue date, at the rate of EUR 29,50 per security. The total value of tranche 1 would amount to EUR 2 billion and would be used to strengthen KBC's core Tier 1 capital immediately. Tranche 2, amounting to EUR 1,5 billion, would be called upon if and when KBC Group's capital basis required it. However, as a consequence of the deterioration of its capital position since the first quarter, KBC announced on 14 May that it will take up the second tranche immediately after the Commission's approval of the measure.
- (19) The EUR 3,5 billion securities issued under the two tranches, will produce an annual interest equal to the higher of:
- (i) EUR 2,51 per security (equivalent to interest of 8,5 %), non-cumulative, payable annually in arrears⁽⁹⁾;
 - (ii) 110 % of the dividend paid on ordinary shares for the fiscal year 2008 (for interest due in respect of the year 2009);
 - (iii) 120 % of the dividend paid on ordinary shares for the fiscal year 2009 (for interest due in respect of the year 2010); or
 - (iv) 125 % of the dividend paid on ordinary shares for the fiscal year 2010 and onwards (for interest due in respect of the year 2011 and onwards).

⁽⁷⁾ CDOs are a type of asset-backed security and a structured finance product in which a distinct legal entity, a special purpose vehicle (SPV), issues bonds or notes against an investment in an underlying asset pool. Pools may differ with regard to the nature of their underlying assets and can be collateralised either by a portfolio of bonds, loans and other debt obligations, or be backed by synthetic credit exposures through use of credit derivatives and credit-linked notes.

⁽⁸⁾ The CVA percentage reflects the probability that MBIA would not be able to perform and is calculated as a % of the mark to market value of the insured Super Senior positions.

⁽⁹⁾ Exceptionally for the year 2009: if the issuer decides to pay an interim dividend in 2009, then KBC will pay to the securities holder an interest equal to EUR 1,25 per security, payable on the payment date of the interim dividend but no later than 31 December 2009, the remainder being due and payable on the tenth banking day following the Annual General Meeting in 2010.

- (20) The interest will only be paid if a dividend is paid on the ordinary shares and will be paid in cash. Furthermore, interest on the securities will only be due and payable on a non-cumulative basis, if and when a dividend is approved, provided that the KBC's capital adequacy position is and remains satisfactory both before and after the payment in the opinion of the Belgian Banking Finance and Insurance Commission ("CBFA").
- (21) With respect to the tranche 1 securities, interest will commence to accrue on the issue date. For tranche 2 securities, interest will commence to accrue as from the day on which the issue price for such tranche 2 securities is paid. Since both tranches are supposed to be issued as soon as the European Commission approves the capital injection measure, the interest for both tranches will start to accrue on the same day. The securities rank *pari passu* with ordinary shares in KBC and with the securities held by the Belgian State. No voting rights are attached to securities.
- (22) The proceeds of the EUR 3,5 billion capital injection will be split between KBC Bank and KBC Insurance in such a way that EUR [0-1] billion will add to KBC Insurance capital; the remaining proceeds ([EUR 2,5-3,5] billion) will flow to KBC Bank Core Tier-1 capital.
- (23) There is one redemption scenario for these securities, which is at the initiative of KBC. KBC has a call option, giving it the right to redeem all or some of the issued securities at a price of EUR 44,25 per security (being 150 % of the issue price), plus payment of any accrued interest, any time after the issue date. This option is conditional on the agreement of the CBFA.
- (24) Subject to applicable law and to corporate governance practices, generally accepted under applicable stock listing regimes, the Belgian authorities will have the right to recommend two Board members at the next general shareholders' meeting (this in addition to the two nominees from the previous measure). The Supervisory Board approval items listed below require approval by one of the investor's nominees:
1. the issue or acquisition of its own shares by the Issuer (other than related to the Securities and other than as part of regular hedging operations and the issuing of shares according to employment schemes);
 2. [...];
 3. acquisition by the Issuer or any of its subsidiaries of a participating interest in the capital of another company amounting to one-quarter or more of the Issuer's consolidated capital and reserves as disclosed in its consolidated balance sheet of the previous quarter or a material increase or decrease of such participating interest;
 4. investments involving an amount equal to one-quarter or more of the Issuer's consolidated capital and reserves as disclosed in its consolidated balance sheet of the previous quarter;
 5. a proposal to wind up the Issuer;
 6. filing of a petition for bankruptcy or moratorium for the Issuer;
 7. proposal for split-off, dissolution of the Issuer;
 8. [...];
 9. a change of the remuneration policy [...]; and
 10. [...].
- (25) One of the nominees will also have a seat on the KBC Group's (including KBC Bank NV and KBC Verzekeringen NV) Audit Committee, Remuneration Committee and Nomination Committee.
- (26) As part of the transaction, KBC commits to develop a sustainable remuneration policy for the Executive Committee and Senior Management. KBC's Executive Committee and senior management incentive schemes will be linked to long-term value creation taking account of risk and restricting the potential for "rewards for failure". KBC's Executive Committee limits exit schemes or statutory compensation for dismissal to twelve months' fixed salary.
- (27) KBC has also provided undertakings with regard to maintaining lending to the real economy. A control mechanism ("opvolgingscomite") will be put in place to follow up on these undertakings.
- Measure 3 — The asset relief measures by the Federal government*
- (28) In order to shield KBC from further write-downs on its CDO portfolio, as well as to boost its capital ratios, the Belgian Federal authorities decided to grant protection on KBC's synthetic CDO portfolio, usually held through its subsidiary KBC Financial Products but sometimes through other structures.
- (29) The Belgian State has granted protection on KBC's CDO portfolio amounting to EUR 20 billion⁽¹⁰⁾. The EUR 20 billion notional exposure to 15 CDOs is made up of EUR 14,4 billion of super senior and class A notes hedged with MBIA, and EUR 5,5 billion of super senior, super mezzanine and class A notes retained by KBC (EUR 4 billion through Assurisk and EUR 1,5 billion through KBC FP).
- (30) The EUR 20 billion transaction is structured in three tranches. The first tranche is constituted by a first loss amounting to EUR 3,2 billion which is borne by KBC. This loss was entirely provisioned for as at 31 March 2009.
- (31) The second part of the transaction deals with the next EUR 2 billion of losses, which are also provisioned for as of 31 March 2009. For any losses within this range (Equity Range), the Belgian State undertakes to subscribe for 90 % of the losses to new KBC shares or hybrid securities at market value⁽¹¹⁾. Effectively, the Belgian State has committed to providing a standby equity facility to KBC that can be triggered by specific loss making events on KBC's CDO portfolio.

⁽¹⁰⁾ KBC originally retained a greater exposure to its CDO portfolio. However, all exposure above EUR 20 billion has been written off, while the portion with Lloyds TSB (EUR 1,6 billion) is not covered by the measure.

⁽¹¹⁾ Average share price in 30 days preceding transaction.

- (32) The Equity Range is subject to several conditions. Firstly, KBC maintains the option to not call the guarantee and, therefore, to opt out from the equity issuance to the State. Secondly, if at the moment when the State bought KBC shares, it would acquire more than 30 % voting rights, which could require it to launch a mandatory takeover bid, it will have the option to subscribe to hybrid capital instead. Thirdly, in the event that the State decides to sell its shares to a third party, KBC has the right to first refusal in relation to this sale.
- (33) The attachment point (i.e. starting point) for the Equity Range was fixed, taking as a reference parameters which would enable KBC Bank to maintain a core tier 1 ratio above [6-9] % and KBC Insurance solvency ratio above [120-160] %. Therefore the parameters were not based on a valuation of the portfolio.
- (34) Finally, the third tranche amounts to EUR 14,8 billion (Cash Range). Any losses exceeding EUR 5,2 billion (EUR 3,2 billion first loss and EUR 2 billion Equity Range) will be split between the State (90 %, i.e. EUR 13,3 billion) and KBC (10 %, i.e. EUR 1,5 billion). The State will compensate KBC in cash for any losses suffered in the cash range. For the third tranche, the attachment point is based on the midpoint between expected losses in Scenario 2 and 3, based on the CDO valuation report of the Belgian State's independent expert [...] (April 2009) ⁽¹²⁾.
- (35) The Guarantee will apply on a transaction basis. As there are covered instruments relating to 15 CDOs (each a transaction), there are thus effectively 15 guarantees ⁽¹³⁾. As a result, each of the 15 synthetic CDOs has a different attachment point and, therefore, a different expected loss. Consequently, the CDOs would need to be assessed individually and the guarantee provided will be individual for each CDOs (i.e. there will not be a single guarantee on the aggregated portfolio).
- ⁽¹²⁾ [...] have provided 4 scenarios which they use to estimate losses under certain conditions. The underlying variables are future house prices (Case-Shiller House Price Appreciation — HPA), corporate default rates and the rate of recovery from MBIA in the case of default. They also provide an estimate of market implied losses, using observable market data to plug into a mark-to-model approach. However [...] have not clarified which scenario they regard as the base case, which would correspond with the Real Economic Value in the Commission's Impaired Asset Communication (IAC). To set the total potential exposure of KBC, [...] considers what the losses would be on the total covered portfolio in the event that MBIA were to partially default on its obligations, with only 32,5 % recovery. In this case, the market implied losses would be EUR 8,5 billion. The midpoint between [...] Scenarios 2 and 3 are used to set the attachment point for the Cash Range and the guarantee fee. Under Scenario 2, house prices follow the base HPA projection while corporate default rates are assumed to double. Under Scenario 3, the HPA projection is stressed by one standard deviation, while historical corporate default rates are assumed to triple.
- ⁽¹³⁾ KBC submits that according to IFRS accounting rules, both the guaranteed CDO portfolio and the guarantee must be measured at fair value. This means that the guarantee must cover one-for-one any changes in the fair value of the guaranteed instruments. If this was not the case, there would be a significant risk that changes in the fair value of the CDOs would continue to affect KBC's P&L, defeating the purpose of the measure. This means that the guarantee must be constructed instrument per instrument and not on the portfolio as a whole.
- (36) MBIA has provided insurance on 11 out of the 15 CDOs. In relation to these instruments, the Belgian Federal authorities shall compensate KBC for losses in case there has been a credit event triggering this insurance and MBIA subsequently fails to perform its obligation. In line with the design of the measure overall, MBIA's obligations are defined on a CDO by CDO basis. Should MBIA later fulfil its obligation, KBC will be required to reimburse any amount already paid out by the State, subject to reasonable expenses.
- (37) The State shall be remunerated in two ways. Firstly, KBC must pay for having the right to an equity injection on standby, which is common in investment banking. The equity commitment fee is set at 650 bp per annum. Therefore, as the equity guarantee amounts to EUR 1,8 billion, the fee will cost KBC approximately EUR 120 million for each year that it is not exercised.
- (38) The aggregate cost of the cash guarantee will amount to approximately EUR 1,13 billion, to be paid in 12 semi-annual instalments. This fee will be equal the expected loss on the third tranche ⁽¹⁴⁾, in the event that the outcome of portfolio corresponds to the average between Scenario 2 and Scenario 3 and a MBIA Credit Valuation Adjustment of 67,5 %.
- (39) The overall impact of both measures as from 31 March 2009 will be the following: increase of KBC Bank Core Tier-1 capital (Pro forma capital ratio) from [...] % to [...] %; or from EUR [...] billion to EUR [...] billion. This is comprised of EUR [2,5-3,5] billion from the 2nd measure by the Flemish government, the recognition by the CBFA of the EUR 1,8 billion equity guarantee as capital, less the insurance premium of EUR 1,2 billion. The Tier-1 ratio rises to 11 %. The guarantee will further reduce Risk Weighted Assets by EUR 6,3 billion. Therefore, the combined effect of both measures will raise KBC Banks capital ratio by 2,47 %. Furthermore, EUR [0-1] billion of the 2nd measure will be used to increase the solvency ratio of KBC Insurance (Pro forma capital ratio) from [...] % to [...] %.

2.4. The initial restructuring plan

- (40) On 18 June 2009 a restructuring plan for KBC has been submitted by the Belgian authorities as a follow-up to measure 1 which was approved by the Commission on 18 December 2008 for a period of six months. The plan contains a preliminary analysis of KBC's Group's business, proposed future strategy, measures proposed to restore viability and repayment of the State resources.

⁽¹⁴⁾ The expected losses in this context have a particular meaning in the analyses done by [...]. The expected losses in the third tranche amount to EUR [...] billion, but this does not mean the expected losses in the first loss and equity tranche are equal to the sum of these two tranches. Indeed the expected losses are the output of stochastic models where a large number of scenarios are run and averaged. To illustrate the methodology used by the experts, if one assumes a portfolio of 10, split in two tranches of 5, and if you run 10 scenarios, 5 of which yield a loss of 2,5 and 5 of which yield a loss of 7,5, the expected loss on the total portfolio is 5. However the expected loss on the first tranche will be 3,75 (5 x 2,5 and 5 x 5), the 7,5 being capped to the maximum loss within the first loss (5) and on the second tranche will be 1,25 (5 x 0 and 5 x 2,5). The total loss reconciling with the average loss of 5 (3,75 + 1,25).

(41) The Belgian authorities inform the Commission that KBC has put in place a taskforce to further develop, optimize and finalise this plan in the coming months and commit to finalise this plan within the timeframe set by the Commission, taking into account measure 2 and 3.

3. POSITION OF THE BELGIAN AUTHORITIES

(42) The Belgian authorities do not contest that the notified measures constitute State aid within the meaning of Article 87(1) EC. However, they request the Commission to declare the notified measures compatible with the Common Market on the basis of Article 87(3)(b) of the EC Treaty, as the interventions are required to remedy a serious disturbance in the economy of a Member State.

(43) KBC, according to the Belgian authorities, is a systemically relevant bank as it is the third largest in Belgium and plays a pivotal role within the Belgian financial system and the Belgian economy as a whole. The Belgian authorities recall that KBC's crucial role was recognised by the Commission in its earlier decision.

(44) According to the Belgian authorities, the measures are necessary to improve KBC's capital position (measure 2) after substantial mark-downs as result of the negative revaluation by the market of CDOs and to eliminate the potential negative impact of KBC's exposure to the impaired assets in its CDO portfolio on future earnings and solvency.

(45) The Belgian authorities regard the measures as fulfilling the requirements of the Recapitalisation Communication (measure 2) and the IAC (measure 3). The Belgian authorities contend that a first estimation of the real economic value of the aggregate CDO portfolio amounts to [...].

(46) The Belgian authorities commit to submit to the Commission an in-depth restructuring plan regarding KBC as referred to in paragraph 55 and Annex 5 of the Commission's Communication of 25 February 2009 on the Treatment of Impaired Assets in the Community Banking Sector. That restructuring plan will take account of the measures granted or envisaged to be granted in favour of KBC by the Belgian authorities in the context of both Case N 602/08 (Commission decision dated 18 December 2008) and the present case. The Belgian authorities reiterated that they submitted a restructuring plan on 18 June 2009 that aims at achieving an in-depth restructuring.

(47) The Belgian authorities have also undertaken to renotify the measure under Article 88(3) EC if either of the following situations arise which make it less likely that the overall return in excess of 10 % p.a. is achieved:

(i) if KBC does not pay a dividend for a period of two consecutive years, or for three years in the next five years.

(48) Unless it can be shown that either of the above scenarios is caused by normal market events or that the overall return will nevertheless be in excess of 10 % per annum, the Belgian authorities will renotify the measure to the European Commission. The European Commission, without calling into question the capital injection, which has been declared compatible with the common market, can in particular require additional behavioural constraints.

(49) [...]

(50) [...]

4. ASSESSMENT

4.1. Existence of aid

(51) The Commission first needs to assess whether the measures 2 and 3 constitute State aid within the meaning of Article 87(1) EC. According to this provision State aid is any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition, by favouring certain undertakings, in so far as it affects trade between Member States.

(52) It is evident that for both measures, State resources are involved, since the Belgium authorities are providing KBC with a EUR 3,5 billion capital injection through the acquisition of the securities and a substantial amount of asset relief through the guarantee arrangement.

(53) Since both measures have been taken for the sole benefit of KBC, the measure is selective. Given that KBC is active in the financial sector, which is open to intense international competition, any advantage from State resources to KBC would have the potential to affect intra-Community trade and to distort competition.

(54) Finally, it has to be examined whether the measures lead to an advantage to KBC for it to constitute State aid.

(55) With regard to measure 2, the Commission notes that the securities acquired by the Belgian authorities have the same characteristics as the recapitalisation of KBC it approved on 18 December 2008⁽¹⁵⁾. In that decision, the Commission concluded that KBC had received a selective advantage since its core Tier 1 capital has been strengthened under conditions that it would not have obtained on the market. Its shareholders' stakes or operational control were not diluted, although certain decisions will require approval by the State's nominees. KBC would not be considered in default if it does not pay the annual coupon since it only has to pay interest in the event that it decides to pay dividends and it can repurchase the securities at a time of its choosing. Without the State intervention, KBC could not have raised such financing in such a short time frame at comparable conditions, especially taking into account the very volatile market circumstances.

(56) As regards measure 3, the Commission notes that this measure releases capital as it reduces the RWA of KBC Bank by EUR 6,3 billion. This measure improves the position of KBC by increasing its capital ratios and by removing a source of volatility on its balance sheet. Given that the market value of the portfolio is less than the point where the guarantee arrangement starts to operate, it is evident that no market operator would provide such an arrangement under similar conditions. This was confirmed by the Belgian authorities in their submissions.

(57) In sum the Commission agrees with the Belgian authorities that the measures in favour of KBC constitute aid in the sense of Article 87(1) of the EC Treaty.

⁽¹⁵⁾ See footnote 1.

4.2. Compatibility of the aid

- (58) Article 87(3)(b) EC empowers the Commission to declare aid compatible with the common market if it is intended “to remedy a serious disturbance in the economy of a Member State”. The Commission would point out that the Court of First Instance has expressly stated that Article 87(3)(b) EC is to be applied restrictively so that the aid may not benefit only one firm or one sector of the economy, but must serve to remedy a disturbance in the whole economy of a Member State⁽¹⁶⁾.
- (59) Given the present circumstances in the financial markets, the Commission considers that the measures may be examined directly under the Treaty rules and in particular under Article 87(3)(b) EC.
- (60) The Commission considers that market conditions deteriorated all over the world since the last quarter of 2008 and certain assets classes are no longer frequently traded. This is problematic for financial institutions because accounting provisions (IFRS accounting standards) might require them to write down these illiquid assets (on the basis of their fair value) to a greater extent than is warranted by their economic value. The uncertainty in the market about the exposure of KBC to further losses emanating from its CDO portfolio, the quality of its hedges, the scale of the write-downs, the fluctuating market value of these assets resulting in P&L volatility and the high leverage ratios have also had an impact on the financial institutions’ overall risk perceptions. The present measures are designed to address these problems. Therefore it finds that the scheme aims at remedying a serious disturbance in the Belgian economy.
- (61) In line with the Commission Communication on “The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis” (“the Banking Communication”)⁽¹⁷⁾, in order for an aid or aid scheme to be compatible under Article 87(3)(b) of the EC Treaty, it must comply with general criteria for compatibility under that Article. These criteria require that the aid has to be *well-targeted* in order to be able to effectively achieve the objective of remedying a serious disturbance in the economy; *necessary*, meaning that it must be of the minimum amount necessary to reach the objective, limiting negative spill-over effects for competitors that have not received aid. The fourth chapter of the Banking Communication, the Recapitalisation Communication⁽¹⁸⁾ and the Impaired Assets Communication⁽¹⁹⁾, then translate these general principles into conditions specific for recapitalisations and impaired asset relief.
- (62) The Commission considers that the appropriate framework for assessing the compatibility of measure 2 are the Banking Communication and the Recapitalisation Communication.
- (63) With regard to measure 3, the Commission notes that it has 2 aspects, the first being a commitment from the Belgian authorities to provide an equity recapitalisation if certain losses occur, and the second being a commitment to compensate further losses on these portfolios through cash. The IAC defines impaired asset relief as all measures whereby a bank is dispensed from the need for severe downward value adjustments of certain asset classes. This is also the case for the present measure. Therefore the present measure must fulfil the conditions for the compatibility of asset relief as spelled out in the IAC⁽²⁰⁾. Because of the inextricable links between both parts of the arrangement, the Commission will assess the whole transaction under the IAC.
- Systemic importance of KBC*
- (64) KBC is the third largest Belgian bank-insurance company. As confirmed by the letter of the National Bank of Belgium (“NBB”), it plays a pivotal role within the Belgian financial system and the Belgian economy as a whole.
- (65) Furthermore, KBC holds a particular importance for the lending to the real economy. Indeed, KBC plays an important role in providing mortgage backed loans to households, consumer loans, and loans to small and medium-sized companies. This crucial role is also evidenced by a condition imposed by the Flemish Region in the term sheet, according to which KBC will continue to provide lending to business and consumers applying its historical credit scoring criteria on a reasonable basis.
- (66) Consequently, KBC is a bank with systemic importance to the Belgian economy and the economies of several Central and Eastern European countries. This has been confirmed by the Commission in its decision of 18 December 2008.
- Measure 2 — The capital injection by the Flemish authorities*
- (67) As regards limitation of the aid to the minimum necessary, the Commission notes that the market has been demanding significantly higher capital ratios since the beginning of the crisis. Because of the downward revaluation of KBC’s synthetic CDOs, the relevant capital ratios of KBC decreased leading to concerns about its ability to absorb further losses. The injection of EUR [2,5-3,5] billion into KBC Bank, which represents 2 % of the pro forma RWA as of 31 March 2009, would increase its Core Tier 1 ratio to [...] % (combined with
- ⁽¹⁶⁾ See in principle Joined Cases T-132/96 and T-143/96 *Freistaat Sachsen and Volkswagen AG v Commission* [1999] ECR II-3663, paragraph 167. Confirmed in the Commission’s decisions in Case C 47/96 *Crédit Lyonnais* (OJ L 221, 8.8.1998, p. 28, point 10.1), Case C 28/02 *Bankgesellschaft Berlin* (OJ L 116, 4.5.2005, p. 1, paragraphs 153 et seq.) and Case C 50/06 *BAWAG*, not yet published, paragraph 166. See Commission Decision of 5 December 2007 in Case NN 70/07 *Northern Rock* (OJ C 43, 16.2.2008, p. 1), Commission Decision of 30 April 2008 in Case NN 25/08 *Rescue aid for WestLB* (OJ C 189, 26.7.2008, p. 3), and Commission Decision of 4 June 2008 in Case C 9/08 *Sachsen LB*, not yet published.
- ⁽¹⁷⁾ Commission Communication on “The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis”, adopted on 13 October 2008 (OJ C 270, 25.10.2008, p. 8).
- ⁽¹⁸⁾ Commission Communication on “The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition”, adopted on 5 December 2008 (OJ C 20, 15.1.2009).
- ⁽¹⁹⁾ Commission Communication on “Treatment of Impaired Assets in the Community Banking sector”, adopted on 25 February 2009.
- ⁽²⁰⁾ For a first application: Cf Commission Decision of 13 March 2009 in case C 9/09 *Dexia*, not yet published.

the asset relief scheme, this ratio would improve to [...] %). The EUR [0-1] billion that is directed to KBC Insurance will increase its solvency ratio from [...] % to [...] %. The Commission notes that these ratios, excluding the effect of the asset relief measures, are similar to those that pertained after the first recapitalisation, which was approved by the Commission. The Commission therefore considers that this capital injection of EUR 3,5 billion is the minimum necessary to remedy concerns about the stability of KBC and thus the Belgian financial system.

- (68) As regards the remuneration of the measure, the Commission is of the opinion that the return on this security can best be compared to a hybrid form of capital, given that the securities also have features similar to hybrid capital, like remuneration through a coupon and the fact that they are non-dilutive, which has a positive effect on the shareholders stake in the company. However, given the additional equity-alike elements of the security and its therefore more uncertain return, its expected return should normally be higher than that expected from other forms of capital under the applicable solvency regulations.
- (69) Following the methodology laid out in the Recapitalisation Communication, the Commission in several cases, including KBC's first recapitalisation, has accepted an expected overall return of 10 %, via mechanisms that are very similar to those used in the case of KBC ⁽²¹⁾, as a sufficient safe harbour return. Conform to this methodology, and in view of the prevailing market conditions, a return on tier 1 capital instruments for a Belgian bank in excess of 10 % would currently be acceptable ⁽²²⁾.
- (70) Belgium considers that there is a high likelihood that an overall return in excess of 10 % will materialise through a combination of the interest payments at 8,5 % (possibly more depending on the level of dividends paid out), and the repurchase option by KBC at a level at EUR 44,25 per security, being 150 % of the issue price. Indeed, Belgium has submitted various scenarios showing that the possible return will be considerable above 10 %.
- (71) It follows from the scenarios submitted by the Belgian authorities that the IRR on the Securities can be estimated at between 14,1 % and 18,7 %. According to the Flemish government, this estimation was made on the basis of a number of conservative assumptions, such as that the required Core Tier 1 ratio will remain at approximately 8 %, that no dividend or moderate dividend will be paid in the next years, and that the underlying profit growth in the next years will be 10 percentage points below profit growth for 2001-2007.
- (72) Taking the above scenario analyses into account, the Commission considers that the expected return on the State's investment is likely to be in excess of 10 %. It recalls that it is the nature of deeply subordinated

capital that some uncertainty to the return remains and it is exactly for this reason as well as in view of the type of instrument that the expected return should be above 10 %.

- (73) In addition, as provided for by the Banking Communication, the aid must be well-targeted in order to be able to effectively achieve the objective of remedying a serious disturbance in the economy; it must, in its amount and form, be necessary to achieve the objective, meaning that the aid measure must be of the minimum amount necessary to remedy the disturbance; also, any positive effects of the measures must be properly balanced against the distortions of competition, in order for the distortions to be limited to the minimum necessary to reach the measures' objectives. Consequently, the Commission positively views the fact that the capital injection is limited to what is necessary to reinforce KBC's capital position and the overall remuneration of the measure. In addition, the Commission notes positively the commitments of KBC concerning the continuation of lending to the real economy.
- (74) Finally the Commission notes that this recapitalisation is the second such measure that KBC has benefitted from since the beginning of the crisis. Given the scale and repeated nature of the State interventions in favour of KBC, the Commission concludes that an in-depth restructuring plan is required.

Measure 3 — The asset relief measures by the Belgian Federal authorities

I. Eligibility of assets

- (75) As regards the eligibility of the assets, the IAC indicates in section 5.4 that asset relief requires a clear identification of impaired assets and that certain limits apply in relation to eligibility to ensure compatibility. In Annex 3 to the IAC, the definition of eligible assets is further elaborated on. In this Annex, CDOs are mentioned as examples of impaired assets which can be included in relief operations without doubts as to their eligibility. The Commission notes in this respect that all assets in the portfolio are CDOs. The impaired assets are therefore sufficiently identified and do not raise issues of eligibility.

II. Transparency and disclosure

- (76) The Commission notes that the IAC demands in section 5.1 full ex-ante transparency and disclosure of impairments by eligible banks on the assets which will be covered by the relief measures, based on adequate valuation, certified by recognised independent experts and validated by the relevant supervisory authority.
- (77) The Commission notes that the Belgian authorities have engaged an independent expert which has valued the portfolio before government intervention. The Commission also observes that the Belgian supervisory authorities have stated, pursuant to point 20 IAC, that they agree with the methodology underpinning the valuation.
- (78) Finally, the Commission notes that the requirements concerning transparency and disclosure concerning the asset portfolio covered by the relief measure are met in principle, with the exception of the issue of proper valuation dealt with separately below.

⁽²¹⁾ N 602/08, recapitalisation of KBC (OJ C 109, 13.5.2009, p. 4), N 528/08, participatie in het kernkapitaal van ING (OJ C 328, 23.12.2008, p. 7), N 569/08, investment in the capital of Aegon NV (OJ C 9, 14.1.2009, p. 3).

⁽²²⁾ As per footnote 22 of the Communication "The recapitalization of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortion of competition".

III. *Management of assets*

- (79) The Belgian authorities have indicated that they are in discussions with KBC concerning the management rights of the portfolio. The Commission notes that KBC is in the process of ensuring that the Belgian authorities will obtain the customary and necessary rights to safeguard its interests and to ensure full compliance with the requirements laid down in the IAC.
- (80) The Commission recalls that the IAC stipulates that, irrespective of the model chosen, it is necessary to ensure clear functional and organisational separation between the beneficiary bank and its impaired assets, notably as to their management, staff and clientele. The Commission expects any future arrangement between the Belgian State and KBC to fulfil these requirements.
- (81) The Commission also observes that KBC will, after taking the first loss, take a loss of 10 % on the whole portfolio. This seems to be in line with point 45 of the IAC, which stipulates that the overall financing mechanism of the asset management should ensure that the bank will have to assume a proportion of the losses. This will incentivise KBC to ensure that the portfolio is managed as efficiently as possible.
- (82) On the whole, the Commission cannot yet conclude whether this condition has been fulfilled.

IV. *Valuation*

- (83) The IAC notes in section 5.5 that a correct and consistent approach to valuation is of key importance to prevent undue distortions of competition. The Commission has to carefully scrutinize the valuation and in particular the underlying general methodology in order to ensure a consistent approach at Community level. For that purpose the Commission has called on the technical assistance provided by its own experts. The Commission notes that the technical experts consider more information is needed.
- (84) The Commission observes that the independent experts hired by the Belgian authorities [...] have determined the market implied loss and the estimated loss per CDO across four different fundamental scenarios. The Belgian authorities have also submitted that according to their preliminary calculations, the real economic value of the aggregate CDO portfolio amounts to EUR [...].
- (85) Although the Commission does not question the qualification of the independent expert and its general approach, it so far has been unable to verify the methodology used to determine the real economic value and to assess whether the conclusions reached in the valuation by [...] is fair. At this stage, the Commission does not have all the information needed, including fundamental assumptions, to conduct a proper assessment (see confirmation by the Commission's technical experts above in point (81)). In particular, the Commission has significant doubts regarding the underlying valuation, including but not exclusively as regards the following issues:
- (a) the accuracy and/or reasonableness of the underlying assumptions and methodology used by the experts of the Belgian authorities to value the CDO portfolio;

- (b) the degree of correlation between the underlying corporate and ABS securities, more specifically how this correlation has been established and subsequently applied to the portfolio. [...] takes a flat correlation of [...] %, without detailed justification. However, given that many of the reference securities appear in more than one CDO, it is important that this figure is substantiated because a higher degree of correlation increases the risk of losses in the senior tranches of CDOs, such as are protected in this measure. Without clearer reasoning as to why the correlation figure chosen by [...] is valid, their valuation is open to question;
- (c) the house price assumptions for the US housing market used in the various stress scenarios. It appears that some of the price data for individual states do not correspond with wider market consensus as to the likely extent of the price declines. Also, the average price increase after 2013, seems at first glance to be too optimistic when taking into account the effect of the steep declines in some states will have on the average house price;
- (d) the corporate default levels, [...], used for some corporates used in the model. The data available to the Commission seems to indicate that the market implied default levels are higher than those used in the valuation model.

- (86) Further doubts as to the appropriateness of valuation cannot be excluded at this stage in view of the fact that the Commission has not yet received full information both on the valuation methodology and on its application to the individual assets covered. A full assessment of the Commission can only be carried out once the Commission is in possession of this information.
- (87) In sum, the Commission at this point cannot determine whether the real economic value and the valuation methodology are fair and cannot exclude that the estimated losses are higher than calculated by the independent expert and intends to assess this in-depth.

V. *Burden sharing*

- (88) As regards burden sharing, the IAC states in section 5.2 the general principle that banks ought to bear the losses associated with impaired assets to the maximum extent. That implies first that the bank should bear the difference between the nominal value and the real economic value of the impaired assets.
- (89) The Commission notes that KBC will take a first loss of EUR 3,2 billion and also retains 10 % of the risk associated with the portfolio. Furthermore, in case KBC decides to use its call option as regards the underwriting commitment in the Equity Range, the Belgian authorities will obtain ordinary shares, meaning that the holdings of the other shareholders will be diluted. The Commission notes favourably that the existence of this equity range ensures that the State will at least gain some ownership of KBC in return for compensating its losses on the CDO portfolio.

- (90) On the other hand, the Commission observes that according to the Belgian authorities the real economic value of the CDO portfolio is below the attachment point for the Equity Range, the first being EUR [...] billion and the latter EUR 16,8 billion. Whether this will have consequences on the amount of aid resulting from the impaired asset relief, the Commission will only be able to determine after receiving the necessary information in the course of the in-depth investigation.
- (91) Furthermore, as discussed above, the valuation of the portfolio has yet to be verified by the Commission and the real economic value still needs to be assessed. Given that the Commission has doubts as regards the correct valuation of the assets prior to government intervention, there are also doubts as regards the necessary degree of burden sharing included in this measure.

VI. Remuneration

- (92) The remuneration paid by KBC to the Belgian authorities is also an important element of burden sharing. The Commission recalls that, as noted in Annex 4 to the IAC, it is necessary for Member States to ensure that “any pricing of asset relief must include remuneration for the State that adequately takes account of the risks of future losses exceeding those that are projected in the determination of the ‘real economic value’”.
- (93) The remuneration associated with the asset relief measure is structured as a combination of an underwriting commitment fee and a guarantee fee. The underwriting commitment fee covers the Equity Range of all the losses on the CDOs. The guarantee fee covers the Cash Range of the losses on the CDOs (calculated per CDO).
- (94) The underwriting fee is calculated by reference to the fee levels investment banks charge for stand-by equity underwritings. The customary fee for this type of underwriting commitment, according to the Belgian authorities, varies between 10 and 15 bps per week. The midpoint of this range (12.5 bps) has been applied to KBC. This amounts to 650 bps per year on the principal amount of EUR 1,8 billion maximum. Furthermore, in the event that KBC does call upon the State to provide an equity investment, the State will subscribe to the newly issued equity at market terms, as per point (31). In case the Belgian authorities, when buying KBC shares, will acquire more than 30 % voting rights, which could require it to launch a mandatory takeover bid, it will have the option to subscribe to hybrid capital instead. The conditions attached to these hybrids have not been communicated to the Commission. Consequently, it has not been able to verify whether adequate remuneration would be paid for them and whether this remuneration amounts to sufficient burden sharing⁽²³⁾.
- (95) The guarantee fee was calculated on the basis of several elements including the notional amount of the CDO portfolio and its parts, either hedged with MBIA or

retained by KBC, a credit value adjustment of 67,5 %, a first loss of EUR 3,2 billion and a valuation of the assets on the basis of a midpoint between Scenarios 2 and 3 as developed by [...]. However, the fee paid for the protection adequately compensates the State for providing capital relief. The measure reduces KBC's RWA by EUR 6,3 billion. This relieves capital of EUR 504 million for KBC, which would usually cost it EUR 35 million⁽²⁴⁾, considerably less than the annual guarantee fee of EUR 221 million.

- (96) The Commission notes however that the amount of the guarantee fee is also dependent on the valuation of the CDO portfolio. As the Commission has expressed doubts on the valuation, it also doubts whether the guarantee fee amounts to sufficient burden sharing. The Commission especially doubts whether the chosen mid-point between Scenarios 2 and 3 is appropriate (see footnote 8).
- (97) In sum, the Commission has doubts whether the condition of the IAC as regards adequate remuneration are met and invites the Belgian authorities to provide more information on this matter.

VII. Temporary compatibility of the measure for six months

- (98) The Commission has been informed by the Belgian authorities that the transaction has to be booked [...], as otherwise the object of the measures, the increase of KBC's solvency ratios in line with market expectations and the reduction of P&L volatility will not be reached. Given that the CDO portfolio has been the source of KBC's difficulties, it is important for the asset relief measures to be implemented in order to address the root cause of the problem and thus avoid further write-downs through P&L. Delaying this measure could result in a further deterioration of the capital base and further uncertainty about KBC. Timely approval will allow sending a clear signal of confidence and stability to the markets. Given the systemic importance of KBC for the financial markets and economy in Belgium and a number of Central European countries, such a signal will also support confidence in the banking sector and financial stability in these countries in times of uncertainty and recession. The need for a timely Commission decision concerning these measures has been confirmed by the Belgian financial supervisor, the CBFA.
- (99) However, the Commission finds that, at this stage, the conditions of the IAC on valuation, burden sharing, remuneration and management of assets are not fulfilled and an in-depth investigation of the portfolio valuation is needed, which the Commission is not in a position to complete in the necessary time frame and on the basis of available information. Nevertheless, in view of the fact that the measure complies with the criteria for eligibility of assets and transparency and disclosure, the Commission can consider approving the asset relief measure as a temporary measure for six months. The Commission considers that any approval should in any event be limited to six months on the basis of Annex 5 to the IAC.

⁽²³⁾ Taking into account current market volatility, it is not unlikely that a switch to hybrids could occur. For example, in case KBC would have called on the underwriting commitment on 17 June 2009 (at a share price of EUR 13,62), the Belgian authorities would have obtained 28 % of the outstanding ordinary shares. In case KBC's share price would decrease, as happened in the days following 17 June, a potential share of more than 30 % becomes increasingly likely.

⁽²⁴⁾ EUR 6,3 billion × Tier 1 ratio of 8 % = EUR 504 million × 7 % (safe harbour capital remuneration less funding costs) = EUR 35 million

(100) The Commission finally notes that in conformity with its decision regarding measure 1, an initial restructuring plan has been submitted by the Belgian authorities on 18 June 2009. The Commission, in line with the principles of the Rescue and Restructuring Guidelines⁽²⁵⁾, therefore considers it justified that the approval of this measure is extended until the Commission reaches its decision on the restructuring plan.

4.3. Viability review and restructuring plan

(101) As regards the need for an assessment of the banks balance sheet and activities, the IAC states that an application for aid by an individual bank should be followed by a full review of that bank's activities and balance sheet, with a view of assessing the bank's capital adequacy and its prospects for future viability. The Commission recalls that paragraph 55 of the IAC states that where the bank has already received State aid in whatever form that either contributes to the coverage or avoidance of losses, or altogether exceeds 2 % of the banks RWA, in-depth restructuring would be required. The Commission considers this to be the case for KBC.

(102) The Commission notes that in line with the 18 December 2008 decision regarding measure 1, the Belgian authorities have submitted a plan for KBC on 18 June 2009. After a preliminary assessment of the plan the Commission agrees with the Belgian authorities that the plan has to be further developed in order to comply with the conditions set out in the IAC. The Commission notes that this plan should cover all three measures and include in-depth restructuring of KBC. The plan should include commitments regarding the reduction of market risk, in particular the reduction of risk weighted assets. Such a reduction could be achieved by divestments, both in core and non-core activities.

(103) The Belgian authorities have provided the necessary commitment to submit a complete in-depth restructuring plan within 3 months following the present decision. Therefore, the Commission will assess the restructuring plan, which will take into account all aid measures granted to KBC including the present ones, at that stage.

5. CONCLUSION

(104) The Commission finds that measure 2 complies with the conditions of the Banking and Recapitalisation Communications as an emergency measure and therefore can approve it for a period of six months. However, the Commission notes that this recapitalisation is the second such measure that KBC has benefitted from since the beginning of the crisis. Given the scale and repeated nature of the State interventions in favour of KBC an in-depth restructuring plan has to be submitted for KBC.

(105) With regard to measure 3, the Commission finds that the measure complies with the conditions on eligibility of assets and transparency and disclosure as stipulated in the IAC and in view of the serious threat to financial stability approves the measure for six months. At the

same time, the Commission has doubts at this stage whether that the measure complies with the conditions relating to, valuation, remuneration and burden sharing and asset management arrangements and opens a detailed investigation.

(106) Concerning measure 1, the Commission is of the view that it is justified to extend the approval of this measure until a decision is reached on the restructuring plan.

DECISION

— The Commission has accordingly decided not to raise objections to measure 2, being the capital injection by the Flemish authorities, on grounds that it is compatible with the EC Treaty, and approves it temporarily as rescue aid for 6 months.

— The Commission finds that measure 3, being the asset relief measure, in favour of KBC is temporarily compatible with the common market as it complies with a number of conditions of the IAC, and with due considerations for the need to preserve financial stability, measure 3 in favour of KBC is accordingly approved for six months.

— However, in the light of the foregoing considerations, the Commission has also decided to initiate the procedure laid down in Article 88(2) of the EC Treaty to verify the conditions of the IAC regarding, valuation (including the valuation methodology) burden sharing, remuneration and asset management arrangements of the measure.

— The Commission requires the Belgian authorities to provide, in addition to all documents already received, information and data needed for the assessment of the compatibility of the aid, including but not exclusively additional information with regard to the methodology report, the correlation between the underlying corporate securities and ABS, the stress scenarios used, the calculation of the guarantee fee and conditions of the hybrids in the Equity Range and the asset management arrangements.

— The Commission requires the Belgian authorities to submit an in-depth restructuring plan, in addition to the initial restructuring plan submitted to the Commission on 18 June 2009, within three months that takes into account the aid granted to KBC through all 3 measures, which the Commission will assess in order to decide about a prolongation of the aid after six months.

— The Belgian authorities are requested to forward a copy of this letter to the potential recipient of the aid immediately.

— The Commission informs the Belgian authorities that it will inform interested parties by publishing this letter and a meaningful summary of it in the *Official Journal of the European Communities*. It will also inform interested parties in the EFTA countries which are signatories to the EEA Agreement, by publishing a notice in the EEA Supplement to the *Official Journal of the European Communities*, and will inform the EFTA Surveillance Authority by sending a copy of this letter. All such interested parties will be invited to submit their comments within one month of the date of such publication."

⁽²⁵⁾ Commission Guidelines on State aid for rescuing and restructuring firms in difficulty (OJ C 244, 1.10.2004, p. 2), point 26.