IV

(Acts adopted before 1 December 2009 under the EC Treaty, the EU Treaty and the Euratom Treaty)

COMMISSION DECISION

of 18 November 2009

on the State aid C 18/09 (ex N 360/09) implemented by Belgium for KBC

(notified under document C(2009) 8980)

(Only the English text is authentic)

(Text with EEA relevance)

(2010/396/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first subparagraph of Article 88(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to those provisions [1],

Whereas:

1. PROCEDURE

(1) By Decision of 18 December 2008 [2] (hereinafter 'the recapitalisation Decision'), the Commission concluded that the EUR 3,5 billion recapitalisation of KBC provided by the Belgian Federal government [3] (hereinafter 'the first recapitalisation') was compatible with the common market as rescue aid on the basis of Article 87(3)(b) of the Treaty for a period of six months. The Commission in its Decision also required the submission of a plan by the Belgian authorities within six months.

(2) On 22 January 2009, the Flemish government and KBC announced a further strengthening of KBC's capital base through a EUR 2 billion recapitalisation by the Flemish government. The Flemish government [4] furthermore committed to provide an additional stand-by facility of EUR 1,5 billion (hereinafter together called 'the second recapitalisation').

(3) On 14 May 2009, the Belgian Federal government [5] and KBC announced that they reached an agreement concerning an asset relief measure (hereinafter 'the State Protection measure') to cover KBC's exposure to Collateralised Debt Obligations (hereinafter 'CDOs'). The Commission received information on the second recapitalisation and the State Protection measure on 18 May, 8 June and 12 June 2009.

(4) The Belgian authorities submitted a restructuring plan for KBC on 18 June 2009 with regard to the first recapitalisation.

(5) The Belgian authorities notified the second recapitalisation and the State Protection measure on 19 June 2009.

(6) On 30 June 2009, the Commission approved the second recapitalisation for a period of six months, subject to the submission of a restructuring plan, and temporarily approved the State Protection measure. At the same time, it opened the procedure under Article 88(2) of the Treaty with regard to the valuation and other aspects of the State Protection measure (hereinafter 'the opening Decision') [6].

[1] Commission Decision in Case C 18/09, *KBC*, (OJ C 216, 10.9.2009, p. 10).

[2] Commission Decision in Case N 602/08, *KBC*, (OJ C 109, 13.5.2009, p. 4). Hereinafter, references to the 'recapitalisation Decision' refer to the Decision mentioned in this footnote.

[3] Belgische federale overheid, les autorités fédérales belges.

[4] Vlaamse overheid, le gouvernement flamand.

[5] For the purposes of this decision, the Commission hereinafter in referring to the Belgian authorities does not distinguish between the Belgian Federal government and the Flemish authorities. Consequently both will be referred to as 'Belgian authorities'.

[6] The opening decision refers to three points: the approval of the second recapitalisation as rescue aid for six months, the temporary approval of the State Protection measure and opening on certain aspects of the State Protection measure.

(7) The opening Decision was published in the *Official Journal of the European Union* ([7]) and interested parties were requested to submit their comments on the aid. In the opening Decision, the Commission required the Belgian authorities to submit an amended restructuring plan that would also take into account the second recapitalisation and the State Protection measure by 30 September 2009. The Commission received no comments from interested parties.

(8) As regards the State Protection measure, the Belgian authorities submitted additional information on 3 July, 21 August, 2, 4, 22, 25 and 30 September and 13, 16 and 20 October 2009.

(9) The restructuring plan was discussed between the Belgian authorities and the Commission services in a series of meetings on 23 July, 6, 18 and 27 August, 9, 10, 14, 15 and 23 September 2009.

(10) The Belgian authorities submitted information concerning the restructuring plan on 2, 4, 10, 11, 16, 17, 22, 24, 25, 28 and 30 September, 1, 16, 19 and 21 October and 3, 4 and 6 November 2009.

(11) On 4 November 2009, the Belgian authorities informed the Commission that for reasons of urgency they exceptionally accept that this Decision is adopted in the English language.

2. DESCRIPTION OF THE BENEFICIARY

(12) The KBC Group NV (hereinafter 'KBC') is the holding company of KBC Bank NV, KBC Verzekeringen NV and KBL European Private Bankers (hereinafter 'KBL EPB'). KBC is an integrated bancassurance group, catering mainly for retail customers, small- and medium-sized enterprises (hereinafter '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 including Ireland and to a lesser extent in the United States of America and Southeast Asia.

(13) For 2008, total assets on the balance sheet of KBC amounted to EUR 355,6 billion and EUR 178,3 billion in risk-weighted assets (hereinafter 'RWA') terms ([8]). It recorded a loss of EUR 2,5 billion in 2008. The market value of KBC has fallen significantly, from EUR 23 billion on 1 August 2008 to EUR 11,8 billion on 23 October 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 (2007 estimates). More detailed information on KBC is provided in section 2.1 of the opening Decision.

(14) Following 2008 third quarter losses of EUR 906 million, resulting mainly from the bank's exposure to its CDOs, Icelandic banks, Lehman Brothers and Washington Mutual, KBC needed to strengthen its capital base. This lead to the first recapitalisation of EUR 3.5 billion by the Belgian authorities in December 2008, described in more detail in section 3 of the first recapitalisation Decision of 18 December 2008 ([9]).

(15) On 15 January 2009, Moody's rating agency announced that it had revised certain key assumptions in its rating of corporate synthetic CDOs. As a result, it decided to downgrade several categories of CDOs, although it did not specify which CDOs were affected. Following that announcement, KBC's share price came under severe pressure. Consequently, KBC decided to fully write-down all non-super senior CDO notes ([10]) in its portfolio originated by KBC Financial Products, a full subsidiary of KBC (hereinafter 'KBC FP') and to strengthen its capital base by means of a second recapitalisation measure subscribed entirely by the Belgian authorities. Section 2.2 of the opening Decision ([11]) describes the circumstances which led to the recapitalisation by the Belgian authorities and section 2.3.1 of that Decision describes the details of the agreement in more detail.

([7]) Commission Decision in Case N 360/09, Second *recapitalisation and asset relief for KBC*, (OJ C 216, 10.9.2009, p. 10). Hereinafter, references to the 'opening Decision' refer to the Decision mentioned in this footnote.

([8]) The RWA of KBC Bank was EUR 141,4 billion at the end of 2008. KBC has significant insurance operations, where the concept of RWA does not apply. For the purposes of comparison, an approximation for the equivalent of RWA for the Insurance part of KBC was created by dividing Insurance solvency capital by 8 %. This gives a Group RWA of EUR 178,3 billion for the end of 2008, which is the figure upon which all aid calculations are based upon in this decision.

([9]) OJ C 109, 13.5.2009, p. 4.

([10]) CDOs generally consist of several tranches which are ranked according to their subordination. Typically KBC's CDOs consist of an equity tranche, a junior tranche, a mezzanine tranche and a super-senior tranche. The equity tranche is the most subordinated and the super-senior tranche is the least subordinated.

([11]) See footnote 1.

(16) The restructuring of the monoline insurer Municipal Bond Insurance Association (hereinafter 'MBIA'), the reinsurer of a significant part of KBC's CDO portfolio (EUR 14,4 billion), in March 2009, increased KBC's counterparty risk and exposure to MBIA. Furthermore, the increased volatility of credit spreads, which had a direct negative impact on the mark-to-market valuation of the CDOs, led to negative value adjustments of EUR 3,8 billion in KBC's accounts for the first quarter of 2009. In order to avoid any further negative impact of the CDO portfolio on KBC's profit and loss account in the future, KBC reached an agreement with the Belgian authorities on 14 May 2009 on a State Protection measure for its super-senior CDO portfolio. Section 2.2 of the opening Decision ([12]) describes the circumstances which led to the creation of the State Protection measure by the Belgian authorities and section 2.3.2 of that Decision describes the details of the agreement between the Belgian authorities and KBC.

3. THE AID MEASURES

(17) KBC has benefited from three aid measures from the Belgian authorities; two recapitalisations and the State Protection measure.

3.1. *THE FIRST AND SECOND RECAPITALISATION*

(18) The first recapitalisation took the form of an injection of EUR 3,5 billion in total of core Tier-1 capital through Yield Enhanced securities issued by KBC and fully subscribed by the Belgian authorities. The issue price is EUR 29,50 per security.

(19) Those perpetual securities will produce a coupon payable each year equal to the higher of:

— EUR 2,51 per security (equivalent to a coupon of 8,5 %), non-cumulative, payable annually in arrears,

— 110 % of the dividend paid on the ordinary shares for the fiscal year 2008,

— 120 % of the dividend paid on the ordinary shares for the fiscal year 2009,

— 125 % of the dividend paid on the ordinary shares for the fiscal year 2010 and onwards.

(20) The coupon will only be paid if a dividend is paid on the ordinary shares, provided that 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 (hereinafter 'CBFA') ([13]). The securities are deeply subordinated, ranking *pari passu* with the ordinary shares.

(21) There are two redemption scenarios, both of which are at the initiative of KBC. In the first scenario, KBC has 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. In the second scenario, at any time after 3 years, KBC can require the Belgian authorities to convert its stake into ordinary shares on a one-for-one basis. If KBC triggers that conversion option, the Belgian authorities have the choice to opt for the alternative redemption of the securities plus payment of accrued interest. More information on the first recapitalisation is contained in section 3 of the recapitalisation Decision.

(22) The second recapitalisation took the form of a capital injection of core Tier-1 capital by the Belgian authorities in the form of securities. The terms of the agreement are practically identical to the first recapitalisation except that the securities are not convertible into ordinary shares, and can only be redeemed at 150 % of the issue price (see section 2.3.1 of the opening Decision).

3.2. *THE STATE PROTECTION MEASURE*

(23) The Belgian authorities have granted protection against realised credit losses on KBC's CDO portfolio for a period corresponding to the maturity of each CDO ([14]). The total portfolio has a nominal value of EUR […] (*) billion. The State Protection measure only covers the super-senior tranche of 15 specific CDOs, which total EUR 20 billion ([15]). That exposure consists 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 ([16]).

(24) The State protection does not cover the equity, junior and majority of the mezzanine tranches of the CDOs. The tranches outside the scope of the State Protection measure amount to EUR 3,9 billion. Losses in those tranches, which KBC will have to bear in full, need to be realised before the more senior guaranteed tranches are affected and the State Protection measure is triggered.

([12]) See footnote 1.

([13]) Commissie voor het Bank-, Financie- en Assurantiewezen, Commission bancaire, financière et des assurances.

([14]) 90 % of the value of the CDOs mature by the end of 2017.

(*) Confidential information, contains business secrets. Where possible, ranges have been provided in […].

([15]) The exact figure is EUR 19,97 billion.

([16]) EUR 4 billion through its subsidiary Assurisk and EUR 1,5 billion through KBC FP.

(25) In addition, KBC has already provisioned for significant mark-to-market losses. In its 2009 first quarter accounts, which were published at the same time as the State Protection measure, KBC had written-down the value of the CDOs covered by the State Protection measure from EUR 23,9 billion to EUR 14,7 billion ([17]). KBC came to that result by writing-down almost all the equity, junior and mezzanine notes of the CDOs to zero as well as carrying out some value adjustments of the super-senior notes in the CDO portfolio. In total, those write-downs amounted to approximately EUR […].

(26) The State Protection measure on the EUR 20 billion super-senior notes is structured in three tranches (see Chart 1 in recital 31 for the structure of the measure). The first tranche is constituted by a first loss amounting to EUR 3,2 billion which is entirely borne by KBC. That loss does not include losses on the equity, junior and mezzanine tranches mentioned in recital 24. If those losses were included, the first loss would be approximately EUR 7,1 billion.

(27) The second tranche of the transaction starts at EUR 16,8 billion and deals with the next EUR 2 billion of losses. In case of losses within this range (hereinafter 'Equity Range'), the Belgian authorities undertake to provide capital to KBC in the form of new KBC shares at market value ([18]) or hybrid securities. The capital provided by the Belgian authorities will cover up to 90 % of the losses in the Equity Range (EUR 1,8 billion). In other words, the Belgian authorities have committed to providing a standby equity facility to KBC that can be triggered by specific losses on KBC's CDO portfolio. The triggering events are defined separately for each CDO, that is, the equity injection option applies on transaction basis ([19]).

(28) The attachment point (that is, the starting point) of EUR 16,8 billion is based on parameters which would enable KBC Bank to maintain a core Tier-1 ratio above 8 % and KBC Insurance a solvency ratio above 150 %. Therefore, the parameters were initially not based on a valuation of the portfolio.

(29) The Equity Range is subject to several conditions. Firstly, KBC maintains the option to not call upon the equity injection and therefore to opt out from the equity issuance to the Belgian authorities. Secondly, if KBC calls upon the Belgian authorities for capital to cover its losses in the Equity Range and the Belgian authorities as a result acquire more than 30 % voting rights, which could require them to launch a mandatory takeover bid, the Belgian authorities will have the option to subscribe to hybrid capital instead. That hybrid capital would be remunerated in approximately the same manner as the securities already issued to the Belgian authorities and would be convertible into ordinary shares, at the option of the Belgian authorities, at the market price at the time of their issue ([20]). Thirdly, in the event that the Belgian authorities decide to sell their shares to a third party, KBC has the right of first refusal in relation to that sale and can purchase those shares at market price.

(30) The third tranche starts at EUR 14,8 billion (hereinafter 'Cash Range'). The Cash Range is effectively a guarantee by the Belgian authorities to compensate KBC in cash for part of the losses occurring in that tranche. Accordingly, any losses on the CDO portfolio exceeding EUR 9,1 billion (EUR 3,9 billion losses in the equity, junior and mezzanine tranches, EUR 3,2 billion first loss and EUR 2 billion Equity Range in the super-senior tranche) will be split between the Belgian authorities and KBC. The Belgian authorities will in that case assume 90 % (EUR 13,3 billion) of the losses and KBC will assume 10 % (EUR 1,5 billion).

(31) As with the equity injection option, the guarantee will apply on a transaction basis. As there are covered instruments relating to 15 CDOs (each a single transaction), there are thus effectively 15 guarantees ([21]). As a result, each of the 15 synthetic CDOs has a different attachment point and therefore a different expected loss. Consequently, the CDOs need to be assessed individually and the guarantee provided will be individual for each CDO (that is, there will not be a single guarantee on the aggregated portfolio). That specific structure was necessary to achieve a perfect match between the mark-to-market value of the guaranteed portfolio and the mark-to-market value of the guarantee with a view to removing profit and loss volatility caused by the fluctuation in value of the CDOs, the ultimate aim of the measure.

([17]) The valuation of the CDOs increased in the second quarter 2009 results, to EUR 16 billion, partially due to improved market conditions.

([18]) Average share price in 30 days preceding transaction.

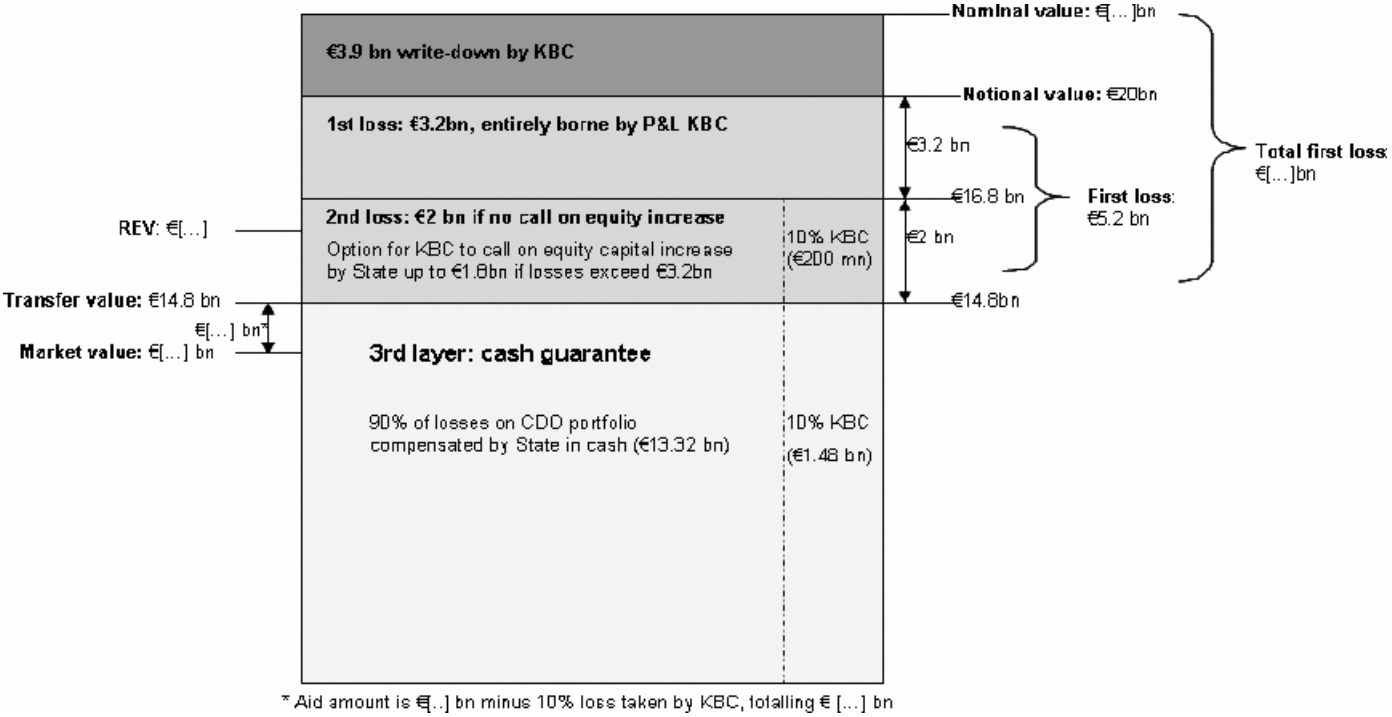
([19]) MBIA has provided insurance on 11 out of the 15 CDOs. In relation to those instruments, the Belgian authorities shall compensate KBC for losses if a credit event triggers that insurance and MBIA subsequently fails to perform its obligation. In line with the design of the measure overall, MBIA's 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.

([20]) In the event that the hybrid instrument is issued, it will be remunerated at the sum of the yield on Belgian 5 year bond, 3 % and five times the median of five-year CDS spreads of KBC calculated over the period starting on 1 January 2007 and ending on 31 August 2008. Using current figures, that would equate to a yield of 8,5 % (2,82 % + 3 % + (5*,0535) = 8,5 %. The issue price of the security would be based on the average share price in the 30 preceding transaction, and the security could be converted to equity on a one-for-one basis.

([21]) KBC submits that according to IFRS accounting rules, both the guaranteed CDO portfolio and the guarantee must be measured at fair value. That means that the guarantee must cover one-for-one any changes in the fair value of the guaranteed instruments. If that was not the case, there would 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. That means that the guarantee must be constructed instrument per instrument and not on the portfolio as a whole.

Chart 1

Structure of the State Protection Measure



Remuneration of the State Protection measure

(32) As regards the Equity Range, KBC pays for the right to an equity injection (hereinafter 'underwriting fee'). The underwriting fee is set at 650 basis points (hereinafter 'bps') per annum. Therefore, as the Equity Range amounts to EUR 1,8 billion, the fee will cost KBC approximately EUR 120 million for each year that it is not exercised, or EUR 718 million in total.

(33) As regards the Cash Range, the aggregate cost of the cash guarantee will amount to approximately EUR 1,33 billion, to be paid in 12 semi-annual instalments (hereinafter 'guarantee fee'). That fee will be equal to the expected loss on the third tranche ([22]), in the event that the outcome of portfolio corresponds to the average between the base scenario and the stress scenario ([23]) and a MBIA Credit Valuation Adjustment of 67,5 %.

([22]) The expected losses in this context have a particular meaning in the analyses done by the Belgian State's expert. The expected losses in the third tranche amounts to EUR 1,33 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 EUR 3,75 (5 × 2,5 and 5 × 5, the 7,5 being capped to the maximum loss within the first loss of 5) and on the second tranche will be 1.25 (5 × 0 and 5 × 2,5). The total loss reconciles with the average loss of 5 (3,75 + 1,25).

([23]) […]

(34) In total, KBC shall pay a fee of approximately EUR 2,04 billion to the Belgian authorities, resulting from the underwriting fee (EUR 718 million ([24]) and the cash guarantee (EUR 1,33 billion ([25]). Both fees are payable in twelve equal semi-annual instalments, beginning in December 2009 and ending in June 2015.

4. THE RESTRUCTURING PLAN

4.1. *THE INITIAL RESTRUCTURING PLAN*

(35) On 18 June 2009, a restructuring plan for KBC was submitted by the Belgian authorities as a follow-up to the first recapitalisation which was approved by the Commission on 18 December 2008 for a period of six months. The plan contained a preliminary analysis of KBC's business, KBC's future strategy, measures to restore viability and repayment of the State measures.

(36) The restructuring plan, however, did not meet the criteria set out in the Restructuring Communication ([26]) as it did not take into account the second recapitalisation and the State Protection measure. Furthermore, the plan did not provide a detailed business plan and did not include measures limiting the distortion of competition.

([24]) The exact figure is EUR 718 958 556.

([25]) The exact figure is EUR 1 325 480 484.

([26]) Commission communication on the return to viability and the assessment of the restructuring measures in the financial sector in the current crisis under the State aid rules, (OJ C 195, 19.8.2009, p. 9).

4.2. *THE FINAL RESTRUCTURING PLAN*

(37) On 30 June 2009, the Commission approved the second recapitalisation for a period of six months and temporarily approved the State Protection measure. At the same time, the Commission gave the Belgian authorities three months (until 30 September 2009) to develop a substantiated restructuring plan, which would take into account all State measures in favour of KBC.

(38) The Belgian authorities submitted the final restructuring plan on the due date. The plan addresses the substantive issues of viability, burden-sharing and limiting distortion of competition. As KBC is organised into 5 different business units, Belgium (Retail), Central and Eastern Europe and Russia (hereinafter 'CEE-R'), Merchant Banking, Europe Private Banking and Shared Services, the restructuring plan is designed along these lines.

(39) According to the restructuring plan, KBC will become a smaller, more focused group, withdrawing from risky activities and countries where it has a limited market presence. KBC will only retain activities that deliver sustainable results on a stand-alone basis. It will also retain its bancassurance model. Within the bancassurance model, KBC will focus on retail, private, SME and mid-cap customers and will primarily concentrate on six countries ([27]). KBC will continue to focus on CEE-R. It also will reduce its overall risk profile, volatility and leverage.

(40) The restructuring plan submitted by the Belgian authorities provides that KBC's balance sheet will decrease on a pro forma ([28]) basis by 20 % in RWA terms and by 17 % on a total asset basis. Viability measures, which are the rundown of the KBC FP portfolio, amount to […] % of the total balance sheet while divestments amount to […] % of the total balance sheet.

(41) The restructuring plan provides that KBC will divest several entities. In its business planning of these divestments, KBC has assumed that the sale prices […]. All sales are expected to happen within […].

4.2.1 ABILITY TO RETURN TO VIABILITY IN BASE AND STRESS CASE

(42) The Belgian authorities have submitted a base and a stress scenario with the aim of demonstrating KBC's ability to achieve long-term viability.

(43) In the base case, it is assumed that GDP will contract in its main markets in the period 2009-2010 followed by a relatively quick recovery in 2011. Equity prices are expected to recover in 2009 or 2010, depending on local market conditions.

(44) […]

(45) KBC expects to meet its internal capital targets in the base case throughout the projection period (2009 to 2013), with Tier 1 at 8,8 % in 2009 and above 10 % thereafter. The composition of KBC regulatory capital will increasingly be dominated by own funds as a result of the proceeds of the divestments which will improve the quality of KBC regulatory capital. In a base case, KBC will first generate surplus capital (when actual capital exceeds internal capital targets of a Tier 1 ratio of 10 %) in 2011. It will therefore start to repay the principal part of the State capital from 2012 onwards.

(46) The Belgian authorities have also submitted a stress scenario. Similar to the base case, GDP will contract in the period 2009-2010, rising thereafter. However, the subsequent economic recovery will be very weak. For example, this scenario predicts that Belgian real GDP will suffer a cumulative fall of […] % between 2008 and 2011, and will not have regained its 2008 level by the end of 2013.

(47) […]

(48) In the stress scenario, KBC expects to be able to meet its internal capital targets in the stress case throughout the projection period. Its Tier 1 ratio will be […] % in 2009 and will remain above […] % from 2010 onwards. This reasonably benign evolution of capital ratios is to due to the fact that the balance sheet of KBC is expected to contract significantly in the stress scenario, since economic activity and hence demand for loans will be much reduced. It will start to generate limited amounts of surplus capital from […], largely due to a sharp fall in RWA rather than profit growth, […].

(49) In the restructuring plan, the Belgian authorities have also described KBC's liquidity position. As of end 2008, KBC had a loan to deposit ratio of 88 %. In the crisis to date, it has not suffered from liquidity problems, and has not had to resort to any State funding guarantee scheme. It has a relatively limited reliance on funding from capital markets. In terms of its funding structure, 64 % of its debt instruments were of duration of longer than 1 year. That funding structure is projected to remain fairly stable over the next few years, with a moderate fall in reliance on wholesale funding. The divestment of some of the entities […] will furthermore strengthen its liquidity position.

([27]) Belgium, Czech Republic, Poland, Hungary, Slovakia and Bulgaria.
([28]) In this case pro forma figures mean that the entities earmarked for divestment or runoff account for 20 % of the total Group's RWA as per end 2008.

4.2.2 RESTRUCTURING MEASURES BY BUSINESS UNIT

Table 1

Restructuring Measures of KBC and timeline of their implementation

[…]

Belgium (Retail)

(50) KBC is one of the top 3 banks in Belgium, and would usually be second or third in terms of its market share of most banking activities. It holds […] % of deposits, generates […] % of loans and accounts for […] % of investment fund business, […] % of life and […] % of non-life insurance.

(51) The Belgian authorities propose that KBC would retain the majority of its activities in Belgium and remain an integrated bancassurance provider. According to the Belgian authorities, these activities are well-integrated under the KBC brand and form part of its core business model.

(52) However, the restructuring plan provides that KBC will sell Centea (agent based banking) and Fidea (agent based insurance). Centea represents between […] % and […] % of the Belgian market in most product segments while Fidea represents around 2 % of the Belgian insurance market. These sales will reduce the RWA of the Belgian banking unit by 16 % (EUR 3,8 billion).

Central and Eastern Europe & Russia

(53) According to the restructuring plan, KBC will retain its presence in 5 (out of 9) countries where it is already well-established. Those countries are, in order of market share in traditional banking (lending and deposits); Czech Republic (22 %), Slovakia (10 %), Hungary (9 %), Poland (4 %) and Bulgaria (3 %). KBC also has insurance operations in each of these countries, in line with the bancassurance model.

(54) KBC will cease its activities in Serbia (market share of KBC 1 %), Russia (1 %), Romania ([…] %, only insurance and leasing activities) and Slovenia ([…] % – KBC has minority stake in the business concerned). KBC will sell its operations in other countries where its market share is relatively small or its operations are not in line with the bancassurance model. It will also sell a Polish consumer finance subsidiary (Zagiel), which was not fully integrated in its Polish operations. Those sales will take place over […], except the Russian activity which is not foreseen until […]. The RWA of the CEE-R banking unit will decrease by 11 % (EUR 4,4 billion).

(55) Furthermore, KBC intends to list 40 % of its banks in the Czech Republic (ČSOB) and Hungary (K & H), which are currently 100 % -owned subsidiaries of KBC. It will list them on the local stock exchanges.

Merchant banking

(56) As regards merchant banking, the restructuring plan provides that KBC will dispose or run-off significant parts of its Merchant Banking Business Unit. As a result, RWA will decrease by […] % (EUR […] billion) in that business unit. KBC FP, the entity that generated all the CDOs, will be run-off over time. KBC will sell its activities in the United Kingdom, […], as well as the Antwerp Diamond Bank, its […], […], […], […] and KBC Private Equity.

(57) KBC will retain the activities which are necessary to service its core SME and corporate clients, mainly Belgian. These are activities such as fundraising and currency transactions. KBC will retain its corporate banking business, foreign branches that are necessary to service local corporate customers with activities abroad, KBC Securities, Market and Assurisk (reinsurance).

Private banking

(58) In accordance with the restructuring plan, KBC will sell all the businesses in its European Private Banking unit. KBC intends to sell these activities in […]. This will reduce RWA by EUR 5,7 billion.

Shared Services

(59) Given the nature of this business unit, the restructuring plan provides that KBC will maintain most activities. KBC will keep activities such as asset management, trade finance, leasing and consumer finance. KBC will divest several activities, such as […], in amongst others […]. As a result of the divestments, RWA will decrease by approximately EUR […] million.

4.2.3. FINANCIAL RESTRUCTURING

(60) In order to both repay the State and maintain 10 % Tier-1 capital, the restructuring plan contains the following financial restructuring measures:

(i) The listing of 40 % of the shares of ČSOB bank in the Czech Republic (estimated value of stake listed: EUR […] billion);

(ii) The listing of 40 % of the shares of K & H bank in Hungary (estimated value of stake listed: EUR […] million);

(iii) The buy-back of hybrids, leading to an estimated positive impact on KBC's core capital of EUR […] million. KBC intends to buy, as it has already done in recent months, these hybrids at below par value, thus generating a profit that boosts core capital;

(iv) The sale and lease back of headquarter offices, estimated to yield EUR […] million upfront;

(v) The sale of Treasury shares (KBC's holding of its own shares), estimated to yield EUR […] million.

Total capital raised as a result of the above measures is envisaged to be around EUR […] billion, mainly achieved by.

4.2.4. REPAYMENT OF THE STATE

(61) As regards the repayment of the Belgian authorities, the restructuring plan provides that, KBC, in a base case, will start to pay coupons from 2011 onwards, meaning that the Belgian authorities would receive EUR 600 million. The reimbursement of the principal amount of the recapitalisations will start once KBC has reinforced its capital position through the divestments and the financial restructuring (from 2012 onwards). As the repayment of the nominal amount of the recapitalisation progresses, the remuneration of the Belgian authorities through the coupon payments declines. KBC plans to start the repayment in 2012 (EUR […] billion) and estimates that the capital injections will be completely paid back […] in the base case.

4.2.5. COMMITMENTS OF THE BELGIAN AUTHORITIES

4.2.5.1. ***Behavioural commitments***

(62) The Belgian authorities commit, within the limits of their respective competences, to ensure KBC's compliance with the commitments listed in recitals 63 to 77 inclusive.

(63) With regard to the duration of these behavioural commitments, the Belgian authorities commit that, without prejudice to the possibility for the Commission to grant an exemption, notably on the basis of a sufficiently reasoned request from the Belgian authorities, the behavioural commitments listed in recitals 63 to 77 inclusive apply for a duration of […] years from the date of the Commission's decision or, until the nominal amounts subscribed to by the Belgian authorities, on 19 December 2008 and on 20 July 2009 respectively, have been redeemed, whichever is earlier ([29]).

(64) The Belgian authorities commit that KBC shall endeavour to maintain its lending policy to the real economy in countries where it has retail operations. The credit provided by KBC will be on commercial terms.

([29]) For the purpose of this commitment package, the redemption of the nominal amounts will be realized when an amount of EUR 7 billion is repaid.

(65) They further commit that KBC will maintain its solvency ratio of core Tier-1 at minimal […] % and its basic own funds at […] % ([30]).

(66) With regard to a ban on acquisitions, the Belgian authorities commit that KBC will refrain from acquiring control, as defined by Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation) ([31]), of financial institutions. KBC will moreover refrain from acquiring control of businesses other than financial institutions if such an acquisition would slow down the repayment of the amount of EUR 7 billion of core Tier-1 Yield Enhanced securities to the Belgian authorities as planned in the restructuring plan that was notified to the Commission on 30 September 2009 and approved by this Decision. Notwithstanding that prohibition, KBC may acquire businesses if it obtains the Commission's approval, in particular if it is considered essential to safeguard financial stability or competition in the relevant markets.

(67) The Belgian authorities commit that KBC will adhere to the following price leadership ban:

(i) In Community-markets in which KBC has a market share of more than [0-10 %] on the product markets as defined in point (ii) below, KBC will not offer more favourable prices on standardized products than the best priced competitor of KBC among the top ten market players in terms of market share on this geographic and product market;

(ii) The product markets to which the condition set out in point (i) applies are limited to: KBC's standardized products on the retail deposit market, deposits for SME's (SME defined according to SME definition as operated by KBC) and retail mortgage market;

(iii) As soon as KBC becomes aware of the fact that it offers more favourable prices for its products than the best priced provider, KBC will as soon as possible adjust, without any undue delay, its price to a level which is in accordance with this commitment;

(iv) That condition does not apply to the Belgian market, where no price leadership ban will apply.

(68) The Belgian authorities also commit that KBC will refrain from mass marketing invoking the measures as an advantage in competitive terms.

([30]) Basic own funds here are equivalent to equity and reserves.
([31]) OJ L 24, 29.1.2004, p. 1.

(69) With regard to the limitation of KBC executive remuneration, the Belgian authorities commit that:

(i) 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'. Exit schemes or statutory compensation for dismissal are limited to twelve months' fixed salary for KBC's Executive Committee Members;

(ii) In addition, Executive Committees of KBC, KBC Bank NV and KBC Verzekeringen NV forego all bonuses for 2008 (cash as well as options and share rewards).

(70) The Belgian authorities commit that KBC will endeavour to ensure, for the benefit of the Belgian authorities, an overall return on the securities subscribed by them of minimum 10 % p.a.

(71) The Belgian authorities commit to re-notify the first recapitalisation under Article 88(3) of the Treaty if either of the following situations arises which make it less likely that the overall return in excess of 10 % p.a. is achieved:

(i) If, from 1 January 2010, KBC does not make a dividend payment during two consecutive years or, from 1 January 2009, does not make a dividend payment during three years within a period of five years; or

(ii) If, after a period of one year where the share price remains on average above 150 % of the issue price of the securities, KBC has not repurchased, or committed to do so within three months, at least 20 % of the original investment of the State.

(72) In the same vein, the Belgian authorities commit to re-notify the second recapitalisation under Article 88(3) of the Treaty if the following situation arises which makes it less likely that the overall return in excess of 10 % p.a. is achieved:

(i) If, from1 January 2010, KBC does not make a dividend payment during two consecutive years or, from1 January 2009, does not make a dividend payment during three years within a period of five years.

(73) Unless in either of the scenarios described in recitals 71 and 72 it can be shown that the non-payment of dividends is caused by normal market events or that despite the non-payment of dividends, the overall return will nevertheless be in excess of 10 % per annum, the Commission, without calling into question the capital injection, which has been declared compatible with the common market, can in the context of the renotification, in particular require additional behavioural constraints.

(74) As regards the remuneration of the alternative securities under the State Protection measure, the Belgian authorities commit that the coupon that will be payable on the alternative class of core capital securities to be issued by KBC if the Belgian authorities were to acquire more than 30 % voting rights under the Equity Range of the State Protection measure, shall be equal to […].

(75) The Belgian authorities also commit that KBC or any of its subsidiaries shall not engage in the origination of Collateralized Debt Obligations ('CDOs') ([32]). It is understood that securitisation transactions which are not caught by this definition of CDOs fall outside the scope of this commitment. This is for instance the case for securitisation transactions for purposes of management of regulatory capital or credit risk or to raise liquidity.

(76) With regard to coupon payments and call options on hybrid capital, unless the Commission otherwise agrees to an exemption, the Belgian authorities commit that:

(i) […];

(ii) […].

([32]) For the purpose of this commitment, a 'CDO' is a credit portfolio securitisation transaction, with the following characteristics: (i) it entails a repackaging of portfolios of assets, and such assets can be bonds, loans, derivatives or other debt obligations, (ii) the credit risk in respect of such assets is repackaged into multiple tranches of securities of different seniority, sold to investors, and (iii) the transaction is mainly arbitrage driven, i.e. the main goal of the transaction is to provide profits from differences between the market price of the underlying assets and the price at which the securitised risk can be sold in structured form.

(77) Finally, the Belgian authorities have committed that KBC will organise the management rights of the Belgian authorities in respect of the guaranteed portfolio under the State Protection measure, in such a way that the interests of the Belgian authorities as the guarantor will be duly guaranteed while preserving a suitable level of flexibility for KBC to react swiftly to changing market circumstances and to make the relevant adjustments and choices as appropriate. The legal documentation of the guaranteed portfolio provides for safeguards to protect third party investors, super senior counterparties and therefore, by extension, the Belgian authorities against possible conflicts of interest in the management of the guaranteed portfolio. In addition to the safeguards under the original legal documentation, the agreement with the Belgian authorities governing the State Protection measure will in particular provide for the right of the Belgian authorities to monitor the management of the guaranteed portfolio. Where appropriate, the Belgian authorities will be granted consent rights to further protect its interests.

4.2.5.2. ***Divestments and run-down of business portfolios***

(78) The Belgian authorities have furthermore committed, within the limits of their respective competences, to use their best endeavours to ensure KBC's compliance with the commitments listed from recitals 79 to 97 inclusive.

(79) KBC will take the necessary steps for the divestment of the entities or assets (hereinafter 'Divestment Business(es)') as listed in recital 80 to be implemented by the time mentioned. Such a divestment shall be deemed implemented when a binding agreement has been entered into by KBC to sell […] in the entity or asset concerned. A legally binding agreement is an agreement which cannot be rescinded unilaterally by KBC and intends to create a legal relationship on which each party can rely and which, in case of termination of the agreement by KBC, would lead to a liability of KBC to the other party. That legally binding agreement may still be subject to a number of customary conditions precedent such as approval by the relevant supervisory authorities.

(80) As regards the divestment businesses, the Belgian authorities commit that KBC will divest the following entities by […]:

(i) […] by […]

(ii) KBL EPB by […]

(iii) […] by […]

(iv) Centea by […]

(v) Fidea by […]

(vi) Antwerp Diamond Bank by […]

(vii) Implementation of divestments of NLB Zagiel […] by […]

(viii) Absolut bank (Russia) by […]

Value Preservation Commitments

(81) With regard to preserving the value of the divestment businesses, the Belgian authorities commit that KBC will ensure that:

(i) the divestment business shall retain tangible and intangible assets owned by it which contribute to its current operation or are necessary to ensure its viability and competitiveness;

(ii) the divestment business shall retain all (a) licences, permits and authorisations issued by any public authority for its benefit; (b) its contracts, leases, commitments and customer orders; and (c) its relevant records which contribute to its current operation or are necessary to ensure its viability and competitiveness;

(iii) the divestment business shall employ the appropriate number of staff with the necessary capabilities to ensure its viability and competitiveness. KBC shall take all reasonable steps, including incentives taking into account industry practice, to encourage all key personnel ([33]) to remain with the Divestment Businesses. It shall also not solicit the key personnel transferred with the Divestment Business. […].

(82) The Belgian authorities commit that KBC shall exercise its best efforts to support the buyers of the Divestment Businesses in migrating to appropriate infrastructure for the ongoing operation of the Divestment Businesses. […].

(83) From the date of this Decision until implementation of the divestment, the Belgian authorities commit that KBC shall preserve the economic viability, marketability and competitiveness of the Divestment Businesses in accordance with good business practice and shall minimise as far as possible any risk of loss of their competitive potential. KBC shall carry on the Divestment Businesses as a going concern in the ordinary and usual course as carried on before the date of this Decision.

([33]) Key personnel means all personnel necessary to maintain the viability and competitiveness of the Divestment Businesses.

(84) The Belgian authorities commit that no acts which might have a significant adverse impact on the Divestment Businesses shall be carried out by KBC. […].

Additional divestment commitments in respect of Centea and Fidea

(85) As regards the prospective buyer(s) of Centea and Fidea, the Belgian authorities have provided the commitment that KBC shall ensure that:

(i) The buyer of Centea does not have a post-acquisition market share of greater than […] in current accounts, savings or mortgages in Belgium.

(ii) The buyer of Fidea does not have a post-acquisition market share of greater than […] on either the life or non-life insurance markets in Belgium.

(86) Furthermore, the Belgian authorities commit that KBC shall make the necessary arrangements to ensure clear identification of the Centea and Fidea businesses and start to prepare their separation from businesses that are integrated in KBC into distinct and separately saleable entities immediately after the Commission's decision. Without prejudice to the value preservation commitments as set out in recitals 81 to 83 Centea and Fidea will be managed as distinct and saleable entities from the date of the Commission's Decision. To ensure that all management decisions between the date of this Decision and the implementation of the divestment are in the best interests of Centea and Fidea with a view to ensuring their continued economic viability, marketability and competitiveness, KBC shall appoint a hold separate manager ([34]) for each of these businesses and shall ensure that the hold separate manager operates independently. That hold separate manager can be the current CEO of those businesses. The hold separate manager will manage these divestment businesses (Centea and Fidea) in their best interest, in common consultation with KBC, as monitored by the Monitoring Trustee.

Monitoring trustee

(87) A monitoring trustee will be appointed who is to report on a six monthly basis to the Commission on compliance by the Belgian authorities and by KBC with the commitments listed in recitals 78 to 86 The monitoring trustee shall be independent, possess the necessary qualifications and shall not be subject to a conflict of interests throughout the exercise of his mandate

([34]) Hold separate manager is the person appointed to manage the day-to-day business of the Divestment Business as monitored by the monitoring trustee.

(88) No later than one month after the adoption of this Decision, the Belgian authorities shall submit a list of one or more persons, as agreed with KBC, whom they propose to appoint as the monitoring trustee(s) to the Commission for approval. The Commission shall have the discretion to approve or reject the proposed trustee(s) based on the criteria outlined in recital 87. If the Commission rejects all proposed trustee(s), KBC and the Belgian authorities will, within one month of being informed of the rejection, propose new candidates which again need to be approved or rejected by the Commission. If all further proposed trustee(s) are rejected by the Commission, the Commission shall nominate a trustee, whom KBC shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

Review of the commitment Package

(89) Where appropriate and on the basis of a sufficiently reasoned request from the Belgian authorities and KBC and taking into consideration the views of the monitoring trustee, the Commission may:

(i) extend the target dates for implementation of the divestments:

(a) as regards the divestments to be implemented […], the target date may be extended […], […], and subsequently by […], […];

(b) as regards the divestment to be implemented […], the target date may be extended by […], […];

Such extension may be granted in particular when the divestments will not be implemented by these dates through no fault of KBC.

KBC will not be obliged to sell a Divestment Business […] except where […], in which case KBC shall not be obliged to sell the relevant Divestment Business […].

(ii) dispense with, amend or replace one or more of the measures, requirements or conditions set out in this Decision.

(90) Any such requests shall be sent to the Commission at the latest two months prior to the target date.

Divestiture trustee

(91) If the divestments have not been achieved by the relevant target dates and no later than one month after the ultimate non-extendable target date, and if no alternative measures have been approved by the Commission, the Belgian authorities shall submit a list of one or more persons, as agreed with KBC, whom they propose to appoint as the divestiture trustee(s) to the Commission for approval. The divestiture trustee shall be independent, possess the necessary qualifications and shall not be subject to a conflict of interests throughout the exercise of his mandate. The Commission shall have the discretion to approve or reject the proposed divestiture trustee(s). If the Commission rejects all proposed divestiture trustee(s), KBC and the Belgian authorities will, within one month of being informed of the rejection, propose new candidates which again need to be approved or rejected by the Commission. If all further proposed trustee(s) are rejected by the Commission, the Commission shall nominate a trustee, whom KBC shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

(92) The Belgian authorities commit that KBC shall grant necessary and reasonable powers of attorney to the divestiture trustee:

(i) to effect the disposal of the Divestment Business (including the necessary powers to ensure the proper execution of all the documents required for effecting the disposal), and

(ii) to take all actions and declarations which are necessary or appropriate to achieve the disposal, including the appointment of advisors to assist with the disposal.

(93) The Commission shall authorize, subject to it having taken into consideration reasonable alternatives as proposed under the review arrangements as set out in recital 89, the divestiture trustee to sell the Divestment Businesses concerned […]. The divestiture trustee shall include in the sale and purchase agreement(s) such customary and reasonable terms and conditions as are appropriate for an expedient sale. The divestiture trustee shall organize the sales process in consultation with KBC so as to ensure a divestment under the best possible conditions, subject to its obligation to divest […] in the trustee divestiture period under the conditions set out in recitals 91 and 92.

(94) In addition, all fees and expenses of the monitoring and divestiture trustees will be borne by KBC.

Run-down of business portfolios

(95) The Belgian authorities commit that KBC will take the necessary steps for the run-down of the business portfolios of the entities listed hereunder to be completed by the target dates as set out for each of these entities. From the date of this Decision until the completion of the run-down, KBC will respect a stand-still with regard to the amount of RWA ([35]) represented by these business portfolios. Concerning this commitment, 'stand-still' means that KBC will not enter into any new business in these business portfolios and that KBC's management decisions with regard to the business portfolios can only have a neutral or decreasing effect on the amount of RWA attributed to these business portfolios at the time of this Decision. KBC will not be obliged to divest or otherwise dispose of portfolio items or to terminate existing contracts under conditions that would result in a loss or a liability for KBC. KBC will thus run-down the following business portfolios:

(i) […] by […]

(ii) KBC FP by […]

(iii) […] by […]

it being understood that certain contracts belonging to the business portfolios as listed above might expire and therefore still remain in KBC's books […].

Listing of two CEE-R assets

(96) The Belgian authorities commit that KBC will carry out the listings of ČSOB (Czech Republic) and K & H bank (Hungary) […].

([35]) After neutralizing the pro-cyclical effect of expected credit defaults.

4.2.5.3. ***Monitoring***

(97) The Belgian authorities commit that KBC provides the Commission with detailed reports on a six-monthly basis through the Belgian authorities. The reports will contain information on the recapitalisation measures (as mentioned in point 40 of the Recapitalisation Communication ([36]), the functioning of the State Protection measure (as mentioned in Annex IV to the Impaired Asset Communication, hereinafter 'IAC' ([37]), and the restructuring plan (as mentioned in point 46 of the Restructuring Communication ([38]). The first report, combining all that information, will be submitted to the Commission no later than six months after the date of this Decision.

5. GROUNDS FOR INITIATING THE PROCEDURE ON THE STATE PROTECTION MEASURE

(98) The Commission recalls that in this case, it opened the formal investigation procedure on the State Protection measure regarding the valuation, remuneration, burden-sharing and asset management arrangements on 30 June 2009.

(99) Regarding the valuation, the Commission had expressed doubts about the underlying assumptions and methodology used by the experts. In particular, the Commission saw a need to verify the correlation assumptions of the Asset Backed Securities (hereinafter 'ABS') and of the corporate debt, the traceability of the house price assumptions and corporate default levels (recital 83 of the opening Decision).

(100) As the remuneration paid by KBC is also dependent on the valuation of the CDO portfolio, the Commission concluded in recital 93 of the opening Decision that further assessment of the matter was necessary. For the same reasons, the Commission expressed doubts whether the State Protection measure provided for sufficient burden-sharing (recital 88 of the opening Decision).

(101) Regarding the asset management, the Commission concluded in recital 80 of the opening Decision that it had insufficient information to conclude whether the arrangements foreseen by the Belgian authorities fulfil the requirements laid down in the IAC.

([36]) Commission Communication on the Recapitalisation of financial institutions in the current financial crisis: limitation of the aid to the minimum necessary and safeguards against undue distortions of competition (OJ C 10, 15.1.2009, p. 2).

([37]) Communication from the Commission on the treatment of impaired assets in the Community banking sector (OJ C 72, 26.3.2009, p. 1).

([38]) Commission communication on the return to viability and the assessment of the restructuring measures in the financial sector in the current crisis under the State aid rules (OJ C 195, 19.8.2009, p. 9).

6. COMMENTS FROM INTERESTED PARTIES

(102) The Commission notes that no comments from interested third parties have been received with regard to the opening Decision on the State Protection measure.

7. COMMENTS FROM BELGIUM

7.1. *THE OPENING DECISION*

(103) The Belgian authorities indicate that they have reviewed the Commission's Decision of 30 June 2009 in which the Commission decided to initiate the procedure laid down in Article 88(2) of the Treaty in order to verify the conditions of the IAC regarding valuation (including the valuation methodology), burden-sharing, remuneration and asset management arrangements of the measure.

(104) The Belgian State believes that each of these elements are adequately addressed by the KBC restructuring plan as filed on 30 September 2009 and by the various commitments that have been offered in connection with that restructuring plan.

7.2. *POSITION OF BELGIUM ON THE RESTRUCTURING PLAN*

(105) The Belgian authorities submit that the restructuring plan complies with all conditions set forth in the Commission's Communication of 23 July 2009 on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules ([39]).

(106) In particular, the Belgian authorities are of the opinion that the restructuring plan ensures that KBC's long-term viability is restored, that KBC provides an important own contribution to the restructuring costs and that distortions of competition are limited by substantial structural and behavioural measures.

8. ASSESSMENT

8.1. *EXISTENCE OF AID*

(107) The Commission must assess whether the measures concerned constitute State aid. Article 87(1) of the Treaty provides that 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 is, insofar as it affects trade between Member States, incompatible with the common market.

([39]) See footnote 38.

(108) The Commission observes that, with regard to the first and second recapitalisation and the State Protection measure, it has already concluded that those measures constitute State aid. For the first recapitalisation, this was established in the Commission's first recapitalisation Decision of 18 December 2008 (recitals 39 to 53 of the recapitalisation Decision). For the second recapitalisation and the State Protection measure, this was established in the Commission's opening Decision of 30 June 2009 (section 4.1 of the opening Decision). The Commission furthermore notes that KBC will, in the context of the restructuring plan, not receive any additional measures and that the rescue aid measures will be converted into restructuring aid.

(109) The Commission therefore has no reason to change its previous assessments. Consequently, the Commission concludes that the first and second recapitalisation and the State Protection measure obtained by KBC constitute State aid.

8.2. *AMOUNT OF AID*

(110) As regards the amount of aid, the recapitalisation measures constitute State aid amounting to the sum of the injected capital, thus in amount of EUR 7 billion.

(111) As regards the aid amount of the State Protection measure, the Commission considers that a distinction should be made between the Equity Range and the Cash Range of the State Protection measure.

(112) The Cash Range is regarded by the Commission to correspond to the asset relief measure. The Impaired Asset Communication states that the amount of aid in an asset relief measure corresponds to the difference between the transfer value of the assets and the market price. In an asset guarantee measure, the Commission considers that the transfer value is the point at which the State compensates the bank for losses in the form of cash. Therefore, in this case, the transfer value of the assets is EUR 14,8 billion ([40]), as the portfolio must suffer actual losses of EUR 9.1 billion (losses of EUR 3,9 billion in the non-super senior tranches, the first loss in the super-senior tranche of EUR 3,2 billion and the equity range EUR 2 billion) that have to be deducted from the EUR […] billion nominal value of the CDO portfolio. The market value of the CDO portfolio at the point of the transaction was EUR […] billion ([41]). The difference between the transfer value and the market value is EUR […] billion, of which 10 % has to be deducted as 10 % of the losses are retained by KBC. This amounts to EUR […] billion.

(113) In addition, the Commission considers that the excess guarantee fee paid by KBC for the Cash Range should be taken into account. The total nominal guarantee fee is EUR 1,33 billion, of which, however, approximately EUR 1 billion (estimated excess guarantee fee ([42]) is above the minimum fee that is required by the Commission in the IAC. The amount of EUR 1 billion therefore needs to be deducted from the amount calculated in recital 112. This leads to a total aid amount for the asset relief measure of approximately EUR 260 million.

(114) Accordingly, the two capital injections and the asset relief part of the State Protection measure together result in aid element of approximately EUR 7,26 billion, which amounts to 4,1 % of RWA of KBC.

(115) Finally, the Equity Range of the State Protection measure is also assessed. The Commission notes that it could be considered as equivalent to a capital injection, given that the CBFA accepts it as regulatory capital which improves the capital position of the bank. Although the measure does not give liquidity and therefore cannot be exactly counted as a direct capital injection, the Commission considers that it could nevertheless be counted as additional aid, possibly up to nominal amount of EUR 1,8 billion. If it is counted as 100 % aid, the total aid element of all measures (two recapitalisations and State Protection measure) amounts to EUR 9,06 billion, or 5,1 % of RWA of KBC.

8.3. *COMPATIBILITY OF THE AID*

8.3.1. LEGAL BASIS FOR THE COMPATIBILITY ASSESSMENT

(116) Article 87(3)(b) of the Treaty 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'. 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) of the Treaty.

([40]) From the EUR 14,8 billion KBC still retains losses of EUR 1,48 billion (10 %).

([41]) The value is the mark-to model value. The same value at the end of second quarter 2009 was increased to EUR 16 billion as per KBC.

([42]) See recital 127 of this Decision.

(117) The Commission has acknowledged that the global financial crisis can create a serious disturbance in the economy of a Member State and that measures supporting banks are apt to remedy this disturbance. This has been confirmed in the Commission's Banking Communication ([43]), its Recapitalisation Communication, its IAC and its Restructuring Communication. In respect of the Belgian economy this was confirmed in the Commission's various approvals of the measures undertaken by the Belgian authorities to combat the financial crisis ([44]) Therefore, as indicated in the recapitalisation Decision and the opening Decision, the legal basis for the assessment of the aid measures should be Article 87(3)(b) of the Treaty.

8.3.2. COMPATIBILITY OF THE STATE PROTECTION MEASURE

(118) As outlined in section 8.2, the Commission considers that, as regards the State Protection measure, a distinction should be made between the Equity Range and the Cash Range of the measure.

(119) The Commission considers that the commitment to inject capital, subject to the trigger event of specific realised losses on the CDO portfolio, associated with Equity Range should be considered as equivalent to a capital injection ([45]) Therefore, its compatibility is assessed under the Recapitalisation Communication.

(120) The Commission considers that the Cash Range, where the State is committed to compensate KBC for losses in cash, should be considered as an asset relief measure. Therefore its compatibility is assessed under the IAC.

The application of the IAC to the Asset Relief Measure

(121) The specific conditions applying to asset relief measures are laid down in the IAC. In line with section 5.2 of the IAC, an asset relief measure must provide for full ex-ante transparency, adequate burden-sharing followed by the correct valuation of the eligible assets and should ensure the correct remuneration of the State for the asset relief measure to ensure shareholders' responsibility and burden-sharing.

(122) The Commission already established that the State Protection measure in favour of KBC complies with the IAC as regards full ex-ante transparency and disclosure and eligibility of assets in the opening Decision. The Commission therefore focuses its assessment on conditions relating to valuation, remuneration and burden-sharing and asset management arrangements, as these were the aspects of the State Protection measure upon which it opened the investigation.

Valuation

(123) Regarding the valuation, the IAC establishes in section 5.5 that a correct and consistent approach to valuation is of key importance to prevent undue distortions of competition. Accordingly, the Commission has carefully scrutinized the valuation and in particular the underlying general methodology in order to ensure a consistent approach at Community level. For that purpose, the Commission called on the technical assistance provided by a panel of valuation experts. In assessing the measure, the Commission also employed asset valuation methodologies which have benefited from the technical assistance provided by experts from the ECB.

(124) In line with paragraphs 40 and 41 of the IAC, the transfer value of the impaired assets must be in line with their real economic value (hereinafter 'REV'). In an asset guarantee measure, the Commission considers that the transfer value is the point at which the State compensates the bank for losses in the form of cash. In this case the transfer value is EUR 14,8 billion, while KBC states that the REV of the portfolio is EUR […] billion. It follows that if the REV is indeed EUR […] billion, then the measure meets the requirements of the IAC as regards valuation, as the transfer value would be below the REV.

(125) As regards the REV of the CDO portfolio, the Commission's doubts have been allayed. Taking into account the prudent assumptions (such as correlation, loss severities and house price appreciation, default probabilities), in combination with reasonable stressed default probabilities, the Commission considers that EUR […] billion ([…] % of the notional value) is a prudent calculation of the REV.

(126) In addition, the estimations of the REV of the portfolio in a stress scenario is approximately EUR […] billion ([…] % of the notional value), which is still above the transfer value. The Commission considers, that this valuation of the REV in a stress scenario can be considered as acceptable based on the assumptions and methodology used.

([43]) 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, (OJ C 270, 25.10.2008, p. 8).

([44]) See amongst others Commission Decision in case N 574/2008, *Garantie Fortis*, (OJ C 38, 17.2.2009, p. 2), Commission Decision in case NN 42/08, *Fortis*, (OJ C 80, 3.4.2009, p. 7), Commission Decision in case NN 57/09, *Rescue aid in favour of Ethias* (OJ C 176, 29.7.2009, p. 1) and the Commission Decisions with regard to KBC (see footnotes 1 and 2).

([45]) See the description of State Protection measure, recitals 27 to 28 of this Decision.

Remuneration

(127) The Commission's doubts regarding the remuneration paid by KBC have been allayed. The Commission notes that the State Protection measure has a capital relief effect of EUR 504 million. As noted in point 21 of IAC and footnote 11 attached thereto, an asset relief mechanism should be remunerated the same way as a capital injection. In normal circumstances such a capital injection would cost in the region of EUR 35 million annually ([46]). That is considerably less than the annual guarantee fee of EUR 221 million (total of EUR 1,33 billion over six years KBC pays. Indeed, KBC pays in excess of EUR 1 billion over and above the minimum remuneration required under the IAC.

Burden-sharing

(128) Regarding 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 REV of the impaired assets. That criterion is fulfilled in this case as the REV of the portfolio corresponds to EUR […] billion ([…] % of the notional value) and the transfer value to EUR 14,8 billion (62 % of the notional value).The transfer value therefore lies below the REV. The figure of the REV has been verified and found reasonable by the Commission's experts. KBC bears losses even beyond the REV. The Commission's doubts with regard to burden sharing have therefore been allayed.

Asset management

(129) Regarding the managements of assets, the Commission notes that the arrangements between the Belgian authorities and KBC comply with the requirements laid down in the IAC. The Belgian authorities have obtained the customary and necessary rights to safeguard their interests as described in recital 62. Accordingly, those rights are to provide safeguards to protect third party investors, super-senior counterparties and therefore, by extension, the Belgian authorities against possible conflicts of interest in the management of the guaranteed portfolio. In addition, the Belgian authorities are provided with the right to monitor the management of the guaranteed portfolio and are granted appropriate rights to further protect their interests.

Conclusion

(130) On the basis of the foregoing, the Commission concludes that its doubts regarding the asset relief measure have been allayed and that the measure is in line with the IAC.

([46]) EUR 6,3 billion * Tier 1 ratio of 8 % = EUR 504 million * 7 % (safe harbour capital remuneration less funding costs) = EUR 35 million.

Application of the Recapitalisation Communication to the equity commitment

(131) The Commission recalls that in the case of losses in the Equity Range, the Belgian authorities have committed to provide capital if KBC so requests. This recapitalisation of KBC in the Equity Range can occur through the issuance by KBC of ordinary shares to the Belgian authorities at market price. If as result of such an issuance the Belgian authorities were to exceed a 30 % shareholding, they will receive hybrid securities. Therefore, for the measure to be compatible, the capital injection committed should be the minimum necessary and should be remunerated in line with the Recapitalisation Communication.

(132) Regarding the remuneration for the Equity Range, the compatibility of the remuneration should be assessed in two ways. Firstly, the State should be remunerated for providing the equity guarantee. Secondly, in the event that it does inject capital, this should be remunerated appropriately.

(133) Regarding the equity guarantee, KBC must pay for having the right to an equity injection on standby. 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 mid-point of this range (12.5 bps) has been applied to KBC. That amounts to 650 bps per year on the principal amount of EUR 1.8 billion. The Commission recalls point 26 of the Recapitalisation Communication, which states that the price of recapitalisations should be in line with the Eurosystem Recommendations of 20 November 2008. These, in turn, state that the required rate of return on ordinary shares should be the equity risk premium of 500 bps per annum ([47]). In this case, the underwriting premium can be considered as the equity risk premium described in the Eurosystem Recommendations. As the underwriting fee is in excess of this threshold, the remuneration is considered sufficient.

(134) Furthermore, in the event that KBC does call upon the Belgian authorities to provide an equity injection, the Belgian authorities will subscribe to the newly issued equity at market terms. In this case the Belgian authorities will obtain ordinary shares and will be remunerated accordingly. This is line with the Annex to the Recapitalisation Communication. In the context of the current crisis, the Commission previously has accepted equity injections where the issue price was based on a market-orientated valuation such as the share price ([48]).

([47]) As no liquidity is provided through the equity guarantee, the component relating to the funding cost of the Government does not apply here.

([48]) See Commission Decision in Case N 507/08, Financial Support Measures to Financial Institutions in the UK (OJ C 290, 13.11.2008, page 4, recital 52).

(135) If the Belgian authorities, when buying KBC shares, were to acquire more than 30 % voting rights, which could require them to launch a mandatory takeover bid, they will have the option to subscribe to hybrid capital instead. The coupon that KBC will have to pay is similar to that for the two already approved recapitalisation measures. In addition, the Belgian authorities have the option of converting these hybrids into ordinary shares at market terms, which is in line with the terms of its subscription to the newly issued equity described above. Therefore the remuneration of the hybrid securities is in line with the Recapitalisation Communication.

(136) As regards the limitation of the aid to the minimum necessary, the Commission notes that the capital injection will only be called upon if the relevant CDO portfolio suffers realised credit losses that exceed EUR 7,1 billion. If that situation arises, KBC, although it has already provisioned for losses exceeding this amount, will likely face significant difficulties and market uncertainties about its financial position. In line with the reasoning given with regard to the first and the second recapitalisations, which established that a properly remunerated capital injection was an appropriate means of restoring confidence in a systemically important bank such as KBC, the Commission considers that it is reasonable to conclude that the commitment to provide capital in case of significant losses on the CDO portfolio is appropriate and to the minimum necessary.

Conclusion

(137) Based on the above the Commission concludes that the conditions of the Recapitalisation Communication are fulfilled.

Conclusion on the State Protection Measure

(138) Given that the terms of the asset relief part of the State Protection measure are in line with the IAC and the terms of the Equity Range are in line with the Recapitalisation Communication, the Commission considers that the aid granted through the State Protection measure is compatible with the common market.

8.3.3. COMPATIBILITY OF THE RESTRUCTURING PLAN

The degree of required restructuring

(139) The Commission observes that the Restructuring Communication does not set criteria for the conditions under which a bank may need to present a restructuring plan, but builds on the criteria laid down in the Recapitalisation Communication and the IAC.

(140) The Commission notes that KBC has received State aid in excess of 2 % of the bank's total RWA. KBC should therefore in line with point 4 of the Restructuring Communication and with point 55 of the IAC, as well as with its previous commitments mentioned in the opening Decision, undergo in-depth restructuring.

The application of the Restructuring Communication

(141) The Restructuring Communication sets out the State aid rules applicable to the restructuring of financial institutions in the current crisis. According to the Restructuring Communication, in order to be compatible with article 87(3)(b) of the Treaty, the restructuring of a financial institution in the context of the current financial crisis has to:

(i) Lead to a restoration of the viability of the bank;

(ii) Include sufficient own contribution by the beneficiary (burden-sharing);

(iii) Contain sufficient measures limiting the distortion of competition.

(i) *Restoration of long-term viability*

(142) The Restructuring Communication sets out in points 9 to 11 that the Member State should provide a comprehensive and detailed restructuring plan which provides complete information on the business model. The plan should also identify the causes of the difficulties faced by a financial institution and alternatives to the restructuring plan proposed. The information submitted by the Belgian authorities meets these requirements.

(143) In assessing a restructuring plan, the Commission must assess whether the bank is able to restore long-term viability without State aid. With respect to KBC, any restructuring plan should demonstrate that it has taken measures to deal with the source of its difficulties, that its business model is viable and that it is able to withstand a realistic stress scenario. It should also indicate, as noted in point 14 of the Restructuring Communication, how the State aid is redeemed or that it is remunerated according to normal market conditions.

(144) The restructuring plan identifies the main causes of the difficulties for the bank, which were mainly attributable to value markdowns on KBC's synthetic CDO portfolio. Those instruments must be marked-to-market with any changes in the market value flowing immediately through the income statement. KBC required two capital injections and an asset guarantee to deal with these losses and their subsequent effect on its capital position.

(145) In order to assess whether KBC can be considered viable, the Commission must assess whether the plan deals with these issues in the CDO portfolio. In this respect, the Commission notes that KBC has ceased to issue CDO instruments. As regards its residual CDO portfolio, KBC's exposure to further losses has been significantly limited. Since EUR 14,8 billion (at 90 %) of the losses on the portfolio has been guaranteed by the State, the portfolio no longer has to be valued at mark-to-market, thus reducing volatility on KBC's balance sheet. Its only remaining exposure is on the small part of the CDO portfolio that is valued above the transfer value of the State Protection measure plus a 10 % exposure to losses in the cash guarantee tranche. Therefore the Commission can conclude that KBC has taken sufficient actions to address the cause of its problems and that any further negative development in its CDO portfolio will not threaten its viability.

(146) KBC also has an ABS portfolio that is not covered by the protection obtained from the Belgian authorities. The Commission observes that KBC has provided information on the remaining exposure ([…]). KBC will absorb any losses on that portfolio (calculated at EUR […] million per annum), which according to KBC does not threaten its viability because of its more conservative risk and maturity profile ([49]). The losses on the ABS portfolio have been taken into account in the financial projections for the restructuring plan.

(147) As regards its business model, KBC intends to continue its bancassurance strategy, albeit within a smaller and more focussed group. It will provide a full range of banking and insurance products to its core customer segments, retail, private SME and mid-cap. It will focus on markets, for example in the CEE-R, where it already has healthy franchises, while withdrawing from markets that it considers high risk or where it has a franchise that is not or cannot become sustainable. KBC has a strong liquidity position. It has a limited reliance on wholesale, particularly short-term, funding and has a loan-to-deposit ratio of less than […] %. Its strong liquidity position is underlined by the fact that even during the most significant disruption in financial markets for many years it did not need to avail of any liquidity assistance from the Belgian State.

(148) The Commission considers that KBC's business strategy, which consists of retail activities combined with cross-selling of insurance products in KBC's core markets, is a viable business model. The Commission considers that the continuation of KBC's operations in the CEE-R, which could be considered as a developing market, is an acceptable strategy, as it allows KBC to leverage its successful business model to a high-growth region, allowing it the possibility to continue to grow and generate profits. This is also important for financial stability concerns, as KBC is an important operator on financial markets in this region and its withdrawal could have destabilising effects. That analysis, as regards financial stability, also applies to KBC's presence in Ireland.

([49]) For accounting purposes, the ABS portfolio was reclassified as 'loans and receivables' at the end of 2008, therefore reducing the volatility of KBC's income statement as negative value adjustments on the portfolio can be spread over time.

(149) According to points 9 and 12 to 15 of the Restructuring Communication, the restructuring plan should also demonstrate how the bank will restore its long-term viability without State aid as soon as possible. In particular, the bank should be able to generate appropriate return on equity, while covering all costs of its normal operations and complying with the relevant regulatory requirements.

(150) The Commission considers that the restructuring plan submitted by KBC meets those requirements as KBC has provided financial projections for the period 2008-2013, giving information on revenues, costs, impairments, profits and capital position for each business unit. The Commission notes that the projections provided are based on reasonable underlying macro-economic assumptions.

(151) In the restructuring plan, KBC assumes that revenues and profits will return to approximately pre-crisis levels in a base case, with revenues of EUR […] billion in 2009, increasing to EUR […] billion in 2013 and a projected net profit (loss) of EUR -[…] billion in 2009 increasing to EUR […] billion in 2013. Most of the impairments will be taken in 2008 (EUR […] billion) and 2009 (EUR […] billion). KBC's Tier-1 ratio will increase from […] % in 2009 to […] % in 2013. Given that the underlying business of KBC (excluding the losses generated by the KBC Financial Products division in CDOs and ABS) continued to generate profits throughout 2008 and 2009 to date, Commission considers the projections feasible.

(152) As regards KBC's ability to withstand a stress scenario, this was described in recital (42) to (49). The Commission considers the scenario generated as reasonable. As the stress scenario demonstrates that KBC will exceed its regulatory capital requirements, KBC can be regarded as meeting the requirements of paragraph 13 of the Restructuring Communication.

(153) Moreover, the Commission notes positively that projected profits will allow the bank to remunerate the State capital adequately and redeem it over time. The repayment of the State capital should be possible without depleting the capital base of the institution, as the KBC's Tier-1 capital ratio is projected to reach […] and exceed it afterwards under every scenario provided in the restructuring plan.

(154) Finally, the plan also lays out a convincing strategy for repaying the Belgian authorities. For the State Protection measure, the fee is paid in cash in 12 semi-annual instalments. As regards the capital injection, KBC starts paying coupons from 2011 and will begin repaying the principal once it begins to generate surplus capital, which under the base case is from 2012 onwards. Taking into account the 50 % penalty, KBC is projected to repay about EUR 7 billion in the years […], which is equivalent to the principal amount of State capital that is received. KBC intends to fully repay the State […]. The projected internal rate of return of the State is 13,9 % ([50]).

(155) Consequently, the Commission considers that the restructuring plan submitted by KBC fulfils the requirements of the Restructuring Communication with regard to the restoration of the long-term viability.

(ii) *Own contribution/burden-sharing*

(156) The Restructuring Communication indicates that an appropriate contribution by the beneficiary is necessary in order to limit the aid to minimum and to address distortions of competition and moral hazard. To that end, firstly, the restructuring costs should be limited while, secondly, the aid amount should be limited and a significant own contribution is necessary.

(157) As regards the limitation of the restructuring costs, the Restructuring Communication indicates in point 23 that the restructuring aid should be limited to cover the costs which are necessary for the restoration of viability. Furthermore, in order to keep the aid limited to a minimum, the banks should first use their own resources to finance the restructuring. Accordingly, the costs associated with the restructuring should not only be borne by the State but also by those who invested in the bank by absorbing losses with available capital and by paying an adequate remuneration for State interventions.

([50]) In terms of IRR (Internal Rate of Return).

1. Limitation of restructuring costs

(158) The Commission observes that the restructuring costs are limited to the costs which are necessary for the restoration of viability.

(159) The Commission observes that the first and second recapitalisations were used by KBC to improve its core Tier-1 capital ratio and to increase the solvency of its insurance business. Those measures, by improving KBC's capital position, have increased its ability to absorb losses. The State Protection measure was used to shield KBC from further write-downs on its CDO portfolio, as well as to increase its capital ratios. That measure has furthermore removed a source of volatility on its balance sheet.

(160) Consequently, those measures have contributed to the restoration of viability of KBC as they have tackled the source of KBC's difficulties, namely the substantial write-downs on its CDO portfolio and the consequences of these write-downs on KBC's capital position. Furthermore, KBC will not be able to use the aid received to expand its business activities through acquisitions as it is limited in this respect by the commitments provided by the Belgian authorities with regard to the acquisition ban (see recital 66).

2. Limitation of the amount of aid, significant own contribution

Limitation of aid

(161) The Commission considers that the amount of aid is limited to the minimum. The Commission recalls that it has already established in the recapitalisation Decision (recital 65), and the opening Decision (recital 71) that the aid is limited to the minimum to ensure the viability of KBC.

(162) In that context, the Commission observes that KBC will adequately remunerate the Belgian authorities for the aid measures it has received. That necessarily limits the amount of aid granted to KBC. With regard to the recapitalisations, KBC will pay the State a coupon of 8,5 % per security if a dividend is paid. KBC is required to redeem the securities at 150 %. As established in the recapitalisation Decision and in the opening Decision, the internal rate of return for the State is projected to be 13,9 %, above the level required by the Commission in the Recapitalisation Communication ([51]). As regards the State Protection measure, the Commission notes that KBC will pay a fee which is approximately […] times higher than that required in the IAC (see recital 127).

([51]) See points 72 and 73 of the first recapitalisation decision and points 69 and 70 of the opening decision.

Own contribution

(163) The Commission furthermore considers that the own contribution by KBC to its restructuring is considerable. KBC, as part of its financial restructuring, will list 40 % of its Czech subsidiary ČSOB and 40 % of its Hungarian subsidiary K & H on the local stock exchanges. That will significantly dilute KBC's shareholding as it is currently 100 % owner of those subsidiaries and provides for a contribution by KBC and its investors. The proceeds of the listing of ČSOB and K & H will increase KBC's own funds and will be used to repay the State.

(164) Furthermore, KBC plans to sell the entire European Private Banking business unit including Vitis (life insurance), thus completely ceasing its activities in that market segment. The proceeds of the sale will also be used to build up KBC's own funds in order to repay the State.

(165) As regards burden-sharing, the Commission observes that in the context of the State Protection measure, KBC, on a CDO portfolio with a nominal value of EUR 23,9 billion, will take a first loss of EUR 9,1 billion. On top of that it will assume a 10 % share of losses in the EUR 14,8 billion super-senior tranche insured by the Belgian authorities.

(166) Finally, the Commission notes that the Belgian authorities have committed that KBC will not pay coupons or call subordinated debt instruments, except where there is a legal obligation to do so. As a result, subordinated debt holders will receive limited remuneration and thus contribute to the restructuring.

(iii) *Measures limiting the distortion of competition*

(167) The Restructuring Communication requires that the restructuring plan proposes measures limiting distortions of competition and ensuring a competitive banking sector. Moreover, they should also address moral hazard issues and ensure that State aid is not used to fund anti-competitive behaviour.

(168) As regards the measures limiting the distortion of competition, the Restructuring Communication indicates that the Commission has to take into account in its assessment the amount of aid, the degree of burden-sharing and the effects the position the financial institution will have on the market after the restructuring. On the basis of that analysis, suitable compensatory measures should be put into place.

(169) The Commission notes that KBC has received a considerable amount of aid, significantly above the 2 % RWA benchmark of the Recapitalisation Communication and the IAC ([52]). Against this background, the Commission concludes that aid to KBC caused distortions of competition on the markets where it has significant presence.

(170) On the other hand, there are several aspects which should be taken into account when assessing the distortions of competition caused by the State aid granted to KBC. Firstly, the main factor behind KBC's difficulties was its exposure to mark-to-market write-downs on its CDO portfolio, rather than excessive risk-taking and hence losses in its core business model. KBC has ceased activities in this area. Secondly KBC pays adequate remuneration for the State aid it has received. The Belgian authorities are projected to receive a return of 13,9 % on their capital injections. With regards to the State Protection measure, the Belgian authorities are guaranteeing the portfolio at a transfer value significantly below its REV while the remuneration it receives for the capital relief and the provision of the equity guarantee is above the Commission guidelines. Thirdly, the listing of ČSOB and K & H on the Czech and Hungarian markets provides for considerable burden-sharing.

(171) Notwithstanding the above, the Commission still considers that suitable measures must be put in place to address the remaining distortions of competition.

(172) KBC will reduce its balance sheet by 20 % in terms of Group RWA on a pro forma basis (17 % in terms of total assets). The reduction will be achieved mainly through divestments ([…]) and the run-down of KBC FP ([…]). As a result, KBC will reduce its market presence in several markets. In this respect, it should be noted that for financial stability reasons KBC will not be required to divest activities in certain countries, as per recital 177. This essentially ring fences around […] of KBC's balance sheet from divestment or runoff.

(173) In particular, KBC proposes to sell Centea and Fidea, which, although they are branded separately, are important parts of its business strategy in Belgium. Centea and Fidea are profitable businesses with a recognisable brand name that are relatively easy to separate from KBC's Belgian business unit. They are two viable and independent entities on the Belgian market, which are self-funded, have a wide range of customer contact points and are profitable. […] It is also prepared to provide back-office services to facilitate the transfer of these entities to a new owner.

([52]) The aid amount received by KBC amounts to between 4,1 % and 5,1 % of its RWA.

(174) In 2008, Centea had a market share in volume terms of […] of mortgages, […] of debit cards (number of cards), […] of current accounts and […] of deposits/savings accounts. It has its own sources of funding and is a net contributor to KBC funding. Centea has a country-wide network of 712 client contact points and a portfolio reflecting a full banking product range. Centea has its own front-office function. Back-office services (including IT-services) are provided by KBC's Shared Services and Operational Business Unit. Fidea has […] of market share in Class 21 life assurance, […] % in Class 23 life assurance, […] in non-life insurance and […] % in health insurance. Table 2 includes KBC, Centea and Fidea's market shares in Belgium as well as the effects of the proposed divestments on KBC's total market share.

Table 2

Selected KBC's market shares in Belgium as of 2008 and the impact of the Centea and Fidea divestments on the KBC's position

[…]

(175) A significant structural measure, such as the creation of a new competitor from an incumbent player with a large market share, can help encourage competition on a previously concentrated market. This applies on the Belgian market, where 4 large players account for the majority of the retail market.

(176) The Commission regards these divestments as appropriate means of increasing competition on the concentrated Belgian retail banking market. With their established brand name and distribution networks, Centea and Fidea constitute attractive targets for competitors wishing to enter the Belgian market or expand their presence there While the market share of these divestments is small in some market segments, the Commission considers that this is counterbalanced by the fact that the entities are relatively self-sufficient and that KBC has committed that the divestments will take place […].

(177) Moreover, KBC will limit its expansion in the CEE-R to countries where it already has a significant presence which represents a curtailment of its prior expansion plans. That can be regarded as limiting the distortion of competition, as KBC will not be using State aid to expand in markets where it does not have a currently viable business or in activities that are not part of its refocused business model. However, the Commission considers it appropriate that KBC is not required to withdraw from all its CEE-R markets, which it considers as core. As described in recitals 12 and 13, KBC is a significant market player in several of those countries. It could be damaging to financial stability in these countries and lending to the real economy if KBC was required to further reduce its presence in the region. The same is true for KBC's presence in Ireland.

(178) Furthermore, the Commission considers that the package of measures sufficiently addresses the issue of moral hazard. KBC has proposed a comprehensive sale of other core businesses (private banking, merchant banking, CEE-R) and non-core businesses as described in section 4.2.2 of this Decision. […] This is a significant reduction in the business activities of KBC.

(179) The Commission notes that the Belgian authorities have provided a detailed timeline of planned divestments, as described in recital 62. The Commission also notes the appointment of hold separate managers for Centea and Fidea, a monitoring trustee and divestment trustees, where appropriate. Such commitments ensure that the majority of the down-sizing of KBC will be carried out in a timely manner. While there is scope for the target dates for divestments to be extended, it will only be upon the specific approval of the Commission.

(180) The Commission notes positively the behavioural commitments provided by KBC and the Belgian authorities, which have been described in more detail in recitals 63 to 77. Those commitments include a commitment to lend to the real economy, a price leadership ban and a ban on mass-marketing the State support, thus preventing KBC to use the aid to fund anti-competitive market conduct. The acquisition ban furthermore ensures that the State aid will not be used to take over competitors.

(181) As regards the price leadership ban, the Commission finds it to be in line with point 44 of the Restructuring Communication as it serves to ensure that State aid cannot be used to offer terms which cannot be matched by competitors which are not in receipt of State aid. The Commission considers the ban appropriate in markets where KBC is well established with a market share of at least [0-10] % and where it does not undertake any pro-competitive structural measures. In this case, the Commission considers it appropriate that the price leadership ban does not apply to Belgium, as the divestment of Centea and Fidea is a significant structural measure which should lead to improved competition on the Belgian market.

(182) Taking into account the extent of burden sharing and likely short timescale for their implementation, the Commission considers that the scale and nature of measures proposed by KBC are sufficient and adequate to address any distortions of competition.

8.3.4. MONITORING

(183) The Commission notes that point 46 of the Restructuring Communication indicates that, in order to verify that the restructuring plan is being implemented properly, detailed regular reports from the Member State are necessary. Accordingly, the Belgian authorities should provide the Commission with such reports every six months, starting from the date of this Decision.

Conclusion on the restructuring plan

(184) The Commission finds that the restructuring plan set out in chapter 4 of this Decision is compatible with Article 87(3)(b) of the Treaty.

9. **CONCLUSION**

(185) Based on the above assessment of the State Protection measure and the restructuring plan of KBC, as well as the commitments provided by the Belgian authorities and KBC, the Commission raises no objection against the restructuring plan and the conversion of the rescue measures into restructuring aid.

HAS ADOPTED THIS DECISION:

Article 1

The State Protection measure which Kingdom of Belgium has implemented in favour of KBC constitutes State aid within the meaning of Article 87(1) of the Treaty, which is compatible with the common market subject to the commitments listed in Annex I.

Article 2

The Kingdom of Belgium shall inform the Commission, within two months of notification of this Decision, of the measures taken to comply with it. Furthermore, the Kingdom of Belgium shall submit detailed regular six-monthly reports, starting from six months after the date of this Decision.

Article 3

This Decision is addressed to the Kingdom of Belgium.

Done at Brussels, 18 November 2009.

For the Commission

Neelie KROES

Member of the Commission

ANNEX

Behavioural commitments

(i) With regard to the duration of these behavioural commitments, the Belgian authorities commit that, without prejudice to the possibility for the Commission to grant an exemption, notably on the basis of a sufficiently reasoned request from the Belgian authorities, the behavioural commitments listed in recitals 63 to 77 inclusive apply for a duration of […] from the date of the Commission's Decision or, until the nominal amounts subscribed to by the Belgian authorities, on 19 December 2008 and on 20 July 2009 respectively, have been redeemed, whichever is earlier ([1]).

(ii) The Belgian authorities commit that KBC shall endeavour to maintain its lending policy to the real economy in countries where it has retail operations. The credit provided by KBC will be on commercial terms.

(iii) They further commit that KBC will maintain its solvency ratio of core Tier-1 at minimal […] % and its basic own funds at […] % ([2]).

(iv) With regard to a ban on acquisitions, the Belgian authorities commit that KBC will refrain from acquiring control, as defined by Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation) ([3]), of financial institutions. KBC will moreover refrain from acquiring control of businesses other than financial institutions if such an acquisition would slow down the repayment of the amount of EUR 7 billion of core Tier-1 Yield Enhanced securities to the Belgian authorities as planned in the restructuring plan that was notified to the Commission on 30 September 2009 and approved by this Decision. Notwithstanding that prohibition, KBC may acquire businesses if it obtains the Commission's approval, in particular if it is considered essential to safeguard financial stability or competition in the relevant markets.

(v) The Belgian authorities commit that KBC will adhere to the following price leadership ban:

(a) In Community-markets in which KBC has a market share of more than [0-10] %, on the product markets as defined in point (ii) below, KBC will not offer more favourable prices on standardized products than the best priced competitor of KBC among the top ten market players in terms of market share on this geographic and product market;

(b) The product markets to which the condition set out in point (i) applies are limited to: KBC's standardized products on the retail deposit market, deposits for SME's (SME defined according to SME definition as operated by KBC) and retail mortgage market;

(c) As soon as KBC becomes aware of the fact that it offers more favourable prices for its products than the best priced provider, KBC will as soon as possible adjust, without any undue delay, its price to a level which is in accordance with this commitment;

(d) That condition does not apply to the Belgian market, where no price leadership ban will apply.

(vi) The Belgian authorities also commit that KBC will refrain from mass marketing invoking the measures as an advantage in competitive terms.

(vii) With regard to the limitation of KBC executive remuneration, the Belgian authorities commit that:

(a) 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'. Exit schemes or statutory compensation for dismissal are limited to twelve months' fixed salary for KBC's Executive Committee Members;

(b) In addition, Executive Committees of KBC, KBC Bank NV and KBC Verzekeringen NV forego all bonuses for 2008 (cash as well as options and share rewards).

([1]) For the purpose of this commitment package, the redemption of the nominal amounts will be realized when an amount of EUR 7 billion is repaid.
([2]) Basic own funds here are equivalent to equity and reserves.
([3]) OJ L 24, 29.1.2004, p. 1.

(viii) The Belgian authorities commit that KBC will endeavour to ensure, for the benefit of the Belgian authorities, an overall return on the securities subscribed by them of minimum 10 % p.a.

(ix) The Belgian authorities commit to re-notify the first recapitalisation under Article 88(3) of the Treaty if either of the following situations arises which make it less likely that the overall return in excess of 10 % p.a. is achieved:

(a) If, from 1 January 2010, KBC does not make a dividend payment during two consecutive years or, from 1 January 2009, does not make a dividend payment during three years within a period of five years; or

(b) If, after a period of one year where the share price remains on average above 150 % of the issue price of the securities, KBC has not repurchased, or committed to do so within three months, at least 20 % of the original investment of the State.

(x) In the same vein, the Belgian authorities commit to re-notify the second recapitalisation under Article 88(3) of the Treaty if the following situation arises which makes it less likely that the overall return in excess of 10 % p.a. is achieved:

(a) If, from 1 January 2010, KBC does not make a dividend payment during two consecutive years or, from1 January 2009, does not make a dividend payment during three years within a period of five years.

(xi) Unless in either of the scenarios described in points (ix) and (x) it can be shown that the non-payment of dividends is caused by normal market events or that despite the non-payment of dividends, the overall return will nevertheless be in excess of 10 % per annum the Commission, without calling into question the capital injection, which has been declared compatible with the common market, can in the context of the renotification in particular require additional behavioural constraints.

(xii) As regards the remuneration of the alternative securities under the State Protection measure, the Belgian authorities commit that the coupon that will be payable on the alternative class of core capital securities to be issued by KBC if the Belgian authorities were to acquire more than 30 % voting rights under the Equity Range of the State Protection measure, shall be equal to […].

(xiii) The Belgian authorities also commit that KBC or any of its subsidiaries shall not engage in the origination of CDOs [1]. It is understood that securitisation transactions which are not caught by this definition of CDOs fall outside the scope of this commitment. This is for instance the case for securitisation transactions for purposes of management of regulatory capital or credit risk or to raise liquidity.

(xiv) With regard to coupon payments and call options on hybrid capital, unless the Commission otherwise agrees to an exemption, the Belgian authorities commit that:

(a) […];

(b) […].

(xv) Finally, the Belgian authorities have committed that KBC will organise the management rights of the Belgian authorities in respect of the guaranteed portfolio under the State Protection measure, in such a way that the interests of the Belgian authorities as the guarantor will be duly guaranteed while preserving a suitable level of flexibility for KBC to react swiftly to changing market circumstances and to make the relevant adjustments and choices as appropriate. The legal documentation of the guaranteed portfolio provides for safeguards to protect third party investors, super senior counterparties and therefore, by extension, the Belgian authorities against possible conflicts of interest in the management of the guaranteed portfolio. In addition to the safeguards under the original legal documentation, the agreement with the Belgian authorities governing the State Protection measure will in particular provide for the right of the Belgian authorities to monitor the management of the guaranteed portfolio. Where appropriate, the Belgian authorities will be granted consent rights to further protect its interests.

[1] For the purpose of this commitment, a 'CDO' is a credit portfolio securitisation transaction, with the following characteristics: (i) it entails a repackaging of portfolios of assets, and such assets can be bonds, loans, derivatives or other debt obligations, (ii) the credit risk in respect of such assets is repackaged into multiple tranches of securities of different seniority, sold to investors, and (iii) the transaction is mainly arbitrage driven, i.e. the main goal of the transaction is to provide profits from differences between the market price of the underlying assets and the price at which the securitised risk can be sold in structured form.

Divestments and run-down of business portfolios

(xvi) The Belgian authorities have furthermore committed, within the limits of their respective competences, to ensure KBC's compliance with the commitments listed from recitals 79 to 97 inclusive.

(xvii) KBC will take the necessary steps for the divestment of the entities or assets (hereinafter 'Divestment Business(es)') as listed in recital 80 to be implemented by the time mentioned. Such a divestment shall be deemed implemented when a binding agreement has been entered into by KBC to sell […] in the entity or asset concerned. A legally binding agreement is an agreement which cannot be rescinded unilaterally by KBC and intends to create a legal relationship on which each party can rely and which, in case of termination of the agreement by KBC, would lead to a liability of KBC to the other party. That legally binding agreement may still be subject to a number of customary conditions precedent such as approval by the relevant supervisory authorities.

(xviii) As regards the divestment businesses, the Belgian authorities commit that KBC will divest the following entities […]:

(a) […] by […]

(b) KBL EPB by […]

(c) […] by […]

(d) Centea by […]

(e) Fidea by […]

(f) Antwerp Diamond Bank by […]

(g) Implementation of divestments of NLB, Zagiel, […] by […]

(h) Absolut bank (Russia) by […]

Value Preservation Commitments

(xix) With regard to preserving the value of the divestment businesses, the Belgian authorities commit that KBC will ensure that:

(a) the divestment business shall retain tangible and intangible assets owned by it which contribute to its current operation or are necessary to ensure its viability and competitiveness;

(b) the divestment business shall retain all (a) licences, permits and authorisations issued by any public authority for its benefit; (b) its contracts, leases, commitments and customer orders; and (c) its relevant records which contribute to its current operation or are necessary to ensure its viability and competitiveness;

(c) the divestment business shall employ the appropriate number of staff with the necessary capabilities to ensure its viability and competitiveness. KBC shall take all reasonable steps, including incentives taking into account industry practice, to encourage all key personnel [1] to remain with the Divestment Businesses. It shall also not solicit the key personnel transferred with the Divestment Business. […].

(xx) The Belgian authorities commit that KBC shall exercise its best efforts to support the buyers of the Divestment Businesses in migrating to appropriate infrastructure for the ongoing operation of the Divestment Businesses. […].

[1] Key personnel means all personnel necessary to maintain the viability and competitiveness of the Divestment Businesses.

(xxi) From the date of this Decision until implementation of the divestment, the Belgian authorities commit that KBC shall preserve the economic viability, marketability and competitiveness of the Divestment Businesses in accordance with good business practice and shall minimise as far as possible any risk of loss of their competitive potential. KBC shall carry on the Divestment Businesses as a going concern in the ordinary and usual course as carried on before the date of this Decision.

(xxii) The Belgian authorities commit that no acts which might have a significant adverse impact on the Divestment Businesses shall be carried out by KBC. […].

Additional divestment commitments in respect of Centea and Fidea

(xxiii) As regards the prospective buyer(s) of Centea and Fidea, the Belgian authorities have provided the commitment that KBC shall ensure that:

(a) The buyer of Centea does not have a post-acquisition market share of greater than […] % in current accounts, savings or mortgages in Belgium.

(b) The buyer of Fidea does not have a post-acquisition market share of greater than […] % on either the life or non-life insurance markets in Belgium.

(xxiv) Furthermore, the Belgian authorities commit that KBC shall make the necessary arrangements to ensure clear identification of the Centea and Fidea businesses and start to prepare their separation from businesses that are integrated in KBC into distinct and separately saleable entities immediately after the Commission's Decision. Without prejudice to the value preservation commitments as set out in points (xix) to (xxi), Centea and Fidea will be managed as distinct and saleable entities from the date of the Commission's Decision. To ensure that all management decisions between the date of this Decision and the implementation of the divestment are in the best interests of Centea and Fidea with a view to ensuring their continued economic viability, marketability and competitiveness, KBC shall appoint a hold separate manager ([1]) for each of these businesses and shall ensure that the hold separate manager operates independently. That hold separate manager can be the current CEO of those businesses. The hold separate manager will manage these divestment businesses (Centea and Fidea) in their best interest, in common consultation with KBC, as monitored by the Monitoring Trustee.

Monitoring trustee

(xxv) A monitoring trustee will be appointed who is to report on a six monthly basis to the Commission on compliance by the Belgian authorities and by KBC with the commitments listed in points (xvi) to (xxiv). The monitoring trustee shall be independent, possess the necessary qualifications and shall not be subject to a conflict of interests throughout the exercise of his mandate

(xxvi) No later than one month after the adoption of this Decision, the Belgian authorities shall submit a list of one or more persons, as agreed with KBC, whom they propose to appoint as the monitoring trustee(s) to the Commission for approval. The Commission shall have the discretion to approve or reject the proposed trustee(s) based on the criteria outlined in point (xxv). If the Commission rejects all proposed trustee(s), KBC and the Belgian authorities will, within one month of being informed of the rejection, propose new candidates which again need to be approved or rejected by the Commission. If all further proposed trustee(s) are rejected by the Commission, the Commission shall nominate a trustee, whom KBC shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

Review of the commitment Package

(xxvii) Where appropriate and on the basis of a sufficiently reasoned request from the Belgian authorities and KBC and taking into consideration the views of the monitoring trustee, the Commission may:

(a) extend the target dates for implementation of the divestments:

(i) as regards the divestments to be implemented […], the target date may be extended […], […], and subsequently […], […];

(ii) as regards the divestment to be implemented […], the target date may be extended […], […];

([1]) Hold separate manager is the person appointed to manage the day-to-day business of the Divestment Business as monitored by the monitoring trustee.

Such extension may be granted in particular when the divestments will not be implemented by these dates through no fault of KBC.

KBC will not be obliged to sell a Divestment Business […] except where […], in which case KBC shall not be obliged to sell the relevant Divestment Business […].

(b) dispense with, amend or replace one or more of the measures, requirements or conditions set out in this Decision.

(xxviii) Any such requests shall be sent to the Commission at the latest two months prior to the target date.

Divestiture trustee

(xxix) If the divestments have not been achieved by the relevant target dates and no later than one month after the ultimate non-extendable target date, and if no alternative measures have been approved by the Commission, the Belgian authorities shall submit a list of one or more persons, as agreed with KBC, whom they propose to appoint as the divestiture trustee(s) to the Commission for approval. The divestiture trustee shall be independent, possess the necessary qualifications and shall not be subject to a conflict of interests throughout the exercise of his mandate. The Commission shall have the discretion to approve or reject the proposed divestiture trustee(s). If the Commission rejects all proposed divestiture trustee(s), KBC and the Belgian authorities will, within one month of being informed of the rejection, propose new candidates which again need to be approved or rejected by the Commission. If all further proposed trustee(s) are rejected by the Commission, the Commission shall nominate a trustee, whom KBC shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

(xxx) The Belgian authorities commit that KBC shall grant necessary and reasonable powers of attorney to the divestiture trustee:

(a) to effect the disposal of the Divestment Business (including the necessary powers to ensure the proper execution of all the documents required for effecting the disposal), and

(b) to take all actions and declarations which are necessary or appropriate to achieve the disposal, including the appointment of advisors to assist with the disposal.

(xxxi) The Commission shall authorize, subject to it having taken into consideration reasonable alternatives as proposed under the review arrangements as set out in recital 89, the divestiture trustee to sell the Divestment business concerned […]. The divestiture trustee shall include in the sale and purchase agreement(s) such customary and reasonable terms and conditions as are appropriate for an expedient sale. The divestiture trustee shall organize the sales process in consultation with KBC so as to ensure a divestment under the best possible conditions, subject to its obligation to divest […] in the trustee divestiture period under the conditions set out in recitals 91 and 92.

(xxxii) In addition, all fees and expenses of the monitoring and divestiture trustees will be borne by KBC.

Run-down of business portfolios

(xxxiii) The Belgian authorities commit that KBC will take the necessary steps for the run-down of the business portfolios of the entities listed hereunder to be completed by the target dates as set out for each of these entities. From the date of this Decision until the completion of the run-down, KBC will respect a stand-still with regard to the amount of RWA [1] represented by these business portfolios. Concerning this commitment, 'stand-still' means that KBC will not enter into any new business in these business portfolios and that KBC's management decisions with regard to the business portfolios can only have a neutral or decreasing effect on the amount of RWA attributed to these business portfolios at the time of this Decision. KBC will not be obliged to divest or otherwise dispose of portfolio items or to terminate existing contracts under conditions that would result in a loss or a liability for KBC. KBC will thus run-down the following business portfolios:

(a) […] by […]

(b) KBC FP by […]

[1] After neutralizing the pro-cyclical effect of expected credit defaults.

(c) […] by […]

it being understood that certain contracts belonging to the business portfolios as listed above might expire and therefore still remain in KBC's books […].

Listing of two CEE-R assets

(xxxiv) The Belgian authorities commit that KBC will carry out the listings of ČSOB (Czech Republic) and K & H bank (Hungary) […].

Monitoring

(xxxv) The Belgian authorities commit that KBC provides the Commission with detailed reports on a six-monthly basis through the Belgian authorities. These reports will contain information on the recapitalisation measures (as mentioned in point 40 of the Recapitalisation Communication [1]), the functioning of the State Protection measure (as mentioned in Annex IV to the Impaired Asset Communication, hereinafter 'IAC' [2]), and the restructuring plan (as mentioned in point 46 of the Restructuring Communication [3]). The first report, combining all that information, will be submitted to the Commission no later than six months after the date of this Decision.

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[1] Commission Communication on the Recapitalisation of financial institutions in the current financial crisis: limitation of the aid to the minimum necessary and safeguards against undue distortions of competition (OJ C 10, 15.1.2009, p. 2).

[2] Communication from the Commission on the treatment of impaired assets in the Community banking sector (OJ C 72, 26.3.2009, p. 1).

[3] Commission communication on the return to viability and the assessment of the restructuring measures in the financial sector in the current crisis under the State aid rules (OJ C 195, 19.8.2009, p. 9).