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In the published version of this decision, some information has been omitted, pursuant to articles 24 and 25 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus […].		**PUBLIC VERSION** **WORKING LANGUAGE** **This document is made available for information purposes only.**

Subject: State aid SA.31883 (N516/2010), Restructuring of Österreichische Volksbanken-AG, Austria

Sir,

The Commission wishes to inform Austria that, having examined the information supplied by your authorities on the aid measures referred to above, it has decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union ("TFEU").

1. PROCEDURE

(1) On 9 December 2008[1] the Commission approved the Austrian bank support scheme, which consisted of a package of measures to ensure the stability of the financial system. The scheme was subsequently prolonged four times[2] and expired on 30 June 2011.

[1] Commission Decision of 9.12.2008 in State aid case N 557/2008 – Maßnahmen nach dem Finanzmarktstabilitäts- und dem Interbankmarktstärkungsgesetz für Kreditinstitute und Versicherungsunternehmen in Österreich, OJ C 3, 8.1.2009, p. 2.

[2] The first extension of the scheme, including certain amendments, was approved on 30 June 2009 (OJ C 172, 24.7.2009, p. 4.), the second extension on 17 December 2009 (OJ C 28, 4.2.2010, p. 6), the third extension on

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(2) In April 2009 Österreichische Volksbanken-AG ("ÖVAG" or "the bank"), the then fourth-largest bank in Austria, was recapitalised with EUR 1 billion under the Austrian bank support scheme. Further, it placed three issues of State guaranteed debt instruments in the market, each of EUR 1 billion, on 9 February, 18 March and 14 September 2009 respectively. Austria provided those aid measures under the assumption that ÖVAG was a sound bank and submitted a viability plan on 29 September 2009.

(3) Further analysis by the Commission led it to conclude that the application of the criteria stipulated in the Annex to the Recapitalisation Communication[3] indicated that the bank could not be considered as sound in the meaning of that Communication at the moment of the recapitalisation. Therefore a restructuring plan was requested. Austria, while maintaining its position that the bank had been sound, notified a restructuring plan for ÖVAG on 2 November 2010. That plan was subsequently supplemented by a number of information submissions.

2. BENEFICIARY AND BACKGROUND OF THE AID MEASURES

2.1. THE BENEFICIARY

(4) ÖVAG is the central institute of Austria's Volksbanks (local credit co-operatives) providing them with centralized back-office services, liquidity management and financial products. Volksbanks are universal banks with local to regional scope of activities. Together with ÖVAG as their central institution they form the Volksbank group. 58.2% of ÖVAG is owned by them through a common holding entity. Additional owners are DZ Bank Group (25%), Victoria Group (10%) and Raiffeisen Zentralbank Österreich AG (6.1%). The remaining 0.7% is in free float. At the end of 2008 ÖVAG was the fourth-largest bank in Austria with a balance sheet total of EUR 55.8 billion[4], an Aa3 rating from Moody's and an A rating from Fitch[5].

(5) ÖVAG's main geographic market is Austria. The bank is also active in a number of Central and Eastern European countries (CEE) where its market shares are mostly small. To a limited extent ÖVAG is also active in Germany in corporate banking and real estate financing.

(6) ÖVAG operates in five business segments: corporate banking, retail banking, real estate, financial markets and banking book/other operations. ÖVAG abandoned public finance and infrastructure financing in 2008 when it sold its stake in Kommunalkredit Austria AG ("KA") to the Republic of Austria for the nominal amount of EUR 1.

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25 June 2010 (OJ C 250, 17.9.2010, p. 4) and the fourth extension on 16 December 2010 (OJ C 20, 21.1.2011, p. 3).

[3] See point 13 and the Annex to the Commission Communication on the recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition, OJ C 10, 15.1.2009, p. 2.

[4] Already down from EUR 78.6 billion total assets as per end 2007. Source: ÖVAG's annual report 2009.

[5] Fitch takes into account the fact that ÖVAG is a member of the protection scheme of the *Volksbanken Verbund*. That is why ÖVAG has the same Long- and Short-term IDR as the whole group ('A' and 'F1' respectively).

Corporate banking

(7) The corporate banking business segment of ÖVAG is served mainly by its subsidiary Investkredit Bank AG[6] ("IK"), which provides corporate lending, factoring, project financing, trade and export financing services to the bank's traditional clients consisting mainly of medium-size companies. IK also took over part of the role of ÖVAG as central institute of the Volksbanks and supports the regional institutes in providing financing to their clients by participating in syndicated loans. ÖVAG's product portfolio is complemented by risk hedging instruments and advisory services in mergers and acquisitions and private equity projects. In mid-2010 ÖVAG's corporate banking segment amounted to EUR 8.7 billion of total assets and EUR [7-9][*] billion of risk weighted assets ("RWA").

Retail banking

(8) ÖVAG offers its retail banking services mainly in CEE countries, where it is represented by VB International AG ("VBI") and VB-Leasing ("VBLI"). The market share of VBI in most cases does not exceed [2-5%]. VBLI in most CEE countries holds around [5-10%] market share. The exceptions with higher market shares are Romania (in terms of credit provided to private clients by VBI: [10-15%]), Bosnia-Herzegovina (VBI: [5-10%], VBLI: [20-30%]) and Croatia (VBLI: [10-15%]). In Austria ÖVAG's subsidiary VB-Leasing Finanzierungs-Gruppe offers retail clients movable property leasing services. In mid-2010 the retail banking segment in CEE countries amounted to EUR 13.9 billion of total assets and EUR [6-8] billion of RWA. At the same time, the leasing operations accounted for EUR [1-4] billion total assets and EUR [1-4] billion RWA.

(9) In Austria retail clients are served only by the regional Volksbanks associated with ÖVAG. However, until the sale of its four retail subsidiaries: Volksbank Wien AG, IMMO-Bank AG and Bank für Ärzte und Freie Berufe AG (in 2009) and Volksbank Linz-Mühlviertel rGmbH (in 2010) ÖVAG was also active in this segment in Austria.

Real estate

(10) ÖVAG's real estate business segment consists of the following business units: Investkredit Bank AG for real estate financing (Austria and CEE), Immoconsult Leasinggesellschaft m.b.H. for real estate leasing (Austria and CEE) and Premiumred Real Estate Development GmbH for commercial real estate project developments (in CEE and South Eastern Europe (SEE)). That segment also used to include Europolis AG, which is a real estate investor and asset manager in Central, Southern and Eastern Europe. However Europolis AG was divested in 2010. Private mortgage financing is not included here as in CEE it is offered by the retail banks of the VBI network. In mid-2010 the segment real estate accounted for EUR 7.6 billion total assets and EUR [3-5] billion RWA.

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6 In the course of the optimisation of its structure after the takeover of IK in 2005, ÖVAG transferred its corporate and real estate activities to IK, while concentrating the back-office functions, treasury and capital market activities in ÖVAG.

* Contains business secrets, where possible, ranges were provided in [brackets]

Financial Markets

(11) The Financial Markets business segment is responsible for treasury services, securities and foreign exchange trading and for the management of interest rate and currency risk within ÖVAG. It acts as a product supplier primarily to the Volksbanks, but also to ÖVAG subsidiaries, corporate and institutional customers, including non-associated banks, in Austria and abroad. Its product range includes traditional funds, certificates, funds and asset management. As per 30 June 2010 the segment accounted for EUR 4.1 billion of total assets and EUR [1-3] billion RWA.

Investment book/other operations

(12) As of the beginning of 2010 all the activities relating to ÖVAG's investment book were centralised in one business segment together with the bank's Asset Liability Management and Liquidity Management divisions, which are responsible for the managing of ÖVAG's long-term interest rate risk and foreign exchange risk, and the subsidiary Back Office Service für Banken GmbH, to which back-office operations of the ÖVAG have been outsourced. As of 30 June 2010 that segment recorded EUR 13.7 billion of total assets and EUR [2-4] billion of RWA.

2.2. DEVELOPMENT SINCE THE BEGINNING OF THE FINANCIAL CRISIS

(13) The sources of ÖVAG's difficulties were manifold. One of the weaknesses of the bank's business model, which was revealed by the crisis, was its reliance on wholesale funding. That dependence is on the one hand the result of the bank's role as central institution of the regional Volksbanks, which provide ÖVAG with their excess liquidity, allowing it to refrain from competing for retail deposits with its owners. On the other hand, access to cheap wholesale financing based on a good rating and offering favourable financing to its clients was the foundation of the business model of KA. That model, however, became untenable once the financial markets became illiquid following the Lehman Brothers' collapse. As a result ÖVAG was forced to sell KA to Austria (see paragraph (6)).

(14) Further, the volatility of the real estate valuations in Europolis' portfolio[7] led to the full impairment of that subsidiary's goodwill, reducing the operating result by EUR 176 million[8].

(15) Finally, the impairments for Lehman Brothers and Icelandic banks reduced the income from financial investments by EUR 141 million. Impairments on the structured credit portfolio amounting to EUR 61 million were also recognised, though they were to some extent covered by risk provisions built up in 2007 for the risks stemming from the sub-prime crisis.

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[7] Europolis is a former real estate subsidiary of ÖVAG. Its area of expertise comprises real estate investments and assets management in Central and South Eastern Europe.

[8] See ÖVAG's annual report 2008, p. 22.

(16) As a result, there was a consolidated loss for the financial year 2008 of EUR 402 million before tax.

(17) The economic down-turn in 2009 confronted ÖVAG with a significant increase of non-performing loans. As a result the bank recognised record risk provisions for credit risks of EUR 863 million (thereof corporate segment EUR 383 million, CEE banks EUR 175 million and real estate segment EUR 169 million)[9].

(18) Further, due to the negative developments on the real estate markets ÖVAG recognised write-downs on its participations and structured credit portfolio amounting to EUR 224 million and EUR 103 million respectively[10].

(19) As a result, ÖVAG recorded a consolidated loss for the financial year 2009 of EUR 944 million before tax.

(20) In July 2009, Moody's downgraded the rating of ÖVAG to Baa1 with a negative outlook.

(21) In 2010 ÖVAG sold its real estate subsidiary Europolis (EUR 1.7 billion of assets). Further divestments implemented were the sale in 2009 and 2010 of its four retail banking subsidiaries in Austria with a balance sheet of EUR 5 billion.

3. THE AID MEASURES

(22) In light of the economic decline and uncertainty leading to unprecedented losses and liquidity shortage, it was decided to strengthen the liquidity and capital position of ÖVAG by means of support measures offered under the Austrian bank support scheme. The following measures were granted to ÖVAG: (i) a EUR 1 billion recapitalisation as well as (ii) State guarantees covering EUR 3 billion of ÖVAG debt instruments. Thanks to the implementation of the recapitalisation the tier-1 ratio of ÖVAG was increased to 9.2% and the equity ratio to 12.5% as per end of 2009.

3.1. RECAPITALISATION OF EUR 1 BILLION

(23) In April 2009, the Republic of Austria signed an agreement with ÖVAG to subscribe participation certificates (*Partizipationsscheine*, "PS") amounting to a total of EUR 1 billion. The issuance took place on 7 April 2009. By means of that instrument the State does not obtain voting rights but a preferential dividend and a conversion option. The instrument is perpetual and is treated as tier-1 core-capital.

(24) The participation certificates carry a preferential dividend of 9.3% p.a., subject to profits. In the sixth and seventh full financial year after the subscription of the instruments the dividend increases yearly by 50 basis points, in the eighth year by 75 and from the ninth financial year onwards by 100 basis points, but only to the maximum of 12-month

9 See ÖVAG's annual report 2009, p. 23.
10 See ÖVAG's annual report 2009, p. 23.

EURIBOR plus 1000 basis points p.a. The payment of dividend is subject to the bank showing a profit and ÖVAG's decision to distribute it. Dividends not paid in one year are not deferred to a later year. The participation certificates absorb losses in proportion to the total loss-absorbing capital.

(25) The bank has the right to redeem all or tranches of the participation certificates at any time. The redemption value in the first ten financial years from the subscription amounts to 100% of the nominal value of the participation certificates, and thereafter 150%.[11]

(26) The State has the right to convert the participation certificates into ordinary shares of ÖVAG. Although until […] such a conversion is subject to agreement by the bank, the bank's consent to the conversion is not necessary in the following cases:

a) The dividend for the financial year 2011 is not paid out fully or partially; or
b) For two consecutive years after 31 December 2011 the dividend is not paid out fully or partially; or
c) On […] the State still holds participation certificates with a nominal value of at least EUR 700 million; or
d) On […] the State still holds participation certificates with a nominal value of at least EUR 400 million.

(27) The impact of the State's recapitalisation on ÖVAG's capital ratios is shown in Table 1 below.

<u>Table 1:</u> The impact of the State's recapitalisation on ÖVAG's capital ratios.

Ratio	March 2009		December 2009		June 2010	
	Factual	Factual + recap	Factual	Theoretical without recap	Factual	Theoretical without recap
Tier-1 ratio	6.86%	9.84%	9.20%	5.64%	8.64%	5.10%
Capital ratio	9.19%	12.17%	12.48%	8.75%	11.36%	<8%

Source: Umstrukturierungsbericht, p. 51.

3.2. GUARANTEES OF EUR 3 BILLION

(28) ÖVAG benefited from government guarantees under the Austrian bank support scheme and issued EUR 3 billion of State-guaranteed bonds in 2009. The details of the issues are presented in Table 2 below.

[11] That redemption value is increased by the percentage points by which the dividend on the PS fell short of the contractual value when distributable yearly profits would have sufficed for the payment, but instead were retained although the bank was not obliged to do so by regulatory or supervisory requirements.

Table 2: ÖVAG's State-guaranteed debt issues in 2009.

Tranche	Nominal value	Date of issue	Maturity	Coupon	Total cost
1.	EUR 1 billion	9.2.2009	9.2.2012	3.000%	[100-200] bp over 6M Euribor
2.	EUR 1 billion	18.3.2009	19.3.2013	3.375%	[100-200] bp over 6M Euribor
3.	EUR 1 billion	14.9.2009	14.9.2012	2.250%	[100-200] bp over 6M Euribor

Source: Umstrukturierungsbericht, p. 37.

4. THE RESTRUCTURING PLAN

(29) In November 2010, Austria submitted ÖVAG's restructuring plan to the Commission. The restructuring plan aimed at a more focused bank and therefore involved a significant reduction of the bank's size through abandonment or downsizing of many non-core activities. More specifically, within the new strategy the bank would focus on its role as central institute for the Volksbanks, cut back its corporate and real estate activities, divest its retail banking activities in CEE and reduce its leasing operations.

(30) In the corporate business segment ÖVAG intended to focus on corporate lending, project financing, mergers and acquisitions, factoring and run down such activities as […]. The bank also intended to review the profitability of its clients in that segment. The resulting volume of RWA in that segment was to amount EUR [4-7] billion.

(31) ÖVAG planned to divest its entire VBI and VBLI business active in CEE. The Austrian leasing business segment was to remain within the bank with projected RWA amounting to EUR [350-450] million.

(32) The restructured real estate business segment was to comprise the following areas: (i) real estate financing, (ii) real estate development and (iii) real estate asset management. […]. ÖVAG also envisaged the review of unprofitable clients in that segment. The targeted volume of RWA in real estate was approximately EUR [1-4] billion.

(33) The financial markets and banking book/other operations business segments were to remain to a large extent unchanged as regards their functions and volumes.

(34) Further, ÖVAG intended to divest its stake in Raiffeisen Zentralbank Österreich AG.

(35) The integration of ÖVAG with its main subsidiary IK was planned as an important measure to achieve synergies and cost savings and was scheduled to be completed by mid-2011. According to the plan, all those measures should have allowed ÖVAG to repay the State capital in an amount of EUR [300-600] million in 2011.

(36) ÖVAG intended to reduce its reliance on unsecured wholesale funding. For that purpose it aimed to increase the […] and to acquire a small online bank from one of the local

Volksbanks[12]. Those two measures were expected to cover approximately EUR [1-3] billion of funding needs in 2011. The intended significant reduction in size should have contributed to lowering financing needs. Those reduced financing needs would in turn lead to a reduction of the funding gap to EUR [1-3] billion in 2011 and 2012 and EUR [1-3] billion in 2014. Finally, the sale of VBI and VBLI was expected to ease funding needs by EUR [2-4] billion in 2012.

(37) The plan envisaged a reduction of the balance sheet total from EUR 91.1 billion (with EUR [35-45] billion RWA) in the third quarter 2008 to EUR [20-30] billion (with EUR [10-18] billion of RWA) in 2016. It would have amounted to a roughly [65-75] % balance sheet reduction and a [65-75] % RWA reduction.

(38) The tables below show the projected profits and capital ratios over the restructuring period in base and pessimistic case scenarios.

<u>Table 3:</u> ÖVAG's main financial performance indicators for 2008-2014 – base case.

		2011	2012	2013	2014	2015	2016
Indicators	**After-tax profit (EUR million)**	[200-250][1]	[80-100]	[100-120]	[120-140	[140-160]	[160-180]
	RWA (EUR billion)	[15-17]	[14-16]	[14-16]	[14-16]	[14-16]	[14-15]
	Core tier-1 ratio (%)[2]	n.a.	[5-6]%	[5-6]%	[5-6]%	[5.5-6.5]%	[6-7]%

Source: Bank's financial planning as of 16 December 2010.
1: including one time-off items such as expected capital gain achieved from the divestment of subsidiaries.
2: according to Basel III.

<u>Table 4:</u> ÖVAG's main financial performance indicators for 2008-2014 – pessimistic case.

		2011	2012	2013	2014	2015	2016
Indicators	**After-tax profit (EUR million)**	[20-40]	[40-60]	[60-80]	[80-100]	[100-120]	[100-120]
	RWA (EUR billion)	[17-19]	[16-19]	[16-19]	[16-19]	[15-18]	[15-18]
	Core tier-1 ratio (%)[2]	n.a.	[4-6] %	[4-6] %	[4-6] %[3]	[4-6] %[3]	[4-6] %[3]

Source: Bank's financial planning as of 16 December 2010.
1: including one time-off items such as expected capital gain achieved from the divestment of subsidiaries.
2: according to Basel III.
3: below the minimum core tier-1 requirement according to Basel III (including capital conservation buffer).

5. THE EVENTS SINCE THE PRESENTATION OF THE RESTRUCTURING PLAN

(39) While ÖVAG was able to record a small profit in 2010, the bank faced more problems in 2011. Moody's downgraded ÖVAG to Baa2 on 6 April 2011.

12 The deposits of that online bank amount currently to about EUR [300-500] million, representing a [3-6] % market share in online banking in Austria. ÖVAG planned to double that volume during the next years.

(40) Although ÖVAG managed to sell VBI, […]. Furthermore, its relatively large Romanian VBI subsidiary, which continues to be heavily affected by […], was excluded from the scope of the transaction. VBLI, ÖVAG's CEE leasing activities, could not be sold at all. ÖVAG did not succeed in selling its stake in RZB.

(41) ÖVAG did not pass the European Banking Authority (EBA) stress test in July 2011. In the simulated worst case scenario its core tier-1 ratio would fall to 4.5% as of 31 December 2012, 0.5% below EBA's defined minimum requirement. On 27 October 2011 ÖVAG publicly announced that EBA had calculated a capital gap of EUR 972 million necessary to reach the minimum required core tier-1 ratio under its worst case scenario.

(42) In August and in September 2011, ÖVAG issued profit warnings and indicated that the bank expects a consolidated loss amounting to approximately EUR 500 to 750 million for the year 2011. As a result no dividend will be paid on any profit-related capital instrument, including State capital.

(43) On 13 October 2011 ÖVAG publicly announced that it would not proceed with the integration of ÖVAG with IK nor with the repayment of the State capital in 2011 as originally planned.

(44) ÖVAG is currently working on a revised restructuring plan. According to a press release of the bank of 13 October 2011 the revised plan tentatively envisages that ÖVAG will consolidate with the local Volksbanks. The aim would be to make all members liable for each others' obligations. The Commission has not been provided with any further information yet.

6. THE POSITION OF AUSTRIA

(45) Austria underlines that ÖVAG is a bank of systemic relevance whose insolvency would have had massive negative implications for the Austrian banking system and the Austrian real economy. That assessment has been confirmed with a letter by the Austrian Central Bank Österreichische Nationalbank.

(46) Austria does not deny the aid character of each of the measures described in the section 3 above. It points out that all measures were granted in compliance with the approved Austrian bank support scheme. Austria maintains that ÖVAG was at the moment of the recapitalisation not a distressed bank in the meaning of the Recapitalisation Communication. Nevertheless, Austria accepted that a restructuring plan for the bank needs to be submitted.

7. ASSESSMENT OF THE AID

7.1. EXISTENCE OF AID

(47) As stated in Article 107(3)(b) TFEU 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 or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.

(48) The Commission recalls that it has already established in the decisions on the Austrian bank support scheme that liquidity guarantees and capital injections given under the scheme constitute aid. That evaluation is not disputed by Austria.

7.2. COMPATIBILITY OF THE AID

7.2.1. APPLICATION OF ARTICLE 107(3)(B) TFEU

(49) Article 107(3)(b) TFEU provides for the possibility that State aid can be regarded as compatible with the internal market where it is granted "*to remedy a serious disturbance in the economy of a Member State*".

(50) 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 that disturbance. The Commission explained its approach in the Banking Communication[13], the Recapitalisation Communication and the Restructuring Communication[14]. The Commission still considers that requirements for State aid to be approved pursuant to Article 107(3)(b) TFEU are fulfilled in view of the reappearance of stress in financial markets. The Commission confirmed that view by adopting the Prolongation Communication in December 2010[15].

(51) In respect to the Austrian economy, the Commission has acknowledged in its approval of the Austrian scheme[16] and in the approval of State aid measures granted by Austria to individual banks[17] that there is a threat of serious disturbance in the Austrian economy and

[13] 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.

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

[15] Communication from the Commission from 1 January 2011, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 329, 7.12.2010, p. 7.

[16] Commission Decision of 9.12.2008 in State aid case N 557/2008 – Maßnahmen nach dem Finanzmarktstabilitäts- und dem Interbankmarktstärkungsgesetz für Kreditinstitute und Versicherungsunternehmen in Österreich, OJ C 3 of 8.1.2009, p. 2; extended by Commission decision N 352/2009 of 30 June 2009 (OJ C 172, 24.7.2009, p. 4.), further extended by Commission decision N 663/2009 of 17 December 2009 (OJ C 28, 04.02.2010, p. 6), further extended by Commission decision N 241/2010 of 25 June 2010 (OJ C 250, 17.09.2010, p. 4) and further extended by Commission decision SA.32018 of 16 December 2010 (OJ C 20, 21.01.2011, p. 3.).

[17] See apart from the decisions on the Austrian bank support scheme Commission Decision in case N698/2009, *Hypo Group Alpe Adria*, OJ C 85, 31.3.2010, p. 21; Commission Decision in case N261/2010, *Second restructuring aid for BAWAG*, OJ C 250, 17.9.2010, p. 5; and Commission Decision in case SA.32745/2011, *Restructuring of Kommunalkredit Austria AG*, OJ C 239, 17.8.2011, p. 2.

that State support of banks is suitable to remedy that disturbance. Therefore, the legal basis for the assessment of the aid measures should be Article 107(3)(b) TFEU.[18]

7.2.2. COMPATIBILITY OF THE AID MEASURES WITH ARTICLE 107(3)(B) TFEU

(52) 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.

(53) The Commission notes that ÖVAG has received capital in excess of 2% of the bank's total RWA, that its recapitalisation was apparently needed to allow the bank to continue operating on a sufficiently sound basis and that the bank did not manage to get the necessary funds on the markets.[19] The bank therefore needs, in line with point 4 of the Restructuring Communication, to undergo in-depth restructuring. Austria is not disputing the need to submit a restructuring plan or for the bank to undergo such in-depth restructuring.

7.2.3. VIABILITY

(54) 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.

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

(56) The Commission notes positively that the restructuring plan identifies and aims at addressing many of the sources of the bank's difficulties, such as losses stemming from KA, VBI or the real estate and corporate business segments. However, in light of ÖVAG's difficulties in implementing the intended divestments and significant further losses expected for the financial year 2011 due mainly to VBI Romania and IK, the Commission has serious doubts that the restructuring plan in its current form allows the bank to solve its problems and establish a viable business model.

[18] It can also be noted that Austria granted the aid to ÖVAG under the Austrian bank rescue scheme which has been authorised by the Commission on the basis of Article 107(3)(b) TFEU.

[19] While later developments can not be considered for the assessment of the soundness of a bank at the time the capital is granted by the State, it nevertheless can be noted that the later developments confirmed the Commission's position in that respect.

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

(58) ÖVAG has provided financial projections for the period 2011-2016, giving information on revenues, costs, profits and capital position for each business unit. In the restructuring plan, ÖVAG assumed that in the base case the projected net profit (loss) will amount to approximately EUR [200-250] million in 2011, EUR [80-100] million in 2012 and will increase to EUR [160-180] million in 2016. ÖVAG's core tier-1 ratio would increase from [5-7%] in 2011 to [6-7%] in 2016. In the light of high loss expected for the year 2011 and ÖVAG's inability to divest VBI Romania and VBLI, which were not included in the financial projections as of 2012 onwards, the Commission considers that it cannot conclude either on the sufficiency of the projected profitability and capital adequacy provided in the restructuring plan or on their feasibility.

(59) Further, the Commission notes that the plan to start repaying State's capital in 2011 and remunerate the remaining PS according to the terms of the recapitalisation has been cancelled. Therefore, the Commission considers that the restructuring plan in its current form does not demonstrate how the bank will restore its long-term viability as soon as possible without continuous reliance on State aid.

(60) As regards ÖVAG's ability to withstand a stress scenario, the financial result and position projected by ÖVAG are presented in Table 4 above. As those projections demonstrate that ÖVAG will meet the minimum regulatory capital requirements only […], ÖVAG cannot be regarded as meeting the requirements of paragraph 13 of the Restructuring Communication. That assessment seems to be confirmed by the fact that ÖVAG failed the EBA stress test in July 2011.

(61) The Commission notes positively that ÖVAG aims at reducing its reliance on unsecured wholesale funding. To that end, it planned to increase the issuance of covered bonds and to acquire an online bank from one of the local Volksbanks. The planned significant reduction in size was also to result in reduced financing needs. However, so far the Commission has not received sufficient information allowing it to verify the appropriateness of the envisaged measures.

(62) Consequently, the Commission considers that the information provided by Austria so far does not allow it to conclude that the restructuring plan submitted by ÖVAG fulfils the requirements of the Restructuring Communication with regard to the restoration of the long-term viability. On the contrary, the developments in 2011 show that a further reaching restructuring than envisaged in the November 2010 plan is required.

7.2.4. BURDEN-SHARING

(63) As stated in points 22 to 24 of the Restructuring Communication, banks and their stakeholders need to contribute to the restructuring as much as possible in order to ensure that aid is limited to the minimum necessary and moral hazard is addressed. It implies that banks use their own resources to finance the restructuring, for instance by selling assets and by paying an adequate remuneration for State interventions, while the stakeholders should absorb the losses of the bank where possible.

(64) The Commission welcomes ÖVAG's efforts to cover its restructuring costs to the maximum extent possible using its own resources, e.g. by the sale of the four Austrian retail subsidiaries and the intention to sell VBI, VBLI and its stake in RZB.

(65) However, in the light of the unsuccessful attempts to divest those stakes, the Commission has doubts whether the own contribution to the restructuring costs by the bank is sufficient.

(66) Furthermore, ÖVAG has so far not remunerated the capital injected by the Austrian State and will not do so for the year 2011 either. Since the financial projections submitted within the restructuring plan do not provide a reliable basis to conclude on the future profitability of the bank, the Commission currently can not conclude that ÖVAG will pay an adequate remuneration to the State in the future.

(67) However, the Commission notes that ÖVAG is paying for its liquidity guarantees a remuneration in line with the Austrian banking scheme, which was designed in line with the Banking Communication.

(68) As regards limitation of the aid to the minimum necessary, the Restructuring Communication in point 23 stipulates that public resources shall not be used to finance market-distorting activities not related to the restructuring process. In that context, ÖVAG’s plan to buy an online bank to secure access to retail deposits should be carefully analysed. While that measure might be acceptable in the context of decreasing ÖVAG’s reliance on wholesale funding, it has to be ring-fenced by behavioural commitments, ensuring that public resources are not misused to distort the market.

(69) Consequently, the Commission considers that the information provided by Austria so far does not allow concluding that the restructuring plan would include sufficient burden-sharing.

7.2.5. LIMITATION OF COMPETITION DISTORTIONS

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

(71) Point 31 of the Restructuring Communication stipulates that when assessing the amount of aid and the resulting competition distortions, the Commission has to take into account both

the absolute and relative amount of the State aid received. In that respect ÖVAG has received State capital equivalent to 3% of RWA. In addition, ÖVAG has obtained liquidity guarantees amounting to 5.3% of the bank's balance sheet.

(72) Pursuant to point 31 of the Restructuring Communication, the Commission has to take into account in its assessment the amount of aid the degree of burden-sharing and the position of the financial institution on the market after the restructuring. On the basis of that analysis, suitable measures to limit distortions of competition need to be put into place.

(73) The Commission welcomes the significant reduction in size pursued by ÖVAG (see recital (37) above), which amounts to [60-75%] in terms of balance sheet and to [60-75%] in terms of RWA, if implemented as laid down in the restructuring plan. However, the Commission notes that it includes the reduction attributable to the sale of KA to Austria. Given the difficulties of KA and the measures Austria needed to grant in order to keep that bank operating, it seems that that divestment might rather have been a measure to support ÖVAG's viability. The Commission will further investigate to what extent ÖVAG's reduction in size can be recognised as a measure for addressing competition distortions.

(74) Consequently, the Commission considers that the information provided by Austria so far does not allow concluding that the restructuring plan provides for sufficient and adequate measures to address the distortions of competition.

7.3. CONCLUSION

(75) It is therefore concluded that, on the basis of the restructuring plan submitted in November 2010 and the further information provided since then, serious doubts remain whether ÖVAG will be able to restore its long-term viability, whether sufficient burden-sharing is achieved and whether adequate measures are taken to limit distortions of competition. On that basis, the Commission has doubts whether the restructuring aid can be considered compatible with the internal market pursuant to Article 107(3)(b) TFEU.

8. DECISION

In the light of the foregoing considerations, the Commission has decided to initiate the procedure laid down in Article 108(2) TFEU with respect to the recapitalisation of EUR 1 billion and the guarantee of EUR 3 billion granted by Austria in favour of Österreichische Volksbanken-AG and requests Austria to submit an amended restructuring plan.

Austria is requested to forward a copy of this letter to Österreichische Volksbanken-AG immediately.

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

If this letter contains confidential information which should not be published, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to publication of the full text of this letter. Your request specifying the relevant information should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State Aid Greffe
B-1049 Brussels
Fax No: +32-2-296 12 42

Yours faithfully,

For the Commission

Joaquín ALMUNIA

Vice-President