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<p>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 [...].</p>	<p style="text-align: center;">PUBLIC VERSION WORKING LANGUAGE This document is made available for information purposes only.</p>
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Subject: C 10/2008 (ex CP 233/07 and ex NN 7/08) IKB, Germany

Sir,

The Commission wishes to inform Germany that, having examined the information supplied by your authorities on the measure referred to above, it has decided to initiate the procedure laid down in Article 88(2) of the EC Treaty.

1. PROCEDURE

- (1) On 3 August 2007, the German authorities provided the Commission with background information on the case. On 6 August 2007, a meeting was held between the German authorities and the Commission. By letter of 8 August 2007 a request for information was sent to Germany to which Germany replied on 11 September 2007. On 17 December 2007 and 11 January 2008 meetings between the German authorities and the Commission services took place. On 15 January 2008 Germany submitted a notification of the measures including a restructuring plan. On 15 February 2008, Germany submitted additional information.

2. DESCRIPTION OF THE MEASURE

2.1. The beneficiary

- (2) The beneficiary is IKB Deutsche Industriebank AG (hereinafter "IKB"). It is a medium-sized private German MDAX-listed bank and has a balance-sheet total of € 52 billion (as per 31.12.2006). Its headquarters are located in Düsseldorf. The main shareholders are state-owned bank Kreditanstalt für Wiederaufbau (hereinafter "KfW") (38 %) and Stiftung Industrieforschung (12 %). The remaining 50 % are free float.
- (3) IKB's core business is to provide long-term financing to companies with annual sales of € 10 million or more. As a significant player in this segment in Germany, the bank finances thousands of medium-sized companies, the so-called "Mittelstand".

- (4) IKB's main shareholder, KfW, is a more than 50 years old German development bank, owned by the federal government (80 %) and the German regional states (20 %). It is one of the ten biggest banks in Germany with a balance-sheet total of € 360 billion (as per 31.12.2006). KfW, as a public-law institution based in Germany, is a promotional bank that supports the economy, society and ecology in Germany, Europe and worldwide. KfW's tasks are the promotion of small and medium-sized enterprises, of housing finance and modernisation, and of education and advanced training, the financing of municipal infrastructure projects, the promotion of export and project finance and of the developing and transition countries and the protection of the environment and the climate. KfW raises the majority of the promotional funds on the capital market. The promotional public mission of the bank is anchored in the KfW law.¹ KfW's public mission activities are covered by the public guarantee mechanisms "Anstaltslast".

2.2. The events triggering the measure

- (5) IKB provided, along with other banks, several liquidity facilities to Rhineland Funding Capital Corporation (hereinafter "Rhineland"), a corporation that invests in structured credit portfolios which include exposures to U.S. subprime real estate loans, and refinances its investments by issuing asset-backed commercial papers. The structured portfolios of Rhineland consisted mainly not super senior tranches. In addition to the engagement in Rhineland, IKB also held investments in the subprime segment via subordinated debt instruments in the structured investment vehicle Rhinebridge and direct investment in Collateralised Debt Obligations (hereinafter "CDOs").
- (6) The total subprime exposure is estimated by IKB to be € 7.7 billion. In the course of the ongoing crisis in the U.S. subprime mortgage market and as a direct consequence of the downgrading of subprime backed assets by the rating agencies, valuations of certain assets traded in this market segment have suffered. This was also the case for Rhineland whose ability to refinance its investment portfolio in the commercial paper market was therefore threatened. Given that the commercial paper market had dried up, it was likely that Rhineland would draw upon the liquidity facilities provided by IKB, not reflected in the latter's balance sheet. Furthermore, the other direct portfolio investments, such as, inter alia, Rhinebridge, were subject to considerable fair-value-fluctuations which had to be accounted according to the International Financial Reporting Standards.

2.3. The first measure

- (7) On 27 July 2007, the German banking supervisory authority "BaFin" was informed by a German bank providing liquidity to IKB that it would withdraw the credit line. BaFin subsequently called KfW, the Ministry of Finance and other concerned parties and announced that it would open the moratorium² on IKB because of a liquidity squeeze on Monday 30 July if those parties did not take over the risks for IKB's Rhineland engagement. In addition it emerged that IKB's subprime exposure was not limited to the

¹ The "KfW Law" was passed in October 1948 by the German Economic Council and went into effect on 18 November 1948. On 16 August 1961 the KfW Law was amended to add a new task in addition to investment and export financing: financing projects in foreign countries, development aid projects in particular.

² Cf. § 47 of the German Banking Act (Gesetz über das Kreditwesen, of 9 September 1998 (BGBl. I page 2776), last amended by Art. 3 of law of 16 July 2007 (BGBl. I page 1330)).

Rhineland engagement but also included the Rhinebridge and other direct subprime portfolio investments.

- (8) On 29 July 2007 BaFin, the Ministry of Finance, KfW and the three major German banking associations³ agreed that KfW would, in coordination with BaFin, intervene by providing a risk shield for IKB. The banking associations orally agreed to take over 30 % of the risks involved in the risk shield, which was formalised in an agreement between KfW and the three banking associations on 16 August 2007.
- (9) In particular, KfW announced that, in order to ensure IKB's liquidity position it would:
 - provide a risk shield as from Monday 30 July 2007 as regards all of IKB's rights (fees) and obligations under the liquidity facilities provided to the Rhineland conduit in the amount of € 8.1 billion (this has in the meantime been reduced to € 6.7 billion, i.a. because of exchange rate developments). The formal assumption of the obligations under the liquidity facilities provided to Rhineland on 29 July 2007 will remain until the maturity or sale⁴ of the structured credit portfolios. The maturity of such portfolios is generally more than 5 years. The parties originally estimated that the facility would be covering losses of about € 2.5 billion;
 - protect IKB against losses in the amount of € 1 billion resulting from Rhinebridge and other direct subprime portfolio investments.
- (10) Altogether Germany originally estimated that the total risks comprised in the risk shield to IKB by KfW and the banking associations amount to € 3.5 billion (€ 2.5 billion Rhineland, € 1 billion from Rhinebridge and other direct subprime portfolio investments⁵), which was later rectified to € 6.15 billion.
- (11) In the original agreement of 29 July 2007 KfW and the banking associations divided the risks resulting from the risk shield as follows:
 - KfW takes over 70 %, without upper limitation concerning Rhineland;
 - the banking associations take over 30 %, limited to € 1 billion.
- (12) The risk distribution between KfW and the banking associations is, within the € 1 billion limit of the banking associations (see the above point), *pari passu* independently of the distribution of the risks between the different risk classes (Rhineland, Rhinebridge or direct investments).
- (13) In addition to their participation in the risk shield, the three banking associations agreed to reopen the closed credit lines towards IKB, which they had closed when the crisis emerged.
- (14) Furthermore, the agreement of 16 August 2007 indicates that KfW will in its role as pool leader negotiate an appropriate fee for the risk shield or reimbursement facilities of the risks covered by the risk shield. The amount of the potential fee or reimbursements will depend on [...]*
- (15) The 30 % part of the banking associations is distributed as follows between the associations:

³ "BdB" – association of German private banks, "BVR" – Association of German cooperative banks, "DSGV" – association of German Saving banks and Landesbanken

⁴ The demand for such portfolios is currently weak and thus market value has considerably decreased. In the case of sale of the portfolio significant losses would be realised.

⁵ KfW intends in the still outstanding agreement to limit its total exposure concerning Rhinebridge and other direct subprime portfolio investments to € 1 billion.

* Parts of this text have been deleted so as not to divulge confidential information; they are indicated by a series of dots between square brackets.

- 50 % Association of German private banks ("BdB");
 - 16.7 % Association of German cooperative banks ("BVR");
 - 33.3 % Association of German Saving Banks and Landesbanken ("DSGV").
- (16) BdB took a share of 50 % because in the case of IKB's insolvency the depositor guarantee fund of the private banks would guarantee up to 30 % of the liable equity of IKB per individual account⁶ held by private and wholesale customers (about € 662 million per account on 26 September 2007).
- (17) The agreement includes [...].

2.4. The second measure

- (18) Due to a further deterioration of the financial markets the granted risk shield proved to be insufficient. On 30 November 2007 KfW and the banking associations covered additional risks estimated at € 350 million (USD 440 million) related to the credit lines. € 150 million were covered by KfW, out of which € 54.3 million in the form of convertible bonds, which KfW intends to convert into shareholder equity with the effect of increasing its share in IKB to 43 %. Further € 150 million were provided by the association of private banks (BdB) and € 50 million by the association of cooperative banks (BVR) and the association of savings banks (DSGV).
- (19) As a result of the provision of the risk shield and the market deterioration KfW had to change its risk assessment and increase its provision/reserve for the coverage of risks from € 2.5 billion to € 4.8 billion.

2.5. The third measure

- (20) As a result of the ongoing deterioration of the financial markets in January 2008 the first two measures again proved to be insufficient to avoid the insolvency of IKB. The German federal government instructed KfW in February 2008 to provide a third, € 2.3 billion support measure for IKB. The federal government therefore provides KfW a conditionally reimbursable loan having a nominal value of € 1.2 billion. Moreover, Germany expects that the banking associations would provide a significant part to the measure. The details of the support measure still need to be determined.

2.6. The restructuring plan

- (21) Germany submitted to the Commission various documents indicating several restructuring measures which have already been introduced to overcome the crisis of the bank and avoid future problems. It is clear that IKB has taken measures simultaneously with intervention by KfW and the banks, in order to analyse the situation, such as commissioning a study by PriceWaterhouseCoopers (PWC). Moreover, as early as 3 September 2007, IKB announced that it would withdraw from its involvement in international structural investments. The restructuring of IKB is based on the above mentioned report by PWC.
- (22) As a consequence of the findings of PWC the new board decided a series of immediate measures of which the main ones are:
- no new activity in structured investment portfolios;

⁶ The depositor guarantee fund of the private banks covers all "non-interbanking" accounts.

- implementation of a comprehensive evaluation of existing assets and implementation of a significantly improved asset management;
 - reintegration of IKB CAM⁷ into IKB AG;
 - reorganisation of risk controlling and new chief risk officer;
 - implementation of a credit risk committee.
- (23) In addition to the immediate measures the main objective of IKB is the refocusing on the core business of the bank. In this context Germany underlines that the crisis did not relate to the core business of IKB but to engagements in structured investment portfolios. The future business model is based on three pillars:
- systematic use of the brand name and the financing competences as a long-term partner for SMEs; enhancement of sales force and completion of the product portfolio;
 - use of sales competence in order to increase structured finance products sales; moderate expansion of international activities;
 - continuation of the real estate and project development finance activities.
- (24) The future business model of IKB will be based on the three core business activities wholesale, real estate and structured finance. The business plan is based on the following assumptions:
- the initial planning until 2010 has been revised significantly downwards in view of the current situation of the financial markets;
 - covering of losses of up to € [...] in the structured investment portfolios through the risk shield;
 - significant reduction of the interest management result;
 - implementation of the measures included in the restructuring plan.
- (25) Germany submitted a prudent base case scenario for the financial years 2008/09 until 2010/11:

In million €	2008/09	2009/10	2010/11
Operating result segments	[...]	[...]	[...]
Securitisation/headquarter	[...]	[...]	[...]
Group result	[...(<100)]	[...]	[...(>100)]

- (26) Germany did not propose any compensatory measures. Instead, it argues that IKB's market shares on the German banking market were insignificant as it states that IKB has only a market share of about [...] % in loans for SMEs, its main business, while its market share for loans to large companies is [...] %. Concerning real estate loans IKB has a market share of [...] %.

2.7. The sales process

- (27) The board of KfW has decided to sell KfW's shares in IKB with the aim of (a) finding a main shareholder who will guarantee the long-term loan receivables of KfW, (b) selling at the highest possible price and (c) [...].

⁷ IKB Credit Asset Management ("IKB CAM") is a 100 % subsidiary of IKB and is responsible for the management of Rhineland Funding.

- (28) KfW will initiate a tender procedure as soon as possible aiming to finalise the sale in the first half of 2008 and will in parallel assure the market conformity of the sales process with an independent evaluation.

3. COMMENTS BY GERMANY

- (29) The German authorities claim that the measures would not involve state aid because they were taken in conformity with the market economy investor principle. This would be evidenced by the considerable private participation in the risk shield.
- (30) Moreover, the German authorities claim that the intervention was based on market economy investor considerations because liquidation would have been more costly for KfW than its financial involvement. It is submitted that the direct cost of an insolvency of IKB would have been € [...(1-2 billion)]. The German authorities explain that the ownership of KfW had a book value of round about € 620 million (based on German accounting rules) which was below the stock market value of IKB, even (but only slightly) the stock market value on 27 July 2007. Moreover, according to the German authorities, KfW would need to write off about € [...] in credits which IKB had passed on to third parties in the context of KfW's development business. This corresponds to [...] % default of the overall amount of credits distributed by IKB on behalf of KfW, assuming that these credits would partially default in the case of insolvency of IKB, which would be directly to the detriment of KfW. In addition, the insolvency of IKB would have triggered a financial crisis which would have resulted in the writing-off of addition credits from the development activities of at least € [...(1-2 billion)].
- (31) In addition, the German authorities recall that the abrupt insolvency of a bank on a Monday morning, which enjoyed one of the best German banking ratings until Friday evening, could have triggered a crisis of confidence towards the whole German financial system. National and international investors could have concluded that the assessment of the risks of German banks is impossible and would probably have withdrawn their investments in the sector.
- (32) Furthermore, Germany argues that, if the Commission were to consider the measures as involving State aid elements, they would in any event qualify as compatible rescue and restructuring aid. Germany argues that a reorganisation of the part of the bank which had given rise to the difficulties would be sufficient as the bank was otherwise healthy.

4. ASSESSMENT OF THE AID

4.1. Existence of aid

- (33) The Commission must first assess whether the measures constitute state aid within the meaning of Article 87 (1) EC. According to this provision state aid is any aid granted by a Member State or through state resources in any form whatsoever which distorts, or threatens to distort, competition by favouring certain undertakings, in so far as it affects trade between Member States.
- (34) The Commission recalls that KfW is publicly owned and has a public mission and considers that the risk shield was granted by KfW “in the interest” of Germany.⁸ Also

⁸ This is in line with constant practice of the Commission, see e.g. Commission Decision of 8 May 2001 in Case C1/2000 *Holzmann*, OJ 2001 L 248, page 46, point 20; Commission decision of 17.01.2003 in case NN 115/2002 *MobilCOM*, OJ 2003 C80, page 1.

the DSGV resources are, on the basis that the Landesbanken and savings banks belong to the public sector, attributable to the State. Measures granted by KfW and DSGV, which cover about 80 % of the risk shield, can thus be considered as “granted by a Member State or through State resources” in the meaning of Article 87 (1) EC.

- (35) The Commission considers further that the measures are imputable to the State. This follows, apart from the fact that KfW is publicly owned, from the strong involvement of BaFin and the Ministry of Finance. It appears that without the strong pressure imposed by the banking authority and the Ministry of Finance on the KfW management during the days preceding the granting of the risk shield KfW would not have taken engagements to such an extent. Also, the first two measures are assumed by KfW itself, i.e. an entity carrying out a public mission, and not by a subsidiary pursuing commercial interests.
- (36) Furthermore, the Commission notes IKB's cross border and international activities, so that any advantage from state resources would affect competition in the banking sector and have an impact on intra-community trade.⁹
- (37) Finally, the Commission has at this stage reasons to consider that the measures could confer a selective advantage upon IKB. The Commission recalls that under Article 87 (1) EC any public intervention that constitutes an advantage for the firm is normally State aid, unless the financial intervention would have also been provided by a market economy investor operating under normal market economy conditions.
- (38) The Commission notes the German position stated above and therefore wishes to investigate whether a market economy investor would have granted the risk shield to IKB under the same conditions as KfW, i.e. would have assumed losses at a total amount of € 2.65 billion¹⁰, and potentially going up to € 8.1 billion.
- (39) The Commission wishes to investigate whether for the first two measures KfW and for the third measure Germany can expect a reasonable return on its investment, which a market economy investor should be able to expect at least in the long term according to settled case law.¹¹ The Commission recalls first of all that in the present case in view of KfW's intention to sell IKB, KfW cannot expect any long term return from the bank itself.¹² In addition, the Commission notes that even though the agreement contains a paragraph concerning the possible negotiation of a fee for the risk shield or reimbursement facilities, no such fee has yet been agreed. This seems to underline that IKB is, on the basis of a realistic market forecast, at the moment not able [...].
- (40) Second, the Commission doubts at this stage the German submission that the intervention would be less costly for KfW and Germany than liquidation.¹³ The Commission notes that the 38 % participation of KfW in IKB must be evaluated ex ante at the time when the investment decision was made.¹⁴ In this respect the Commission

⁹ Commission Decision in Case C50/2006 of 27.06.2007 *BAWAG*, not yet published, point 127.

¹⁰ 70% of the total risk shield which was originally estimated at € 3.5 billion.

¹¹ Joined cases T-129/95, T-2/96 and T-97/96 *Neue Maxhütte Stahlwerke* [1999] ECR II-17, para.116 and Joined cases T-228/99 and T-233/99 *Westdeutsche Landesbank Girozentrale* [2003] ECR II-435, para. 314.

¹² Joined Cases C-278/92, C-279/92 and C-280/92 *Hytasa* [1994] ECR I-4103, paragraph 22.

¹³ Joined cases T-129/95, T-2/96 and T-97/96 *Neue Maxhütte Stahlwerke* [1999] ECR II-17, para.124. However, the winding up costs are normally difficult to calculate and estimates are faced with uncertainties, see for example Commission Decision in Case C28/2002 *Bankgesellschaft Berlin*, OJ 2005 L 116, page 1, points 163 *et seq.* Also Commission Decision in Case C50/2006 of 27.06.2007 *BAWAG*, not yet published, point 166.

¹⁴ Joined cases T-129/95, T-2/96 and T-97/96 *Neue Maxhütte Stahlwerke* [1999] ECR II-17, para.121.

recognises that the book value of IKB was indeed € 620 million. However given that the share price of IKB has dropped significantly before KfW's intervention the Commission will have to assess whether the real value of KfW's holding in IKB at the time of the intervention was still above or at least equal to this book value. Furthermore based on the submitted information the Commission can not assess the underlying default risk of around [...] % from the credits passed on in the development business. It notes that Germany has not provided evidence to underline the plausibility of KfW's estimation. The same applies to the claimed threat of indirect losses as a consequence of a general banking crises, which seem purely hypothetical. In any event, the Commission notes that structural development financing is part of KfW's public mission business and not part of the function of KfW as normal credit institute. It is therefore to investigate whether losses from this business can be considered as a cost which also a market economy investor would have considered.¹⁵ Finally, the Commission notes that the estimated losses under the risk shield were in fact not limited to € 2.5 billion, but unlimited. Although it might be argued that this was theoretical, it was nevertheless required by BaFin and was a *conditio sine qua non* for avoiding the moratorium. A market economy investor would also have considered this in the balancing.

- (41) Third, the Commission doubts that the measures do not involve state aid because of the private participation in the risk shield. The Commission recalls that where a public shareholder acts in parallel with other private investors, the provision of capital needs to be proportionate, and must be provided under the same conditions¹⁶ and industrial rationale.¹⁷ The Commission notes that KfW agreed to bail out IKB even before the private participation was confirmed (see above point (8)). Moreover, while the banking associations capped their share in the risk shield to € 1 billion (approximately 30 %), KfW did not do so and is thus by far more exposed than the banking associations. In any event, the participation of KfW in the risk shield, even after subtracting the potential direct losses resulting from its ownership, with a claimed value of € [...(1-2 billion)], was still [...] that of the banking pool altogether. Therefore, the Commission doubts that KfW did intervene in a way comparable with the banking pool. The same reasoning applies for the third measure where the federal state provided € 1.2 billion of the total amount of € 2.3 billion and is thus by far more exposed than the banking associations, even if the insolvency of IKB would trigger a guarantee mechanism which is designed to spread the burden across the banking sector. The federal state would thus only be indirectly be affected by a general banking crisis.
- (42) Finally, Germany claims that a general crisis of the German banking sector could be of impact for KfW. However, the Commission finds it difficult to accept that this was a measure in the general interest of the German financial market, as the capped share of the banking associations in the risk shield of € 1 billion (approximately 30 %) is in no relation to the >95 % market share of their member banks in Germany and therefore does not reflect their potential risk exposure in case of effects on the German financial market.¹⁸ Instead, it rather appears that the (limited) participation of the banking associations was the consequence of the high pressure of BaFin and the Ministry of Finance. In addition, if KfW intervened in the interest of the government to avoid a

¹⁵ See in this respect joined cases T-129/95, T-2/96 and T-97/96 *Neue Maxhütte Stahlwerke* [1999] ECR II-17, para. 119.

¹⁶ Communication on public undertakings in the manufacturing sector, OJ 1993 C 307, page 3.

¹⁷ Commission Decision in Case C25/2002 *Carsid*, OJ 2005 L 47, page 28, at points 67 to 70.

¹⁸ The Commission further notes that the other owners of IKB did not participate in the support measure.

general crisis, this would rather be an argument against the market conformity of its measures.

- (43) Therefore the Commission, at this stage, has serious doubts, that a market economy investor in the situation of KfW would have provided the measure, so that it seems to constitute state aid in the sense of Article 87 (1) EC.

4.2. Compatibility

- (44) In view of the above, the Commission must further assess the compatibility of the assumed aid. In view of the fact that IKB was a company in difficulty the aid can essentially be assessed under Article 87 (3) (c) EC, and in particular under the Community guidelines on State aid for rescuing and restructuring firms in difficulty¹⁹ (hereinafter “the Guidelines”), and in exceptional cases also under Article 87 (3) (b) EC.

4.2.1. Application of the Guidelines

- (45) The Guidelines state that a firm is in difficulty where it is unable, whether through its own resources or with the funds it is able to obtain from its owner/shareholders or creditors, to stem losses which, without outside intervention by the public authorities, will almost certainly condemn it to going out of business in the short or medium term.
- (46) The Commission is of the opinion that, without the risk shield, it is highly unlikely that IKB would have been able to cope with the liquidity squeeze for much longer. Furthermore, the risk shield was required by BaFin and was a *conditio sine qua non* for avoiding the moratorium.
- (47) Consequently, given its financial situation at the time the risk shield was granted, IKB was clearly a company in difficulty in the sense of the Guidelines.

4.2.2. Rescue aid

- (48) The Commission wishes to investigate whether the aid could be found compatible as rescue aid under the Guidelines.
- (49) The Commission notes that aid must comply with the conditions of point 25 (a) of the Guidelines, according to which rescue aid must be provided by way of a loan or guarantee for a loan and any loan must be reimbursed and any guarantee ended within a period of not more than six months after the disbursement of the first instalment to the firm. An exception may however be made from the restriction as to form of rescue aid in the banking sector²⁰, in order to enable the credit institution in question to continue temporarily carrying on its banking business in accordance with the prudential legislation in force. Notwithstanding this, aid granted in the form other than loan guarantees or loans fulfilling the conditions in point 25 (a) should fulfil the general principles of rescue aid and cannot consist of structural financial measures related to the bank's own funds.²¹

¹⁹ Communication from the Commission Community guidelines on State aid for rescuing and restructuring of firms in difficulty, OJ 2004 C 244, page 2.

²⁰ See footnote to point 25(a) of the Guidelines.

²¹ See Commission Decision of 5 December 2007 in case NN 70/2007, *Northern Rock*, not yet published, point 43.

- (50) The Commission understands that in the present case KfW assumes in the long term all of IKB's rights and obligations under the risk shield provided for the liquidity to Rhineland and the other structural investments. Thus KfW covered losses of specific non-performing assets. The consequence was that the assets remained valuable and no value adjustments, generating additional losses in the accounts had to be carried out. IKB's core capital ratio could thus be prevented from decreasing below the minimum statutory requirements. This could be understood as having an effect and character similar to that of a capital injection.²² The measures do therefore not seem temporary and reversible.²³

4.2.3. Restructuring aid

- (51) The Guidelines set the conditions to be fulfilled for a restructuring aid to be compatible. While the Commission does not exclude that the aid might constitute compatible restructuring aid, it is at this stage not sure whether the submitted restructuring plan complies with the conditions of points 32-51 of the Guidelines. In particular the Commission has the following doubts.

Long-term viability / restructuring plan (points 34 to 37 of the Guidelines)

- (52) The Commission has not been provided with a comprehensive restructuring plan. However, it notes that IKB has provided a series of documents which might be capable of qualifying as restructuring plan, i.e. as a basis for evaluating the restoration of viability.
- (53) However, the Commission needs to further investigate whether the internal measures indicated are sufficient to restore the long-term viability of IKB. The Commission views positively that IKB abandons the main loss making activities. However, the Commission is also aware that these activities were the most important source of revenue of IKB. It is therefore not sure whether IKB can simply continue without its portfolio investment activities and thereby restore its viability. This is even more so as IKB may be confronted with additional difficulties due to the ongoing deterioration of the financial markets as a consequence of the subprime crisis. In this context, the Commission recalls Germany's indication that the success of the reorganisation and the continuation of the bank depend very much upon a new strategic partner who will allow IKB to benefit from cost and revenue synergies and strengthen its capital basis. Consequently, the Commission can at this stage not ascertain that viability will be restored.
- (54) In any event, the Commission also notes that the Guidelines require as part of the restructuring plan the provision of forecasts of the company's business development for several years as well as scenarios reflecting best case, worst case and intermediate assumptions in order to underline the robustness of the restructuring plan. The German authorities have however only submitted key financial data for a base case scenario.

²² Cf. Commission decision in case C44/03 *Bank Burgenland*, OJ 2005 L 263/8, para. 36 and Commission Decision of 27.6.2007 in Case C50/2006 *BAWAG*, not yet published, points 166.

²³ In any event, the Commission also notes that the guarantee was not limited to six months and no undertaking was given at the time it was granted to stop the guarantee or to provide a restructuring or liquidation plan to the Commission within six months as required by point 25 (c) of the Guidelines. This issue could have however been overcome by the provision of a reasonable restructuring plan within the time limit.

Avoidance of undue distortions of competition (points 38 to 42 of the Guidelines)

- (55) The Commission doubts that the measures already taken or planned by IKB would be sufficient to avoid undue distortions of competition. The mere fact that IKB has small market shares in its core markets, as indicated above in point (26), does not free a company from compensatory measures.
- (56) Thus the Commission considers that compensatory measures could be necessary in order to limit the distortions of competition created by the aid. Moreover, the Commission is at this stage not sure whether the planned withdrawal from certain non-core activities can be accepted as compensatory measures, as they seem in any event necessary for the restoration of viability.

Aid limited to the minimum (points 43 to 45 of the Guidelines)

- (57) The Guidelines lay down that the own contribution must be as high as possible and must reach, for a large undertaking like IKB, at least 50 % of the restructuring costs.
- (58) So far Germany did neither indicate the total amount of the restructuring costs nor the part of the restructuring costs borne by IKB itself or the present and the future owners, which would be the basis for calculating the own contribution. In any event, the Commission will have to investigate whether the private sector participation in the risk shield could be regarded as own contribution. The Commission has therefore doubts whether the contribution of IKB is the maximum possible and reaches at least 50 % of the restructuring costs.

4.2.4. Article 87 (3) (b) EC

- (59) The aid could finally in principle be considered under Article 87 (3) (b) EC, which allows aid to remedy a serious disturbance in the economy of a Member State. However, the Commission would first like to point out that the Court of First Instance has stressed that Article 87 (3) (b) EC needs to be applied restrictively so that aid cannot be benefiting only one company or one sector but must tackle a disturbance in the entire economy of a Member State.²⁴ The Commission has consequently decided that a serious economic disruption is not remedied by an aid that "*resolve[s] the problems of a single recipient [...], as opposed to the acute problems facing all operators in the industry.*"²⁵ Also in all cases of banks in difficulty, the Commission has to date not relied on this provision.²⁶
- (60) The Commission observes that the problems of IKB are due to a very specific (risky) investment model for which IKB did not have sufficient liquidity as security while many other banks have indeed managed to overcome similar problems. Therefore, the

²⁴ Cf. in principle case Joined Cases T-132/96 and T-143/96 *Freistaat Sachsen and Volkswagen AG Commission* [1999] ECR II-3663, para. 167

²⁵ See Commission Decision in case C 47/1996, *Crédit Lyonnais*, OJ 1998 L 221/28, point 10.1.

²⁶ See Commission Decision in case C 47/1996, *Crédit Lyonnais*, OJ 1998 L 221/28, point 10.1, Commission Decision in Case C28/2002 *Bankgesellschaft Berlin*, OJ 2005 L 116, page 1, points 153 *et seq* and Commission Decision in Case C50/2006 *BAWAG*, not yet published, points 166, Commission Decision of 5 December 2007 in case NN 70/2007, *Northern Rock*, not yet published, point 38.

present case seems rather to be based on individual problems, and thus requires tailor made remedies, which can be addressed under the rules for companies in difficulties.²⁷

5. CONCLUSION

(61) In conclusion, the Commission has doubts on the basis of the available information that the measures of KfW in favour of IKB comply with the market economy investor test. Thus these measures will have to be assessed under Article 87 (1) EC. The Commission has at this stage doubts that the measures can be found compatible with the common market pursuant to Article 87 (3) (c) EC.

DECISION

In the light of the foregoing considerations, the Commission has decided to initiate the procedure laid down in Article 88(2) of the EC Treaty and requires Germany, within one month of receipt of this letter, to provide in addition to all documents already submitted, all information and data needed for the assessment of the existence and compatibility of the aid, and in particular:

- a detailed quantification of all risks (liquidity and default) covered by the risk shield (Rhineland, Rhinebridge, balance sheet);
- detailed description of the third measure granted by the federal government and the banking associations and explanation of the motivation of Germany to avoid the insolvency of IKB,
- an explanation for the disproportionate participation of KfW in the risk shield;
- copies of all contractual agreements between IKB and KfW, and KfW and the banking associations;
- explanations about the intention of KfW to limit its risk exposure related to the balance sheet risks of IKB;
- explanation as regard the intention to amend a remuneration or repayment clause for the risk shield;
- a detailed description of any envisaged and further possible compensatory measures
- information about the state of play of the sales process.

Germany is requested to forward a copy of this letter to the potential recipient of the aid immediately.

The Commission wishes to remind Germany that Article 88 (3) of the EC Treaty has suspensory effect, and would draw your attention to Article 14 of Council Regulation (EC) No. 659/1999, which provides that all unlawful aid may be recovered from the recipient.

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

²⁷ In any event, Germany has not provided substantive evidence that such banking crises would have had an effect on the entire German economy.

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
Rue de la Loi/Wetstraat, 200
B-1049 Brussels
Fax No: +32-2-296 12 42

For the Commission

Neelie KROES
Member of the Commission