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In the published version of this decision, some information has been omitted, pursuant to articles 30 and 31 of Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus […]	PUBLIC VERSION This document is made available for information purposes only.

Subject: State aid SA.34720 (2015/C) (ex 2013/N) – Denmark
Aid for the restructuring of Vestjysk Bank

Sir,

The Commission wishes to inform Denmark that, having examined the information supplied by your authorities on the aid 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.

I. PROCEDURE

(1) During 2012, the Danish authorities entered into a dialogue with the Commission to discuss the problems which were being faced by the Danish bank Vestjysk Bank A/S ("Vestjysk Bank" or the "the Bank").

(2) On 25 April 2012, the Commission found three measures in favour of Vestjysk Bank and Aarhus Lokalbank to constitute State aid within the meaning of Article 107(1) TFEU. However, on the basis of the assessment, the measures were found to be temporarily compatible with the internal market for reasons of financial stability. The measures were accordingly approved for six months or, if Denmark submitted an in-depth restructuring plan within six months from the date of the Decision, until the Commission has adopted a final decision on that restructuring plan. The temporary approval and the three aid measures are detailed in

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Commission Decision SA.34423 ("the Rescue Decision")[1]. The Danish authorities submitted a preliminary version of the restructuring plan for Vestjysk Bank on 18 April 2012 which included a set of commitments as the starting point for discussions concerning the restructuring plan.

(3) Between April 2012 and August 2013, the Commission and the Danish authorities discussed the restructuring plan in a series of meetings, phone conferences and written correspondence.

(4) In August 2013, the Danish authorities informed the Commission that […]* and the discussions concerning the restructuring of the Bank were suspended. However, discussions concerning the restructuring of the Bank resumed in April 2014 when the Danish authorities informed the Commission that […].

(5) The Danish authorities subsequently submitted revised versions of the restructuring plan for the Bank to the Commission on 5 September 2014, 12 November 2014 and 9 February 2015.

(6) On 6 May 2015 the Commission sent a letter to the Danish authorities which formally requested information concerning the long-term viability of Vestjysk Bank. The Commission received a response on 10 June 2015 including the latest version of the restructuring plan. The Danish authorities also informed the Commission that the Danish Financial Services Authority (DFSA) was due to conduct an on-site inspection into the Bank during the summer of 2015. The Commission received a summary of the report concerning the DFSA's site inspection on 4 November 2015.

(7) By letter of 6 November 2015, Denmark agreed to waive its rights deriving from Article 342 TFEU in conjunction with Article 3 of Regulation 1/1958[2] and to have the present decision adopted and notified in English.

II. DESCRIPTION

2.1 The beneficiary

(8) Vestjysk Bank was formed in 1874 and is a regional bank in Denmark with branches in Jutland and Funen; Aarhus Lokalbank started operating in 1908, and at the end of 2011 those banks had a balance sheet of DKK 29.2 billion (EUR 3.9 billion) and DKK 4.4 billion (EUR 600 million) respectively.

(9) The Danish State became a major shareholder in both banks (it had a stake of 53.1% in Vestjysk Bank and 45.2% in Aarhus Lokalbank) following a recapitalisation under the recapitalisation scheme in 2009 and a conversion of the capital injection into share capital on 20 February 2012[3].

* Confidential information.

[1] Commission Decision SA.34423, OJ C 348, 03.10.2014, p. 2.

[2] Council Regulation No 1 determining the languages to be used by the European Economic Community, OJ 17, 6.10.1958, p. 385.

[3] **Vestjysk Bank** raised State hybrid core capital with an original principal of DKK 1.44 billion (EUR 194 million), of which DKK 287.6 million (EUR 39 million) plus accrued interest of approximately DKK 8.7 million (EUR 1.2 million) was converted into shares in Vestjysk Bank. In the period 2009 - 2011 Vestjysk Bank has paid coupons amounting to a total of DKK 312.8 million (EUR 42 million) to

(10) On 28 February 2012, the Danish authorities informed the Commission that Vestjysk Bank and Aarhus Lokalbank were about to merge as each faced an increased risk of becoming a distressed bank. The resulting merged entity was subsequently known as Vestjysk Bank as Aarhus Lokalbank ceased to exist after the merger.

(11) The Danish State's share capital in Vestjysk Bank has increased since 20 February 2012, as on 31 October 2013 Vestjysk Bank performed two consecutive conversions of government-held hybrid debt instruments4 into equity in line with the conditions set out in the recapitalisation scheme of 2009. The Danish State currently holds 80.62% of the shares of Vestjysk Bank. In addition, the Danish Financial Stability Company, which is wholly owned by the Danish State, holds 0.86% of the share capital, which means the Danish State currently holds 81.48% of the share capital and voting rights in Vestjysk Bank.

(12) According to the Bank's half-year report, at June 2015 Vestjysk Bank was the tenth-largest bank in Denmark and its consolidated Financial Statements showed a total balance sheet of DKK 22 102 million, of which the loan portfolio amounted to DKK 14 035 million. In addition, total retail deposits amounted to DKK 16 844 million.

(13) Vestjysk Bank is active in all business segments, but focusses on loans and guarantees to real estate (20% of outstanding loans and guarantees) and agriculture, hunting forestry and fisheries (another 20% of the outstanding loan and guarantees).

(14) The shares of Vestjysk Bank are listed on the Copenhagen Stock Exchange.

2.2 The aid measures examined in the Rescue Decision

(15) On 13 April 2012 the Danish authorities notified to the Commission the following measures for Vestjysk Bank:

- Measure 1 - Completion of a capital raise of the Bank with net proceeds of between DKK 250 and DKK 300 million;

- Measure 2 – Raising of new subordinated loan capital with a principal of DKK 200 million[5];

the Danish State. The coupon interest rates were set at 9.69% and 10.19% per annum, depending on whether they included the conversion option fee.

Aarhus Lokalbank has raised State hybrid core capital with an original principal of DKK 177.8 million (EUR 24 million), of which DKK 142.2 million (EUR 19 million) plus accrued interest totalling DKK 5 million (EUR 0.7 million) was subsequently converted into shares in Aarhus Lokalbank. In the period 2009 - 2011 Aarhus Lokalbank paid coupons amounting to a total of DKK 25.9 million (EUR 3.5 million) to the Danish State. The coupon interest rates were set at 10.92% and 11.42% per annum, depending on whether they included the conversion option fee.

4 On 31 October 2013, the conversion of DKK 323 million plus the accrued interest (approximately DKK 15 million) of State hybrid capital was concluded, increasing the Danish State's shareholding to 65.96%, while the stake of the Danish Financial Stability Company reached 1.5%. Including the latter, the Danish State's shareholding increased to 67.46%. On 20 January 2014, the conversion of DKK 575 million plus the accrued interest (approximately DKK 12.6 million) was concluded, increasing the Danish State's shareholding to 80.62%. In addition, the Danish Financial Stability Company held 0.86%.

5 The Commission raised no objections to Measure 2 as described in the Rescue Decision on the basis it did not constitute State aid.

- Measure 3 - Sale of a minority shareholding in the amount of DKK 175 million (EUR 23 million) that the Bank owned in a Danish mortgage credit institution to the Danish Central Bank;

- Measure 4 - Individual State guarantees for new bonds for up to DKK 8.6 billion (EUR 1.154 million).

(16) In April 2012 the Commission temporarily approved for six months measures 1, 3 and 4.[6] The subordinated loan in Measure 2 was funded entirely by private investors and was thus not considered to be State aid.

(17) On 28 June 2012, Vestjysk Bank received a final binding undertaking from the Danish Financial Stability Company in respect of Measure 4, which limited the individual State guarantees for liabilities to DKK 6.8 billion (EUR 914 million).

(18) The gross proceeds from Measure 1 amounted to DKK 318.7 million, (net proceeds of DKK 300 million) and the State participated with DKK 166 million (EUR 22 million). Measure 3 gave rise to a capital relief effect of 0.60% by reducing the risk weighted assets ("RWAs") of the Bank.

(19) The final amount of support resulting from the implementation of the three measures described in the Rescue Decision was DKK 7 293.7 million (EUR 979 million).

2.3 Capital shortfall in Q2 2014.

(20) The DFSA fixed Vestjysk Bank's individual capital adequacy requirement at 10.9% as at 31 December 2013 as part of the individual capital adequacy requirements of Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (CRD IV)[7].

(21) On 1 April 2014, Vestjysk Bank informed the DFSA and the Commission that as at 31 March 2014 Vestjysk Bank's individual capital adequacy stood at 10%, thus breaching the requirement. The DFSA therefore ordered Vestjysk Bank to file a plan for the re-establishment of capital ('the Capital Plan') before 7 April 2014.

(22) On 20 May 2014, Vestjysk Bank and Denmark informed the Commission of the Bank's Capital Plan. The Capital Plan included a Liability Management Exercise (LME)[8] and a further sale of Vestjysk Bank's shareholding in the Danish mortgage

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[6] A detailed description is given in the Rescue Decision.

[7] Directive of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, OJ L 176, 27.06.2013 p, 338.

[8] Transaction 1: Issuance of a new subordinated loan of DKK 87.5 million provided by Nykredit Bank A/S and a separate loan of DKK 12.5 million provided by Arbejdernes Landsbank A/S. The new loans replaced an existing loan of DKK 100 million by Nykredit Bank A/S redeemed at par;
Transaction 2: Modification of the terms and conditions of DKK 75 million hybrid core capital in order to comply with CRD IV rules and eligibility.
Transaction 3: Issuance of a new subordinated loan of DKK 50 million provided by […]. The new subordinated loan replaces an existing loan of DKK 50 million that shall be redeemed at par.

credit institution (DLR Kredit A/S) for a value of approximately DKK 250 million[9].

(23) On 23 October 2014, all transactions related to the Capital Plan were concluded, which resulted in an individual capital adequacy of 12.7%.

2.4 The draft restructuring plan

(24) Denmark committed to submit an in-depth restructuring plan for Vestjysk Bank within six months from the date of the Rescue Decision. To ensure compliance with the Restructuring Communication[10], the submission of a restructuring plan would need to demonstrate how the viability of the Bank would be restored, contain adequate burden-sharing measures and contain provisions to limit competition distortion[11].

2.4.1 The principles of restructuring

(25) Vestjysk Bank's draft restructuring plan has been updated several times because Vestjysk Bank failed to achieve its projected profitability. The latest version was received in June 2015. Overall, the Danish authorities consider that Vestjysk Bank's past efforts and the restructuring plan have led to a viable yet still vulnerable bank.

Profit & Loss and Balance sheet projections

(26) The restructuring plan covers the period up until 2017 and assumes that the balance sheet of the Bank will continue to reduce until 2017. The restructuring plan also projects a steady positive evolution in the Bank's profitability, aiming at a return to profitability in 2015, albeit at a low level. The key figures of the financial projections from the June 2015 restructuring plan are shown in Table 1.

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9 The sale agreement of sector shares in DLR Kredit A/S was completed on 23 October 2014. The shares were sold to […] private banks ([…]). The completion resulted in an increase in Vestjysk Bank's surplus solvency in relation to its individual capital adequacy requirement at the level of DKK 200 million, equivalent to 1.0 percentage point.

10 Commission 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 C195, 19.8.09, p 9 (Restructuring Communication).

11 See footnote 10 of the Restructuring Communication.

Table 1: Financial projections (P&L and Balance sheet) for Vestjysk Bank (in DKK million)

P&L	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Interest Income	1494	1262	1022	[900-950]	[850-900]	[850-900]
Interest Expense	727	520	365	[300-350]	[250-300]	[250-300]
Net Interest Income	892	814	697	[600-650]	[600-650]	[600-650]
Total Income	1282	1235	1053	[900-1000]	[900-1000]	[900-1000]
Total Provisions	1478	1028	535	[250-300]	[250-300]	[200-250]
Operational costs	588	542	509	[450-500]	[450-500]	[450-500]
Profit after tax	-1399	-442	-191	[25-75]	[100-150]	[150-200]
Cost-to-Income Ratio	55.30%	48.90%	53.20%	[50-60%]	[50-60]	[50-60%]
Return on Equity after tax	-106.30%	-46.90%	-17.50%	[0-5%]	[5-10%]	[5-10%]
FTE	621.3	562.9	524	[480-510]	[470-500]	[460-490]
Branches	24	20	20	[18-22]	[18-22]	[18-22]
Balance sheet	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Net Loan Book	20697	17360	14714	[13.000-14.000]	[13.000-14.000]	[13.000-14.000]
Total assets	32765	26112	21804	[20.000-22.000]	[19.000-21.000]	[19.000-21.000]
Deposits	18057	17877	18768	[17.000-19.000]	[16.000-.18.000]	[16.000-.18.000]
Central Bank Funding	3002	4700	0	[0-10]	[0-10]	[0-10]
Own funds (Capital + reserves)	992	887	1287	[1.350-1.450]	[1.450-1.550]	[1.550-1.650]
RWAs	25595	20335	17927	[16.000-17.000]	[16.000-17.000]	[15.000-16.000]
Loan-to-Deposit ratio	114.6%	97.1%	78.4%	[70-80%]	[70-80%]	[70-80%]
TIER 1 ratio	10.90%	11.30%	9.90%	[10-11%]	[11-12%]	[12-13%]

(27) Taking into account the restructuring efforts undertaken by Vestjysk Bank since the Rescue Decision, the projected total balance sheet reduction is [30-40%] in 2017 compared to its 2012 level. The Bank expects to achieve that reduction through (i) a decrease of the net loan portfolio by[30-40%]; (ii) a [90-100%] reduction of Central Bank funding; and (iii) a [5-10%]decline in deposits.

(28) The net income of Vestjysk Bank is expected to be improved by the projected steady decrease of loan loss provisions ([40-50%] decrease year-on-year 2014-2015) and a projected decrease in interest expenses (decrease of [20-30%] between 2014 and 2017). At the same time, net interest income is expected to continue falling (in particular in 2015 while more or less stable thereafter), while net fee income is expected to rise over the projection period.

(29) The restructuring plan projects a weak return to profitability in 2015 ([25-75]). Taking into account the projected decrease in impairments, costs and increasing profits, the Bank projects DKK [150-200] profits after tax in 2017 (compared to a DKK 1 399 million loss in 2012), a cost-to-income ratio of [50-60%] (compared to 55.3% in 2012) and capital ratio under Basel III (CET1) rules of [12-13%].

Loan impairments

(30) Vestjysk Bank has faced significant impairment losses since the Rescue Decision. Loan impairments amounted to DKK 1 515 million in 2012, to DKK 1 073 million in 2013 and DKK 683 million in 2014.

(31) The majority of the loan impairments derive from the real estate segment and the agriculture, hunting, forestry and fishing segment. Those segments make up respectively 20.5% and 54.6% of Vestjysk Bank's total impairments from 2012 until 2015.

(32) The Bank recognises that the significant amount of loan impairments adversely affects its viability. The restructuring plan projects that Vestjysk Bank will be able to rebalance its loan portfolio towards the retail segment, allowing for a better risk diversification.

(33) Vestjysk Bank intends to achieve that outcome by minimising its exposure through a reduction in lending in its most troubled portfolios: (1) agriculture, hunting, forestry and fishing; (2) building and construction; and (3) real estate. According to the latest restructuring plan, Vestjysk Bank will cap its gross lending in those three categories so as to decrease its gross lending in agriculture, hunting, forestry and fishing by[30-40%]; in building and construction by[20-30%]; and in real estate by[30-40%].

(34) It should however be noted that the restructuring plan projects that agriculture, hunting forestry and fishing segment and the real estate segment will remain strategic segments for the Bank.

Operational costs

(35) Vestjysk Bankprojects to reduce its operational costs by a reduction in Full Time Equivalents (FTE) and a reduction of its number of branches.

(36) The restructuring plan projects a decrease of FTE from 501 in 2015 to [460-490] in 2017, which is a reduction of [3-4%]. Taking into account the restructuring efforts already performed since 2012 (621.3 FTE), the total FTE reduction is [20-30]%.

(37) Vestjysk Bank also intends to reduce its operational costs by a reduction of its commercial footprint. Vestjysk Bank projects to further reduce its branch network to [18-22] branches by the end of 2017, compared to 24 in 2012. That fall represents a reduction of [10-20%].

(38) On 14 September 2015, Vestjysk Bank announced that it intended to carry out further staff redundancies in its branch network and central services. Vestjysk Bank will reduce the number of FTE from 510 to around [450-480]. Taking the efforts from 2012 until 2015 into account, the total reduction will be [20-30]%. Vestjysk Bank expects the staff reduction to save at least DKK 25 million annually. The impact of that announcement was not included in the June 2015 restructuring plan.

Credit policy

(39) As explained in recital ((27), Vestjysk Bank projects a reduction of its balance sheet until 2017 and a rebalancing of the loan book (see recital ((33)). To achieve those ambitious goals, Vestjysk Bank has updated its credit policy:

a. the Bank will not enter in agreements with new customers within the […] business. However, a change of debtors can be accepted if the Bank obtains a lower credit risk and better settlement prospects. Existing customers may (to a limited extent) obtain financial support for the completion of projects, provided that the target for reducing exposure within real property is observed;
b. no financing of assets outside the scope of the Bank's ordinary market area; i.e. areas where the Bank has no representation by way of branches or has not established sufficient market knowledge, unless the customer provides own financing of at least [40-50%], and the Bank obtains a charge against realisable securities that are regarded as unconditionally good;
c. no expansion of the overall loans/guarantees within the agricultural sector. The only exception would be transfers of distressed agricultural properties to new/existing customers resulting in the Bank's credit position being strengthened. The Bank will continue to help good customers with smaller projects/expansions provided that the Bank's target for reducing exposure within agriculture is observed; and
d. the Bank will create a complete reporting of all the credit engagements towards its credit committee, which will have the final decision power on all loans starting from DKK [5-10] million. Loans starting from DKK [0-5] million will also be subject to the final decision power of a modified form of the credit committee which does not include the executive managers of the Bank. Loans which fall below that latter threshold will be approved based on strict and prudent guidelines. The board of directors always has the final responsibility to grant loans.

(40) Taking Vestjysk Bank's updated credit policy and the reduced loan book into account, the restructuring plan projects that the volume of RWAs in Vestjysk Bank will decrease by [30-40%] by the end of 2017 as compared to 2012 (from DKK 25.595 billion in 2012 to DKK [15000-16000] in 2017).

2.4.2 Liability Management Exercises

(41) During the past years, Vestjysk Bank performed several LMEs to strengthen Vestjysk Bank's capital.

(42) On 13 December 2012 the DFSA gave its approval for Vestjysk Bank to repurchase two Tier 2 instruments12, up to a nominal value of NOK 135 million (approximately EUR 18.36 million) and NOK 180 million (approximately EUR 24.48 million) on a continuous basis until 31 March 2013. The approval was conditional upon a purchase rate of 55% of the principal or lower.

(43) On 18 February 2013, the DFSA gave its approval for Vestjysk Bank to repurchase two different subordinated loans of DKK 25 million and DKK 50 million granted by […], which is affiliated with […]. The Bank repurchased DKK 50 million of the subordinated debt, plus non-accrued interest at a rate of 66.67 % of the principal. At the same time, released DKK 75 million deposits plus non-accrued interest from Vestjysk Bank.

(44) The DFSA simultaneously gave its approval for Vestjysk Bank to repurchase an additional amount of the Tier 2 instruments described in recital ((42) up to a nominal value of DKK 100 million at a maximum rate of 55%.of the principal That repurchase could take place until 31 March 2013.

(45) On 13 June 2013, the DFSA approved another repurchase of subordinated loan capital granted by […] (ISIN NO0010313349) on a continuous basis until 30 June 2013 up to a nominal value of NOK 40 million (approximately EUR 5.2 million). The DFSA approval was conditional upon a rate significantly below par, with a maximum of 62% of the principal plus accrued interest.

2.4.3 The DFSA inspection

(46) The DFSA conducted an on-site inspection into the Bank during the summer of 2015. The inspection consisted of a functional examination in which the Bank's loan book and a number of other areas were reviewed against a risk-based assessment.

(47) As part of the inspection, the DFSA reviewed 63 of the largest loans in the Bank (all were in excess of DKK 43.6 million); only 6% of the loans reviewed were subject to normal credit risk without signs of weakness, and the inspection identified Objective Evidence of Impairment (OEI) for approximately 76% of the loans reviewed. The DFSA found that for 30 of the largest agricultural loans 69% of loans displayed OEI, and only 3% were subject to normal credit risk without signs of weakness – the DFSA did not identify any evidence of additional impairments for those loans.

(48) The DFSA inspection report concludes that the risk profile of the Bank is influenced by its lending to the agricultural and real estate sectors and defines both segments as high risk areas. According to the DFSA report, Vestjysk Bank's lending to the agricultural segment and the real estate segment is clearly above its

[12] With ISIN NO 0010331499 and ISIN NO 0010313349.

peers in the Danish banking market (22.6% and 19.4% of the Bank's lending operations compared to 10.7% and 13.3% of the lending operations of its peers, respectively.)

(49) The DFSA concludes that as of 31 March 2015, a further DKK 116.5 million impairments had been discovered and needed to be provisioned for. Vestjysk Bank has informed the DFSA that DKK 61.7 million of the amount was already recognised in the half year report 2015.

III. ASSESSMENT OF THE MEASURES

Existence of State aid

(50) In recitals (47) to (67) of the Rescue Decision, the Commission assessed whether measures 1, 3 and 4 could be considered as State aid[13]. It concluded there that measures 1, 3 and 4 constituted State aid within the meaning of Article 107(1) TFEU.

Compatibility of the aid

(51) In recitals (74) to (107) of the Rescue Decision, the Commission found measures 1, 3 and 4 to be temporarily compatible with the internal market for reasons of financial stability. The measures were accordingly approved for six months or, if Denmark submitted an in-depth restructuring plan within six months from the date of that Decision, until the Commission had adopted a final decision on that restructuring plan.

(52) The Restructuring Communication explains that in order to be compatible with the internal market on the basis of Article 107(3)(b) TFEU, the restructuring of a financial institution in the context of the financial crisis must lead to a restoration of the viability of the bank, or a demonstration of how it can be wound up in an orderly fashion.

Restoration of long-term viability

(53) The latest draft restructuring plan anticipates that Vestjysk Bank's viability will be restored within a reasonable time frame, based on the operational measures referred to in recitals (35) to (38).

(54) However, the Commission doubts whether the latest draft restructuring plan provides sufficient grounds to ensure the viability of Vestjysk Bank within the restructuring period.

(55) The Bank's balance sheet is projected to decrease from DKK 32 765 million in 2012 to DKK [19.000-21.000] at the end of 2017. The strong decrease ([35-45%]) is a consequence of the Bank's efforts to reduce its loan book, but also of the macro-economic environment (which includes increasing losses in the agricultural sector) which has resulted in customers either leaving the Bank or defaulting on their loans.

[13] Measure 2 as described in the Rescue Decision was deemed to not constitute State aid.

(56) In 2014, Vestjysk Bank recorded a loss of DKK 191 million. For the first half of 2015 the Bank was able to report a profit of DKK 45 million. The core income of the Bank reached DKK 495 million, compared to DKK 564 million in the first half of 2014. However, taking into account the Bank's recent history, it is the Commission's view that the mid-year profit for 2015 is not sufficient to assume a durable return to profitability. Since 2012, Vestjysk Bank's end-year results have been heavily influenced by the impairments on the bank's credit portfolio; Table 2 compares the Bank's mid-year and end-year profits:

Table 2: Mid-Year and End-Year profits

Year	Profit
2012 Mid-Year End-Year	DKK 1 million (profit) DKK 1 448 million (loss)
2013 Mid-Year End-Year	DKK 98 million (loss) DKK 442 million (loss)
2014 Mid-Year End -Year	DKK 41 million (profit) DKK 191 million (loss)

Net income

(57) Net income has decreased between 2012 (DKK 782 million) and 2015 (DKK [500-550] million). The Bank however projects net income to remain more or less stable (DKK [500-550]in 2015, DKK [500-550]in 2016 and DKK [500-550]in 2017). Net income is projected to be influenced by a stabilisation of the net interest income, an increase in net fees and commissions and a decrease in the operational costs.

(58) Net interest income is expected to remain stable as well (DKK [600-650]in 2015 to DKK [600-650]in 2017). The stabilisation of the net interest income is caused by a stabilisation of the loan book of Vestjysk Bank and a projected decrease in interest expenses.

(59) The majority of Vestjysk Bank's loan book matures within one year ([60-65%]of the loans to clients). In consequence, the stabilisation of the loan book is largely dependent on Vestjysk Bank's ability to generate sufficiently new business at sufficiently high margins. The Danish authorities have not been able to provide clear and sufficiently granular information on how that replenishment of the loan book will be realised and at which margins. As such, the Commission cannot verify the projections.

(60) The Financial Stability Report for the first half of 2015 by the Danish Central Bank confirms that lending margins in Denmark will remain under pressure and will continue to limit banks' capacity to increase their net interest income by raising lending rates.

(61) The restructuring plan projects interest expenses to decrease by [20-30%]between 2014 and 2017. That fall results from the full repayment of the Individual State Guarantees (Measure 4 of the Rescue Decision) and a projected decrease of the Bank's deposit rates.

(62) Vestjysk Bank currently has a deposit surplus of DKK 4.8 billion (loan-to-deposit ratio of 75%). Its deposit base has remained fairly stable during the past year due to Vestjysk Bank's pricing policy and its loyal customer base. That stable deposit base has allowed the Bank to change its funding profile from a large dependence on

wholesale and central bank funding to being fully funded by deposits. The Bank is therefore more resilient towards stresses on the interbank markets, but it is also an indication of the Bank's limited profitable investment opportunities.

(63) The Commission considers that the high amount of high priced deposits will have a negative impact on the Bank's net interest income. While deposit rates are falling in the Union, high competitive pressure on deposit rates in Denmark pushes the Bank to offer an average deposit rate that is higher than that of its competitors. Vestjysk Bank projects that its deposit surplus will allow it to gradually decrease the cost of deposits (while remaining above average market prices) but the size of the interest rate decrease and the impact thereof is not clear from the information submitted to the Commission.

(64) The projected decrease of deposit rates and strong competitive pressures do not seem to align with each other and the Commission questions how Vestjysk Bank will reduce the deposit rates in a competitive deposit market. The Commission also questions the potential competition distortions that arise if Vestjysk Bank offers higher deposit rates than its unaided competitors.

(65) The Bank projects its net fee and commission income to increase over the projection period (from DKK [250-300] in 2015 to DKK [300-350] in 2017). The increase reflects a higher level of activity in the areas of customers' securities trading and an extraordinarily high level of re-mortgaging seen in the first half of 2015.

(66) The Commission questions the sustainability of the increased net fee and commission income. Re-mortgaging is an activity typically only undertaken when interest rates are decreasing. Vestjysk Bank projects the interest rate level to remain low (and stable) in Denmark. The consequence would be that re-mortgaging activity will slow down as soon as interest rates have stabilised or start to increase. The Commission also questions the long-term impact of the re-mortgaging activity on the net interest income of Vestjysk Bank. The new (and probably lower) mortgage rates will lower the Bank's future profit-generating capacities.

(67) Vestjysk Bank projected a minor decrease in operating expenses from DKK [500-550] in 2015 to DKK [500-550] in 2017. That decrease is explained by a reduction in the number of employees (see recitals ((35) to ((37)) and a tight cost management.

(68) That slight decrease in operational costs is reflected in the cost-to-income ratio of the Bank ([50-60%] in 2015 and [50-60%] in 2017). However, those figures do not take into account the additional restructuring measures Vestjysk Bank announced in a press release of 14 September 2015. The Commission acknowledges that the decrease in operational costs will be larger when the additional measures described in that press release materialise.

(69) Due to the projected stabilisation of net income and the decrease of loan impairments and provisions (see recitals ((70) to ((76)), the Bank expects to achieve a return on equity (ROE) after tax of [5-10%] in 2017 (compared to -106.3% in 2012) according to the restructuring plan. The Commission questions whether that sharp increase in ROE after tax is realistic, taking into account the large uncertainties related to the profitability of the new business and the reduction in impairments.

Loan impairments and provisions

(70) As stated in recital ((30) Vestjysk Bank has had to book significant provisions since the Rescue Decision (DKK 1 515 million in 2012, DKK 1 073 million in 2013 and DKK 683 million in 2014). As a result, the accumulated impairment ratio stood at 16.4% in the first half of 2015 and 16.7% at the end of 2014.

(71) According to the latest restructuring plan, Vestjysk Bank's 2017 loan book will be largely composed of loans to retail customers (households, excl. mortgages: ([30-40%]); agriculture, hunting, forestry and fishing ([10-20%]); real estate ([20-30%]); and building and construction ([0-5%]). Taking into account that the majority of the provisions the Bank had to book since 2012 derive from the real estate segment and the agriculture, hunting, forestry and fishing segment (respectively 20.5% and 41.6% of Vestjysk Bank's total impairments from 2012 until 2015) the Commission questions whether Vestjysk Bank's projected loan book composition will lead to a return to viability.

(72) Vestjysk Bank projects a strong decrease in the annual flows of provisions (new provisions) that have to be recorded and ultimately a decrease of the stock of provisions. In 2012, Vestjysk Bank had to record new provisions for DKK 1 478 million, while the projections for 2017 are limited to DKK [200-250]. Vestjysk Bank states such a decrease is possible due to improving macro-economic circumstances and an improved risk management.

(73) Comparing the flow of new provisions since 2012, an overall decline is evident. The latest restructuring plan provides however no further information on the reasons behind the projected decrease of impairments. Based on the current macro-economic circumstances the Commission questions whether the projected decrease in impairments is not overly optimistic. The Commission's doubts are based on the macro-economic evolutions, the conclusion of the DFSA Inspection Report and the Financial Stability Report by the Danish Central Bank.

(74) The most critical sector of the Bank's loan book, namely agriculture, hunting, forestry and fishing has suffered an increased need for impairments. That increase is especially clear in the sub-sectors of pork (+ 319% between 2013 and 2014) and milk (+25% between 2013 and 2014), which are the two most important sub-segments of the agriculture, hunting, forestry and fishing segment. The overall development of the agricultural segment and the low level of settlement prices remains a challenge for the Bank.

(75) The Commission's doubts on the projected decrease in provisions are also confirmed by Vestjysk Bank's report for the first half of 2015. That report shows a provisioning level that is still unsatisfactorily high, but slightly decreasing. The impairment ratio14 reached 0.8% for the first half of 2015, compared to 0.9% in H1 2014. The agriculture, hunting, forestry and fishing segment remained the largest contributor to the impairment charges.

(76) The conclusion of the DFSA's inspection report and the additional impairments reported therein confirm the Commission's point of view that Vestjysk Bank's risk profile and viability are under pressure due to its lending to the agricultural and real

[14] Impairments booked in the period over the total loan book.

estate sectors. The DFSA inspection report also notes that impairments could significantly increase in the event of further adverse economic trends, or in the event of inadequate control. The DFSA recommends Vestjysk Bank to strengthen its capital to cover for those potential future impairments.

(77) The Danish Central Bank's Financial Stability Report for the first half of 2015 confirms that the agricultural sector has experienced increasing losses. It also mentions that margins will remain under pressure and will continue to limit banks' capacity to decrease impairments.

Capital requirements

(78) According to the 2015 half-year results, the Bank's CET1 capital totalled DKK 1 319 million at the end of June 2015, giving a CET1 ratio of 7.5%, compared to 7.8% in June 2014. At the same time, the Bank's total Tier 1 capital ratio increased to 10.3% compared to 9.6% at the end of June 2014.

(79) The overall CET1 capital requirement for the Bank (minimum requirement + additional solvency requirement) is 7%. Thus, according to the half year report the Bank had a very small surplus (0.5% or DKK 84 million) at the end of June 2015. Compared to end 2014, the surplus decreased from DKK 125 million to DKK 84 million. That drop can be explained by the combination of realised losses and an increase of the minimum CET1 capital requirement from 4% to 4.5%.

(80) As stated in recital ((76), the DFSA informed Vestjysk Bank through its DFSA inspection report that if any additional impairments have to be accounted for due to further adverse economic trends (or in the event of inadequate control), the Bank should strengthen its capital.

(81) As a result of the identified loan impairments in the DFSA inspection report, the Bank has calculated the individual solvency need as being 10.5% as of 30 June 2015. The DFSA concludes by stating that the solvency need of 10.5% covers the current risks of the Bank.

(82) The Danish Central Bank's Financial Stability report for the first half of 2015, states that the combination of increasing capital requirements, very low interest rates and limited demand for new loans will create extremely competitive conditions for customers. The Financial Stability Report further explains that the implementation of the requirements in CRD IV/CRR has entailed an enhanced framework for the Danish requirements. At end-2014, all systemic and non-systemic credit institutions except Vestjysk Bank and one other Danish financial institution complied with the fully phased-in 2019 capital requirements. Vestjysk Bank would therefore have to continue to strengthen its capital to comply with capital requirements.

(83) Based on the DFSA inspection report and the Danish Central Bank's Financial Stability report for the first half of 2015, the Commission questions whether Vestjysk Bank's capital position is sufficiently strong to endure additional impairments.

Burden-sharing

(84) To be in line with the Restructuring Communication, a restructuring plan must demonstrate how the viability of the Bank would be restored, contain adequate burden-sharing measures and contain provisions to limit competition distortion.

(85) The Danish authorities and Vestjysk Bank have tried to ensure sufficient burden-sharing through conducting several LMEs, providing a sufficient remuneration for the recapitalisation and the individual government guarantees.

(86) The different LME transactions described in recitals ((41) to ((45) have been the main contributors to burden-sharing. According to Commission guidance15 LMEs should significantly reinforce the viability of the Bank while the bank and the investors contribute to the greatest possible extent to the restructuring costs. That outcome is translated into the following two operational consequences:

a. The premium to the market price reflected in the buyback price should not exceed 10 percentage points of the principal; and
b. The buyback prices should not exceed 90% of principal.

(87) The LMEs described in recital ((42) were concluded at an average price of 48.72% of the principal and 45.05% of the principal respectively. Both prices were well below the DFSA's limit of 55 of the principal and respect the boundary of 90% of the principal. Market research has shown that the average price offered for each instrument was less than 10 percentage points of premium to the market price.

(88) The repurchase of the subordinated capital granted by […] and described in recital ((43) was performed at an average price of 66.67% of the principal (67% if the non-accrued interest is included), well below 90% of the principal. The Commission's assessment of the repurchase price has shown that the premium that was offered to the investors was below 10%.

(89) The repurchases of subordinated capital described in recital ((44) were completed on 3 April 2013 for a price of 52.39% of the principal, well below 90% of the principal and within the boundaries of 10% premium to the market price.

(90) The repurchase described in recital ((45) was completed on 13 June 2013 and was performed at an average price of 62% of the principal, 2 percentage points above the market price of 50% plus the premium of 10%. Vestjysk Bank thereby overpaid the holders of the subordinated debt instruments by an amount corresponding to 2% of the principal (or NOK 800,000, approximately EUR 104,000). The Commission thus concludes that that transaction was not in line with the Restructuring Communication's goal of adequate burden-sharing.

(91) The transactions described in recital ((22), which were part of Vestjysk Bank's plan to address its capital shortfall in 2014, cannot be classified as a pure buy-back as they involve the subscription of new subordinated debt in parallel. In addition they were part of a capital plan that if not approved would have left Vestjysk Bank with a capital shortfall, potentially requiring additional State aid. The Commission

[15] See Commission memo 09/441 and the accompanying press release by the Commission on 8 October 2009.

therefore concludes that those transactions are in line with the Restructuring Communication.

(92) The Danish State participated in the capital raise on the basis of its stake in both Vestjysk Bank A/S and Aarhus Lokalbank A/S. As a result, the State provided 52.1% of capital injected in Vestjysk Bank. The gross proceeds from the issue amounted to DKK 318.7 million, while the Danish State participated with DKK 166 million.

(93) As regards remuneration to the State for its participation in the capital raise, it is noted that the 2011 Prolongation Communication[16] provides guidance on the conditions for State recapitalisations in the form of ordinary shares. According to that Communication, the remuneration for such recapitalisations should be assessed on the basis of the discount to the share price adjusted for the dilution effect or the TERP[17] (theoretical ex-rights price) immediately prior to the announcement of the capital injection.

(94) The subscription rate of the rights issue in which the State participated was set at DKK 10.4 per share. That subscription rate entails a discount of 43.1% from a stock price of DKK 17.1 in the beginning of 2012, representing a discount on the TERP of 24.5%. On the day of the completion of the rights issue stock price per share was DKK 16, meaning the discount on the TERP was 21%. The Commission concludes that the discount ensures that the State will receive an adequate remuneration for its participation in the capital raise.

(95) Vestjysk Bank had to pay a risk-based guarantee commission for the individual guarantee described in recital (34) of the Rescue Decision. The base rate for determining the guarantee commission was set at 1.35%, to which an incremental additional guarantee charge of 0.65% in the first year, 0.75% in the second and 0.90% in the third year and onwards for the duration of the guarantee must be added. That remuneration of the guarantee is well above what the 2011 Prolongation Communication requires.

(96) The sale of the minority stake in a Danish mortgage credit institution to the Danish Central Bank had a capital release effect which is similar to a recapitalisation. The measure has not been remunerated separately. According to recital (94) of the Rescue Decision, the Commission will take the lack of remuneration for Measure 3 into account when determining the depth of the restructuring of Vestjysk Bank. Nevertheless, the Commission will also take into account the following mitigating factors: the nature of Measure 3, the fact that the remuneration received for Measure 4 exceeds Commission requirements for compatibility of guarantees with the internal market and the limited distortion of competition caused by the aid amount in Measure 3.

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[16] Communication from the Commission on the application, from 1 January 2012, of State aid rules to support measures in favour of banks in the context of the financial crisis (2011 Prolongation Communication) OJ C 356, 6.12.2011, p 7.

[17] See footnote 16 of the 2011 Prolongation Communication.

Limiting distortions of competition

(97) According to the Restructuring Communication, a restructuring plan should propose effective and proportionate measures which limit distortions of competition. Such measures should be specifically designed to address distortions identified on the market where a beneficiary bank operates. The nature and form of such measures depends on two criteria: (1) the amount of aid and the conditions and circumstances under which the aid was granted; and (2) the characteristics of the market, or markets on which the beneficiary bank will operate. Finally, the Commission is careful to pay attention to the risk that restructuring measures may undermine the internal market.

(98) As mentioned in recitals ((25) to ((40), Vestjysk Bank intends to reduce its commercial footprint by reducing its branch network. The combination of a reduction of the branch network and the characteristics of the Danish banking market will affect Vestjysk Bank's capacity to generate new business and gather new deposits, thereby contributing to a limitation of the distortions of competition. However, taking into account the large amount of aid received by Vestjysk Bank, the Commission questions the impact of the proposed staff reduction of 25.96% between 2012 and 2017 in its branch network and central services on the risk of competition distortion

IV. CONCLUSION

The Commission concludes that the draft restructuring plan does not provide sufficient information to ensure the Bank's return to viability and does not allow the Commission to conclude that the competition distortions are limited to a minimum. The Commission also concludes that one of the repurchasing transactions led to an insufficient amount of burden-sharing. The Commission has therefore decided to open the formal investigation procedure pursuant to Article 4(4) of Regulation (EC) No 2015/1589[18].

In the light of the foregoing considerations, the Commission requires Denmark, within one month of receipt of this letter, to provide all documents, information and data needed for assessment of the compatibility of the aid/measure. Otherwise the Commission will adopt a decision on the basis of the information in its possession. It requests your authorities to forward a copy of this letter to the potential recipient of the aid immediately.

The Commission notes that Denmark agreed to have the present decision adopted and notified in English

The Commission wishes to inform Denmark 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

[18] With effect from 14 October 2015, Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, OJ L 83, 27.3.1999, p. 1., was repealed and replaced by Regulation (EU) No 2015/1589 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union (codification), OJ L 248, 24.9.2015, p. 9. All the procedural steps taken during the course of the proceedings were adopted under Regulation (EC) No 659/1999. Any reference to Regulation (EC) No 659/1999 may be construed as a reference to Regulation (EU) No 2015/1589 and should be read in accordance with the correlation table in Annex II to the latter regulation.

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 Competition
State Aid Greffe
B-1049 Brussels
Stateaidgreffe@ec.europa.eu

Yours faithfully
For the Commission

Margrethe VESTAGER
Member of the Commission

CERTIFIED COPY
For the Secretary-General,

Jordi AYET PUIGARNAU
Director of the Registry
EUROPEAN COMMISSION