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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 This document is made available for information purposes only.

Subject: State Aid SA.38664 (2014/N), Lithuania
Additional notification to SA.36248 – Liquidation aid for resolution of AB Ukio Bankas

Sir,

1. PROCEDURE

(1) By decision of 18 August 2013, ("**the Original Decision**")[1], the Commission approved liquidation aid for the resolution of AB Ukio Bankas ("**Ukio bank**" or "**the bank**").

(2) On 21 February 2014, the Lithuanian authorities reported that the Deposit Guarantee Fund ("**the Fund**")[2] had compensated the buyer of the assets and liabilities of Ukio bank with an additional LTL 128,5 million (EUR 37,2 million[3]) in cash over and above the limit approved by the Original Decision.

[1] Case SA.36248, Liquidation aid for the resolution of AB Ukio Bankas, OJ C 117, 16.04.2014, p. 1.

[2] Deposits at Ukio bank were insured by the State Enterprise "Deposit and Investment Insurance" up to the amount of EUR 100 000. The Fund is administered by that State Enterprise.

[3] All the conversion in the decision are made at a fixed exchange rate of EUR 1 = LTL 3,4528.

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(3) On the basis of multiple electronic mail exchanges, Lithuania notified that additional compensation on 28 April 2014.

(4) Between then and 6 June 2014, there have been several interactions between the Lithuanian authorities and the Commission services.

(5) Lithuania accepts that exceptionally the decision is adopted in English.

2. FACTS

2.1 Description of Ukio bank and AB Siauliu Bankas

(6) Ukio Bank was established in 1989. It was a small commercial bank providing banking, financial, investment, life-insurance and leasing services to individuals and companies. It operated mostly in Lithuania but had also three representation offices in Ukraine, Russia and Kazakhstan. Its ordinary shares were traded on the NASDAQ OMX Vilnius Stock Exchange since June 1998 and on the Official List since 13 July 2006.

(7) On 12 February 2013, when the Board of the Bank of Lithuania adopted a Resolution on the Moratorium of the Ukio bank restricting its activities and appointed a temporary administrator, the bank had 12 branches, 49 client service departments and 841 employees. Its total assets amounted to approximately LTL […][*] billion (EUR […] million). Its market share was 7,28% in deposits and 3,16% in loans at national level. On 2 May 2013, the court adopted a decision of the bankruptcy of Ukio bank. Further details of that process are set out in recitals 5 to 7 of the Original Decision.

(8) AB Siauliu Bankas ("**Siauliu bank**" or "**the buyer**") is a Lithuanian credit institution which just before the acquisition of Ukio bank, as of 31 December 2012, had LTL 2 931 million (EUR 848,9 million) of total assets, 162 000 customers, 14 branches, 42 client service units and 481 employees. Its market share at that time was 4,99% in deposits and 3,88% in loans at national level. Further details of its market position are set out in recitals 21 to 23 of the Original Decision.

2.2 Resolution Ukio bank through assets and liabilities sale to Siauliu bank

2.2.1 The aid approved by the Original Decision

(9) Following the appointment of a temporary administrator, on 12 February 2013 Siauliu bank acquired parts of assets and liabilities of Ukio bank ("**the Transfer Package**")[4] in an open competitive process[5]. Overall, approximately 80% of the assets and liabilities of Ukio bank were transferred to Siauliu bank. Because the liabilities in the Transfer Package exceeded the assets, in order to allow for the sale the Fund provided LTL 799 million (EUR 231,4 million) of cash injection to cover the difference between the liabilities and assets of Ukio bank transferred to the buyer. The remaining assets and liabilities of Ukio bank were put in special administration and liquidation ("**the Rump Ukio**").

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[*] Confidential information.

[4] For more detail of the Transfer Package see recitals 27 to 31 of the Original Decision.

[5] For more detail on the sale process see recitals 14 to 20 of the Original Decision.

2.2.2 Transfer Agreement

(10) The agreement between Ukio bank, Siauliu bank and the Fund for the transfer of assets and liabilities was made on the basis of a preliminary evaluation of the assets and liabilities. In order to secure the rights of the creditors of Ukio bank, that agreement foresaw, among others, the following safeguards in relation to the assets transferred to Siauliu bank:

a) An auditor, KPMG, would complete a comprehensive assessment and evaluation of the assets and liabilities of Ukio bank ("**final valuation**") by mid-August 2013. Following the final valuation, the initial consideration paid by the Fund would be revised and the adjusted consideration was to be calculated as the difference between the finally evaluated value of assets and liabilities assumed by Siauliu bank. If the initial consideration was higher than the adjusted consideration, Siauliu bank would pay Ukio bank the difference in cash. If the adjusted consideration was higher than the LTL 799 million, Siauliu bank could cover the difference by selecting any additional assets left in Ukio bank which Ukio bank would be obliged to transfer to Siauliu bank at a fair market value. If the value of assets acquired by Siauliu bank was not sufficient to cover the difference and Siauliu bank, Ukio bank and the Fund failed to agree on another solution, both the Fund and Siauliu bank could terminate the agreement for the transfer of assets and liabilities, in which case a full restitution would be effected;

b) If within a period of two years the assets transferred from Ukio bank to Siauliu bank were sold by Siauliu bank at a higher price than the acquisition price, Siauliu bank would repay 60% of the difference to Ukio bank.

(11) It was established that the final assessment and valuation of assets and liabilities would be performed under the same assumptions and methodology used in the preliminary evaluation. Siauliu bank had no role in the final assessment.

2.3 Additional compensation after the final valuation

(12) On 21 February 2014, the Lithuanian authorities reported that after the final valuation of the transferred assets and liabilities KPMG determined that the compensation for the buyer should have been LTL 128,5 million (ca. EUR 37 million) higher than the LTL 799 million approved in the decision (hence LTL 928 million in total)[6]. However, as confirmed by KPMG, the assets that remained in Ukio bank after the transaction were deemed unacceptable (in amount and quality)[7] for a transfer and hence could not serve as compensation to the buyer. Given that the alternative for the State was a much more costly restitution of the deal (which

[6] Following the results of the final valuation of assets and liabilities, the total fair value of assets transferred to Siauliu bank amounted to LTL 1 797 606 while the total amount of liabilities amounted to LTL 2 725 303.

[7] As of 31 December 2013, Ukio bank's assets amounted to LTL 301 million (EUR 87,1 million) and included the following categories of assets: i) Ukio bank's investments outside of Lithuania, ii) loans issued to the shareholders of the bank and persons associated with the shareholders of the bank, and iii) certain non-performing loans. Approximately 70% of those assets are problematic and have a number of related unresolved legal issues and are subject to on-going litigation procedures or are pledged to the creditors of Ukio bank. Approximately 20% of the assets remaining in Ukio bank are low-value objects for which the costs associated with their administration and realization would be disproportionate to their value. As a result, those assets have little or no relation to the banking business of Siauliu bank. The remaining 10% of the assets are funds recovered from the creditors of Ukio bank since the start of bankruptcy procedure and funds used for administration of the bank. All of those assets have been repeatedly reviewed by Siauliu bank and have been deemed unacceptable due to their composition and status.

was estimated by the temporary administrator as being between LTL [1-2] billion of costs to establish a State-owned bridge bank and LTL [2-3] billion of estimated costs of payment of insured deposits in case of liquidation of the whole bank), on 23 December 2013 the Lithuanian authorities, without prior consent from the Commission, agreed to compensate the buyer with LTL 128,5 million in cash provided by the Fund to Siauliu bank.

3 POSITION OF LITHUANIA

(13) Originally, the position of the Lithuanian authorities was that the additional compensation does not constitute State aid. Therefore it was implemented without prior notification to the Commission.

(14) After consultation with the Commission services, the Lithuanian authorities submitted a notification in which they recognise that the intervention of the Fund in Ukio bank may involve State aid but consider that such aid would be compatible with the internal market on the basis of Article 107(3)(b) of the Treaty on the Functioning of the European Union ("the Treaty"), as the intervention was necessary to remedy a serious disturbance in the Lithuanian economy.

4 ASSESSMENT OF THE MEASURES

4.1 Existence of State Aid

(15) The Commission must assess if the additional compensation of LTL 128,5 million constitutes new State aid. In line with the assessment of the measure in the Original Decision, the additional compensation for the liquidation of Ukio bank is imputable to the State (recitals 53 to 58 of the Original Decision), selective in nature (recital 60) and likely to affect trade between Member States and distort competition (recitals 61 and 62). The Commission therefore concludes that the additional compensation constitutes State aid.

(16) The Commission needs to identify the beneficiary of the measure.

(17) With regard to Siauliu bank, the Commission must assess whether it benefits from the LTL 128,5 million additional compensation as a purchaser of the assets and liabilities of Ukio bank. According to point 80 of the 2013 Banking Communication[8], in order to ensure that no aid is granted to the buyer of a financial institution or parts of it, it is important that certain requirements are met, and in particular that i) the sale process is open, unconditional and non-discriminatory; ii) the sale takes place on market terms; and iii) the State maximises the sale price for the assets and liabilities involved.

(18) The Commission already concluded in the Original Decision that those requirements were met and the conditions at which buyer purchased the assets and liabilities resulted from a competitive process. Now, it must now establish if the compensation received by Siauliu bank in the form of additional cash fell within the initially agreed contract.

(19) The purchase agreement contemplated an adjustment mechanism which could be applied both ways. It could be applied in favour of Siauliu bank, if the fair value of the purchased assets and liabilities assessed by auditor was lower than the fair value initially estimated, and against it, if the fair value was higher than that

[8] Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 2016, 30.07.2013, p. 1.

initially estimated. Therefore, the Member State and Siauliu bank as the successful bidder in the sales process had already established at the closing of the deal that if justified by the final valuation the buyer would be compensated for the difference between the market price of assets and liabilities by choosing extra assets from the Rump Ukio. Moreover, although the contract did not stipulate compensation in form of cash as such, it did specify that if a transfer of assets from Ukio bank to Siauliu bank would not cover the difference between assets and liabilities assumed by Siauliu bank as they were finally evaluated, Siauliu bank, Ukio bank and the Fund could find another solution. Ultimately, the buyer received as much as it was initially envisaged by means of the additional compensation. The payment in form of cash from the Fund to Siauliu bank, as an alternative solution, can be considered equivalent to a payment in kind (assets) given that the valuation of assets was done at fair value.

(20) In addition, according to the Lithuanian authorities, the final valuation of assets and liabilities was objective and impartial. The Commission received evidence that the auditor responsible for conducting both the preliminary and final valuation of assets acted independently and used a methodology and assumptions which were defined in advance.

(21) The Commission notes also that the total liquidation aid of LTL 928 million including the additional compensation remains less costly than liquidation of Ukio bank (for which the costs are estimated at between LTL [1-2] billion for establishing a temporary State-owned bridge bank and LTL [2-3] billion of compensation to insured depositors in case of bankruptcy).

(22) Therefore, on the basis of the information provided by Lithuania, the Commission considers that the Ukio sale process was open and competitive. Given that the adjustment paid upon final valuation was foreseen in the initial purchase contract, the transaction is aligned with the contract and therefore it is also the result of the open and competitive sale process. Siauliu bank has therefore not received any additional advantage.

(23) With regards to the Rump Ukio, that entity is under bankruptcy proceedings. As it no longer holds a banking license and cannot provide financial services, it no longer conducts economic activities in the market. Moreover, it cannot re-enter the market. It can therefore be concluded that Ukio bank is not a beneficiary under the present decision.

(24) On the other hand, with regard to the transferred assets and liabilities of Ukio bank, the Transfer Package accounts for a substantial part of Ukio bank's balance sheet (80%). It is made of both assets and liabilities and, more specifically, of a portfolio of customers which are incorporated into the buyer's business plan. Moreover, the buyer is also taking part of the bank's infrastructure (some client service units). The transferred business will therefore be allowed to continue providing the same range of banking and financial services to its customers as Ukio bank did before the sale ("**the legacy business**") and will clearly continue to carry out economic activity within the combined entity.

(25) The Commission therefore considers that the legacy business transferred to Siauliu bank is the beneficiary of the measure.

4.2 Legal basis for the compatibility of the aid

(26) Article 107(3)(b) of the Treaty empowers the Commission to find that aid is compatible with the internal market if it is intended "to remedy a serious disturbance in the economy of a Member State". 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[9]. The Commission confirmed that view by adopting the 2013 Banking Communication[10].

(27) In respect of the Lithuanian economy that assessment has been confirmed in the Commission's various approvals of the measures undertaken by the Lithuanian authorities to combat the financial crisis[11]. In addition, a disorderly liquidation of Ukio bank's business would create a serious disturbance for the Lithuanian economy.

(28) Therefore, the legal basis for the assessment of the measures is Article 107(3)(b) of the Treaty.

4.3 Compatibility

Compatibility of the measure with the Restructuring Communication

(29) The Restructuring Communication sets out the State aid rules applicable to the restructuring and winding-up of financial institutions in the current financial crisis. According to the Restructuring Communication, in order to be compatible with the internal market under Article 107(3)(b) of the Treaty, the restructuring of a financial institution in the context of the current financial crisis must (i) lead to a restoration of the viability of the bank, or to the orderly winding-up thereof; (ii) ensure that the aid is limited to the minimum necessary and include sufficient own contribution by the beneficiary (burden-sharing); and (iii) contain sufficient measures limiting the distortion of competition.

(30) Since the measure was granted on 23 December 2013, it falls within the scope of the 2013 Banking Communication, which lays down additional requirements in terms of burden-sharing and minimisation of the aid to the minimum.

4.3.1 Restoration of viability within Siauliu bank

(31) In the present case, the Lithuanian authorities have chosen to sell the selected assets and liabilities of Ukio bank via a competitive tender procedure and to resolve the remaining activities of Ukio bank. The Commission concluded in the Original Decision that the integration of the legacy business into Siauliu bank would enable the former's long-term viability to be restored[12]. Regarding the additional aid, the Commission considers that it enables the integration of the transferred activity into Siauliu bank to be finalised, given that without that aid the agreement would be terminated and therefore the liquidation of Ukio bank in its entirety would be

[9] This has been confirmed in the Banking Communication (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), the Recapitalisation Communication (Communication from the Commission – 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), the Impaired Asset Communication and the Restructuring Communication (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).

[10] Point 6.

[11] See e.g. Fifth prolongation of the Lithuanian bank support scheme – H1 2013 SA.36047 (2013/N), OJ C132, 9.05.2013, p.5.

[12] For more details of that assessment see recitals 67 to 77 of the Original Decision.

necessary. The Commission concludes that the additional aid, by allowing the integration into Siauliu bank, ensures the long-term viability of the legacy business.

Liquidation of Ukio bank

(32) While the selected assets and liabilities were transferred to Siauliu bank, the remainder of Ukio bank being under bankruptcy proceedings will be resolved and cease to exist. The bank will not pursue any new business.

4.3.2 Own contribution and burden-sharing

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

(34) The additional aid was determined by the final valuation of assets and liabilities performed by an auditor as had been initially agreed. The valuation was objective and impartial. The Commission received evidence that KPMG, which was responsible for conducting both the preliminary and final valuation of assets, acted independently and on the basis of a methodology and assumptions which were defined in advance.

(35) Under 2013 Banking Communication, equity, hybrid capital and subordinated debt holders must fully contribute to offset any losses. In this case, burden-sharing has been satisfied by the fact that the rest of Ukio bank has been put in liquidation and neither the shareholders nor the subordinated debt holders are expected to recuperate anything given the value of Ukio bank's assets and liabilities. The expected value of the assets is between LTL […] million and LTL […] million ([…]% of those assets are under litigation and the remainder are bad quality loans) as compared to the value of liabilities of around LTL 1 600 million (including LTL 93 million of subordinated loans and LTL 422 million of capital). In addition, the bank itself has contributed to the cost of restructuring by transferring […] proportion of its better quality assets to Siauliu bank.

(36) The additional cash injection can be compared with the alternative scenario of a termination of the agreement that could give rise to the liquidation of the whole bank (and costs of between LTL [1-2] billion for establishing a temporary State-owned bridge bank and LTL [2-3] billion of compensation to insured depositors in case of bankruptcy).

(37) The Commission thus concludes that the amount of aid can be deemed limited to the minimum necessary.

4.3.3 Limiting distortion of competition

(38) Finally, section 4 of the Restructuring Communication requires that the restructuring plan contains measures limiting distortions of competition. Such measures should be tailor-made to address the distortions on the markets where the beneficiary bank operates post-restructuring. The nature and form of such measures depend on two criteria: first, the amount of the aid and the conditions and circumstances under which it was granted and, second, the characteristics of the markets on which the beneficiary will operate. Furthermore, the Commission must take into account the extent of the Ukio bank's own contribution and burden-sharing over the restructuring period.

(39) The Commission considers that the LTL 128,5 million of additional aid does not affect the balance of burden-sharing as assessed in the Original Decision[13]. The nominal amount of the additional aid remains moderate and the competition distortion is mitigated by the fact that Ukio bank was a very small operator with a very limited market presence on the national Lithuanian market. The market share of the transferred assets amounts to merely 3% of the total Lithuanian banking sector assets. In addition the distortion of competition is mitigated by the competitive sale process.

(40) In light of the above, it can be concluded that the distortions of competition created by the aid are minimised.

4.4 Conclusions on the existence of aid and compatibility with the internal market

(41) The Commission concludes that the additional compensation to the buyer of Ukio bank, namely the cash injection of LTL 128,5 million, constitutes State aid in favour of the legacy business pursuant to Article 107(1) of the Treaty.

(42) The Commission finds that the liquidation aid in favour of the legacy business is compatible with the internal market for reasons of financial stability on the basis of Article 107(3)(b) of the Treaty.

5 CONCLUSION

The Commission notes that Lithuania put the State aid measure into effect, in breach of Article 108(3) of the Treaty. However, on the basis of the foregoing assessment, the aid measure is found compatible with the internal market pursuant to Article 107(3)(b) of the Treaty. The Commission therefore does not raise any objection against the State aid.

Lithuania exceptionally accepts that the present decision be adopted in the English language, for reasons of urgency.

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http://ec.europa.eu/competition/elojade/isef/index.cfm

[13] For more details of that assessment see recitals 88 to 94 of the Original Decision.

Your request should be sent by registered letter or fax to:

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Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President