

Italian Measures for the Stabilization of the Banking System

Milan/Rome
October 2008

In response to the global financial crisis, the Italian government recently adopted its bank stabilization and liquidity enhancement package, granting extraordinary powers to the Ministry of Economy and Finance (the “Ministry”). A first set of emergency measures was introduced after the October 7, 2008 “ECOFIN” meeting (Law-Decree No. 155 of October 9, 2008, or “Decree 155”), followed by another set of measures adopted on October 13, 2008 (“Decree 157”) in furtherance of the consensus reached at the Paris Eurozone Summit on October 12, 2008.¹

A. **Bank Recapitalization**²

Pursuant to Decree 155, the Ministry, under certain conditions (among others, the existence of a plan for the stabilization and strengthening of a bank’s financial soundness with a minimum duration of 36 months), is empowered to subscribe directly³ for newly issued shares of Italian banks that, according to the Bank of Italy, are undercapitalized (*inadeguatezza patrimoniale*).⁴

¹ Both decrees are effective from their respective dates of issuance, but must be ratified by Parliament within 60 days thereafter.

² Capital injections by EU Member States must comply with the state aid rules under the EC Treaty. On October 13, 2008 the European Commission released a communication regarding “the application of state aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis”. See the Alert Memorandum dated October 17, 2008 prepared by our Brussels Office (available at http://www.cgsh.com/european_commission_guidance_on_state_aid_and_the_financial_crisis/)

³ Within 30 days from the effective the date of Decree 155, the Ministry must issue regulations setting forth the conditions for the subscription of the shares. The Ministry’s implementing regulations will need to clarify whether the provisions described in this Section A. only apply with respect to direct share acquisitions by the Ministry or, more likely, also where the Ministry guarantees the subscription of a rights issue.

⁴ Prior to the Ministry’s intervention, the Bank of Italy will have to verify (i) the need for the bank to be recapitalized, (ii) the adequacy of the bank’s stabilization and strengthening plan and (iii) the consistency with such plan of the dividend policy approved by the bank’s shareholders for the period in which the plan is being implemented.

Decree 155 does not indicate a maximum amount set aside by the Government for the recapitalization initiatives. The resources necessary for each transaction will be identified by a decree of the Prime Minister.

The instruments to be issued to the Ministry will be preferred shares, with priority in dividend distributions.⁵

Once the Ministry becomes a shareholder, the bank's stabilization and strengthening plan may not be amended without the prior approval of the Ministry, following consultation with the Bank of Italy.⁶

With respect to shares acquired by the Ministry in cooperative banks, the statutory rules regarding participation limits (*e.g.*, the per-shareholder participation in a *banca popolare* may not exceed 0.5% of the bank's share capital) are suspended. Moreover, as long as the Ministry remains a shareholder, the one shareholder-one vote rule (regardless of the size of the interest held) shall not apply.⁷

Decree 155 also exempts the Ministry from the mandatory tender offer obligation applicable to a party acquiring more than 30% of the share capital of a listed company.

B. Bank Administration Procedures

Decree 155 provides that, if a bank incurs in a crisis situation (including a liquidity crisis) that could jeopardize the stability of the financial system, the Ministry may put it under extraordinary administration (*amministrazione straordinaria*), whereby the corporate bodies of the bank are replaced by two commissioners appointed by the Ministry, or compulsory administrative liquidation (*liquidazione coatta amministrativa*).⁸

⁵ Decree 155 is silent as to whether such preferred shares would be voting or non-voting instruments. Under Italian law, preferred shares generally entitle the holder to vote only in extraordinary general meetings. The actual regime applicable to these shares will need to be specified by the implementing regulations of Decree 155 and Decree 157.

⁶ Thus far, no bank has resorted to the government's equity participation program. Unlike other government programs, the Italian legislation does not contemplate executive compensation caps, nor does it impose minimum lending obligations on the recipient banks. However, such requirements might be introduced by the implementing regulations.

⁷ The wording of Decree 155 seems to repeal the one shareholder-one vote principle with respect to the interests held by any shareholder of a cooperative bank in which the Ministry invests (and not only to the shares acquired by the Ministry). This reading will need to be revisited in light of the implementing regulations of Decree 155 and Decree 157. This provision assumes that the interest that the Ministry would acquire in a cooperative bank would be a voting interest.

⁸ This measure extends to the liquidity crisis scenario the regime generally applicable to banks in case of significant management irregularities, material breaches of the law or by-laws, or extreme urgency and severe losses.

The Ministry may take the capital strengthening measures described in Section A above with respect to banks that have become subject to one of the procedures described in this Section B.

C. **Emergency Liquidity Assistance**

Decree 155 empowers the Ministry to guarantee loans granted by the Bank of Italy to Italian banks or Italian branches of foreign banks in order to cope with emergency liquidity crises.⁹

Further, if the Bank of Italy extends a secured loan to respond to the liquidity needs of a bank, the related security interest (pledge or assignment of receivables) is deemed to be duly perfected on the execution date of the security agreement, regardless of the compliance with the formalities required under Italian law to render security interests enforceable *vis-à-vis* the debtor and third parties. The Bank of Italy's secured loans are not subject to clawback under Italian insolvency rules.

D. **Government Deposit Guarantee**¹⁰

Decree 155 empowers the Ministry to issue, for a 36-month period following its effective date, state guarantees to depositors with respect to deposits held by Italian banks.¹¹ Such state guarantees on bank deposits would appear to supplement the existing bank-funded deposit guarantee schemes. Under Italian law, since 1996 the maximum guaranteed amount may not be lower than Euro 103,291.38 per depositor.¹² The new provision could be read as contemplating a general guarantee by the Italian government for all bank deposits regardless of their size. However, a more conservative reading would interpret this rule as a back-up guarantee in case of default of the deposit insurance schemes and, possibly, as an extension of the state guarantee to bank customer assets which are not covered by the deposit guarantee schemes.

⁹ According to the Bank of Italy, the emergency liquidity assistance program is a tool to grant credit as a last resort in extraordinary circumstances, absent any other market solution.

¹⁰ State guarantees covering the liabilities of financial institutions are subject to EU state aid rules (see footnote 2 above).

¹¹ Within 30 days from the entry into force of Decree 155, the Ministry shall issue regulations laying down the operating mechanisms of the guarantee.

¹² Membership of the *Fondo Interbancario di Tutela dei Depositi* is mandatory for Italian banks (other than cooperative banks, which have created a separate fund) and Italian branches of non-EU banks and is voluntary for Italian branches of EU banks.

E. **Further Stabilization and Liquidity Enhancement Measures**

Further to the measures agreed at the Paris Eurozone Summit, Decree 157¹³ empowers the Ministry, until December 31, 2009, to:

(i) guarantee, on market terms, bank liabilities with maturities of up to five years issued after October 13, 2008;

(ii) temporarily swap, on market terms, liabilities bearing the same features as the liabilities referred to in (i) and financial instruments held by banks, for Italian government bonds¹⁴; and

(iii) guarantee, on market terms, transactions carried out by banks in order to obtain securities eligible for refinancing with the European Central Bank.¹⁵

Prior to the Ministry's intervention, the Bank of Italy is required to assess the adequacy of the capital position of the applicant bank and its ability to meet its obligations.

The measures referred to in (i), (ii) and (iii) above may also be taken with respect to banks that have already undergone the recapitalization procedure described in Section A above.

The Ministry's claims arising from transactions entered into under (i), (ii) or (iii) above will be automatically secured by a first priority lien on all movable and immovable assets (*privilegio generale*) of the relevant bank.

¹³ Unlike Decree 155, Decree 157 does not set a deadline by which the implementing ministerial decrees must be issued.

¹⁴ In a press release issued on October 13, 2008 (the "[October 13 Press Release](#)"), the Bank of Italy announced that "in order to increase the recourse of banks operating in Italy to European Central Bank refinancing and augment the liquidity of their securities portfolios" it has decided "to activate a new facility for temporary swaps between government securities held by the Bank of Italy and assets held by Italian banks." According to the October 13 Press Release, "the transactions will be renewable, have a maturity of one month, and be remunerated with a 1 per cent fee on an annual basis. Banks will be able to swap debt instruments in various currencies and with a rating lower than that of eligible collateral with the European Central Bank. Transactions will be carried out twice a week and the facility's total amount may reach Euro 40 billion." The first swaps may be made starting from October 16, 2008.

¹⁵ The criteria, terms and conditions of the transactions referred to in (i), (ii) and (iii) will be determined by a Ministry decree, after consultation with the Bank of Italy. In the October 13 Press Release, the Bank of Italy also announced its decision to reduce from Euro 1,000,000 to Euro 500,000, with immediate effect, the minimum threshold for loans to be eligible for refinancing transactions, without prejudice to further adjustments in accordance with the European Central Bank guidelines.

Please do not hesitate to contact Giuseppe Scassellati-Sforzolini in our Rome office (+39 06 695 221) or Valentina Zadra in our Milan office (+39 02 726 081) should you have any questions concerning the above.

CLEARY GOTTLIEB STEEN & HAMILTON LLP

MILAN

Via San Paolo 7
20121 Milan, Italy
39 02 72 60 81
39 02 86 98 44 40 Fax

NEW YORK

One Liberty Plaza
New York, NY 10006-1470
1 212 225 2000
1 212 225 3999 Fax

WASHINGTON

2000 Pennsylvania Avenue, NW
Washington, DC 20006-1801
1 202 974 1500
1 202 974 1999 Fax

PARIS

12, rue de Tilsitt
75008 Paris, France
33 1 40 74 68 00
33 1 40 74 68 88 Fax

BRUSSELS

Rue de la Loi 57
1040 Brussels, Belgium
32 2 287 2000
32 2 231 1661 Fax

LONDON

City Place House
55 Basinghall Street
London EC2V 5EH, England
44 20 7614 2200
44 20 7600 1698 Fax

MOSCOW

Cleary Gottlieb Steen & Hamilton LLP
CGS&H Limited Liability Company
Paveletskaya Square 2/3
Moscow, Russia 115054
7 495 660 8500
7 495 660 8505 Fax

FRANKFURT

Main Tower
Neue Mainzer Strasse 52
60311 Frankfurt am Main, Germany
49 69 97103 0
49 69 97103 199 Fax

COLOGNE

Theodor-Heuss-Ring 9
50668 Cologne, Germany
49 221 80040 0
49 221 80040 199 Fax

ROME

Piazza di Spagna 15
00187 Rome, Italy
39 06 69 52 21
39 06 69 20 06 65 Fax

HONG KONG

Bank of China Tower
One Garden Road
Hong Kong
852 2521 4122
852 2845 9026 Fax

BEIJING

Twin Towers – West
12 B Jianguomen Wai Da Jie
Chaoyang District
Beijing 100022, China
86 10 5920 1000
86 10 5879 3902 Fax