

The EU Legal Framework for Crisis Management
A comparison with the Italian law

European Financial Markets Lawyers Group

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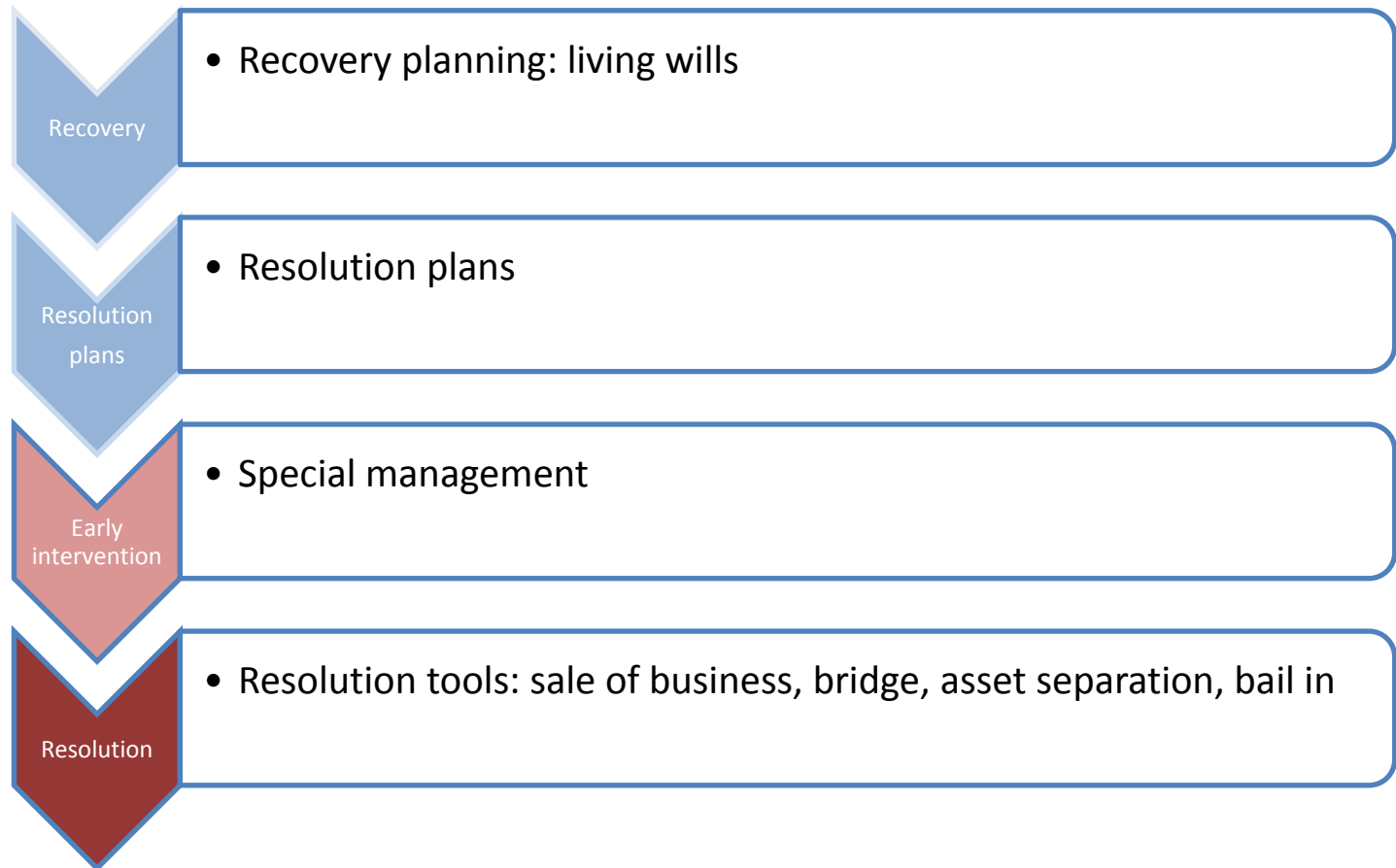
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The EU Framework for the Recovery and Resolution of Credit Institutions and Investment Firms

EU - Background

- G20 commitment: allowing an orderly exit from the market of failing banks; limiting the use of taxpayers' money for the bail –out;
- Target: in particular cross border banks;
- How: harmonization of national laws on recovery and resolution of credit institutions and investment firms: granting CAs the same tools to address systemic failures;
- Entry into force : 2015; bail in 2018;

EU - A gradual approach



EU -Recovery plans

Intra-group financial support

- Living wills: for the group and for each entity part of the group;
- Living wills to include arrangements for intra-group support;
- Intra- group support to be approved by supervisors and shareholders of all participating entities;
- Safeguards : supervisor of the transferor has the power to prohibit/ a transfer of assets if there is a threat to liquidity, solvency, or financial stability;
- Support to be triggered if there is reasonable prospect that it will redress the financial difficulties of the entity receiving support : restore financial viability of the group,

EU - Resolution planning

Preventative powers

- Resolution plans prepared by resolution authorities with supervisors;
- Plans with different scenarios: details on tools to be applied in critical situation;
- Powers to request firm to provide information on structure of bank/group (annex B);

EU - Resolution planning

Preventative powers

- Powers in cases where there are impediments to the resolvability of the entity:
 - Reducing the complexity through legal and operational structures in order to ensure the separation of critical functions;
 - SLAs to cover the provision of critical functions;
 - Limiting maximum individual and aggregate exposures;
 - Reporting requirements;
 - Limiting or ceasing activities;
 - Restricting or preventing the development of new business lines or products;
 - Issuing convertible capital instruments;

EU - Early intervention Special management

- **When financial situation/solvency is deteriorating, but still in going concern:**

1. Art. 136 CRD : increase capital requirements, applying specific provisioning policy, restructuring the business, operation or network, limiting bonus, reduction of risks in activities, products systems, use of profits to strengthen the capital base;

IN ADDITION

- Require the institution to implement measures of the recovery plan;
- Draw up action programme and timetable for implementation;
- Require management to convene , or convene directly, the shareholders' meeting, propose the agenda and the adoption of certain decisions;
- Require the institution to draw up a plan for restructuring of debt with creditors;

EU -Early intervention Special management

Stopping
bad
managem
ent and
decline

- Appointment of special manager to replace the management of the institution;
- Limited period of tie: 1 year;
- Duty to take all necessary measures and to promote solutions to redress the situation and restore sound and prudent management;
- Powers: increase of capital, reorganization of ownership structure, takeover by sound institutions;
- The appointment of a special managers is not an enforceable event according to FCD nor an insolvency proceeding;

EU -Resolution objectives

Authorities are required to choose the tools and powers that best achieve the following objectives:

- Ensuring continuity of critical functions;
- Avoiding effects on financial stability, including contagion and maintaining market discipline;
- Protecting public funds – minimising reliance on public support;
- Avoid unnecessary destruction of value and seek minimising the cost of resolution;
- Protect depositors and investors (DGD + ICS);
- Protect clients funds and assets;

EU – Resolution powers Art. 57

To require any person to provide information

To take control of an institution under resolution

To transfer shares and other instruments

To transfer debt instruments

To transfer to another person specified rights, assets or liabilities of an institution under resolution

To write down or convert the instruments referred to in Art 52 into shares

To reduce the principal amount of or outstanding amount due in respect of eligible liabilities

To cover eligible liabilities into ordinary shares

To cancel debt instruments

To cancel shares

To require an institution to issue new shares

To require the conversion of debt

To amend or alter the maturity of debt

To remove or replace the senior management

EU -Principles governing resolution

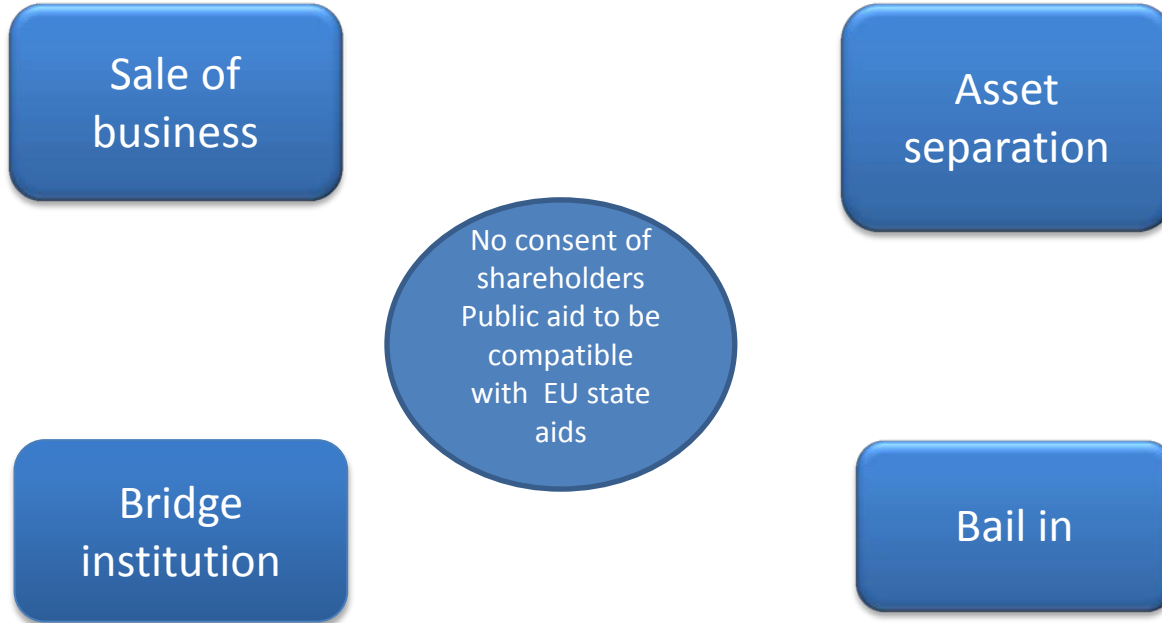
- Losses, once identified through a valuation process should be allocated between shareholders and creditors in accordance with the hierarchy of claims;
- Shareholders bear first losses;
- Creditors; creditors of the same class can be treated differently for public interest reasons (i.e. Financial stability); departure from insolvency law;
- Specific hierarchy for bail in;

EU -Resolution triggers

Conditions:

- The institution is failing or likely to fail;
- Having regard to timing and other relevant circumstance, there is no reasonable prospect for an alternative private sector or supervisory action other [...] that would prevent the failure;
- Resolution is in the public interest;
- Failing or likely to fail:
 - The institution is in breach or will be in breach on CRD: withdrawal of authorization, because the institution is likely to incur into losses that will deplete all or substantially its own funds;
 - Assets will be less than liabilities;
 - The institution will be unable to pay its obligations;
 - Extraordinary public financial support is required.

EU -Resolution tools



EU- Bail in

Statutory, comprehensive approach

Purposes

- a) Recapitalising the institution to the extent sufficient to comply with the conditions of its authorization or
- a) Converting to equity or reduce the principal amount of claims or debt instruments that are transferred to a bridge institution;
- a) **Only if there is a realistic prospect that bail in with other tools will restore the long term viability of the bank and its financial soundness.**

EU- Bail in - Scope

Scope: all liabilities that are not excluded. Excluded liabilities:

Guaranteed deposits

Secured liabilities

Any liability arising from client assets/money

Liabilities with original maturity of less than 1 month

Liabilities arising from labour contracts; commercial or trade creditor for the provision of goods/services essential for daily functioning; taxes and social security authorities;

Derivatives: in principle in the scope, with the possibility to exclude them if their inclusion will not help achieving continuity of critical functions or ensuring financial stability, preventing contagion...

EU – Bail in

Minimum amount ; hierarchy

Institutions should have at all time a sufficient minimum requirement for liabilities subject to bail in: percentage to be established by resolution authorities;

Hierarchy of claims:

- Equity
- Additional T1
- Tier 2
- Subordinated debt that is not AT1 or T2
- Subordinated senior debt

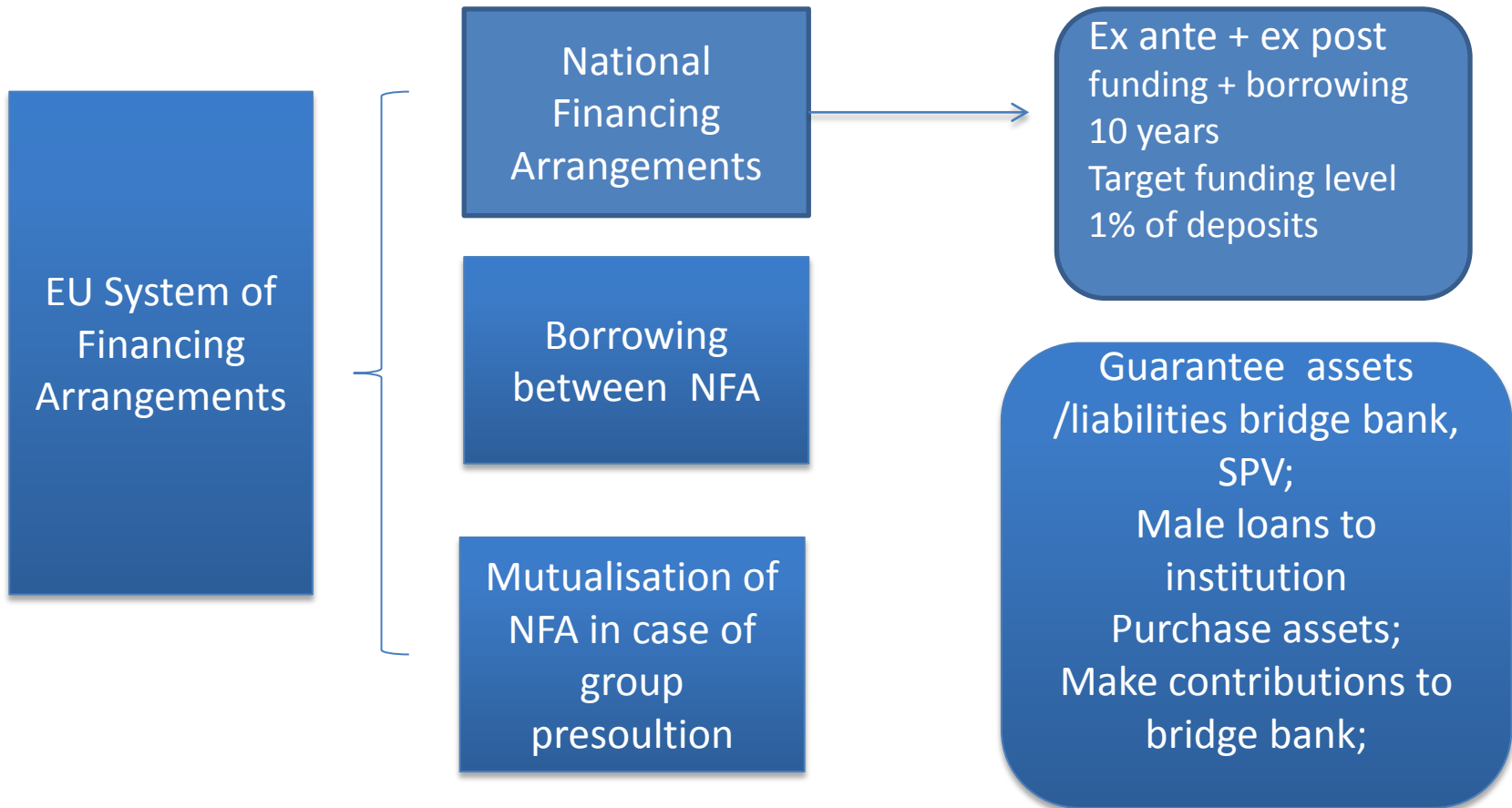
EU – Bail in

Safeguards on contracts

- Powers to temporarily suspend the termination rights against a failing institution under resolution: until 5 pm next day;
- Termination rights on contracts remaining within the failing institution would resume at the end of the suspension period; however;
- Transfer to a third party (sale of asset or bridge bank) is not an event of default triggering termination right;
- Protection of financial collateral, set off and netting agreements;
- Protection of security arrangements and structured finance arrangements;
- Protection of market infrastructures;

EU

EU System of Financing Arrangements

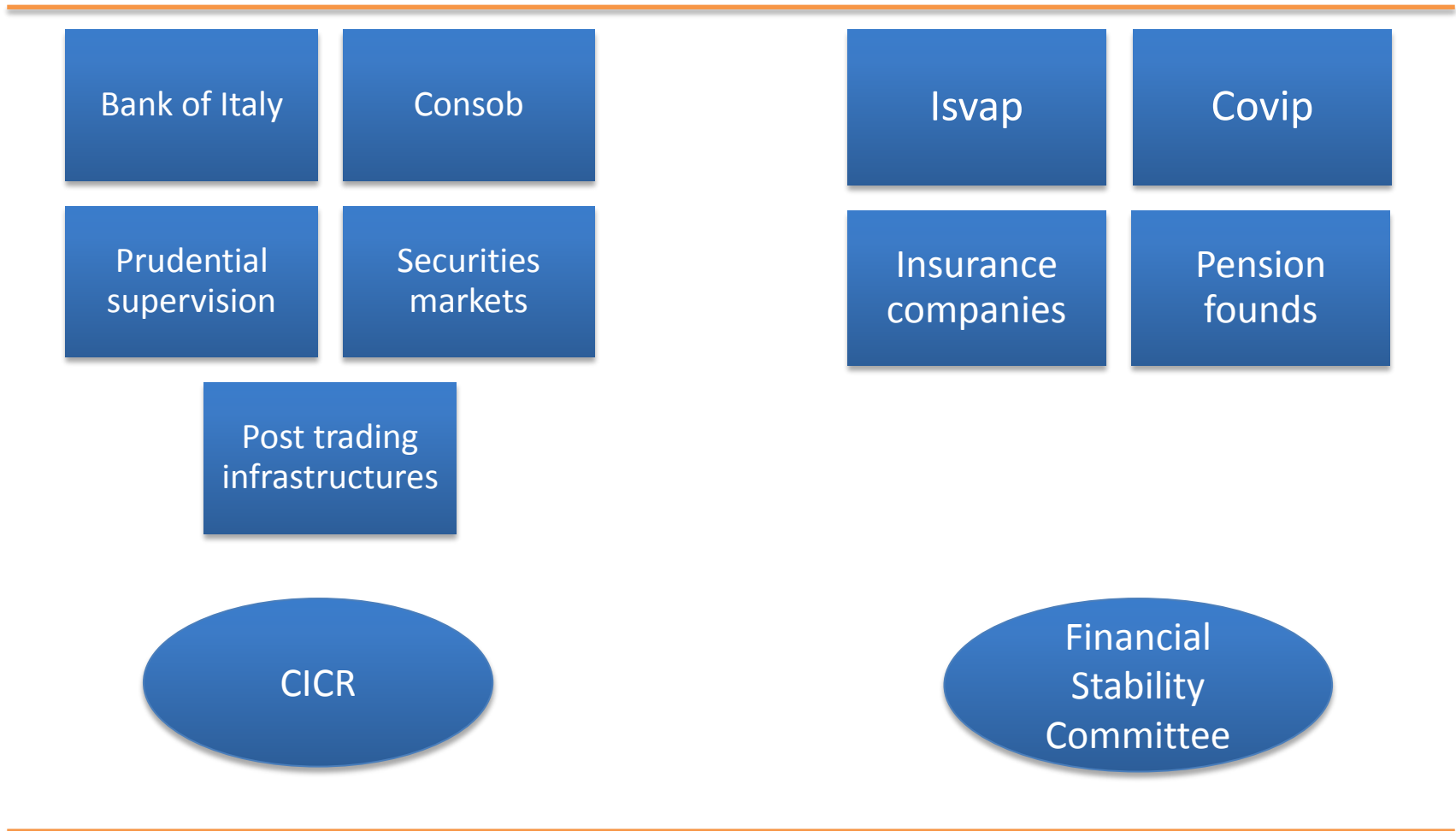


The Italian Legal Framework for Crisis Management

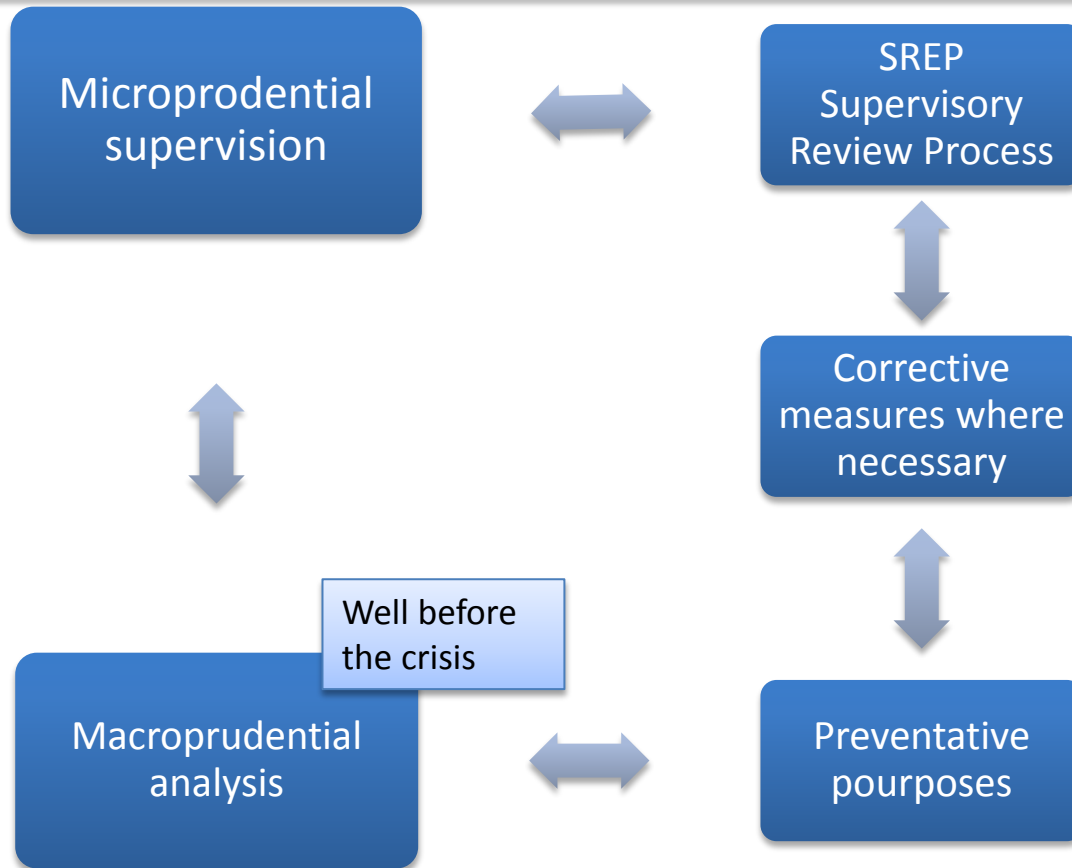
Crisis management in Italy

- Banking Consolidated Law Dlg 385/1993 provides with a toolkit of measures to be used in case of banking difficulties;
- Competent authority: Bank of Italy (supervisory and resolution authority);
- Crisis management: part of the objective of ensuring the sound and prudent management of the intermediaries, stability, efficiency and competitiveness of the financial system;

IT -The supervisory set up



IT - Supervisory methodology



IT - Supervisory powers – going concern

Ordinary powers Art. 53
TUB

Corrective actions

Proportional
approach

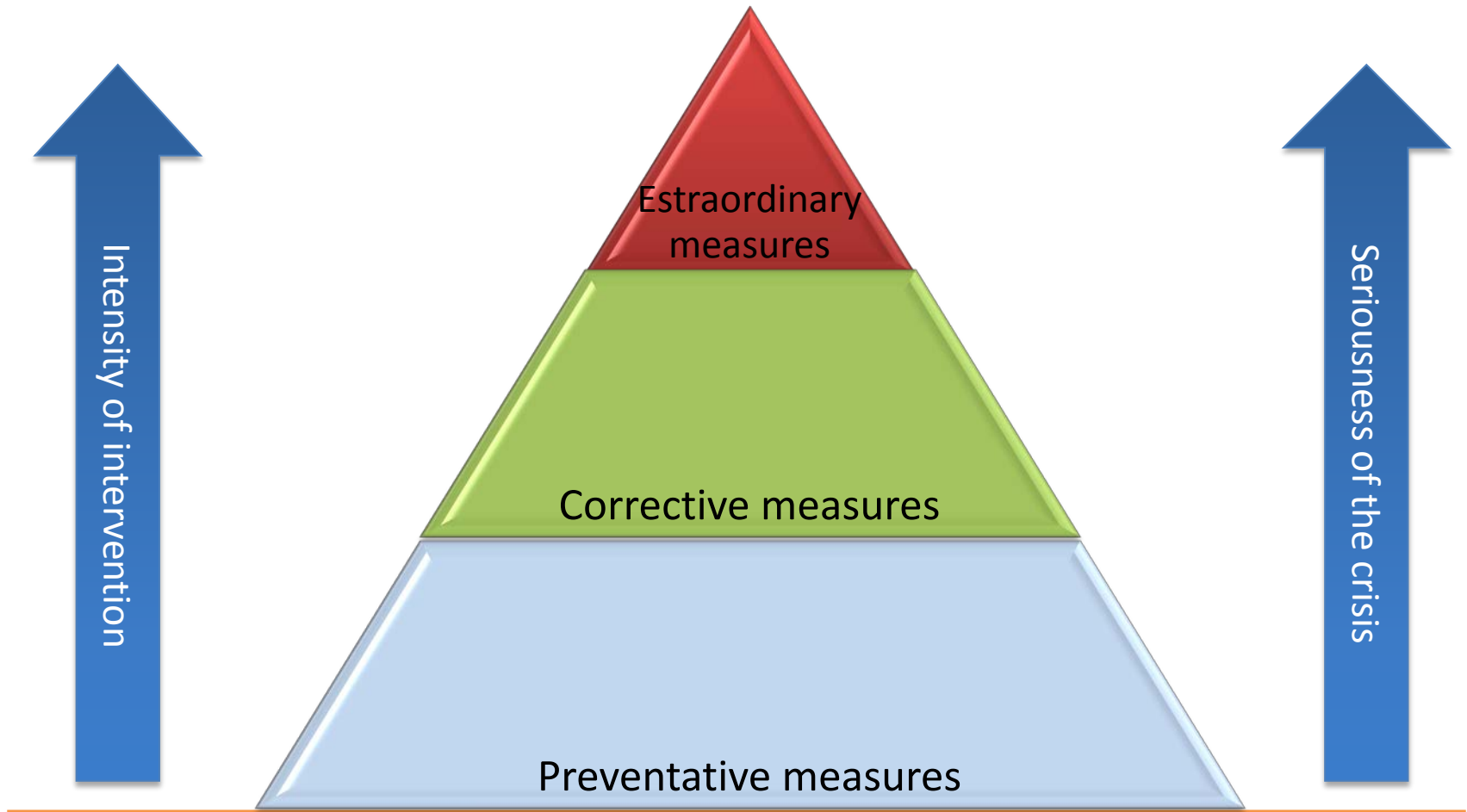
Convene directors , members of the board of auditors, managers to examine the situation;

Convening the gov bodies of the bank; set the agenda and proposing the adoption of certain decisions:
replacing board members and auditors, reorganisation of activities, requalification of businesses, reduction of costs, increase capital, prohibition of dividends' distribution; mergers with other institutions;

Require capital requirements higher than minimum; restrictions on certain transactions;

Art.78 Prohibition from undertaking new transactions or order the closure of branches not complying with law;

IT - The graduation of the forms of intervention



Bank of Italy managing crisis/supervisory approach

- Protection of business continuity (through M&A, purchases and assumptions);
- Preserve market discipline: priority to private sector solutions;
- Reducing moral hazard: DGS are financed by banks;

IT - Crisis management tools

Special administration

- Replacement of management and controlling bodies
- Qualitative and quantitative triggers
- Max 2 years

Provisional administration

- Emergency situation: Bank of Italy to propose replacement of management and controlling bodies
- Qualitative and quantitative triggers
- Max 2 months

Compulsory administrative liquidation

- Irreversible crisis situation, last resort measure
- Exceptionally serious irregularities, declaration of insolvency
- Withdrawal of banking licence, bank ceases to exist, liquidation of assets and liabilities

IT - Crisis management tools

Special administration

Triggers : qualitative and quantitative	Serious administrative irregularities, violation of laws, [...] Forecast of serious capital losses; Request by administrative bodies or EGM;
Effects (going concern)	Replacement with special administrators and set up of oversight committee;
Aims of the procedure	Ascertaining the bank's situation Eliminating irregularities; Promoting solutions in the interest of depositors;
Procedure	Bank of Italy – Decree of MEF; Max 2 years;

IT - Special administration

Scenarios



Bank will go back to ordinary administration (reorganization plan)

Acquisition of control by an other bank

Merger with an other bank

Voluntary / compulsory administrative liquidation

Bank of Italy powers

Oversees the special bodies management and the follows up the procedure;

Issues instructions to special bodies in order to establish special safeguards or limitation on the management of the bank;


Authorises important decisions of the special bodies;

Authorizes the convening of shareholders 's meeting for decision related to the solution of the crisis;

Approves the financial statements drawn up by the special bodies at the end of the proceeding.

IT - Crisis situation

Provisional management

 <p>Provisional management</p>	Triggers (qualitative and quantitative)	Same as for special administration
	Effects (going concern)	Replacement with special administrators and set up of the oversight committee
	Aims of the procedure	Ascertaining whether the irregularities can be overcome; Suspension of administrative bodies;
	Procedure	Officers of Bank of Italy may be appointed as administrators. 2 months.

IT - Compulsory Administrative Liquidation

Crisis :
irreversible situation
Compulsory
Administrative
Liquidation



Triggers	Exceptionally serious administrative, management irregularities and violation of laws, regulation, by laws Forecast of exceptionally serious losses of capital Request by administrative bodies or EGM; Declaration of insolvency by a court;
Procedure	Proposal of Bankit to MEF; MEF's Decree revoking banking licence; Appointment of liquidators and oversight committee; Judicial declaration of insolvency;
Aims of the procedure	Liquidation of the bank ; the bank ceases to exist; assessment of liabilities of the bank , liquidation of the assets and payment to creditors

IT - Compulsory Administrative Liquidation

Compulsory Administrative Liquidation

Effects

On corporate bodies: banking activity is interrupted; existing corporate bodies are replaced by liquidator(s);

On the bank: suspension of payment of liabilities as from the entering into force of liquidating bodies;

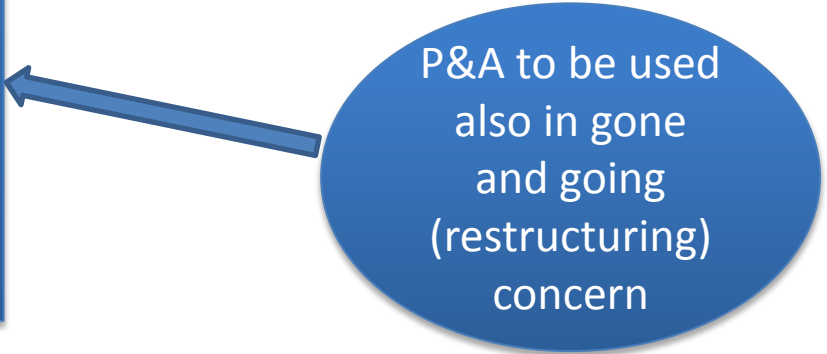
On creditors: rules on concursus creditorum;

On contracts: liquidators have the power to suspend not enforced contracts;

IT - Liquidation of assets

Liquidation by assets (piece meale liquidation);
Bulk sale;
Securitisation of assets;
Transfer of assets and liabilities to another bank;
Transfer of insured deposits to another bank (P&A) ;

P&A to be used
also in gone
and going
(restructuring)
concern



IT - Powers of Bank of Italy

- Ascertainment of the existence of requirements for triggering the compulsory liquidation and proposal to MEF;
- Appointment , removal or replacement of liquidators and members of the oversight committee;
- Issuing of guidelines for the implementation of liquidation and authorization of certain decisions to be taken by the oversight committee;
- Authorization for launching legal liability action against members of the dissolved board/governing bodies;
- Examination of annual report and of liquidation report (to be drafted according to Bankit instructions).

IT - Banking group

- Art. 60 Banking group : composed either by mother company (bank) or by holding company controlling banks and other companies;
- Art.61(4): mother company exerts a **managing and coordination** function: it issues rules addressed to the members of the Group aimed at implementing Bank of Italy instructions (pv stability of the Group);
- Rules for crisis management aim at ensuring a coordinated and single approach for the Group;
- Crisis management procedures (special administration or compulsory liquidation) can be triggered both at mother company level and subsidiary level.

Bail in

- Last resort resolution tool: gone concern scenario
- Closed bank scenario only: to set up a bridge bank
- Application: based on objective pre-determined trigger criteria
- Activation: judgment of competent authorities
- Bail in to liquidate institutions that cannot be wound down through other tools

Thank you for your attention!

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