



OPINION OF THE EUROPEAN CENTRAL BANK

of 3 February 2017

**on liquidity support measures, a precautionary recapitalisation and other urgent provisions for
the banking sector
(CON/2017/01)**

Introduction and legal basis

On 27 December 2016 the European Central Bank (ECB) received a request from the Italian Minister of Economy and Finance (hereinafter the 'Minister') for an opinion on a Decree law on urgent measures for the protection of savings in the banking sector (hereinafter the 'Decree law'). The Decree law was adopted by the Italian Government on 23 December 2016 and has already entered into force. The Decree law must be converted into law by the Parliament within 60 days of publication in the Gazzetta Ufficiale, and amendments may be introduced during this conversion process.

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the third and sixth indents of Article 2(1) of Council Decision 98/415/EC¹, as the Decree law relates to (1) the European System of Central Banks' (ESCB's) basic task of implementing the Union's monetary policy pursuant to Article 127(2), first indent, of the Treaty, (2) the specific tasks conferred upon the ECB pursuant to Article 127(6) of the Treaty concerning policies relating to the prudential supervision of credit institutions, (3) the Banca d'Italia and (4) rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the Decree law

1.1 The Decree law envisages a number of urgent measures affecting the banking sector. The most significant measures aim to establish a legal framework to provide extraordinary public financial support to Italian banks² under the conditions and within the limits set by Regulation (EU) No 806/2014 of the European Parliament and of the Council³ (hereinafter the 'SRM Regulation') and

¹ Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions (OJ L 189, 3.7.1998, p. 42).

² Banks having their registered office in Italy. See Article 1(2) of the Decree law.

³ Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010 (OJ L 255, 30.7.2014, p. 1).

the Italian transposition of the Bank Recovery and Resolution Directive (hereinafter the 'BRRD')⁴, according to which, in order to remedy a serious disturbance in the economy of a Member State and preserve financial stability, the provision of such public financial support does not imply that the receiving bank is failing or likely to fail for the purposes of triggering a resolution action. While the extraordinary public support is available to all Italian credit institutions fulfilling the relevant criteria under the Decree law, the first beneficiary under the framework is intended to be Banca Monte dei Paschi di Siena (hereinafter 'MPS'), and the Decree law contains specific provisions for the application of the measures to MPS. The Decree law provides for three categories of extraordinary public intervention, which reflect the three forms envisaged in Article 18(4)(d) of the SRM Regulation and Article 32(4)(d) of the BRRD: liquidity support provided by (1) a State guarantee of banks' newly issued liabilities⁵ or (2) a State guarantee of emergency liquidity assistance (ELA) operations conducted by the Banca d'Italia⁶, or (3) a precautionary recapitalisation⁷, whereby the State injects capital into a bank by subscribing to and purchasing its ordinary shares.

1.2 *Liquidity support measures*

The Decree law establishes the conditions and the procedure for the Ministry of Economy and Finance (hereinafter the 'Ministry') to guarantee the liabilities of Italian banks until 30 June 2017⁸. Such a State guarantee may only be issued for debt instruments which meet the criteria defined by the Decree law and which also have a residual maturity of no less than three months and no more than five years (or seven years in the case of covered bonds)⁹, and will never be provided for liabilities that may qualify as regulatory own funds¹⁰. The amount of any such guarantee is limited to what is strictly necessary to restore the bank's medium- to long-term funding capacity and, in general, must not exceed regulatory own funds¹¹. The criteria and limitations set out in the Decree law are largely derived from the Commission's Communication on applying State aid rules in the context of the financial crisis (hereinafter the '2013 Banking Communication')¹².

1.3 Further to the 2013 Banking Communication, the procedure for requesting a State guarantee is subject to different requirements, depending on the bank's situation¹³. Support may be provided through a guarantee scheme authorised *ex ante* by the Commission to banks which (1) meet own

⁴ Directive 2014/59/EU of the European Parliament and of the Council of 15 July 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council (OJ L 173, 12.6.2014, p. 190).

⁵ See Article 32(4)(d)(ii) of the BRRD and Article 18(4)(d)(ii) of the SRM Regulation.

⁶ See Article 32(4)(d)(i) of the BRRD and Article 18(4)(d)(i) of the SRM Regulation.

⁷ See Article 32(4)(d)(iii) of the BRRD and Article 18(4)(d)(iii) of the SRM Regulation.

⁸ This date may be further extended by a maximum of six months by a decree issued by the Ministry, subject to prior approval of the European Commission. See Article 1(4) of the Decree law.

⁹ See Article 2 of the Decree law.

¹⁰ See Article 5 of the Decree law.

¹¹ See Article 3 of the Decree law.

¹² See the European Commission's 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 ('Banking Communication') (OJ C 216, 30.7.2013, p. 1), in particular paragraphs 59 and 60.

¹³ See Article 4 of the Decree law, which reflects paragraph 57 et seq. of the 2013 Banking Communication.

funds requirements under Article 92 of the Capital Requirements Regulation (CRR)¹⁴ and (2) do not have a 'capital shortfall' (which means a current or potential inadequacy of own funds with respect to the requirements of Article 92 of the CRR in combination with any other specific mandatory requirements established by the competent authority) according to a national, Union or Single Supervisory Mechanism-wide stress test or asset quality review. Access to the State guarantee for banks which do not meet either of these two criteria, but which nevertheless have positive equity and are in urgent need of liquidity support, is subject to an individual notification and approval by the Commission¹⁵. The relevant competent authority, namely the ECB or the Banca d'Italia, depending on the significance of the requesting credit institution for purposes of Council Regulation (EU) No 1024/2013¹⁶ (hereinafter the 'Single Supervisory Mechanism (SSM) Regulation'), assesses the fulfilment of these criteria. All other aspects of the bank's application, both for significant and less significant institutions, are managed by the Banca d'Italia. Where the application is subject to individual notification, or in any situations where the nominal amount of the instruments for which the guarantee is requested exceeds EUR 500 million and 5 % of the total liabilities of the bank, a restructuring plan must be submitted by the bank within two months of the guarantee being issued, confirming the bank's profitability and funding capacity in the long term without public support¹⁷. The restructuring plan must be assessed by the Commission. A restructuring plan is also required whenever the Ministry is notified of a request to activate the guarantee, and in such situations the plan must be provided within two months of the activation request¹⁸.

- 1.4 Under the Decree law, the Minister is also authorised to issue a guarantee to supplement the collateral, or its realisation value, mobilised by Italian banks to guarantee ELA operations conducted by the Banca d'Italia, in compliance with the systems established by the ECB.¹⁹ A bank benefitting from the guarantee on ELA is required to submit a restructuring plan confirming its profitability and funding capacity in the long term without public support, in order, in particular, to limit reliance on temporary liquidity assistance provided by the Banca d'Italia.

1.5 *Precautionary recapitalisation*

Under the Decree law, the Ministry is authorised, until 31 December 2017, to intervene by means of a precautionary recapitalisation of a bank, by subscribing to or purchasing shares issued by Italian banks or parent undertakings of banking groups²⁰. Such intervention may only be requested

14 Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

15 An individual approval is also required to access the measure for banks under resolution and bridge banks: see Article 4(3) of the Decree law.

16 See Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (OJ L 287, 29.10.2013, p. 63).

17 See Article 7(5) of the Decree law.

18 See Article 8(3) of the Decree law, reflecting para. 59(e) of the 2013 Banking Communication.

19 See Articles 10 and 11 of the Decree law.

20 See Article 13(2) of the Decree law.

- by a bank which, based on an adverse scenario under a national, Union or SSM-wide stress test exercise, needs to strengthen its capital²¹.
- 1.6 Prior to the request for State support, a bank is required to submit a capital raising plan to the competent authority, namely the ECB for significant credit institutions and the Banca d'Italia for less significant institutions. The adequacy of the plan is assessed by the competent authority, which must inform the bank and the Ministry of its assessment. If the plan is assessed as being insufficient, the bank may directly request State intervention. If the plan is assessed as being sufficient, the bank must implement the plan and update the competent authority regarding the results of the measures adopted; the Ministry is informed of the outcome by the competent authority. If the measures prove to be insufficient to achieve the plan's objectives, even before they are fully completed, the bank may submit a request for State intervention.²²
- 1.7 The request for State intervention must be submitted to the Ministry and to the competent authority, including the ECB in the case of significant credit institutions (and to the Banca d'Italia in such cases, where it is not the competent authority), and must include, *inter alia*²³: (1) a list of the bank's instruments and loans which would be subject to burden-sharing measures, indicating their economic value; (2) an estimate of the actual value of the bank's assets and liabilities, for the purposes of assessing compliance with the 'no-creditor-worse-off-than-in-insolvency' principle; and (3) a restructuring plan, drawn up in accordance with the Union's State aid framework. Within 60 days of receiving the request for State intervention, the competent authority must communicate to the bank and to the Ministry the bank's regulatory capital need²⁴.
- 1.8 The precautionary recapitalisation is conditional on the Commission's approval of the restructuring plan pursuant to the Union's State aid framework, and is executed via two decrees issued by the Minister. The precautionary recapitalisation may only be implemented if the bank is not deemed to be failing or likely to fail and there are no grounds for write-down or conversion under the Italian transposition of the BRRD or the SRM Regulation. Banks will be regarded as not being in either of these situations in the absence of any statement to that effect by the competent authority²⁵.
- 1.9 While in principle only newly issued shares may be subscribed by the Ministry²⁶, the Decree law authorises the Ministry to purchase shares resulting from the conversion of subordinated instruments in the implementation of the burden-sharing measures²⁷.
- 1.10 *Collateralisation of the Banca d'Italia's liquidity operations*
- The Decree law amends the Italian transposition²⁸ of Directive 2002/47/EC of the European Parliament and of the Council²⁹, by introducing, for operations conducted by the Banca d'Italia to

21 See Article 14(1) of the Decree law.

22 See Article 14 of the Decree law.

23 See Article 15 of the Decree law.

24 See Article 16(1) of the Decree law.

25 See Article 18(6) of the Decree law.

26 See Article 19(1) of the Decree law.

27 See Article 19(2) of the Decree law. Such purchases are allowed in the context of a settlement mechanism envisaged by the Decree Law in order to end or prevent disputes between the bank and the retail holders of its subordinated instruments which have been converted into shares.

28 Legislative Decree no. 170/2004 (*Gazzetta Ufficiale* No 164, 15.7.2004).

address liquidity needs and secured by the pledge of a credit claim or a loan assignment, a special regime³⁰ for the Banca d'Italia, on: (i) the effects *vis-à-vis* third parties of the pledge or the loan assignment, which is more favourable than the ordinary regime laid down in the Italian Civil Code, and (ii) the inapplicability of bankruptcy provisions on clawback actions. Moreover, the Decree law introduces a new provision that excludes the exercise of set-off rights against the Banca d'Italia for claims *vis-à-vis* the assignor or the pledgor of collateral³¹.

1.11 *Assessments of contributions due to the national resolution fund*

Finally, the Decree law confers on the Banca d'Italia the power to determine additional contributions to be paid to the national resolution fund to cover any obligations, losses, costs or any other liabilities borne by the fund in relation to the resolution actions³².

2. General observations

2.1 *Proper timing to consult the ECB*

The ECB only received the consultation request on 27 December 2016, despite the fact that the Decree law entered into force on 23 December 2016. As underlined in several ECB opinions³³, the ECB must be consulted at an appropriate stage in the legislative process. Consultation should take place at a time that enables the relevant national authority to take the ECB's opinion into account before the provisions in question are adopted³⁴. In the Italian legal system, a decree law, adopted by the Government, enters into force following publication in the *Gazzetta Ufficiale* and must be submitted on the same day of adoption to Parliament for conversion into law. If not converted within 60 days of publication, the decree law is rendered invalid *ab initio*. Amendments may be introduced during the conversion process. In the light of the foregoing, the ECB should be consulted before the adoption of a decree law by the Government.

2.2 *Compliance with the Union's legal framework*

National legislative provisions aimed at providing public support to the banking sector need to fully comply with Union law, including the criteria governing the provision of extraordinary public financial support to credit institutions under the SRM Regulation and the BRRD and the related communications of the Commission on the application of State aid rules to support measures for banks.

2.3 *The role of the ECB as competent supervisory authority*

The Decree law envisages a role for the ECB, as the competent supervisory authority for significant

²⁹ Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements (OJ L 168, 27.6.2002, p. 43).

³⁰ This regime was already in force on the basis of temporary provisions.

³¹ See Article 26(1)(b) of the Decree law, amending Article 3 of Legislative Decree no. 170/2004.

³² See Article 25 of the Decree law.

³³ See, for example, ECB Opinion CON/2012/64. All ECB opinions are available on the ECB's website at www.ecb.europa.eu.

³⁴ See the second sentence of Article 4 of Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions (OJ L 189, 3.7.1998, p. 42); see also paragraph 4.1 of the Guide to consultation of the European Central Bank by national authorities regarding draft legislative provisions, which is available on the ECB's website at www.ecb.europa.eu.

banks within the Single Supervisory Mechanism, in the procedures leading to the provision of public support by the State, including the assessment of the fulfilment of the own funds requirements, the determination of the size of the capital shortfall in the light of the results of the relevant stress test exercise and the review of the adequacy of banks' capital raising plans submitted prior to the application for precautionary recapitalisation. The ECB emphasises that its role in this respect is derived from Union rather than national law, in particular the SSM Regulation. In principle, national law cannot on its own, without proper support in EU law, transfer responsibilities to a Union institution such as the ECB. The attribution of the role envisaged for the ECB under the Decree law is broadly consistent with the specific prudential supervisory tasks conferred on the ECB under the Union legal framework governing banking supervision. The ECB understands the provisions of the Decree law conferring certain obligations on the competent authority as, in the case of the ECB, requests that the ECB may choose to comply with at its discretion, in accordance with the principle of sincere cooperation under Article 4(3) of the Treaty on European Union, whereby the Union and the Member States shall, in full mutual respect, assist each other in carrying out tasks which flow from the Treaties. The ECB stresses the importance of ensuring cooperation and the exchange of information between the Italian authorities and the competent supervisory authority, in accordance with this framework.

2.4 *Consultation of the ECB on future implementing rules under the Decree law*

The ECB understands that the Minister may adopt implementing rules on the provisions of the Decree law³⁵. In this respect, the ECB expects to be consulted on significant proposed implementing rules to be adopted on matters falling within the ECB's fields of competence³⁶.

3. **Specific observations on the liquidity support measures**

3.1 *Interaction of the State guarantee with the monetary policy of the euro area*

As stated in previous opinions on guarantee schemes for the liabilities of banks³⁷, the ECB reminds the consulting authority that government guarantees for bank debt should, when implemented: (i) address the funding problems of liquidity-constrained solvent banks by improving the functioning of the market for bank debt of longer-term maturities; (ii) preserve the level playing field among financial institutions and avoid market distortions; and (iii) ensure consistency in the management of Eurosystem liquidity. In this regard, it is stressed that it is of the utmost importance that support operations conducted by national authorities do not in any way affect the conduct and the implementation of monetary policy in the euro area³⁸.

³⁵ See Articles 12 and 23(1) of the Decree law.

³⁶ See the definition of 'draft legislative provisions' in Article 1(1), and also the sixth indent of Article 2(1) of Decision 98/415/EC.

³⁷ See paragraph 3 of Opinion CON/2012/4.

³⁸ In particular, the ECB reiterates its view, already stated in various opinions, that the extension of a State guarantee to cover interbank deposits should be avoided, as this could entail distortions in national segments of the euro area money market (see, for example, paragraph 3.1 of Opinion CON/2009/73).

3.2 *Minimum maturity of debt instruments benefiting from a State guarantee*

While the ECB understands that a State guarantee would only be available for debt instruments with a residual maturity of at least three months, the ECB notes that a separate provision of the Decree law envisages the provision of guarantees that are limited to financial instruments with a maturity not exceeding two months³⁹. The ECB suggests that the Decree law be clarified in order to remove any legal uncertainty which may arise in this respect.

3.3 *Emergency liquidity assistance operations collateralised by a State guarantee and the prohibition of monetary financing*

Regarding the provisions of the Decree law authorising the Minister to provide a State guarantee on ELA loans provided by the Banca d'Italia, the ECB notes that ELA, granted by a Eurosystem national central bank (NCB) independently and at its full discretion to a solvent financial institution on the basis of collateral security in the form of a State guarantee, is in principle possible, provided that a number of conditions are met in order to ensure the NCB's compliance with the monetary financing prohibition under Article 123 of the Treaty⁴⁰. The relevant conditions are the following: (i) it must be ensured that the credit provided is as short term as possible; (ii) there must be systemic stability aspects at stake; (iii) there must be no doubts as to the legal validity and enforceability of the State guarantee under the applicable national law; and (iv) there must be no doubts as to the economic adequacy of the State guarantee, which should cover both principal and interest on the loans, thus fully preserving the NCB's financial independence⁴¹. These elements are reflected in the Decree law, including the State guarantee's aim of preserving financial stability, and that the guarantee must be irrevocable and cover the principal amount of the loan and any interest. It is noted that the guarantee is not a first demand guarantee, but rather benefits from the prior execution, by the Banca d'Italia, of the collateral mobilised by the bank in order to access ELA funding.

3.4 *The definition of capital shortfall in the context of a request for a State guarantee*

Regarding the definition of 'capital shortfall' in the context of a request for a State guarantee, the ECB understands that this definition encompasses, in line with pre-existing supervisory decisions and practice, the threshold used in the relevant national, Union or SSM-wide stress test or asset quality review which combines own funds requirements under Article 92 of the CRR with the additional benchmarks established by the competent authority.

4. **Specific observations on the precautionary recapitalisation**

4.1 *The need to inform the Ministry of the outcome of the assessment of a capital raising plan*

The ECB understands that the requirement, under Article 14 of the Decree law, to inform the Ministry of the outcome of the assessment of the capital raising plan and of the measures adopted

³⁹ See Article 7(7) of the Decree law.

⁴⁰ The financing by an NCB of an insolvent credit institution would be incompatible with the monetary financing prohibition since the NCB would be assuming a government task.

⁴¹ See paragraph 2.2 of Opinion CON/2016/55, paragraph 4.11 of Opinion CON/2008/42, paragraph 3.9 and footnote 34 of Opinion CON/2008/48, and paragraph 4.3 and in particular footnote 20 referring to Opinion CON/2008/46, which refers to paragraph 4.3 of Opinion CON/2008/58.

will apply only in connection with the request for precautionary recapitalisation from the bank itself. Indeed, when the capital raising plan to remedy the shortfall is drafted and assessed by the competent authority there may be no evidence of any need for and/or no intention on the part of the bank to apply for a precautionary recapitalisation.

4.2 *Assessment by the competent authority of the bank's regulatory capital need*

The ECB understands that the reference in Article 16 of the Decree law to the 'regulatory capital need' of a bank, regarding which the competent authority is required to inform the Ministry and the bank, is to be read, in line with Articles 32(4)(d) of the BRRD and 18(4)(d) of the SRM Regulation, as referring to the capital shortfall established in the national, Union or SSM-wide stress tests, asset quality reviews or equivalent exercises conducted by the ECB, the European Banking Authority or national authorities.

5. The exclusion of set-off rights with respect to claims mobilised as collateral

- 5.1 The ECB considers the Decree law's provision aimed at excluding set-off risks associated with credit claims accepted by the Banca d'Italia as collateral, which would also apply to Eurosystem credit operations, to be in line with the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB'). Protecting the European System of Central Banks (ESCB) against potential losses arising from the acceptance of such collateral is in line with the requirement laid down in the second indent of Article 18.1 of the Statute of the ESCB, pursuant to which lending by the ESCB central banks must be based on adequate collateral. The ECB notes that in recent years other euro area Member States have also enacted statutory provisions which exclude set-off risks related to credit claims mobilised as collateral for central bank operations. While in certain Member States the relevant statutory provisions, similar to the Decree law, only exclude set-off rights for credit claims mobilised as collateral for operations with that particular Member State's central bank, some Member States also have statutory provisions that, apart from their own NCBs, also provide protection for the ECB and other ESCB NCBs.⁴²

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 3 February 2017.

[signed]

The President of the ECB

Mario DRAGHI

⁴² See Opinion CON/2016/37, paragraphs 1.1, 1.3, 2.3 and 2.4.