Emergency liquidity assistance: Italian state guarantee for newly issued liabilities

On 23 December 2016, the Italian government issued Law Decree No. 237 (the "Decree") which sets out "urgent measures to protect public savings in the credit market" in order to prevent or remedy serious turbulence in the economy and preserve financial stability.

The Decree has since been converted into law by Law No. 15 of 17 February 2017 and applied from 23 December 2016 (and from 22 February 2017 with respect to the provisions of the Decree amended by the conversion Law).

What is the new state guarantee?

The Decree authorizes the Italian Minister for Economic Affairs and Finance (the **MEF**) to grant a state guarantee (the **Guarantee**) in respect of newly issued liabilities of banks that have a registered office in Italy (**Italian Banks**). The state guarantee is available until 30 June 2017 although this period may be extended by up to 6 months by the MEF, subject to the approval of the European Commission.

The Guarantee is an unconditional, irrevocable and first demand guarantee and covers both capital and interest. It is only available to banks that meet certain capital requirements and in relation to certain debt instruments that have specific structural features.

What types of instruments are eligible for the Guarantee?

Debt instruments issued by Italian Banks that have the following features may be eligible for the Guarantee:

- issued after 23 December 2016 or, in respect of existing issuance programs, subject to specified terms of duration;
- principal amount to be repaid in full;
- fixed rate interest;
- denominated in Euro;
- no subordination;
- that are not structured securities, complex products or instruments which incorporate a derivative component.

What are the capital requirements that banks need to meet?

General Aid Regime: In order to qualify for the Guarantee, a bank must meet the following capital requirements:

- full compliance with the requirements relating to own funds referred to in Article 92 of EU Regulation No. 575/2013; and
- evidence that no stress test has shown any current or future failure of its own funds.

Compliance with these conditions is checked by the Bank of Italy or, if a significant bank, the European Central Bank, in accordance with the Single Supervisory Mechanism.

If a Bank receives a Guarantee in respect of instruments that have a nominal value greater than €500m and 5% of its total liabilities, it will need to submit a restructuring plan to confirm its profitability and long-term funding capacity without recourse to public support, within two months of receiving the Guarantee.

Individual Aid Regime: If a Bank does not meet any of the above requirements, a Guarantee will only be available if a Bank urgently needs liquidity support and the following conditions are met:

- the Bank has positive net assets; and
- the European Commission takes a positive decision in light of European legislation on state aids applicable to liquidity measures in the context of a financial crisis.

Under the Individual Aid Regime, for the entire period of effectiveness of the Guarantee, the bank must not:

– distribute dividends;
– make discretionary payments on Additional Tier 1 capital instruments;
– buy-back its own Core Tier 1 capital and Additional Tier 1 capital instruments, without prior authorisation from the European Commission; and
– acquire new shares, except for acquisitions compliant with European legislation on state aids.

A Bank will also need to submit, within two months of receiving a Guarantee, a restructuring plan to confirm its profitability and long-term funding capacity without recourse to public support.

Emergency liquidity assistance guarantee

In addition to the above guarantee regime for newly issued liabilities, the Decree also authorizes the MEF to issue a State guarantee to integrate collateral, or its realizable value, allocated from Italian Banks to secure funds disbursed by the Bank of Italy where they are facing a liquidity crisis (emergency liquidity assistance).

A Bank in receipt of this guarantee will need to provide, within 2 months, a restructuring plan to confirm its profitability and long-term funding capacity without recourse to public support.

Final thoughts

This Decree is designed to help Italian banks in need of additional capital and unable to raise capital on their own. The capital injection will alleviate the problem for some weak banks and help the whole system achieve more stability, enhance the Italian economy and strengthen the investors' trust in the Italian banking system.

General market conditions in the EU may entail systemic risks for a single Member State or for the whole European economic area and therefore setting up of public financial support tools (such as these) which may be utilized if and when needed may preserve financial stability and avoid market turmoil.

Contacts

Federico Del Monte
Partner, Italy
T +39 02 7202521
federico.delmonte@hoganlovells.com

Corrado Fiscale
Partner, Italy
T +39 02 72025252
corrado.fiscale@hoganlovells.com

Giulia Arenaccio
Counsel, Italy
T +39 06 6758 23 1
giulia.arenaccio@hoganlovells.com

Annalisa Feliciani
Counsel, Italy
T +39 06 6758 23 1
annalisa.feliciani@hoganlovells.com