EUROPEAN CENTRAL BANK

EUROSYSTEM

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ECB-PUBLIC

OPINION OF THE EUROPEAN CENTRAL BANK

of 25 March 2015

on the reform of popolari banks

(CON/2015/13)

Introduction and legal basis

On 20 February 2015, the European Central Bank (ECB) received a request from the Ministry of Economy and Finance for an opinion on Article 1 of Decree-Law No 3 of 24 January 2015 on urgent measures for the banking system and investments (hereinafter the 'Decree-Law')[1].

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/EC[2], as the Decree-Law relates to the Banca d'Italia and to the supervisory tasks conferred upon the ECB and to 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 Popolari banks are currently set up as cooperative companies limited by shares. Their distinguishing features are, inter alia, the fact that shareholdings are limited to 1 per cent of share capital, except where a bank's articles of association provide for lower limits (between 0.5 and 1 per cent), the 'one member one vote' principle, and the fact that the board of directors reserves the right to approve the admission of new members. The purpose of Article 1 of the Decree-Law is to reform popolari banks by amending Legislative Decree No 385 of 1 September 1993[3].

1.2 A distinction can be made between popolari banks which are relatively small and have limited territorial coverage, and those which have cross-border operations or are listed on the stock exchange. In line with this distinction, the Decree-Law divides popolari banks into two categories, depending on the value of their total assets. Those with assets of more than EUR 8 billion are obliged to either convert to joint-stock companies (with subsequent application to them of the ordinary regime for such companies), wind up or reduce their assets to below that threshold. In order to facilitate such a conversion, the qualified majority voting threshold has been lowered for approving changes to the legal form of a popolare bank, as well as for decisions on mergers and acquisitions.

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1 *Gazzetta Ufficiale della Repubblica Italiana* No 19, 24.01.2015.

2 Council Decision 98/415/EC of 29 June 1998 on the Consultation of the European Union by national authorities regarding draft legislative provisions (OJ 189, 3.7.1998, p. 42).

3 *Gazzetta Ufficiale della Repubblica Italiana* No 230, 30.09.1993

1.3 Popolari banks with assets of EUR 8 billion or less are also affected by the Decree-Law. In contrast to the current regime, under the Decree-Law, a popolare bank's memorandum of association may allow for the issuance of financial instruments bearing certain economic and administrative rights. Owners of these financial instruments may, where so provided by the memorandum of association, exercise voting rights up to a maximum of one third of the total votes in the general assembly of shareholders and appoint as many as one third of the members of the managing and supervisory bodies of the bank[4]. Furthermore, company members who are legal persons may cast up to five votes if the memorandum of association so provides. In addition, under the Decree-Law, where proxy voting is allowed, the applicable voting right ceiling should not be set below 10 and may be increased to 20. A popolare bank with assets below the EUR 8 billion threshold will apply the lower qualified majority voting threshold, should it decide to convert into a joint-stock company. In addition, the requirement that the majority of directors are appointed from among the members or, where members are legal entities, from among persons designated by them, is removed.

1.4 Finally, under the Decree-Law, the right to redeem shares in the event of withdrawal from the cooperative, even in the event of transformation, death or exclusion of shareholders[5], may be limited by the Banca d'Italia if such measure is deemed necessary in order to preserve the adequacy of the Common Equity Tier 1 capital.

2. The appropriate time to consult the ECB

2.1 The ECB must be consulted at an appropriate stage in the legislative process. This should be at a time that enables the ECB to adopt its opinion in all required language versions and that enables the authority initiating the legislative provision to take the ECB's opinion into account before it decides on the substance[6].

2.2 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 to Parliament for conversion into law. If not converted within 60 days of publication, the decree-law is rendered invalid with retroactive application. In the light of the above, the ECB should be consulted before the adoption of a decree-law[7].

2.3 In the present case, as the Decree-Law was adopted and published on 24 January 2015, not only was the ECB not consulted before its adoption but the submission of the consultation request was unnecessarily delayed. The request was received by the ECB on 20 February 2015, when the Ministry of Economy and Finance asked the ECB to consider the consultation as a matter of

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4 More specifically, holders of financial instruments, in accordance with the memorandum of association, might appoint up to one third of the supervisory board members and one third of the management board members in case of two-tier governance system (Article 1(1)(d)(1) of the Decree- Law, amending Article 150-bis(2) of Legislative Decree No 385 of 1 September 1993, in conjunction with Article 2544(2) of the Civil Code) or - alternatively - up to one third of the directors in case the one-tier governance system applies (Article 1(1)(d)(1) of the Decree- Law, amending Article 150-bis(2) of Legislative Decree No 385 of 1 September 1993, in conjunction with Article 2544(3) of the Civil Code).

5 Amendments made by the Chamber of Deputies in the process of conversion exclude the power of the Banca d'Italia to limit the right to redeem shares in case of death of the shareholder.

6 See Title IV, Section I of the Guide to consultation of the European Central Bank by national authorities regarding draft legislative provisions, which is available from the ECB's website.

7 See ECB Opinion CON/2012/64.

urgency in view of the short deadline for conversion. This situation is unfortunate and the ECB would like to emphasise to the Ministry the need for proper consultation.

3. General observations

3.1 The ECB welcomes the proposed reform of popolari banks as an essential step towards addressing shortcomings regarding their governance, and supports the Italian authorities in giving this reform permanent effect without delays.

3.2 The ECB understands that the Decree-Law addresses certain rigid features of the governance framework of popolari banks with the aim of: (i) enhancing the effective monitoring power of the shareholders vis–à–vis the management; (ii) increasing the banks' capital-raising capacity; (iii) reducing the risk of concentration of power in a minority group of shareholders, and; (iv) providing opportunities to look for synergies and economies of scale, resulting in efficiency gains within the banking segment, for instance through mergers and acquisitions.

3.3 The ECB notes that popolari banks with assets above EUR 8 billion represent a significant proportion of the popolari segment in terms of loan amounts, number of branches and number of employees. Therefore, the threshold set for mandatory conversion seems to be expedient for the achievement of the objectives of the Decree-Law for a significant part of the popolari segment of the Italian banking sector. The ECB understands that the asset size criterion is coherent with the current distinctions between popolari banks with a wide territorial and operational outreach, having a business model similar to the one adopted by commercial banks, and those with a cooperative and mutual banking model. In light of this, the ECB welcomes the Decree-Law, which realigns the company and governance structure of larger popolari banks with those of their commercial peers while not prejudicing the ability of popolari banks to finance the local regional economy.

3.4 As far as popolari banks with assets of EUR 8 billion or less are concerned, the ECB would like to emphasise the importance of measures aimed at strengthening their governance structures. A more appropriate structure could help enhance their risk management capabilities, their internal capital generation ability as well as their potential for attracting additional capital, and their competence to withstand financial and economic crises of significant magnitude. This would enable popolari banks to continue to provide credit to the regional and local economies even during difficult times.

3.5 Given the importance of the Decree-Law in addressing one of the vulnerabilities of the Italian banking sector, the ECB strongly supports the essential elements of the proposed reform which it feels should not be substantially amended. The ECB, furthermore, advocates for its timely implementation.

4. Supervisory implications for larger popolari banks

4.1 The ECB notes that most of the popolari banks with assets above EUR 8 billion are directly supervised by the ECB. Against this backdrop, the ECB welcomes the Decree-Law, which is intended to reshape the governance structure of popolari banks with a wider territorial and operational outreach.

4.2 Under the current prudential regulatory framework, both strong governance arrangements and a solid capital structure are crucial concerns for the banking supervisor. To this end, the ECB notes that the transformation of the biggest popolari banks into joint-stock companies would facilitate their ability to raise capital and enhance the shareholders' control over the management. In addition, this could make it easier for the capital instruments issued to be included as part of the fulfilment of the Common Equity Tier 1 requirements. Under Regulation (EU) No 575/2013 of the European Parliament and of the Council[8], as supplemented by Commission delegated Regulation (EU) No 241/2014[9], for capital instruments to qualify as Common Equity Tier 1 a number of conditions, in addition to those applicable to capital instruments issued by joint stock companies, have to be met.

4.3 The transformations envisaged by the Decree-Law will lead to substantial changes, particularly with regard to the capital structure and the governance arrangements of the credit institutions undergoing such transformation. To that end, the ECB notes that, pursuant to Article 9(1), subparagraph 2, Article 4(1)(e) and Article 4(3) of Council Regulation (EU) No 1024/2013[10], and Article 104(1)(b) of Directive 2013/36/EU of the European Parliament and of the Council[11], the ECB shall have all the powers of the competent and designated authorities under the applicable Union law to ensure compliance with requirements regarding robust governance arrangements with regard to significant institutions. These powers include assessing whether such arrangements would jeopardise the safety and the soundness of the credit institution in question, and whether the changes to its governance structure are consistent with the credit institution's sound and prudent management and with SSM standards.

4.4 Moreover, the ECB welcomes the fact that Decree-Law explicitly confers upon the Banca d'Italia the capacity to limit the shareholders' redemption rights should the exercise thereof cause the banks' own funds to be reduced, as this explicit conferral will facilitate the exercise of the powers of the supervisory authority. In light of the competences conferred on the ECB by Article 4(1)(d) and the second subparagraph of Article 9(1) of Regulation (EU) No 1024/2013, i.e. to ensure compliance with own funds requirements, the ECB notes that, for significant institutions, it is for the ECB alone to assess in each case whether such limitation of the shareholders' redemption rights is necessary. Finally, it is understood that the Decree-Law is without prejudice to other supervisory,

8 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).

9 Commission delegated Regulation (EU) No 241/2014 (OJ L 74, 14.3.2014, p. 8).

10 Council Regulation (EU) No 1024/2013 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).

11 Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

enforcement and sanctioning powers conferred on the ECB. This does not prejudice the Banca d'Italia's regulatory powers under the Decree-Law.

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

Done at Frankfurt am Main, 25 March 2015.

[signed]

The President of the ECB

Mario DRAGHI