
European Commission

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Subject: State aid n° SA.35137 (2012/N) – Italy

Rescue aid to Monte dei Paschi di Siena S.p.A.

Sir,

1. Procedure

(1) On 12 July 2012, Italy informed the Commission about an envisaged recapitalisation of Monte dei Paschi di Siena S.p.A. ("MPS").

(2) Between July and December 2012, the envisaged recapitalisation and its terms were discussed in a number of conference calls. Additional information exchanges by electronic mail took place frequently.

(3) Italy notified the recapitalisation measures covered by this decision to the Commission by letter of 7 December 2012, registered with the Commission on the same date.

(4) For reasons of urgency, Italy accepts that exceptionally the decision is adopted in English.

2. Description

2.1 Beneficiary

(5) MPS is an Italian listed bank, which was privatised in 1995. The privatisation had been implemented by transferring the banking business (and assets) of the former public credit institution to a newly established private stock company and by transforming the legal nature of the former public credit institute in a foundation (Fondazione Monte dei Paschi di Siena – "the Foundation"). The members of the
Foundation's board are appointed by the local authorities of Siena, and are statutorily bound to pursue exclusively social welfare projects.

(6) Initially the Foundation held 100% of MPS. It remains the major shareholder of MPS today with a stake of 37.56%. The other shareholders as of 30 November 2012 are Finamonte S.R.L. (4%), Unicoop Firenze S.C.R.L. (2.73%), J.P. Morgan Securities Limited (2.53%) and various companies under the influence of AXA SA (2.53%). The remainder 53.19% is floating and belongs to shareholders with a stake lower than 2%.

(7) As of December 2011 "Gruppo Monte dei Paschi di Siena" was the third-largest Italian banking group in terms of total assets (EUR 240 billion), branches (2 909) and employees (31 170).

(8) That group is composed of a large number of national and foreign companies. In particular, as of December 2011, MPS had the sole control of the following entities: Agrisviluppo S.p.A., Italy (99,07 %), Cassa di Risparmio di Biella d Vercelli S.p.A., Italy (60,42%) - MPS Tenimenti Poggio Bonelli e Chigi Saracini Soc. Agricola S.p.A., Italy (100,00%) and banking subsidiaries in France, Belgium, Ireland and Luxembourg. As of December 2011, MPS had also the joint control of Banca Popolare di Spoleto S.p.A., Italy (26,01%).

(9) MPS offers a wide range of financial services to private, corporate and institutional customers and public authorities. It operates across Italy and in several international markets, ranging from traditional lending to retail and corporate customers (including leasing, factoring and consumer credit), to asset management (through equity interest in AM Holding), private banking, investment banking and corporate finance. MPS also provides bancassurance and pension products through the strategic partnership with AXA.

(10) In 2011, MPS posted a loss of EUR 4 685 million; according to Q3 figures for 2012 the loss for 2012 amounts to EUR 1 664 million.

2.2. The first recapitalisation

(11) In 2009 MPS issued EUR 1.9 billion of hybrid capital instruments (so-called "Tremonti bonds", hereinafter "old instruments") subscribed by Italy under the first Italian recapitalisation scheme approved by the Commission on 23 December 2008. The old instruments were hybrid capital that counted as "Core Tier 1" capital and had a fixed remuneration in case of profit.

(12) The terms of the old instruments pursuant to the scheme included amongst others:

(a) The same subordination as ordinary shares; losses that reduce the beneficiary' supervisory capital beyond 8% are absorbed in the same proportion by the special bonds subscribed by the State and the value of share capital and reserves.

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1 Recapitalisation measures in favour of the financial sector in Italy, Case N 648/08, OJ C 88, 17.4. 2009, as modified in Case N 97/09, modification to the recapitalisation measures in favour of the financial sector in Italy, OJ C 88, 17 April 2009.
(b) Interests are non-cumulative and are paid whenever and to the extent of the bank’s distributable profits.

(c) The interest rate is calculated as the higher of the following three elements:

- 8.5% of the nominal value for the years 2009, 2010, 2011 and 2012, 9% for the years 2013, 2014, 2015 and 2016, then increased by 0.5% every two years (i.e. 9.5% for 2017 and 2018 and so on, up to 15% for year 2039 and subsequent years) or;

- 105% of the dividend distributed in whatever form in relation to the profits of 2009, 110% for 2010, 115% for 2011 – 2017, and 125% for 2018 and subsequent years or, with a cap of 15% of the nominal value;

- starting from fiscal year 2011, the yield on 30-year Treasury bonds (BTP) increased by 300 basis points, then from fiscal year 2013 and for all the subsequent years the same BTP yield increased by 350 basis points.

(d) Early redemption option for the beneficiary of the recapitalisation:

- The redemption price is capped to a percentage of the nominal value which is equal to: 100% if redemption occurs until 30 June 2013 and 110%, if redemption occurs between 1 July 2013 and 30 June 2015.

- For the following years, the redemption price should be calculated as the higher between 110 % of the nominal value of the recapitalisation instrument issued by the beneficiary and bought by the State and the market value of the outstanding underlying shares of the beneficiary bank considered, capped to a percentage of the nominal value which is equal to: 130%, if redemption occurs between 1 July 2015 and 30 June 2016; 140%, if redemption occurs between 1 July 2016 and 30 June 2019; 150%, if redemption occurs between 1 July 2019 and 30 June 2022; 160%, if redemption occurs from 1 July 2022 onwards.

2.3 The recapitalisation measures

(13) On 8 December 2011, the European Banking Authority ("EBA") issued a recommendation for banks to have a Core Tier 1 (CT1)\(^2\) capital ratio of 9%, after accounting for an additional temporary buffer against sovereign risk holdings as of 30 September 2011. For MPS that recommendation meant it had a capital shortfall of approximately EUR 3.3 billion.

(14) At the beginning of January 2012, MPS submitted a “capital plan” to the Bank of Italy in order to address the shortfall. The plan entailed inter alia capital management initiatives, the optimisation of risk weighted assets and the disposal of assets.

(15) The plan was partially implemented, but on 22 June 2012 MPS informed the Bank of Italy that it would not be able to fill the remaining shortfall by 30 June 2012 as envisaged.

(16) Consecutively, the Bank of Italy ("BoI") determined that MPS had a capital shortfall between EUR 1.3 billion and EUR 1.7 billion as measured against the EBA requirements. Those estimates have been subsequently increased up to a total of EUR 2 billion, factoring in potential capital needs that may arise due to possible incorrect accounting representation of certain structured financial transactions entered into by MPS before 30 September 2011, which are currently being investigated by the BoI.

(17) Accordingly, the board of directors of MPS authorised the issuance of the hybrid capital instruments referred to in articles 23-sexies of Law Decree n. 95 of 6 July 2012 (the "new instruments"), which are eligible as regulatory CT1 (in compliance with EBA Recommendation of 8 December 2011) for an overall maximum amount of EUR 3.9 billion, which Italy intends to subscribe. That amount includes a replacement of the outstanding old instruments of EUR 1.9 billion with new instruments.

(18) More specifically, the new instruments will also be a perpetual hybrid that is in principal pari passu with common shares (however common shares will absorb losses until the capital ratio is 8%, as described in recital (12)(a)). The instrument bears a 9.0% annual coupon with a "step-up" clause of 0.5% every two years. Moreover, coupon payment is ensured through an alternative coupon satisfaction mechanism ("ACSM"), obliging MPS to pay the coupon (partly) in kind in the event of losses or insufficient distributable profits. Alternative coupon payments shall be made by assigning to Italy new MPS shares or by issuing to Italy new instruments in lieu of the cash payment. The amount of shares shall be based on the market price of MPS shares.3

(19) For the coupon accrued in 2012 MPS can assign to Italy new hybrid capital instrument in lieu of the cash payment. That payment would in principle be due on 1 July 2013, but can be made in advance, at MPS’s discretion. As a result, the interests due (at the currently applicable rate of 9%) on the EUR 1.9 billion of old instruments for the period from 1 January 2012 to 31 December 2012, (totalling EUR 171 million) will be paid by issuing and assigning to Italy new instruments of the same amount.

(20) Moreover, as in the old instruments, an early redemption option for MPS of the recapitalisation remains possible, whereby the redemption price is set at 100% of the nominal value if redemption occurs by 30 June 2015, 105% of the nominal value if redemption occurs by 30 June 2017, and with a subsequent increase of 5% every two years.

3 The market price will be calculated on the basis of the average of market price of the shares over ten consecutive days preceding the approval of MPS' balance sheet by its Board of Directors.
3. **POSITION OF THE ITALIAN AUTHORITIES**

3.1. Position of the Italian authorities on the recapitalisation measure

(21) The Italian authorities accept that the measure constitutes additional State aid in the amount of EUR 2 billion (which means, adding the previous aid, EUR 3.9 billion in total) but consider that the proposed measure is compatible with the internal market on the basis of Article 107(3)(b) of the Treaty on the Functioning of the European Union ("the TFEU"), as it is necessary to remedy a serious disturbance in the Italian economy. The Italian authorities submit in particular that the replacement of the old instruments with the new instruments will be done so as to meet the compatibility requirements for State aid, and in order to obtain at least as much remuneration for the aid as the State would have received had the old instrument remained in MPS.

(22) In particular, the Italian authorities submit that the measures are (i) appropriate and well-targeted; (ii) necessary and limited to the minimum amount necessary; and (iii) proportionate as designed to minimize negative spill-over effects on competitors.

(23) The Italian authorities submit that the proposed measure is required to bring MPS's capital position in line with EBA's capital requirements. In addition, the BoI has confirmed in a letter that for prudential reasons it considers it necessary for the time being that the EUR 2 billion are added to MPS capital, as notified by Italy. Moreover, the Italian authorities explain that they have chosen to recapitalise MPS by means of hybrid instruments as they consider it to be a viable bank that can pay the interest due and redeem the instrument within the next years.

3.2. Commitments of the Italian Authorities

(24) The Italian authorities have provided the following commitments:

(a) to ensure that recapitalisation provided by the Republic to Banca Monte dei Paschi di Siena (MPS) will not exceed the amount of the recapitalisation determined by the Bank of Italy as being necessary, provided that such amount does not exceed the maximum amount set by Article 23-sexies of Law Decree No. 95 as of 6 July 2012;

(b) to notify any further support to MPS;

(c) taking into account that the Republic will subscribe instruments other than shares, to ensure an appropriate remuneration of the recapitalisation provided by the Republic to MPS;

(d) to impose on MPS a dividend ban until the Commission adopts a restructuring decision;

(e) to impose on MPS not to carry out advertising referring to the Republic's support and not to employ any aggressive commercial strategies which would not have taken place without the Republic's support;

(f) to procure that MPS' restructuring plan shall entail pre-defined maximum limitations in the monetary remuneration (fixed and variable) policy for the
members of the bodies and management of the beneficiary financial institution and that in the meanwhile ongoing compliance shall be ensured with the Bank of Italy regulations implementing provisions of Directive 2010/76/EC (so-called CRD 3) and relating CEBS (now EBA) Guidelines of on Remuneration Policies and Practices of 10 December 2010;

(g) to impose that the value of the shares issued due to the "alternative coupon satisfaction mechanism" (ACSM) will be determined in line with market practice and to procure that, should the ACSM apply, MPS shall pay coupons only in the form of shares until Commission adopts a restructuring decision, except for financial year 2012 for which in case of advance payment of coupons they will be paid in the form of instruments only;

(h) to impose on MPS for the whole rescue period a ban on payment of coupon on hybrid capital subject to a distributable profits payment test, unless such payments are triggered pursuant other contractual provisions or only payment deferral is consented and to procure that MPS will not pay coupon on hybrid capital until the Commission adopts a restructuring decision, unless it has a legal obligation to proceed with such payment even in the absence of distributable profits, irrespective of the possibility to defer such payment;

(i) that according to Article 23-octies of Law Decree No. 95 as of 6 July 2012 the Republic will submit the restructuring plan delivered by MPS within six months from the date of the decision approving the rescue aid, independent of whether pursuant to the rules set out in the Recapitalisation Communication it is considered to be fundamentally sound or distressed. Article 23-octies of Law Decree No. 95 as of 6 July 2012 requires that the restructuring plan to be submitted shall comply with the principles set out in the Restructuring Communication in order to re-establish the individual financial institution's long-term viability without continued reliance on State support, while containing adequate burden-sharing measures and measures to limit distortions of competition;

(j) to impose on MPS to not acquire for the whole rescue period any stake in banks, financial intermediaries and insurance undertakings and to procure that MPS shall not acquire any stake in any undertaking until the Commission adopts a restructuring decision. This commitment does not cover: (i) acquisitions that take place in the ordinary course of the banking business in the management of existing claims towards ailing firms; (ii) the acquisition, as recommended by Bank of Italy and subject to the approval of the Commission services, of a special purpose vehicle owning real estate assets under MPS’ management, for the purpose of restructuring its real estate portfolio.

4. ASSESSMENT

4.1. Existence of State Aid

(25) According to Article 107(1) TFEU, State aid is any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort
competition by favouring certain undertakings or the production of certain goods, in so far as it affects trade between Member States.

(26) The qualification of a measure as State aid requires that the following conditions are met: a) it must be financed by a Member State or through State resources; b) it must grant an advantage liable to favour certain undertakings or the production of certain goods; c) the measure must distort or threaten to distort competition; d) and the measure must have the potential to affect trade between Member States. The Commission in that context observes that the Italian authorities do not dispute that the measure constitutes State aid.

(27) The new instruments of EUR 3.9 billion will be exclusively subscribed by Italy. The measure therefore entails State resources.

(28) Moreover, the notified recapitalisation of EUR 3.9 billion allows MPS to remain above the EBA minimum solvency ratio. In the current economic circumstances, and given the losses posted by MPS in recent years and the modest forecasted profitability for the next years, it is highly doubtful that MPS would have been able to raise capital on the market. For those reasons the new measure entails an advantage to MPS.

(29) Given that MPS is and will be active in the financial sector, which is open to intense international competition, any advantage from State resources to the bank has the potential to affect intra-Union trade and to distort competition. The measure therefore constitutes State aid within the meaning of Article 107(1) TFEU.

4.2. Compatibility

(30) Article 107(3)(b) TFEU empowers the Commission to find that aid is compatible with the internal market if it is intended "to remedy a serious disturbance in the economy of a Member State". The Commission has acknowledged that the global financial crisis can create a serious disturbance in the economy of a Member State and that measures supporting banks are apt to remedy that disturbance. That assessment has been confirmed in the Recapitalisation Communication⁴ and the Restructuring Communication⁵. The Commission still considers that requirements for State aid to be approved pursuant to Article 107(3)(b) TFEU are fulfilled in view of the reappearance of stress in financial markets. The Commission confirmed that view by adopting the 2010 Prolongation Communication⁶, which prolongs until 31 December 2011 the application of State aid rules to support measures in favour of banks in the context of the financial crisis. The Commission has since extended the

application of those rules beyond 31 December 2011 (the "2011 Prolongation Communication").

(31) In respect of the Italian economy that analysis has been confirmed in the Commission's approval of various measures undertaken by the Italy authorities to combat the financial crisis.\(^{8}\)

(32) Any uncertainty regarding the fulfilment of regulatory requirements could directly affect the financial markets and thus the entire economy of a Member State. In light of the current fragile situation of the financial markets, the Commission continues to base its assessment of State aid measures in the banking sector on Article 107(3)(b) TFEU.

(33) On the basis of Article 107(3)(b) TFEU, the general principles applicable for State aid granted to financial institutions are set out in point 15 of the Banking Communication\(^ {9}\). Accordingly, the aid must be appropriate to achieve the objective of remedying a serious disturbance in the economy, limited to the minimum necessary in view of the objective pursued, and proportionate in that it minimises negative spillover effects on competitors, other sectors and other Member States.

(34) The Recapitalisation Communication translates those general principles into specific compatibility conditions.

(35) First, in order to be compatible, the aid must be appropriate. The aim of the aid is to eliminate the threat to the stability of the Italy economy stemming from any solvency problems of MPS. Capital injections into banks are in principle an appropriate instrument to help banks to resist the consequences of the financial crisis, providing a cushion to absorb losses, to fulfil regulatory capital requirements, to ensure lending to the real economy, and to prepare a bank's return to long-term viability or its orderly winding up.

(36) The Commission considers that the aid instruments chosen by the Italian authorities, i.e. the subscription of the new instruments is an appropriate means to address MPS's solvency problems. The aid will prevent the breach of EBA's minimum capital requirements.

(37) Second, the Commission has to assess whether the aid is necessary and limited to the minimum necessary. In the absence of the aid, the capital ratios of MPS would have otherwise not been sufficient to meet the EBA requirements. The Commission considers that the aid is limited to covering MPS immediate capital needs, catering also for further foreseeable risk factors which could endanger compliance with EBA minimum capital ratios in the coming months, such as the potential capital needs that may arise due to possible incorrect accounting representation of certain structured financial transactions entered into by MPS before 30 September 2011, as described in recital (16).


It should also be noted that the new measure replaces the EUR 1.9 billion of the old instrument. As regards EUR 1.9 billion the new instruments do thus not provide MPS with further resources but instantly replace the existing ones. Moreover, the new elements do also not provide MPS with a better instrument in terms of the conditions attached to it, in particular not regarding the remuneration.

The terms of the remuneration are indeed not altered to the benefit of MPS. It should be recalled that the coupons on the old instruments are not cumulative, and that the old instrument did not entail an ACSM. Moreover, according to Italy and based on the current profitability forecasts, MPS would not be obliged to pay any remuneration for 2012 and 2013 under the terms of the old instrument given the absence of sufficient distributable profits. However, the replacement will result in a payment also for interests accrued in 2012 and 2013 as MPS will have to pay (in cash, hybrids and shares) even if it records losses. As a result, Italy will receive EUR 171 million of new instruments (for the 2012 coupon on the old instruments), and additional cash or MPS shares for the interests accrued on old instruments from 1 January 2013 until the date of their redemption and replacement with the new instruments. In the counterfactual scenario of not replacing the old with the new instrument, Italy would not receive any coupon on the EUR 1.9 billion in that period. Moreover, the new instrument will bear a higher interest rate than the old. The only change in the conditions that could be considered as advantageous to MPS relates to the redemption value, which currently stands at 100% of the nominal value for both instruments. However, a difference as regards the redemption mechanism to the benefit of MPS could theoretically only arise if the instrument was redeemed before 2017. That difference can at most amount to 5-10% of the nominal value of the instrument and is thus more than offset by the higher and certain coupon payment that Italy will receive for 2012 (9%) and 2013 (9%). Consequently, the replacement of the old instrument with the new contributes to limiting the aid to the minimum necessary.

Furthermore, the Commission must assess whether there is an appropriate own contribution by the beneficiary, which is ensured if the remuneration for the aid is adequate. The coupon that MPS is obliged to pay, initially amounting to 9% with a step up of 0.5% every two years, is in line with the requirements of point 27 in conjunction with point 44 of the Recapitalisation Communication.

Points 9 and 13 of the 2011 Prolongation Communication provide that hybrid instruments should in principle contain an ACSM whereby coupons which cannot be paid in cash should be paid in newly issued shares, using the market price as a benchmark share price. The Commission considers that the new instruments contain an ACSM that is consistent with these requirements.
(42) As for the first payment of the coupon which will be made in additional new instruments, the Commission firstly recalls that the EUR 171 million were accrued on the old instrument that Italy was not obliged to replace. Furthermore, the Commission recalls the underlying rationale of the ACSM is to ensure an appropriate burden-sharing by the bank itself, and that the limited possibility to make the alternative payment in the form of hybrids and not in shares can be consistent with that objective. As MPS intends to raise capital on the market in 2014 and the issuance of shares to the State rather than hybrids could possibly jeopardise this intention, accepting payment through further hybrids under the particular circumstances of the case at hand, is consistent with the overall objective of limiting State aid to minimum necessary.

(43) Finally, the limitation of the aid to the minimum is supported by a commitment of Italy ensuring that MPS will not release reserves in order to record a profit and thereby pay coupon to hybrid capital holders, and by a ban on paying dividends for the duration of the rescue period. The Commission thus concludes that the notified aid is necessary in that it is limited to the minimum amount.

(44) Third, the Commission has to verify whether the aid is proportionate. In that respect, the Commission takes note of Italy's commitments as described above in recital (24), in particular those relating to an acquisition ban, a prohibition to carry out advertisement referring to the State support or to engage in aggressive commercial strategies, and that during the rescue phase MPS' monetary remuneration policy for the members of the bodies and management will be in line with the BoI respective regulations and EBA's Guidelines of on Remuneration Policies and Practices of 10 December 2010.

(45) The Commission considers that these commitments limit the distortions of competition resulting from the aid to an acceptable degree and therefore finds the aid proportionate.

(46) In sum, the Commission concludes that the aid measure is appropriate to rescue MPS in the short-term and will for the time being not entail an undue distortion of competition. The Commission however reiterates that it needs to be provided with a restructuring plan at the latest six months from the date of the present decision and that the approval of the aid is limited until the Commission takes a final decision on the restructuring plan, which Italy will submit within six months.

(47) In view of the elements set out above, it can be concluded that the capital measures of EUR 3.9 billion in favour of MPS can, in view of the commitments provided by Italy, be temporarily approved as rescue aid until the Commission takes a final decision on the restructuring plan.

4.4. Conclusions on the existence of aid and compatibility

(48) The Commission observes that the recapitalisation of MPS through hybrid capital of EUR 3.9 billion constitutes State aid within the meaning of Article 107(1) TFEU.

(49) The Commission finds that the aid in favour of MPS is temporarily compatible with the internal market for reasons of financial stability on the basis of Article 107(3)(b)
TFEU, in light of the commitments of Italy referred to in recital (24), until the Commission takes a final decision on the restructuring plan.

5. CONCLUSION

The Commission has accordingly decided:

– to consider the aid to be temporarily compatible with the internal market pursuant to Article 107(3)(b) of the Treaty on the Functioning of the European Union, until the Commission takes a final decision on the restructuring plan, which Italy will submit within six months from the date of the decision.

– The Commission notes that Italy exceptionally accepts that the adoption of the Decision be in the English language

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Your request should be sent by registered letter or fax to:

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Yours faithfully,
For the Commission

Joaquín ALMUNIA
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