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1 Introduction

On 27 January 2017, Single Resolution Board (SRB) chair Elke König said[1] *[ ] . ba . . a e a. ce BT 0 a .70 52[T] [( ) f 10-(202B d)15 a1 (a)- (ac d)5 a . . Ma fdBT 0 .70 527 T [( )1 ca be. e ed f e fa . . . e a e b . e. e a. e ec . e . a . e c , . ced . e . [...]. e e . a. afe e f. e . f . e fe* –. Under the current European Union frameworks for dealing with banking problems, resolution is seen as an exception to be allowed only if liquidation under national insolvency proceedings would not be warranted. This is the case when the bank provides *cC ac .a(.M 0 (a. .) 2)2 (ETEMC , a a*

2 The Veneto and Vicenza cases

On 23 June 2017, Veneto Banca and Banca Popolare di Vicenza– were declared to be *fa ˛ ˛ ˛ ˛ e˛ fa ˛*– by the European Central Bank (ECB) in its capacity as supervisor for euro-area significant institutions[3]. The two banks had already been among the Italian institutions that failed the ECB's comprehensive assessment in 2014. In 2016, they benefitted from €3.5 billion in investment from the Italian bank-funded *A ˛a e* fund, but their financial positions deteriorated further in 2017 (Merler, 2017a), ultimately resulting in a combined capital need of €1.2 billion. In March 2017, the two banks requested precautionary recapitalisations, which however would have required the capital shortfall to be covered by private means as a pre-condition (Merler, 2017b). The ECB eventually deemed the banks' business plans not credible. This negative assessment opened up the possibility of either resolution or liquidation, with the decision referred to the Single Resolution Board (SRB). The SRB decided that public interest in resolution was not present, because neither of the banks provided critical functions and their failure was unlikely to have a significant adverse impact on financial stability.

Table 1: Assets and liabilities acquired by Intesa (ISP)

A ☒		☒	
☒ - -	3.8	☒ - -	9.3
☒ - - ☒	30.1	☒ - - ☒	25.8
A ☒	8.8	☒ (☒)	11.8
	0.02	☒	2.6
☒	3.01	☒	1.8
☒ (. ☒ A)	51.3	☒	51.3

Source: Bank of Italy (2017).

As a result, Veneto Banca and Banca Popolare di Vicenza were wound down under Italian insolvency law on 25 June 2017. Italian law provides for several insolvency procedures: banks and other financial institutions – and other selected types of enterprises – are subject to *f ˛ ced ad ˛ ˛ a / e˛ ı da* –(*L ı da e C a a A ˛ ˛ a / a* (Baker McKenzie, 2017); see Box 1 in section 4.2 for details). In the context of liquidation, shares (mostly owned by *A ˛a e*) and subordinated debt were wiped out to meet the minimum burden-sharing requirement established in the European Commission's 2013 Communication on State Aid to Banks. The performing parts of the banks' assets were acquired by Intesa San Paolo – Italy's second largest bank – together with some of the liabilities, most notably deposits and senior debt (see Table 1 for details). Intesa paid a symbolic sum of €1 for the acquisition, and benefitted from a €4.8 billion cash injection by the state. Of this, €3.5 billion was intended to ensure that the acquisition would not undermine Intesa's equity ratios, while €1.3 billion was destined to cover the costs of closing branches and managing dismissal/redeployment of the staff of the banks being liquidated. Intesa was also granted state guarantees that could potentially total up to €12 billion[4]. Of this, up to €6.35 billion might cover the repayment of debt held that was deemed to be not good after due diligence; up to €4 billion might constitute a buffer for currently performing debts that are high risk; and the remaining guarantee of up to €2 billion might cover potential legal risks of the banks being liquidated. The non-performing parts of the two banks' balance sheets were transferred to SGA (*S c e , e ˛a Ge e d A /*) – a

[3] ☒ : https://www.bankingsupervision.europa.eu/press/pr/date/2017/html/ssm.pr170623.en.html.

[4] ☒ 99 25 2017.

vehicle set up for the rescue of Banco di Napoli at the end of the 1990s – with aim of maximising the recovery over time.

The cases of Veneto Banca and Popolare di Vicenza are reminiscent of that of Banca Romagna Cooperativa (BRC), a significantly smaller[5] Italian lender liquidated in July 2015 (Merler, 2016). BRC’s assets and liabilities were transferred to Banca Sviluppo, part of the Italian ICCREA Group. In the process, BRC equity and junior debt remained in the liquidation estate – similarly to what happened in the Veneto and Vicenza cases. The BRC operation was conducted under national insolvency law by selling only parts of assets and liabilities out of liquidation. The Italian mandatory deposit guarantee scheme for the sector (FGDCC) covered the negative difference between the transferred assets and liabilities – an action that qualified as state aid, because it was beyond the DGS’ pay-out function. This was authorised by the European Commission. The scale of the BRC case was obviously much smaller than the Veneto and Vicenza cases, and the cost of the operation for the Mutual Bank Deposit Guarantee Fund (FGDCC) was estimated at the time as €260.8 million maximum (European Commission, 2015).

Because of the structure of the operation, the Veneto Banca and Banca Popolare di Vicenza cases have also been compared to the case of the Spanish Banco Popular, which was acquired for a symbolic amount of €1 by Banco Santander. In contrast to the two Italian banks, however, Banco Popular was put in resolution by the SRB for public interest reasons. The similarity between the Italian and Spanish cases stems from the fact that the sale and transfer of part of the failing banks’ balance sheets to a buyer is also foreseen as a resolution tool under Article 38 BRRD. Mesnard *et al.* (2017) highlights also that the measures imple-

anks’ balance s56 BDC1.1 sh2 (te)-I5ity failin-3.9 (o I)oeym1y muc

3.2 Use of public funds

One important point to note is that the two options differ quite significantly when it comes to the scope of EU legislation applicable to the use of public funds (Figure 1).

If a bank is declared by the ECB to be failing or likely to fail[11], the precautionary recapitalisation option is not available, and the choice is between liquidation or resolution. If the bank is put into resolution, the Single Resolution Mechanism Regulation (SRMR) requires that the bank's losses be covered by the bail-in of shareholders and creditors up to 8 percent of the bank's liabilities, before the Single Resolution Fund (SRF) can be accessed. Depending on the composition of individual banks' balance sheets, this may imply the bail-in of senior debt and potentially even uncovered deposits. The use of funds from the SRF is anyway subject to the Commission's State aid assessment. State aid is possible in the context of liquidation – in the form of *liquidation aid* – and it is subject to the State aid discipline, including the burden-sharing requirements laid out in the 2013 Communication. The rationale underlying aid in liquidation is that while the winding up of small banks is not expected to have systemic effects, it may still have important local effects. Currently, it is for Member States to decide whether liquidation may harm the local economy, and whether the use national funds is warranted to mitigate the damage – although liquidation aid would then need to be cleared by the Commission.

[illegible]

[C . e e ,] e e ee a d a eed a d e c ad , ea e a ed a a e de e f e ba f e a e a d a d a e d - ba ce e ca ec –

financial institutions – as well as other selected types of enterprises – are subject to a regime called *f. ced ad . . a / e. ı da* –(*L ı da e C a a A . . a / a,* LCA). Under the LCA framework, liquidators are nominated by the Bank of Italy, which enjoys a high degree of oversight over the process. Unlike other procedures – and unlike what happens in other countries such as Spain – there is no delegated judge, and the LCA is mainly administrative in nature (Baker McKenzie, 2017; see Box 1 for details). This probably reflects the intention to ensure a swift liquidation for entities that are perceived as critical, taking them out of the traditionally long Italian judicial procedure. The Italian Parliament voted on 11 October 2017 on a new law that will streamline insolvency and bankruptcy in Italy. Among other changes, the new law reduces the scope of the LCA, but does not change its applicability to banks and financial institutions[15].

BOX 1: Liquidation in Italy and in Spain

In **Italy**, *. ı da e c a a a . . a / a*--

A second issue related to the national character of insolvency frameworks is the potential for them to be altered under national law. In its assessments published on 23 June 2017[16], the SRB stated that in order to assess the need to take resolution action based on the resolution objectives of protecting depositors and investors and protecting client assets and client funds, a comparison was made between the hypothetical resolution action and LCA proceedings. The SRB specifically states that:

> since . a. . J e c , . ceed . (e LCA) a. . f . e . a . fe a , . c a e f e . a e , . f . c c . . d a e bee . a . fe . ed ca e f . e . ac , ca be c c . ded a LCA , . ceed . c . . d ee e e . e . b . ec / e e . a ee e –[17].

The SRB also observes that[18]:

> N . a . I a . a . J e c , . ceed . . . d ac e e e . e . b . ec / e e . a ee e a . e . , . ce . . c , . ceed . . d a . e . . e a c , a ab . e de . ee f , . ec f . de , . . . , / e . . , e c . e . , c . e . ' f d a d a . e . . –

So, in the context of the SRB's assessment, d ¬ , f e . . . de . a . . J e c , . ceed . – refers for the SRB to the LCA proceedings[19], and when discussing the Italian LCA and its degree of creditor protections, the SRB makes no mention of additional public funds[20].

> H e e , e , e . ec a . f e . e . e c / e . a e I a . a Dec ee f 25 J e 2017[21] . a e a : [ ] e ba . . . . be , . LCA a , . / ded [f . b] e [I a . a] Ba . La [Te U c Ba ca]. H e e , e . d a . . da , . ce- d . e a . c f . . d , . / e . e . . da a e e ec : . e ef . e a , , . , . a e e / . a e a . a a e c . . f e . . , . add a . . . . e . . e , ec . ef . e ee e Ba . La – [author's translation]

This wording suggests that the regime actually implemented was a modified version of the ordinary liquidation proceedings, by the addition of liquidation aid. The recital of the actual Decree text offers a similar view when pointing out that:

> W . ea . . e . f , . b . c . . , , . , e , . ace e f [e ba . .] a f . ced

others – by the chairman of the European Banking Authority Andrea Enria who stressed that creditors in liquidation should not be better off than in resolution[22]. The fact that insolvency the cases of Veneto and Vicenza. In order to avoid this uncertainty, the best option would be to further harmonise insolvency laws, possibly introducing an EU-wide regime.

For banking union to function properly, banks, creditors and taxpayers deserve to have certainty about the rules governing liquidation. This objective would best be served by a single EU insolvency regime to complement the current EU framework for resolution, and by a clarification of the extent to which Member States have discretion to establish the *fiscal* public interest when it comes to liquidation aid.

References

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SRB (2017c) 'Decision of the Single Resolution Board in its executive session of 23 June 2017 concerning the assessment of the conditions for resolution in respect of Veneto Banca S.p.A., non-confidential version', SRB/EES/2017/11, Single Resolution Board

SRB (2017d) 'Notice summarising the effects of the decision taken in respect of Banca Popolare di Vicenza S.p.A.', Single Resolution Board