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**“THE REFORM OF THE ITALIAN MUTUAL BANKS:
THE IMPLICATIONS ON THEIR OPERATIONS”**

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A handwritten signature in black ink, appearing to read "Rosario", written over a horizontal line.

ABSTRACT

Questa tesi ha lo scopo di analizzare la riforma delle Banche di Credito Cooperativo in Italia emanata nel febbraio 2016 che prevede la riorganizzazione del credito cooperativo secondo il modello del gruppo bancario cooperativo regolato dal contratto di coesione. Nel primo capitolo viene analizzato il testo della Legge 14 Febbraio 2016 n. 18, TUB, considerandone i relativi effetti. Nel secondo capitolo vengono studiati i modelli di Crédit Agricole e Rabobank, considerati i principali gruppi bancari cooperativi in Europa che potrebbero essere considerati come esempi per la riforma delle BCC italiane. Nel terzo capitolo, vengono analizzati i principi finanziari che potrebbero rappresentare una guida per la redazione del contratto di coesione. I principi finanziari considerati sono quelli sui quali si basano alcune rilevanti istituzioni finanziarie, quali, il Fondo Interbancario di Tutela di Depositi, le Agenzie di Rating e quelli contenuti nei piani di recupero bancari redatti dall'European Banking Authority. Nel quarto capitolo vengono valutati i possibili scenari ai quali potrebbe portare lo sviluppo della riforma. In conclusione emerge che il contratto di coesione dovrebbe essere basato su un sistema di indicatori e misurazione dei rischi volto a monitorare l'adeguatezza patrimoniale, la liquidità e la solvibilità di ogni banca aderente al gruppo al fine di identificare tempestivamente situazioni di criticità finanziaria. Per quanto riguarda il nuovo riassetto organizzativo del credito cooperativo italiano, un accordo definitivo non è ancora stato raggiunto, tuttavia attualmente la formazione di due gruppi bancari cooperativi sembra essere quella più probabile.

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INTRODUCTION

Mutual Banks have traditionally represented an important portion of the Italian banking business, with strong ties to local businesses. The Article 45 of the Italian Constitution recognizes the social function of the mutual sector, characterized by a mutual cooperation without goals of private speculation.

In Italy two kinds of mutual banking systems are present, the Banche del Credito Cooperativo (BCCs) and the Banche Popolari. However, despite their common mutual nature, they have developed different characteristics through the years. While the Banche Popolari have progressively moved by their original nature, transforming themselves into joint-stock companies, the BCCs have always remained deeply rooted in the local territory of their competence maintaining their mutual features.

In my thesis I will focus on the BCCs and on the current reform that aims to improve their structure considered no more suitable to survive in an always more complex financial landscape characterized by the consequences of the financial crisis of 2007-2008, by the evolution of the regulation and supervision systems and by the needs of change required by the technological progress. This situation is not different by the one faced by the whole banking system. However, the BCCs find themselves in a weak situation as their model of governance limits their capacity to increase their capital and the strong link to the local territory does not allow an adequate diversification level exposing the banks to high risks of financial distress.

The Italian Credito Cooperativo is a system based on a network comprising 381 cooperative banks including Banche di Credito Cooperativo, Casse Rurali, Casse Raiffeisen in Alto Adige and several service companies, all working together to guarantee a complete and diversified range of products in accordance with their cooperative values. The associative structure is subdivided into three levels: local (BCCs), regional (Local Federations) and national (Federcasse). The individual BCCs are associated with the Local Federations (representing one or more regions) which in turn are members of Federcasse, the Italian Federation of BCCs. Federcasse represents and protects the rights of its associated banks, offering them legal, fiscal, and organizational assistance, providing also support in communications and training leading benefits to the entire Cooperative Credit system.

The first Italian cooperative bank was Cassa Rurale di Loreggia founded in 1883 by Leone Wollemborg, in the province of Padova. During the fascist period many cooperative banks were

ordered to close. However, after the second World War, the advent of the Italian Republic and of the Italian Constitution have recognized the social role of the mutual cooperatives, relaunching Casse Rurali and Artigiane. In 1950 Federcasse (Federazione Italiana delle Casse Rurali e Artigiane), originally founded in 1909, was reformed and became a member of Confcooperative in 1967. Iccrea (Istituto di Credito delle Casse Rurali e Artigiane) was founded in 1963, with the goal of facilitating, coordinating and improving the activities of individual cooperative banks through financial intermediation and assistance. In 1993 the Casse Rurali e Artigiane changed their name into Banche di Credito Cooperativo (BCCs). In the same year the Consolidated Banking Law (Testo Unico Bancario) came into force, lifting the legal limitations which had previously governed the banking operations of cooperative banks.

Nowadays, the BCCs reform is thought to provide a solution to the weaknesses of the cooperative sector to enforce BCCs and to enable them to compete at European level. The aim of this thesis is to analyse the current reform evaluating the effects of the new Law at structural and national level.

In the first chapter I will analyse the text of the reform, the Law of 14th February 2016 N. 18, highlighting the main innovations introduced in the system and considering the main implied financial effects. In the second chapter I will study the two main European mutual banking groups: Crédit Agricole and Rabobank, deepening the mechanisms of their internal structure such as the cross-guarantee system and the regulation of the internal relationships between the holdings and individual member banks. Because of their success, these two models may provide a good example for the developing of the Italian reform. Following, in the third chapter I will analyse the principles used by some relevant financial institutions, such as rating agencies, the FITD, and the banks recovery plans provided by EBA, in order to determine the main financial principles that may represent a guide for the formation of the cohesion contract. After that, the fourth chapter aims to provide an analysis of the possible scenarios that could take place as a consequence of the reform. I will analyse the main consequences in the Italian system considering possible advantages and disadvantages, providing in conclusion my personal considerations about the emerged elements.

CHAPTER 1 – THE REFORM OF THE ITALIAN MUTUAL BANKS: ANALYSIS OF THE NEW LAW

1.1 THE MUTUAL SECTOR AND THE BANCHE DI CREDITO COOPERATIVO: A COMPLEX FINANCIAL LANDSCAPE

The mutual credit covers a special role in the Italian banking system. The Article 45 of the Italian Constitution recognizes the social function of the mutual sector characterized by mutual cooperation without goals of private speculation.

A relevant part of the Italian mutual sector is represented by the cooperative banks (BCCs)¹ considered “banche cooperative a mutualità prevalente”.

Their mutual nature is represented by two main aspects:

- The principle of prevalence that recurs when more than the 50% of the risk activities, such as loans, are addressed to shareholders or to risk-free assets.
- The earnings distribution. In accordance with the Art. 37 TUB², the BCCs have to assign their profit for the 70% to legal reserves and for a further 3% to a mutual fund for the promotion and development of the cooperative sector. The remaining part of earnings has to be assigned to mutual and charity purposes. The legislation provides a limit for the dividend distribution to shareholders.

Other aspects that characterize the BCCs are:

- Economic democracy among shareholders. The minimum number of shareholders per BCC is 200 (in case this number decreases, new shareholders have to be reinstated within one year, otherwise the liquidation of the bank would start). The voting right principle is “one head one vote”. Every shareholder disposes of just one vote regardless of his participation amount that cannot exceed 50 thousand euro (in order to avoid disparities among shareholders that may hamper the mutual functions).

¹ In English the expression “mutual banks” is referred to all the financial institutions part of the mutual sector without distinguishing between Popular Banks and Cooperative Banks. In this thesis both the expressions “mutual banks” and “cooperative banks” will be used in reference to the BCCs.

² Art. 37, TUB. Utili. 1. Le banche di credito cooperativo devono destinare almeno il settanta per cento degli utili netti annuali a riserva legale. 2. Una quota degli utili netti annuali deve essere corrisposta ai fondi mutualistici per la promozione e lo sviluppo della cooperazione nella misura e con le modalità previste dalla legge. 3. La quota di utili che non è assegnata ai sensi dei commi precedenti e che non è utilizzata per la rivalutazione delle azioni o assegnata ad altre riserve o distribuita ai soci deve essere destinata a fini di beneficenza o mutualità.

- Strong local presence. BCCs operate in a limited geographical and they provide their services for that territory, also called “territory of competence”. At least the 95% of their risk activities of each single BCC has to be exercised in its area of competence. Also BCCs’ shareholders are people and companies that work in that specific territory.

Because of their nature, BCCs are subject either to the banking regulations that aim to protect savings and to ensure financial stability, either to regulations thought to protect their mutual values.

As stated by the Art. 2 of the BCCs Corporate Statute, “the Bank aims to serve the interests of its stakeholders and members of the local community through the provision of financial operations and services, to improve their moral, cultural and economic conditions, promoting collaboration and teaching the benefits of saving and forward planning as well as encouraging social unity and responsible, sustainable growth in the surrounding territory. The Bank distinguishes itself through its support for the community and its commitment to further the common good.”

Most cooperative banks have been designed to perpetually accumulate capital, building an always larger intergenerational endowment³. However, this structure appears to be inadequate to the current financial landscape characterized by financial troubles and instability caused by the financial crisis of the 2007-2008, by the evolution of the vigilance and supervision procedures and by the continuous needs of change required by the technological progress. In this scenario, BCCs find themselves caught between their capital-accumulating set-ups and pressures to increase their profitability.

The main financial issues currently faced by BCCs regard:

- Difficulties in raising capital: the cooperative governance framework combined with restricted voting rights makes raising capital particularly difficult, especially at the time of distress when financial resources are urgently needed. BCCs can only raise new cooperative capital by increasing their membership or by asking existing members to buy more shares. However, in time of difficulties, many members and clients may not be in a position to provide significant amounts of fresh capital. Indeed, members usually buy just the minimum number of shares needed to gain access to the benefits that derive from the cooperative’s activities without considering it as a financial investment (that

³ W. Fonteyne, July 2007, Cooperative Banks in Europe. “The capital of the cooperative banks is not owned by the current members but by the cooperative itself. The capital is available for use by current members, under the implicit or explicit understanding that they will grow it further and pass it on to the next generation of members.”

would bring very low dividends). Furthermore, often legal restrictions recur that limit the total value of shares a shareholder can hold. Another way to raise new capital may be represented by the issuance of particular securities but these tools would require high remuneration. Therefore, in both cases raising capital would be complex and time-consuming.

- Difficulties of adaptation to a changing environment: cooperative banks may have more difficulties adjusting to adverse circumstances as BCCs are usually based on high fixed costs and their rigid structure does not allow a fast reaction to external changes.
- Agency problems: The cooperative governance structure limits shareholders control over management. The 'one member-one vote' principle and ownership limits result in owner-manager conflicts in accordance with the agency cost theory as small shareholders typically do not have the incentive to exert effective control over management.
- Difficulties to implement expansionary paths: expansionary policies put significance pressure on cooperative's solvency and liquidity. As new acquisitions (unless they have the form of mergers with larger institutions) cannot be financed through the issuance of new equity but they have to be paid through the issuance of new debt causing a deterioration in the balance-sheet.

In many European Countries, in order to face these structural issues, cooperative banks have turned into commercial financial institutions losing their cooperative features to increase their capital access. However, many other Countries think that this is not the solution to the problem. This is the case of Italy that argues to support its cooperative banking system, aware of its relevant social role in the past and of the important contribution that it can still offer: to provide people with the tools and resources to collectively and individually help themselves.

1.2 OVERVIEW OF THE BCCs REFORM

As we have seen in the previous chapter, BCCs find themselves in a particularly weak position in the current financial context. Their governance structure limits their capacity to access to financial resources and the territorial constraints do not allow an adequate diversification level, bringing to higher risks. Because of that, BCCs had to increase their levels of coverage dramatically affecting their auto financing possibilities. This in turn has increased the exposure of BCCs to financial tensions because of their financial difficulties of increasing their capital in accordance with the measures and the speed of intervention required by the national and European regulations.

In light of the elements considered in the previous paragraph, it seems to be necessary to support the mutual sector promoting a greater integration level.

The increase of competition and the continuous technological progress represent a threat for the business model of the BCCs. Indeed high investments in technology and in modernization of distribution channels are needed but they could be possible only in presence of economies of scale.

This appears to be far from the reality of BCCs that still operate with a traditional business model and with old distribution networks. Because of their small dimensions they are characterized by rigid cost structures that do not allow to increase the level of efficiency. Also the capital constraints regarding shareholders represent an obstacle to the recapitalization of BCCs.

It seems clear that a reform of the BCCs is needed in order to adapt the structure of the Italian BCCs to the current financial landscape. In particular, the reform focuses on the improvement of the governance model and on the development of an efficient guarantee system.

Governance

As regards the governance, BCCs may benefit from the territorial feature as being close to the local communities would allow a better understanding of local requirements and therefore to improve the service provision. However, these advantages could recur only in presence of a healthy and prudent territorial link. Indeed several times conflicts of interests and local

influences have been observed that have affected decisions of investments and of credit allocation bringing to a loss of efficiency and to higher risks.

These weaknesses related to the governance, may be solved by the formation of larger institutions such as banking groups. In order to align the Italian BCCs with the European evolution, the Bank of Italy has promoted a solution that aims to aggregate the Italian BCCs in one or more cooperative banking groups. Indeed, a cooperative banking group with a holding company that disposes of an adequate level of capital and able to access to capital markets can ensure support to BCCs in financial troubles. The relationships between the holding company and the member BCCs are regulated by the contract of cohesion that has the role to ensure the respect of the prudential requirements, the well-functioning and the cohesion of the group. A high integration level, an adequate capitalization level and the capacity to attract investors may create the basis for an increase in efficiency and in the quality of the governance of the single BCCs.

Another important point is the democratization aspect. This involves a high involvement of shareholders in the decision-making process of the banks as they can offer a key contribution in the product, service and policies development. Building solid relationships with customers may represent a great form of value added for the bank.

In sum, the governance has to ensure the development of a prudent and healthy management of the group, the efficiency of the internal control mechanisms and the respect of the prudential capital requirements of each member BCC. The contract of cohesion has to promote high and homogeneous quality standards within the group based on the evaluation of the competences of the member banks' exponents and on the merit recognition.

Cross-guarantee system

Another relevant goal of the reform is to create an internal guarantee mechanism to allow to move financial resources throughout the group on the base of the individual needs of each member BCC.

A cross-guarantee system has been introduced, in accordance to which member banks are required to intervene in solid. The interventions can be either in a vertical sense from the holding to the BCCs either in a horizontal sense among BCCs. In order to ensure the financial stability

of each single BCC the commitment of each bank is proportional to its patrimonial disposals and it is limited to the capital exceeding the individual capital requirements (free capital).

The guarantee in solid of the group has a double function. An internal function of intra-group financial support in cases of insolvency or liquidity problems of member BCCs and an external one in favour of creditors in case of breach of the obligations of a member bank.

The cross-guarantee scheme is regulated by the Art. 4 (127)⁴ of the CRR, that emphasises the prompt transfer of the financial resources from the committed BCCs to the holding. To allow resources to flow throughout the group, it is necessary to eliminate all the possible legislative constraints that may hamper the transition of the resources. Also, it is required the constitution ex ante of specific capital and liquidity buffers (in particular CET1) in order to ensure the prompt availability of the resources in accordance to the regulations. Each member bank issues financing shares that have to be subscribed by the holding to meet the early intervention measures.

Each BCC will be asked to participate to the prompt available funds on the base of its Risk-Weighted Assets (RWA) and of its free capital. It is estimated that, in the context of a group, the cross-guarantee system will increase the CET1 ratio of the BCCs in deficit from an average value of 10,1% to 12,3%.

Regarding the subjects of the reform instead, we find the following bodies:

- the holding company;
- the provincial groups;
- the territorial sub-groups.

⁴ Art. 4 (127), CRR. “Cross-guarantee scheme” means a scheme that meets all the following conditions:

- (a) the institutions fall within the same institutional protection scheme as referred to in Article 113(7);
- (b) the institutions are fully consolidated in accordance with Article 1(1)(b), (c) or (d) or Article 1(2) of Directive 83/349/EEC and are included in the supervision on a consolidated basis of an institution which is a parent institution in a Member State in accordance with Part One, Title II, Chapter 2 of this Regulation and subject to own funds requirements;
- (c) the parent institution in a Member State and the subsidiaries are established in the same Member State and are subject to authorisation and supervision by the same competent authority;
- (d) the parent institution in a Member State and the subsidiaries have entered into a contractual or statutory liability arrangement which protects those institutions and in particular ensures their liquidity and solvency, in order to avoid bankruptcy in the case that it becomes necessary;
- (e) arrangements are in place to ensure the prompt provision of financial means in terms of capital and liquidity if required under the contractual or statutory liability arrangement referred to in point (d);
- (f) the adequacy of the arrangements referred to in points (d) and (e) is monitored on a regular basis by the competent authority;
- (g) the minimum period of notice for a voluntary exit of a subsidiary from the liability arrangement is 10 years;
- (h) the competent authority is empowered to prohibit a voluntary exit of a subsidiary from the liability arrangement;

Holding

The holding is the main body of the group. It has a central role as it is required the enforcement of financial stability, competition, efficiency and healthy and prudent management of the member BCCs. In accordance with the Law 14th February 2016, n.18, the holding must have the following characteristics:

- its legal basis is in Italy;
- it has to be in form of S.p.A.;
- it has to be authorized at the exercise of the banking activity in accordance with the Art. 14⁵ TUB;
- its capital is owned for more than the 50% by the member BCCs;
- its capital has to meet the 1 billion euro threshold;
- it must dispose of organizational structures that allow the exercise of its direction and coordination activities and to ensure the access to the international banking procedures.

The holding has to ensure the protection of the mutual principles of the single BCCs. Among the others, the main powers of the holding consist in:

- the direction and coordination of the group;
- the issuance of disposals for member BCCs and in the control their observation;
- the monitoring of early warning indicators;
- the corrective interventions in cases of deviation from the strategy;
- the distribution of the advantages derived from the activities of the group;
- operations of proportional sanctions.

The holding is owned for the majority by the member BCCs that therefore can exercise their control over it. The other part of its capital instead is open to capital market investments. In this

⁵ Art. 14, TUB. Autorizzazione all'attività bancaria. 1. La Banca d'Italia autorizza l'attività bancaria quando ricorrano le seguenti condizioni: a) sia adottata la forma di società per azioni o di società cooperativa per azioni a responsabilità limitata ; a-bis) la sede legale e la direzione generale siano situate nel territorio della Repubblica b) il capitale versato sia di ammontare non inferiore a quello determinato dalla Banca d'Italia; c) venga presentato un programma concernente l'attività iniziale, unitamente all'atto costitutivo e allo statuto; d) sussistano i presupposti per il rilascio dell'autorizzazione prevista dall'articolo 19 per i titolari delle partecipazioni ivi indicate; e) i soggetti che svolgono funzioni di amministrazione, direzione e controllo siano idonei, ai sensi dell'articolo 26; f) non sussistano, tra la banca o i soggetti del gruppo di appartenenza e altri soggetti, stretti legami che ostacolano l'effettivo esercizio delle funzioni di vigilanza . 2. La Banca d'Italia nega l'autorizzazione quando dalla verifica delle condizioni indicate nel comma 1 non risulti garantita la sana e prudente gestione.

way it can have access to higher amounts of financial resources strengthening the financial soundness of the group.

Furthermore, the holding company is required to have organizational structures able to intermediate the BCCs with the capital markets and the relationship with the BCE regarding reserve requirements and operations of monetary policy. The capacity of the holding to provide technological and operational support to the member BCCs is an element of efficiency and competition of the CBG. Furthermore it represents an element of alignment to the other European Countries.

Essential is also the capacity of the holding to exercise its powers of direction and coordination in full autonomy with its own structures. Only some secondary activities can be assigned to third parties.

Provincial Groups

Another figure present in the group is the ‘provincial group’ thought for BCCs that operate exclusively in the province of Trento and Bolzano.

The provincial group is regulated in the following way:

- the holding must have its legal basis in the province of Trento or Bolzano and it must have the form of S.p.A.;
- the minimum capital requirement of the holding is equal to 250 million euro;
- it must be authorized to the exercise of the banking activities in accordance with the Art. 14 TUB;
- the group can exercise its activities exclusively in the provincial territory of its competence. It is allowed the exercise external to the territory of competence only if they do not exceed the 5% of risk activities of each single bank.

Territorial sub-groups

Other subjects recognized by the reform are the ‘territorial sub-groups’. These groups are banking sub-systems that would be coordinated by a sub-holding. The territorial sub-groups would be formed (and included in the group) only in cases of necessity to establish a stronger

territorial link. Indeed, it could be made only by banks with legal basis within the same region. The minimum dimension required for the territorial sub-groups corresponds to at least the 10% of the total RWA of the BCCs part of the group. The sub-holding exercises support operations for the holding company coordinating and directing the member banks of the sub-group.

The contract of cohesion

The contract of cohesion must ensure the coherence of the strategy and of the operational objectives of the entire group together with the integration and efficiency of the systems of management and control of the whole group.

The role of the holding company and the regulation of its powers appear to be of central importance in the contract. Indeed, throughout its activities, the holding has to enforce the financial stability of the member BCCs, guaranteeing high efficiency, competition and the protection of the mutual principles. Furthermore, it states the principles for the correct provision of the holding's activities of direction and coordination in order to ensure a healthy and prudent management of the group.

As regards the governance, the goal is to promote in every component of the group high quality standards based on the recognition of merits in order to guarantee a healthy and prudent management of the member BCCs without compromising their autonomy. To do that, the statutes of the member BCCs have to include in the regulation of the mechanisms of formation of the internal bodies a phase of consultancy, in which the holding expresses its opinions on the candidates. An analogue mechanism is provided for the revocation of the members. These powers are recognized to the holding by the Art. 37-bis TUB toward all the member BCCs.

Regarding internal control systems, the holding has to implement the risk profile (Risk Appetite Framework – RAF⁶) and the methodologies of risk measurement at consolidated level. All the internal control activities of the group including internal audit and risk assessment procedures development have to be assigned to the holding company. Furthermore, the holding has to verify the policies of risk management of the member BCCs. The internal control activities are based on a system of early warning indicators that allow to monitor the risks of the member BCCs and to guarantee the prompt provision of the intra group support measures.

⁶ RAF can be defined as the total impact of risk an organisation is prepared to accept in the pursuit of its strategic objectives (KPMG).

The holding has to issue dispositions about the following areas:

- the whole process of granting of credit and the risk measurement;
- the funding policies, determining in which measure each bank contributes to provide financial resources to the group and operations of risk and liquidity management;
- the investment strategies and the management of the connected risks.

The advantages derived from the activities of the group have to be distributed among member BCCs in relation to their performance. The banks in charge of higher guarantee commitments have to be compensated by an adequate level of advantages.

Formation of the Cooperative Banking Group

The first step of the procedure is to ensure the presence of all the elements required. The bank that intends to become the holding of the group must submit to the Bank of Italy an instance together with:

- a scheme of the cohesion contract (already including the cross-guarantee scheme);
- the list of the BCCs that intend to join the group and all their statutes.

The Bank of Italy controls that all the elements meet the characteristics required by the law (TUB) regarding the exercise of the banking activities, capital thresholds and schemes of the cohesion contract and of the guarantee system suitable to ensure the prudent and healthy management of the group.

Vigilance

The holding is in charge to issue dispositions to ensure the respect of the prudential requirement of the group such as capital buffers, liquidity levels and the homogeneity of the methodologies of risk measurement of the whole group. The holding homogenises the criteria of the methodologies for the documents ICAAP prepared by each single BCC in order to ensure the reliability of the process of determination of the ICAAP of the group. The holding's dispositions have to ensure also the respect of the other prudential regulations (such as transparency, internal controls and governance). Furthermore, in accordance to the Art. 61 comma 4⁷, TUB, the

⁷ Art. 61 comma 4, TUB. La capogruppo, nell'esercizio dell'attività di direzione e di coordinamento, emana disposizioni alle componenti del gruppo per l'esecuzione delle istruzioni impartite dalla Banca d'Italia

holding has to ensure the execution of the instruction of the authority of vigilance, Banca d'Italia and it must also submit periodical reports and further information required for the formation of the consolidated balance sheet of the group.

As the formation of the contract of cohesion is still under discussion, in the following chapters I will try to determine the financial and prudential principles on which the cohesion contract should be based. To do that, I will analyse the financial criteria used by other financial institutions such as the FITD, the rating agencies and by the banks' recovery plans, trying to reach my own conclusions.

nell'interesse della stabilità del gruppo. Gli amministratori delle società del gruppo sono tenuti a fornire ogni dato e informazione per l'emanazione delle disposizioni e la necessaria collaborazione per il rispetto delle norme sulla vigilanza consolidata.

1.3 ANALYSIS OF THE LAW 14th FEBRUARY 2016, N. 18

The new financial scenario followed by the global financial problems has put in strain the Italian banking system with the risk of failure of the major Italian mutual banks.

To face this situation of emergency, the Italian government has issued a specific decree-law putting particular emphasis on mutual banks governance reforms.

As we have seen in the previous paragraph, the aim of the reform is to re-organize the Italian BCCs in a cooperative banking group under the direction and control of a holding company. In this way, the BCCs would see their financial position strengthen. Indeed, the large size of the group would allow them to have access to higher amounts of financial resources. Therefore, their financial soundness would increase and the cross-guarantee system would allow a high and fast mobility of financial resources throughout the group to support the member BCCs in financial troubles.

The Law n. 18 was issued as a decree-law by the government the 14th February 2016 and was approved by the Italian parliament the 25th March 2016.

It is structured in four main parts called “Capo I”, “Capo II”, “Capo III” and “Capo IV”.

Following, I will analyse the Law providing an overview of the whole regulation and deepening in particular the Capo I as it regards the main focus of the thesis: the formation and the functions of the Cooperative Banking Group.

Capo I

The Article 1 explains all the amendments to the Law 1st September 1993, n. 385 (Testo Unico Bancario).

In particular, through the amendments provided to the Article 37-bis of the Law 1st September 1993, n.385, it introduces the concept of “Cooperative Banking Group” (Gruppo Bancario Cooperativo).

It is highlighted the role of the holding company that controls and coordinates the activities and functions of the other banks part of the group. The holding company must have the form of S.p.A. and a capital of minimum one billion euro. Its capital is owned for the majority by the BCCs part of the group.

The relations between the holding and the member BCCs are regulated by the “Cohesion Contract” that indicates the holding company in charge of the direction of the group and regulates its powers. Among the others, the main powers of the holding include:

- the development of the strategic activities of the group;
- the development of coordination and control functions in order to ensure the respect of the financial prudential requirements provided by the banking and financial law for the cooperative banking group;
- the cases in which the holding can nominate or revoke a component of the group;
- the exclusion of a BCC from the group in case it does not respect the measures provided by the cohesion contract;
- the criteria of compensation and distribution of the advantages arising from the activities of the group;
- the conditions of adherence to the contract other than the conditions of exclusion from the group.

The statute of the holding has to indicate the maximum number of shares (with corresponding voting rights) that can be owned by each shareholder. Furthermore, the contract must establish a cross-guarantee system in accordance to which, the BCCs guarantee in solid the obligations subscribed by the holding.

The acceptance or rejection of the requests of adhesion, or the exclusion of a single BCC from the group has to be authorized by the Bank of Italy that has to control that the prudential financial constraints are maintained.

Another aspect regards the role of the Minister of Economic and Finance. The Article 37-bis recognizes his power to take measures to ensure the organizational and dimensional adequacy of the group. With the authorization of the Bank of Italy, the Minister can issue a decree-law to establish the minimum number of member BCCs of the group and he can establish different patrimonial participation levels of the BCCs in order to ensure the stability of the group. Moreover, he can provide the modalities to protect the different cultural features of the BCCs of the territory of Trento and Bolzano.

The Bank of Italy covers a role of vigilance as it ensures the prudent management and efficiency of the group, in particular with reference to the minimum organizational and operational requirements of the holding, the minimum content of the cohesion contract and the minimum patrimonial requirements of each single member BCC.

“Art. 1

Modifiche al decreto legislativo 1° settembre 1993, n. 385

"Art. 37-bis

Gruppo Bancario Cooperativo

1. Il gruppo bancario cooperativo e' composto da:

a) una societa' capogruppo costituita in forma di societa' per azioni e autorizzata all'esercizio dell'attivita' bancaria il cui capitale e' detenuto in misura maggioritaria dalle banche di credito cooperativo appartenenti al gruppo, che esercita attivita' di direzione e coordinamento sulle societa' del gruppo sulla base di un contratto conforme a quanto previsto dal comma 3⁸ del presente articolo. Il medesimo contratto assicura l'esistenza di una situazione di controllo come definito dai principi contabili internazionali adottati dall'Unione europea; il requisito minimo di patrimonio netto della societa' capogruppo e' di un miliardo di euro;

b) le banche di credito cooperativo che aderiscono al contratto e hanno adottato le connesse clausole statutarie;

c) le societa' bancarie, finanziarie e strumentali controllate dalla capogruppo, come definite dall'articolo 59⁹.

⁸ Art. 37-bis comma 3, Law 14th February 2016, n.18, TUB. Il contratto di coesione che disciplina la direzione e il coordinamento della capogruppo sul gruppo indica:

a) la banca capogruppo, cui e' attribuita la direzione e il coordinamento del gruppo; b) i poteri della capogruppo che, nel rispetto delle finalita' mutualistiche, includono: 1) l'individuazione e l'attuazione degli indirizzi strategici ed obiettivi operativi del gruppo nonche' gli altri poteri necessari per l'attivita' di direzione e coordinamento, proporzionati alla rischiosita' delle banche aderenti, ivi compresi i controlli ed i poteri di influenza sulle banche aderenti volti ad assicurare il rispetto dei requisiti prudenziali e delle altre disposizioni in materia bancaria e finanziaria applicabili al gruppo e ai suoi componenti; 2) i casi, comunque motivati ed eccezionali, in cui la capogruppo puo', rispettivamente, nominare, opporsi alla nomina o revocare uno o piu' componenti, fino a concorrenza della maggioranza, degli organi di amministrazione e controllo delle societa' aderenti al gruppo e le modalita' di esercizio di tali poteri; 3) l'esclusione di una banca dal gruppo in caso di gravi violazioni degli obblighi previsti dal contratto e le altre misure sanzionatorie graduate in relazione alla gravita' della violazione.

⁹ Articolo 59, TUB. Vigilanza su base consolidata. 1. Ai fini del presente capo: a) il controllo sussiste nei casi previsti dall'articolo 23 (1); b) per "societa' finanziarie" si intendono le societa' che esercitano, in via esclusiva o prevalente: l'attivita' di assunzione di partecipazioni aventi le caratteristiche indicate dalla Banca d'Italia; una o piu' delle attivita' previste dall'articolo 1, comma 2, lettera f), numeri da 2 a 12; altre attivita' finanziarie previste ai sensi del numero 15 della medesima lettera; le attivita' di cui all'articolo 1, comma 1, lettera n), del decreto legislativo 24 febbraio 1998, n. 58 (2); b-bis) per "di partecipazione finanziaria mista" si intendono le societa' di cui all'articolo 1, comma 1, lettera v), del decreto legislativo 30 maggio 2005, n. 142 (3); c) per "societa' strumentali" si intendono le societa' che esercitano, in via esclusiva o prevalente, attivita' che hanno carattere ausiliario delle attivita' delle societa' del gruppo, comprese quelle consistenti nella proprieta' e nell'amministrazione di immobili e nella gestione di servizi anche informatici.

c-bis) eventuali sottogruppi territoriali facenti capo a una banca costituita in forma di società per azioni sottoposta a direzione e coordinamento della capogruppo di cui alla lettera a) e composti dalle altre società di cui alle lettere b) e c).

1-bis. Le banche di credito cooperativo aventi sede legale nelle province autonome di Trento e di Bolzano possono rispettivamente costituire autonomi gruppi bancari cooperativi composti solo da banche aventi sede e operanti esclusivamente nella medesima provincia autonoma, tra cui la corrispondente banca capogruppo, la quale adotta una delle forme di cui all'articolo 14, comma 1, lettera a)¹⁰; il requisito minimo di patrimonio netto è stabilito dalla Banca d'Italia ai sensi del comma 7-bis¹¹.

2. Lo statuto della capogruppo indica il numero massimo delle azioni con diritto di voto che possono essere detenute da ciascun socio, direttamente o indirettamente, ai sensi dell'articolo 22, comma 1 (TUB)¹².

3. Il contratto di coesione che disciplina la direzione e il coordinamento della capogruppo sul gruppo indica:

a) la banca capogruppo, cui è attribuita la direzione e il coordinamento del gruppo;

b) i poteri della capogruppo che, nel rispetto delle finalità mutualistiche, includono:

1) l'individuazione e l'attuazione degli indirizzi strategici ed obiettivi operativi del gruppo nonché gli altri poteri necessari per l'attività di direzione e coordinamento, proporzionati alla rischiosità delle banche aderenti, ivi compresi i controlli ed i poteri di influenza sulle banche aderenti volti ad assicurare il rispetto dei requisiti prudenziali e delle altre disposizioni in materia bancaria e finanziaria applicabili al gruppo e ai suoi componenti;

2) i casi, comunque motivati ed eccezionali, in cui la capogruppo può, rispettivamente, nominare, opporsi alla nomina o revocare uno o più componenti, fino a concorrenza della

¹⁰ Art. 14, TUB. Autorizzazione all'attività Bancaria. 1. La Banca d'Italia autorizza l'attività bancaria quando ricorrano le seguenti condizioni: a) sia adottata la forma di società per azioni o di società cooperativa per azioni a responsabilità limitata.

¹¹ Art. 37-bis, comma 7-bis, Law 14th February 2016, n. 18, TUB. La Banca d'Italia, al fine di assicurare la sana e prudente gestione, la competitività e l'efficienza del gruppo bancario cooperativo, nel rispetto della disciplina prudenziale applicabile e delle finalità mutualistiche, detta disposizioni di attuazione del presente articolo e dell'articolo 37-ter, con particolare riferimento: c) ai requisiti specifici, compreso il requisito minimo di patrimonio netto della capogruppo, relativi ai gruppi bancari cooperativi previsti dal comma 1-bis.

¹² Articolo 22 comma 1, TUB. Partecipazioni indirette e acquisti di concerto. 1. Ai fini dell'applicazione dei capi III e IV del presente Titolo si considerano anche le partecipazioni acquisite o comunque possedute per il tramite di società controllate, di società fiduciarie o per interposta persona.

maggioranza, degli organi di amministrazione e controllo delle società aderenti al gruppo e le modalità di esercizio di tali poteri;

3) l'esclusione di una banca dal gruppo in caso di gravi violazioni degli obblighi previsti dal contratto e le altre misure sanzionatorie graduate in relazione alla gravità della violazione;

c) i criteri di compensazione e l'equilibrio nella distribuzione dei vantaggi derivanti dall'attività comune;

d) i criteri e le condizioni di adesione, di diniego all'adesione nonché di esclusione dal gruppo, secondo criteri non discriminatori in linea con il principio di solidarietà tra le banche cooperative a mutualità prevalente. Non è in ogni caso ammesso il recesso.

4. Il contratto di cui al comma 3 prevede la garanzia in solido delle obbligazioni assunte dalla capogruppo e dalle altre banche aderenti, nel rispetto della disciplina prudenziale dei gruppi bancari e delle singole banche aderenti.

5. L'adesione, il rigetto delle richieste di adesione e l'esclusione di una banca di credito cooperativo sono autorizzati dalla Banca d'Italia avendo riguardo alla sana e prudente gestione del gruppo e della singola banca.

...

7. Il Ministro dell'economia e delle finanze, al fine di assicurare l'adeguatezza dimensionale e organizzativa del gruppo bancario cooperativo, può stabilire con proprio decreto, sentita la Banca d'Italia:

a) il numero minimo di banche di credito cooperativo di un gruppo bancario cooperativo;

b) una soglia di partecipazione delle banche di credito cooperativo al capitale della società capogruppo diversa da quella indicata al comma 1, lettera a), tenuto conto delle esigenze di stabilità del gruppo;

c) le modalità e i criteri per assicurare il riconoscimento e la salvaguardia delle peculiarità linguistiche e culturali delle banche di credito cooperativo aventi sede legale nelle regioni a statuto speciale e nelle province autonome di Trento e di Bolzano.

7-bis. La Banca d'Italia, al fine di assicurare la sana e prudente gestione, la competitività e l'efficienza del gruppo bancario cooperativo, nel rispetto della disciplina

prudenziale applicabile e delle finalita' mutualistiche, detta disposizioni di attuazione del presente articolo e dell'articolo 37-ter, con particolare riferimento:

a) ai requisiti minimi organizzativi e operativi della capogruppo;

b) al contenuto minimo del contratto di cui al comma 3¹³, alle caratteristiche della garanzia di cui al comma 4¹⁴, al procedimento per la costituzione del gruppo e all'adesione al medesimo;

c) ai requisiti specifici, compreso il requisito minimo di patrimonio netto della capogruppo, relativi ai gruppi bancari cooperativi previsti dal comma 1-bis¹⁵.

Following, the amendments to the Article 37-ter of the Law 1st September 1993, n.385 regulate the formation of the cooperative banking group. The bank that aims to cover the role of holding company must submit to the Bank of Italy a scheme of the cohesion contract in accordance with the Article 37-bis together with a list of the BCCs that want to join the group.

The Bank of Italy controls that all the requirements provided by the Article 37-bis are met. In particular, it checks the adequacy of the patrimonial level of the group required for the prudential management of the group.

Once the controls of the Bank of Italy have been developed, the BCCs can sign the cohesion contract with the holding in accordance with the Article 37-bis.

Then, the cohesion contract is transmitted to the Bank of Italy that registers the group in the specific groups register.

¹³ Art. 37-bis, comma 3, Law 14th February 2016, TUB. L'esclusione di una banca dal gruppo in caso di gravi violazioni degli obblighi previsti dal contratto e le altre misure sanzionatorie graduate in relazione alla gravita' della violazione.

¹⁴ Art. 37-bis, comma 4, Law 14th February 2016. Il contratto di cui al comma 3 prevede la garanzia in solido delle obbligazioni assunte dalla capogruppo e dalle altre banche aderenti, nel rispetto della disciplina prudenziale dei gruppi bancari e delle singole banche aderenti.

¹⁵ Art. 37-bis, comma 1-bis, Law 14th February 2016. Le banche di credito cooperativo aventi sede legale nelle province autonome di Trento e di Bolzano possono rispettivamente costituire autonomi gruppi bancari cooperativi composti solo da banche aventi sede e operanti esclusivamente nella medesima provincia autonoma, tra cui la corrispondente banca capogruppo, la quale adotta una delle forme di cui all'articolo 14, comma 1, lettera a); il requisito minimo di patrimonio netto e' stabilito dalla Banca d'Italia ai sensi del comma 7-bis.

“Art. 37-ter

Costituzione del gruppo bancario cooperativo

1. La banca che intenda assumere il ruolo di capogruppo ai sensi dell'articolo 37-bis, comma 1, lettera a), trasmette alla Banca d'Italia:

a) uno schema di contratto conforme a quanto stabilito ai sensi dell'articolo 37-bis;

b) un elenco delle banche di credito cooperativo e delle altre società che intendono aderire al gruppo bancario cooperativo.

2. La Banca d'Italia accerta la sussistenza delle condizioni previste ai sensi dell'articolo 37-bis e, in particolare, il grado di adeguatezza patrimoniale e finanziaria del gruppo e l'idoneità del contratto a consentire la sana e prudente gestione del gruppo.

3. A seguito dell'accertamento previsto dal comma 2, le banche di credito ((cooperativo)) stipulano con la capogruppo il contratto di cui all'articolo 37-bis e provvedono alle necessarie modifiche statutarie, che sono approvate con le maggioranze previste dall'articolo 31, comma 1”.

The Article 2 states the enactments that a cooperative bank has to follow in order to join a Cooperative Group or to become the holding company. Legal terms, deadlines, required documentation and procedures are explained. Within 90 days from the inscription of the group in the groups register (from the Bank of Italy), a BCC can ask to join the group at the same conditions of the other BCCs. The holding communicates the acceptance or rejection of the request within 30 days from its reception. If the holding does not provide any answer, the request is considered accepted. In case of rejection, an answer of the holding is sent to the BCC and to the Bank of Italy (in accordance to the Article 37-bis, comma 5 of the Law 1st September 1993, n. 385) explaining the reasons of its decision.

The Law leaves open a way out for the BCCs that decide to do not join the cooperative banking group. These BCCs have to assume the form of S.p.A. (individually or even jointly with other BCCs) authorized to the exercise of the banking activity. At the moment of the formation of the new society, the BCC has to pay to the State an amount of money equal to the 20% of its capital at the 31st December 2015. After that, the BCC has to modify its corporate object in order to exclude the exercise of the banking activity and to maintain just the mutual functions. In case the BCC does not obtain the authorization to form another S.p.A. independent from the group, the BCC is obliged to join an already existing cooperative group within the following 90 days.

“Art. 2

Disposizioni attuative

1...la comunicazione di cui all'articolo 37-ter, comma 1¹⁶, e' inviata alla Banca d'Italia entro 18 mesi dall'entrata in vigore delle disposizioni emanate ai sensi dell'articolo 37-bis, ((commi 7 e 7-bis))¹⁷, del decreto legislativo 1° settembre 1993, n. 385.

2... entro 90 giorni dall'iscrizione nel registro delle imprese di cui al comma 4¹⁸ dell'articolo 37-ter del decreto legislativo 1° settembre 1993, n. 385, una banca di credito cooperativo puo' chiedere di aderire a un gruppo costituito ai sensi dell'articolo 37-bis alle medesime condizioni previste per gli aderenti originari. L'organo amministrativo della capogruppo, sentito l'organo di controllo, comunica alla richiedente la deliberazione assunta entro 30 giorni dal ricevimento della domanda di adesione. In caso di mancata risposta nel termine previsto la domanda si ha per accolta.

In caso di diniego dell'adesione, la decisione e le motivazioni, nel rispetto di quanto previsto dall'articolo 37-bis, comma 3, lettera d)¹⁹, poste a base della delibera, sono comunicate dalla capogruppo alla banca richiedente e alla Banca d'Italia ai fini dell'autorizzazione prevista dall'articolo 37-bis, comma 5²⁰, del decreto legislativo 1°

¹⁶ Art. 37-ter comma 1, Law 14th February 2016, n.18, TUB. 1. La banca che intenda assumere il ruolo di capogruppo ai sensi dell'articolo 37-bis, comma 1, lettera a), trasmette alla Banca d'Italia: a) uno schema di contratto conforme a quanto stabilito ai sensi dell'articolo 37-bis; b) un elenco delle banche di credito cooperativo e delle altre societa' che intendono aderire al gruppo bancario cooperativo.

¹⁷ Art. 37-bis, comma 7 and 7-bis, Law 14th February 2016, n.18, TUB. 7. Il Ministro dell'economia e delle finanze, al fine di assicurare l'adeguatezza dimensionale e organizzativa del gruppo bancario cooperativo, puo' stabilire con proprio decreto, sentita la Banca d'Italia: a) il numero minimo di banche di credito cooperativo di un gruppo bancario cooperativo; b) una soglia di partecipazione delle banche di credito cooperativo al capitale della societa' capogruppo diversa da quella indicata al comma 1, lettera a), tenuto conto delle esigenze di stabilita' del gruppo; c) le modalita' e i criteri per assicurare il riconoscimento e la salvaguardia delle peculiarita' linguistiche e culturali delle banche di credito cooperativo aventi sede legale nelle regioni a statuto speciale e nelle province autonome di Trento e di Bolzano.

7-bis. La Banca d'Italia, al fine di assicurare la sana e prudente gestione, la competitivita' e l'efficienza del gruppo bancario cooperativo, nel rispetto della disciplina prudenziale applicabile e delle finalita' mutualistiche, detta disposizioni di attuazione del presente articolo e dell'articolo 37-ter, con particolare riferimento: a) ai requisiti minimi organizzativi e operativi della capogruppo; b) al contenuto minimo del contratto di cui al comma 3, alle caratteristiche della garanzia di cui al comma 4, al procedimento per la costituzione del gruppo e all'adesione al medesimo; c) ai requisiti specifici, compreso il requisito minimo di patrimonio netto della capogruppo, relativi ai gruppi bancari cooperativi previsti dal comma 1-bis.

¹⁸ Art. 37-ter comma 4, Law 14th February 2016, n.18, TUB. 4. Il contratto e' trasmesso alla Banca d'Italia, che provvede all'iscrizione del gruppo nell'albo dei gruppi. Successivamente, si da' corso all'iscrizione nel registro delle imprese ai sensi dell'articolo 2497-bis, secondo comma, del codice civile".

¹⁹ Art. 37-bis, comma 3, Law 14th February 2016, n.18. 3. d) i criteri e le condizioni di adesione, di diniego all'adesione nonche' di esclusione dal gruppo, secondo criteri non discriminatori in linea con il principio di solidarieta' tra le banche cooperative a mutualita' prevalente. Non e' in ogni caso ammesso il recesso.

²⁰ Art. 37-bis, comma 5, Law 14th February 2016, n.18. L'adesione, il rigetto delle richieste di adesione e l'esclusione di una banca di credito cooperativo sono autorizzati dalla Banca d'Italia avendo riguardo alla sana e prudente gestione del gruppo e della singola banca.

settembre 1993, n. 385. Nei casi di cui al presente comma, la richiesta di adesione a un gruppo bancario cooperativo si ha per accolta qualora la banca di credito cooperativo abbia in precedenza fatto parte di un accordo di responsabilita' contrattuale che tuteli tutte le parti aderenti ed, in particolare, garantisca la loro liquidita' e solvibilita'.

3. Le banche di credito cooperativo autorizzate alla data di entrata in vigore delle disposizioni emanate ai sensi dell'articolo 37-bis, (commi 7 e 7-bis)²¹, del decreto legislativo 1° settembre 1993, n. 385, che non aderiscono a un gruppo bancario cooperativo, assumono le deliberazioni previste dall'articolo 36²² del decreto legislativo 1° settembre 1993, n. 385, o deliberano la liquidazione entro il termine indicato ai commi 1 e 2²³ (del presente articolo). Resta fermo quanto previsto dall'articolo 150-bis, comma 5²⁴, del decreto legislativo 1° settembre 1993, n. 385, come modificato dal presente decreto.

3-bis. In deroga a quanto previsto dall'articolo 150-bis, comma 5, del decreto legislativo 1° settembre 1993, n. 385, la devoluzione non si produce per le banche di credito cooperativo che, entro sessanta giorni dalla data di entrata in vigore della legge di conversione del

²¹ Art. 37-bis, comma 7 and 7-bis, Law 14th February 2016, n.18, TUB.7. Il Ministro dell'economia e delle finanze, al fine di assicurare l'adeguatezza dimensionale e organizzativa del gruppo bancario cooperativo, puo' stabilire con proprio decreto, sentita la Banca d'Italia: a) il numero minimo di banche di credito cooperativo di un gruppo bancario cooperativo; b) una soglia di partecipazione delle banche di credito cooperativo al capitale della societa' capogruppo diversa da quella indicata al comma 1, lettera a), tenuto conto delle esigenze di stabilita' del gruppo; c) le modalita' e i criteri per assicurare il riconoscimento e la salvaguardia delle peculiarita' linguistiche e culturali delle banche di credito cooperativo aventi sede legale nelle regioni a statuto speciale e nelle province autonome di Trento e di Bolzano. 7-bis. La Banca d'Italia, al fine di assicurare la sana e prudente gestione, la competitivita' e l'efficienza del gruppo bancario cooperativo, nel rispetto della disciplina prudenziale applicabile e delle finalita' mutualistiche, detta disposizioni di attuazione del presente articolo e dell'articolo 37-ter, con particolare riferimento: a) ai requisiti minimi organizzativi e operativi della capogruppo; b) al contenuto minimo del contratto di cui al comma 3, alle caratteristiche della garanzia di cui al comma 4, al procedimento per la costituzione del gruppo e all'adesione al medesimo; c) ai requisiti specifici, compreso il requisito minimo di patrimonio netto della capogruppo, relativi ai gruppi bancari cooperativi previsti dal comma 1-bis.

²² Art. 36 Law 1st September 1993, n.385, TUB. Fusioni e trasformazioni. 1. La Banca d'Italia autorizza, nell'interesse dei creditori e qualora sussistano ragioni di stabilita', fusioni tra banche di credito cooperativo e banche di diversa natura da cui risultino banche costituite in forma di societa' per azioni.

1-bis. In caso di recesso o esclusione da un gruppo bancario cooperativo, la banca di credito cooperativo, entro il termine stabilito con le disposizioni di cui all'articolo 37-bis, comma 7, previa autorizzazione rilasciata dalla Banca d'Italia avendo riguardo alla sana e prudente gestione della banca, puo' deliberare la propria trasformazione in societa' per azioni. In mancanza, la societa' delibera la propria liquidazione.

²³ Art. 2, comma 1, 2, Law 14th February 2016, n.18, TUB. 1. La comunicazione di cui all'articolo 37-ter, comma 1, e' inviata alla Banca d'Italia entro 18 mesi dall'entrata in vigore delle disposizioni emanate ai sensi dell'articolo 37-bis, (commi 7 e 7-bis), del decreto legislativo 1° settembre 1993, n. 385. 2. Entro 90 giorni dall'iscrizione nel registro delle imprese di cui al comma 4 dell'articolo 37-ter del decreto legislativo 1° settembre 1993, n. 385, una banca di credito cooperativo puo' chiedere di aderire a un gruppo costituito ai sensi dell'articolo 37-bis alle medesime condizioni previste per gli aderenti originari. L'organo amministrativo della capogruppo, sentito l'organo di controllo, comunica alla richiedente la deliberazione assunta entro 30 giorni dal ricevimento della domanda di adesione.

²⁴ Art. 150-bis, comma 5, TUB. Nei casi di fusione e trasformazione previsti dall'articolo 36, nonche' di cessione di rapporti giuridici in blocco e scissione da cui risulti una banca costituita in forma di societa' per azioni, restano fermi gli effetti di devoluzione del patrimonio stabiliti dall' articolo 17 della legge 23 dicembre 2000, n. 388.

presente decreto, presentino alla Banca d'Italia, ai sensi dell'articolo 58²⁵ del decreto legislativo n. 385 del 1993, istanza, anche congiunta, di conferimento delle rispettive aziende bancarie ad una medesima società per azioni, anche di nuova costituzione, autorizzata all'esercizio dell'attività bancaria, purché la banca istante o, in caso di istanza congiunta, almeno una delle banche istanti possieda, alla data del 31 dicembre 2015, un patrimonio netto superiore a duecento milioni di euro, come risultante dal bilancio riferito a tale data, su cui il revisore contabile ha espresso un giudizio senza rilievi.

3-ter. All'atto del conferimento, la banca di credito cooperativo conferente versa al bilancio dello Stato un importo pari al 20 per cento del patrimonio netto al 31 dicembre 2015, come risultante dal bilancio riferito a tale data, su cui il revisore contabile ha espresso un giudizio senza rilievi.

3-quater. A seguito del conferimento, la banca di credito cooperativo conferente, che mantiene le riserve indivisibili al netto del versamento di cui al comma 3-ter, modifica il proprio oggetto sociale per escludere l'esercizio dell'attività bancaria e si obbliga a mantenere le clausole mutualistiche di cui all'articolo 2514²⁶ del codice civile, nonché ad assicurare ai soci servizi funzionali al mantenimento del rapporto con la società per azioni conferitaria, di formazione e informazione sui temi del risparmio e di promozione di

²⁵ Art. 58, Law 1st September 1993, n.385, TUB. Cessione di Rapporti Giuridici. 1. La Banca d'Italia emana istruzioni per la cessione a banche di aziende, di rami d'azienda, di beni e rapporti giuridici individuabili in blocco. Le istruzioni possono prevedere che le operazioni di maggiore rilevanza siano sottoposte ad autorizzazione della Banca d'Italia. 2. La banca cessionaria dà notizia dell'avvenuta cessione mediante iscrizione nel registro delle imprese e pubblicazione nella Gazzetta Ufficiale della Repubblica italiana. La Banca d'Italia può stabilire forme integrative di pubblicità. 3. I privilegi e le garanzie di qualsiasi tipo, da chiunque prestati o comunque esistenti a favore del cedente, nonché le trascrizioni nei pubblici registri degli atti di acquisto dei beni oggetto di locazione finanziaria compresi nella cessione conservano la loro validità e il loro grado a favore del cessionario, senza bisogno di alcuna formalità o annotazione. Restano altresì applicabili le discipline speciali, anche di carattere processuale, previste per i crediti ceduti. Nei confronti dei debitori ceduti gli adempimenti pubblicitari previsti dal comma 2 producono gli effetti indicati dall'articolo 1264 del codice civile. 5. I creditori ceduti hanno facoltà, entro tre mesi dagli adempimenti pubblicitari previsti dal comma 2, di esigere dal cedente o dal cessionario l'adempimento delle obbligazioni oggetto di cessione. Trascorso il termine di tre mesi, il cessionario risponde in via esclusiva. 6. Coloro che sono parte dei contratti ceduti possono recedere dal contratto entro tre mesi dagli adempimenti pubblicitari previsti dal comma 2 se sussiste una giusta causa, salvo in questo caso la responsabilità del cedente. 7. Le disposizioni del presente articolo si applicano anche alle cessioni in favore dei soggetti, diversi dalle banche, inclusi nell'ambito della vigilanza consolidata ai sensi degli articoli 65 e 109 e in favore degli intermediari finanziari previsti dall'articolo 106.

²⁶ Le cooperative a mutualità prevalente devono prevedere nei propri statuti: a) il divieto di distribuire i dividendi in misura superiore all'interesse massimo dei buoni postali fruttiferi, aumentato di due punti e mezzo rispetto al capitale effettivamente versato; b) il divieto di remunerare gli strumenti finanziari offerti in sottoscrizione ai soci cooperatori in misura superiore a due punti rispetto al limite massimo previsto per i dividendi; c) il divieto di distribuire le riserve fra i soci cooperatori; d) l'obbligo di devoluzione, in caso di scioglimento della società, dell'intero patrimonio sociale, dedotto soltanto il capitale sociale e i dividendi eventualmente maturati, ai fondi mutualistici per la promozione e lo sviluppo della cooperazione. Le cooperative deliberano l'introduzione e la soppressione delle clausole di cui al comma precedente con le maggioranze previste per l'assemblea straordinaria.

programmi di assistenza. Non spetta ai soci il diritto di recesso previsto dall'articolo 2437²⁷, primo comma, lettera a), del codice civile. In caso di inosservanza degli obblighi previsti dal presente comma e dai commi 3-bis e 3-ter²⁸, il patrimonio della conferente o, a seconda dei casi, della banca di credito cooperativo e' devoluto ai sensi dell'articolo 17 della legge 23 dicembre 2000, n. 388²⁹. In caso di mancato ottenimento delle autorizzazioni indicate al comma 3-bis entro il termine stabilito dal comma 1³⁰, la banca di credito cooperativo puo' chiedere l'adesione a un gruppo cooperativo gia' costituito entro i successivi novanta giorni. In caso di diniego dell'adesione si applica il comma 3³¹.

4. In caso di inosservanza di quanto previsto dal comma 3, la Banca d'Italia assume le iniziative necessarie per la revoca dell'autorizzazione all'esercizio dell'attivita' bancaria.

5. Le banche di credito cooperativo autorizzate alla data di entrata in vigore del presente decreto, si adeguano a quanto previsto dall'articolo 34, comma 1³², del decreto legislativo 1° settembre 1993, n. 385, entro 60 mesi dalla data di entrata in vigore del presente decreto.”

Furthermore, the Article 2-bis considers the foundation of a temporary fund for cooperative banks (Fondo Temporaneo delle Banche di Credito Cooperativo). This fund (promoted by the Federazione italiana delle banche di credito cooperative-casse rurali ed artigiane) is a mutual-

²⁷ Art. 2437 codice civile. Diritto di Recesso. Hanno diritto di recedere, per tutte o parte delle loro azioni, i soci che non hanno concorso alle deliberazioni riguardanti: a) la modifica della clausola dell'oggetto sociale, quando consente un cambiamento significativo dell'attivita' della societa'.

²⁸ Art. 3-bis, Law 14th February 2016 n. 18, TUB. In deroga a quanto previsto dall'articolo 150-bis, comma 5, del decreto legislativo 1° settembre 1993, n. 385, la devoluzione non si produce per le banche di credito cooperativo che, entro sessanta giorni dalla data di entrata in vigore della legge di conversione del presente decreto, presentino alla Banca d'Italia, ai sensi dell'articolo 58 del decreto legislativo n. 385 del 1993, istanza, anche congiunta, di conferimento delle rispettive aziende bancarie ad una medesima societa' per azioni, anche di nuova costituzione, autorizzata all'esercizio dell'attivita' bancaria, purché la banca istante o, in caso di istanza congiunta, almeno una delle banche istanti possieda, alla data del 31 dicembre 2015, un patrimonio netto superiore a duecento milioni di euro, come risultante dal bilancio riferito a tale data, su cui il revisore contabile ha espresso un giudizio senza rilievi. Art. 3-ter. All'atto del conferimento, la banca di credito cooperativo conferente versa al bilancio dello Stato un importo pari al 20 per cento del patrimonio netto al 31 dicembre 2015, come risultante dal bilancio riferito a tale data, su cui il revisore contabile ha espresso un giudizio senza rilievi.

²⁹ Art. 17 Law 23rd December 2000. La soppressione da parte di societa' cooperative o loro consorzi delle clausole di cui al predetto articolo 26 comporta comunque per le stesse l'obbligo di devolvere il patrimonio effettivo in essere alla data della soppressione, dedotti il capitale versato e rivalutato ed i dividendi eventualmente maturati, ai fondi mutualistici.

³⁰ Art. 2, comma 1, Law 14th February 2016, n.18, TUB. 1...la comunicazione di cui all'articolo 37-ter, comma 1, e' inviata alla Banca d'Italia entro 18 mesi dall'entrata in vigore delle disposizioni emanate ai sensi dell'articolo 37-bis, (commi 7 e 7-bis), del decreto legislativo 1° settembre 1993, n. 385.

³¹ Art. 2, comma 3, Law 14th February 2016, n.18, TUB. Le banche di credito cooperativo autorizzate alla data di entrata in vigore delle disposizioni emanate ai sensi dell'articolo 37-bis, (commi 7 e 7-bis), del decreto legislativo 1° settembre 1993, n. 385, che non aderiscono a un gruppo bancario cooperativo, assumono le deliberazioni previste dall'articolo 36 del decreto legislativo 1° settembre 1993, n. 385, o deliberano la liquidazione entro il termine indicato ai commi 1 e 2 (del presente articolo).

³² Art. 34, comma 1, Law 1st September 1993, n.385, TUB. Soci. 1. Il numero minimo dei soci delle banche di credito cooperativo non può essere inferiore a cinquecento. Qualora tale numero diminuisca, la compagine sociale deve essere reintegrata entro un anno; in caso contrario, la banca è posta in liquidazione.

insurance tool of private nature thought to support consolidation processes between cooperative banks and it has.

It operates with full autonomy as an insurance tool to support consolidation processes of BCCs. The terms and conditions of its intervention are stated in its statute. The adhesion to the fund recurs within 30 days from the approval of its statute. At the moment of the adhesion to the fund, all the deals in course deriving from the management of the Fund are transmitted to the holding company according to the agreements previously taken by each single BCC.

“Art. 2-bis

Fondo temporaneo delle banche di credito cooperativo.

2. Il Fondo opera in piena autonomia decisionale quale strumento mutualistico-assicurativo e puo' favorire, in base a quanto definito nel proprio statuto, processi di consolidamento e di concentrazione delle banche di credito cooperativo. Sono definiti nello statuto il sistema contributivo, il limite massimo di impegno per singolo intervento nonche' il limite massimo al richiamo di fondi dalle banche aderenti.

3. L'adesione al Fondo avviene entro trenta giorni dalla data di approvazione del relativo statuto”.

This first section of the new law will become the focus of our attention in the following chapters.

Capo II

The second section regards the warranty on securities.

Articles 3, 4 and 5 regulate guarantees and structure of securities. They specify what classes of titles can be issued and in which modalities. Warranties for senior titles can be provided by the Italian State for a certain time of period (a maximum of 36 months from the entry into force of this decree) but only if they reach a certain level of rating. Otherwise, specific contracts can be stipulated in order to hedge the financial risk. Particular credit measures have to be taken to maintain a minimum level of financial flexibility to match creditworthiness of senior titles.

Following, Articles 6 and 7 state the characteristics of senior and mezzanine titles in terms of remuneration, refund of capital and rate of interests. Then, they provide a list of titles and charges in order of priority of payments.

Articles 8 and 9 refer to the state warranty on credit default swaps (CDS). As specified also in the previous Articles, the state guarantee can be granted only to senior titles when some requirements are met. The amount of the state guarantee compensation is defined as a basket of swap contracts valued on the base of the rating score assigned by rating agencies. In addition, the Article 9 provides the analytical mathematical procedure to determine the CDS value and the annual compensation of the state guarantee.

The Article 10 states that the guarantee can be allowed by a decree issued by the Minister of Economy and Finance.

The Article 11 provides clarifications on how the warranty can be enforced, specifying procedures, clauses and terms of payments.

In the end, Articles 12 and 13 explain that financial resources available for the purposes of this second section are represented by a special fund of 120 million euro for the year 2016. Then they give information on how these measures can be implemented by the Minister of Economy and Finance.

Capo III

This section treats tax application on crisis procedures. It provides the fiscal criteria to apply to banks subjected to resolution. Among the others, the main aspects specify that grants received as donations by banks in crisis situations are excluded from the calculation of taxations. Furthermore, it introduces an amendment to the fiscal policy regarding real estate transfers in judicial sales, stating new clauses and new taxations.

Capo IV

In the last part of the Law, the Article 17 regards management and protection of savings. It provides some endowments that argue to improve the management of savings in order to foster lending to businesses. It allows Italian and European FIA (Fondi d'Investimento Alternativo)

to invest in credits not only in favour of consumers but also in favour of companies, indicating all the criteria and applicable laws.

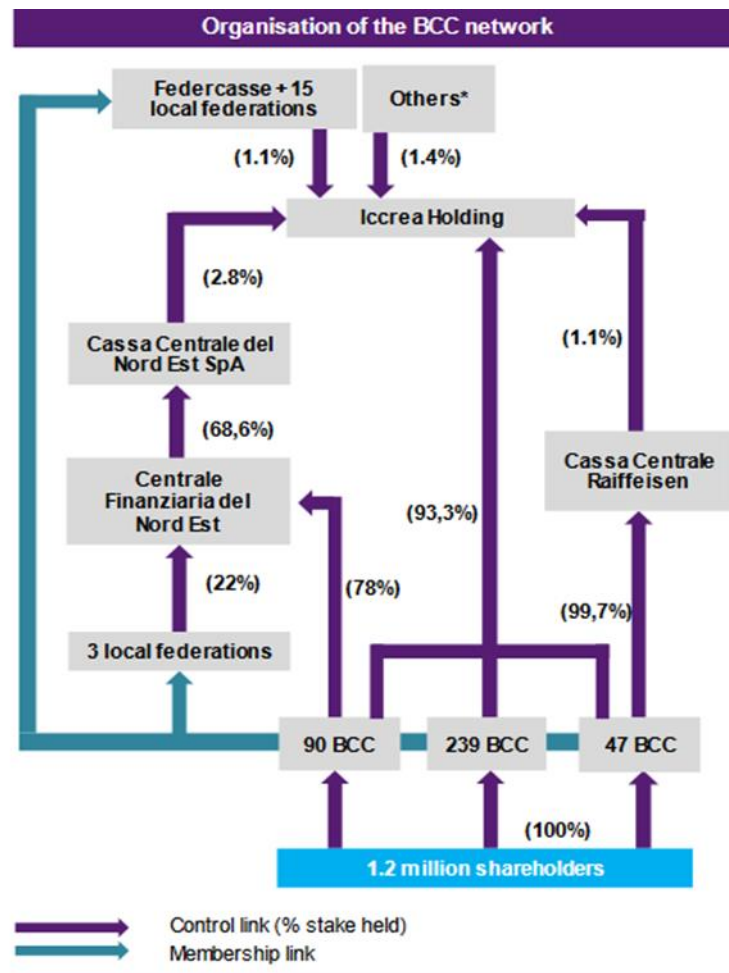
Following, subjects such as calculation of financial interests, bank checks and bank instruments of payment are regulated applying little endowments to previous laws.

The last Article is the number 18 that states the rules of the entry into force of the current Law.

1.4 CONSEQUENCES OF THE NEW LEGISLATION

How many cooperative banking groups could be created as a result of the reform?

The actual Italian mutual banking system has the following structure:



As we can see from the graph, the three main Italian cooperative institutions are:

- Iccrea Holding SpA in Rome, with a capital of 1 billion euro;
- Cassa Centrale Raiffeisen in Bolzano with a capital of 300 million euro;
- Cassa Centrale Banca in Trento with a capital of 250 million euro.

The initial proposal of the reform regarded the formation of a main CBG under the control of Iccrea Holding in Rome and a provincial group under Cassa Centrale Raiffeisen in Bolzano. Then, in the last months Federcasse has evaluated the possibility of the creation of a third group under Cassa Centrale Banca (CCB) in Trento. This possibility has been taken into consideration

after CCB refused the aggregation to the Iccrea's CBG, stating that the conditions for the creation of a unique group do not recur.

This decision is linked mainly to the regional cultural and territorial features. Indeed, the Italian region Trentino-Alto Adige has always maintained its own identity through the years developing financial institutions very close to its territory. Therefore, local institutions aim to continue to run their local mutual system with full autonomy and to develop their territory as they have always done in the past. CCB represents an important network for more of the 50% of Italian BCCs especially regarding the supply of IT services and management consultancy services. Furthermore, CCB's group has shown to have a high level of financial soundness, efficiency and transparency. It has applied very straight and prudent credit policies that have allowed to reduce the level of risk of its financial activities and to better face the financial crisis of 2008. Because of these reasons, CCB may have the suitable characteristics to embody the role of holding company.

Therefore, the actual BCCs scenario includes the formation of a main CBG directed by Iccrea (meeting the 1 billion euro threshold) and the possible establishment of a second group under Cassa Centrale Banca in Trento. A provincial group will be formed in Bolzano under Cassa Centrale Raiffeisen.

Even for the creation of a second CBG, the capital threshold is of 1 billion euro. The role of holding company would be embodied by Cassa Centrale Banca and at the moment it seems that it may include 15 BCCs from the north until the south of Italy.

The reform recognizes also a possible 'way-out' for BCCs that decide to do not join any group. It provides three different possibilities:

- BCCs can continue to operate as independent entities only if they meet a capital threshold of 200 million euro and they pay a 20% tax on their capital. Furthermore, BCCs that opt for the way-out have to transfer their banking activity into a company in form of S.p.A (that can be also of new-constitution). The cooperative bank will continue to exist (changing its corporate purpose) and it will own the majority of the S.p.A.'s shares therefore exercising the control over it. The indivisible legal reserves will remain under the cooperative. In this way the cooperative bank will lose its credit activities but it will maintain its mutual nature.

- BCCs with a capital inferior than 200 million euro can remain out of the cooperative banking group only if they agree to merge with greater institutions meeting together the 200 million euro threshold.
- Another form of way-out is represented by the right of recession from the cooperative banking group that allows BCCs to exit from the Iccrea's group in a second moment. In this case, BCCs can choose between the liquidation of their activity or their transformation in S.p.A.

These measures aim to foster the aggregations between BCCs as less than 20 BCCs currently meet the 200 million euro threshold. Indeed, in the reform's vision, BCCs cannot remain on their own but they have to be part of large networks. This would allow a higher protection level and therefore a major financial soundness of the system.

The 'way-out' has been object of many debates. The main critic regards the incentive of this mechanism to the formation of small S.p.A. groups and the merger of small BCCs. Indeed, the cooperative banking group under Iccrea risks to be formed by weak BCCs as the most solid BCCs would probably opt for the way-out. Therefore, this would not solve the problem of financial instability. Moreover, the small S.p.A. groups (that will be created with the way-out) would be controlled by cooperative institutions with the same problems of governance and territoriality.

However, only three BCCs (meeting the minimum capital threshold of 200 million euro) have opted for the way out while all the other institutions have decided to join the cooperative banking group with unique holding. The banks that have decided to remain out of the group are: Banca di Cambiano, Chianti Banca (both from Toscana) and Cassa Padana (from Brescia, Lombardia). Therefore it seems that the cooperative sector will still go toward a more integrated sector developed around the figure of Iccrea holding.

In the fourth chapter I will deepen the effects of the reform trying to understand what the main consequences would be and evaluating other proposals of reform.

CHAPTER 2 – ANALYSIS OF FOREIGN COOPERATIVE BANKING MODELS: CRÉDIT AGRICOL AND RABOBANK

2.1 COOPERATIVE BANKING GROUP MODELS IN EUROPE: DEVELOPMENT OF NETWORK CENTRAL INSTITUTIONS

Among Europe, cooperative banks have experienced different developments. However some features are common in many European models. In particular, it emerges the increasing role of the network central institutions (NCI) based on high levels of cooperation.

The main reason of the NCIs development was the need to manage liquidity and access to capital markets as the small dimensions of member banks did not allow them an adequate diversification level and an adequate access to financial resources in case of need.

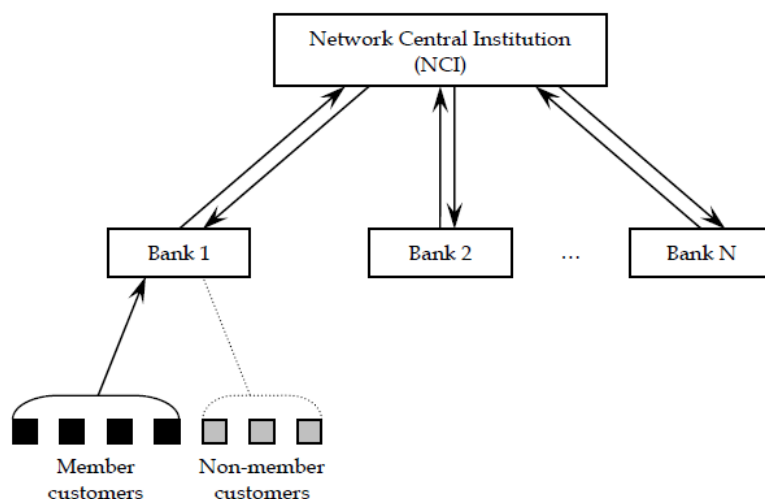
Moreover, cooperative banks can obtain further relevant advantages from operating in a well-integrated network. Among the main important benefits we find:

- economies of scale linked especially to administration functions. In this way even small cooperative banks can benefit from scale economies that they would not be able to produce on their own because of their sizes;
- often, the NCI include an internal central bank that exercises control functions within the network providing liquidity and solvency intermediation. Furthermore, it provides services such as treasury, risk management and product development within the group granting high levels of efficiency;
- the high level of cooperation represents a guarantee of repayment for customers, enhancing the banks 'opportunity to raise funding;
- member banks may benefit from the reputation of being part of a credible and sound network, increasing confidence with customers.

However, the overall advantages depend on the nature of the NCI and on how member banks can continue to exercise their activities. Indeed, the NCI may also represent a threat for member banks if it pursues objectives that are not in line with the principles of the member banks. Another issue that may emerge is the so called 'appropriability hazard', the risk that counterparts may act opportunistically to obtain the advantages generated by the group activity. It is therefore important to recognize to the central institution an appropriate level of authority and control. Furthermore, several preventive measures have to be applied, such as submission

of prudential reports of the member banks to the central institutions, standardized risk-management practices and the development of compulsory audit procedures).

The affirmation of the NCI models in Europe has brought to the development of a ‘circular authority’ recurring in the high integrated cooperative banks. It may be represented by the following scheme:



This model shows a first level relationship between member customers and member banks. Member customers (who represent the majority of the members) exercise their powers by voting for their cooperative bank in accordance with the ‘one-head, one-vote’ principle. Then, we find a higher-level relationship between cooperative banks and the NCI. In most of the cases, member banks own the majority of the NCI’s capital that guarantees their control over the central institution. The central body in turn provides direction and coordination all over the group, monitoring and safeguarding the network’s financial resources and mutual functions reducing the member banks ‘autonomy.

Therefore in this model we can distinguish two different relationships:

- a ‘bottom-up’ authority represented by the two-layer control exercised by member customers and member banks over the central institution;
- a ‘top-down’ authority exercised by the central institution toward the group through direction and coordination functions.

Among Europe, different NCI show different degree of centralization that vary considerably between countries and also within countries. The Italian and Spanish models are considered to be less centralised than the Austrian, German, Dutch, Finnish and French models.

The following table summarizes the characteristics of all the main European banking groups:

Cooperative bank	A. Basic Co-operative Group		B. Decentralised Cooperative Group (Article 113(7) CRR)		C. Consolidated Cooperative Bank (Article 10 or Article 113(6) CRR)			
	<i>Cajas Rurales (Spain)</i>	<i>BCC (Italy)</i>	<i>Raiffeisen banks (Austria)</i>	<i>Volks- and Raiffeisenbanks (Germany)</i>	<i>Raiffeisen (Switzerland)</i>	<i>Crédit Agricole Group (France)</i>	<i>OP (Finland)</i>	<i>Rabobank (Netherlands)</i>
- No Institutional Protection Scheme or Cross Guarantee	x	x						
- Centralized functions in the group are very limited	x	x						
- Institutional Protection Scheme			x	x				
- Centralised functions in the group are limited			x	x				
- Local banks supervised independently by national supervisor	x	x	x	x				
- No management instructions by central body to local banks	x	x	x	x				
- Cross Guarantee System					x	x	x	x
- Consolidated supervision by European Central Bank					x	x	x	x
- Many functions in group are centralized					x	x	x	x
- Central body has mandate to issue instructions to local banks					x	x	x	x
- Central group binding decisions					x	x	x	x

Source: author, based on research and questionnaires among these cooperative banking groups

We can see from the table above that Spain and Italy operate with a quite flexible system, without institutional protection schemes and cross guarantee mechanisms. Also, the banks operate with large autonomy as centralized functions are very limited. Because of these aspects they are considered to be low-integrated systems and not financially sound.

As regards Austria and Germany, they cooperative banks are more integrated but do not have a central institution that exercises supervisory functions over the local cooperative banks.

While, Crédit Agricole, Rabobank, Raiffeisen and OP are very well integrated groups. The group-level entities are able to issue instructions to local banks in order to guarantee the union of the group and the development of a common cooperative strategy.

We can say that the international landscape provides different examples of possible lines of BCCs reform. However, the main current European models that I will consider in my thesis are:

- Crédit Agricole in France;
- Rabobank in Netherlands.

In both cases, a corporate central control has been adopted in order to ensure a self-discipline of the group and a cost-control within the group. Moreover, in some cases, the central

institutions have been listed in order to access capital markets leading to an overall growth of the banking system.

In the following paragraph I will analyse Crédit Agricole and Rabobank Group in order to have a better understanding on their working and on their internal mechanisms of control and guarantee as their examples may be taken into consideration as possible guides for the reform of the Italian BCCs.

2.2 ANALYSIS OF CRÉDIT AGRICOLE GROUP

Crédit Agricole (CA) is the first mutual bank in France and one of the most important in Europe in terms of market share, earnings and total capital.

The identity of the group is strictly linked to its cooperative nature as it was founded in 1890 with the aim to provide financial support to the agricultural sector.

After the Second World War, Crédit Agricole, as the other large cooperative French groups, were subject to state's ownership and to very restrictive regulations in accordance to which cooperative banks were assigned to collect deposits that could only be used to buy government bonds. Through the years some amendments were issued to reduce these restrictions, but it was only starting from 1984 that the new Banking Law (Banking Law no. 84-46 of 24 January 1984) and further following provisions have started a deregulation process setting the privatization and the consolidation of the sector.

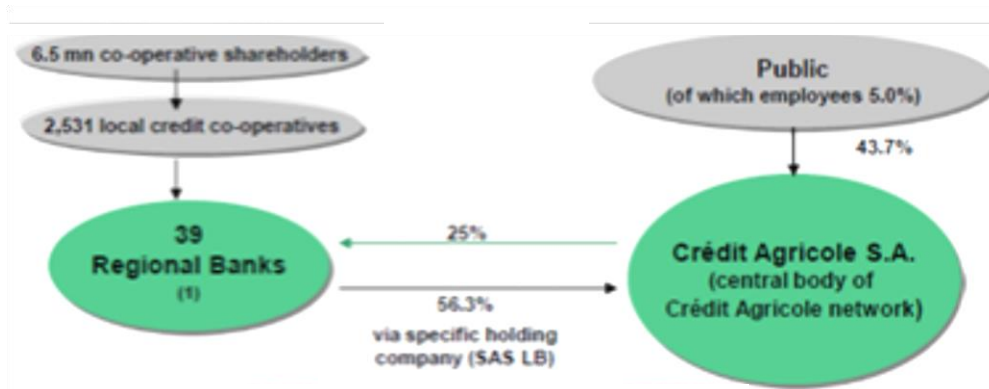
This reform of the sector has made cooperative banks to grow through mergers and acquisitions strategies over the past two decades. Thanks to these processes, CA has become today one of the largest cooperative banking group in the world offering a wide range of banking services (e.g. insurance services, asset management, wholesale banking). It is important to highlight that despite of its sharp growth in activities and dimensions, CA has strongly maintained its cooperative nature, providing two-thirds of their loans to small-size enterprises and to households.

As regards the governance, Crédit Agricole could be defined as a member-centric model based on the 'one-member, one-vote' principle. Shareholders are entitled to annual dividends and a part of the profit has to be allocated to legal reserves.

As stated by Di Salvo, 2002, network collaboration is an emerging characteristic of cooperative banks, particularly prominent in the French model. Indeed, the structure of the group is a three-tier structure that includes local, regional and national layers. As central network institution, it is a well-integrated cooperative bank. Its pyramidal structure is characterized by a top-down authority which opposes the bottom-up ownership of members. At each level, the local institutions have delegated a great variety of functions to central bodies (such as risk management, mutual support, investment activities, debt issuance, group representation and IT support) which give them significant power over the local institutions. In particular, under the

French Monetary and Financial code, the central organs are required to guarantee the liquidity and solvency of the entities within their networks.

Crédit Agricole’s structure can be represented by the following scheme:



As we can see, the foundation of the group is represented by the Local Credit Co-operative banks. Crédit Agricole Group includes 2,531 Local Banks with 5.5 million member shareholders consisting primarily of individuals, farmers, and agricultural cooperatives. The local banks own all the share capital of the 39 regional banks that in turn hold the majority of Crédit Agricole S.A. (CASA), providing funding to the local banks.

The SAS La Boétie is the holding company through which the regional banks control the 56.7% of Crédit Agricole S.A. The purpose of SAS Rue La Boétie is to hold enough shares to ensure that it always owns at least 50% of the share capital and voting rights of Crédit Agricole S.A.

Crédit Agricole S.A. is the listed company, central body of the group. It owns the 25% the regional banks ‘capital and it is owned for the 56.7% by them. It is required to monitor financial and credit risks and to take all the necessary measures to ensure satisfactory liquidity and solvency levels of each member of the group.

In terms of mutual support, CA group is based on a cross-guarantee system that calls for the use of the group’s resources to serve the debt of regional institutions, guarantying all obligations of Crédit Agricole S.A. to third parties.

Through these mutual support mechanisms, the level of risk incurred by creditors of CASA and by those of the regional banks are identical, and bondholders of CASA are ultimately

protected by the whole capital cushion of the regional banks. This has resulted in the assignment of identical credit ratings between the regional banks and CASA.

Moreover, its solidarity mechanism allows a high internal flexibility and capital circulation. The group's primary objective in managing liquidity is to ensure that it has always sufficient resources to meet its requirements in the event of any financial crisis.

Each regional bank makes deposits in the CASA, which uses the funds to settle payments on behalf of the group and to provide liquidity loans to regional banks which need liquidity support.

In accordance with the Basel III, there are two bail-in mechanisms that are triggered when:

- Crédit Agricole S.A. Group's phased-in CET1 ratio drops below 5.125%;
- Crédit Agricole Group's phased-in CET1 ratio falls below 7%.

French banking laws establish liquidity, solvency, administrative and management rules for all three levels of the Crédit Agricole group.

Through authority delegated by the Bank of France, the CASA exercises regulatory authority over its regional banks, particularly in the area of liquidity, solvency, and governance.

Credit Agricole S.A. is subject to the articles of association provided by the Monetary and Finance Code.

The Article 1 states the object of the group is to facilitate and promote the activities and development of all the group members and it has to act as a unique financial institution.

“1. Crédit Agricole S.A. operates as a central financial institution and ensures that the Group acts as a single financial unit in its dealings with third parties with the object of optimising the financial management of funds and, in return, the allocation of the financial resources so collected.”

In accordance to the Article 3, the holding has to ensure the cohesion of the group and the compliance of the group's activities to the regulations and applicable laws other than to the financial solvency and liquidity requirements.

“3. Crédit Agricole S.A. ensures the cohesion of the Crédit Agricole Mutuel network, the proper operation of the credit institutions that are a part thereof, and compliance by such institutions

with the applicable laws and regulations by exercising administrative, technical and financial supervision thereof; it guarantees the liquidity and solvency of the entire network and all institutions affiliated therewith.”

As regards the internal control procedures, Crédit Agricole complies with the laws and regulations of French credit institutions and investment companies. The main legislative and financial sources for Crédit Agricole are:

- the French Monetary and Financial Code;
- the decree of 3 November 2014, relating to the internal control of banks;
- all texts relating to the conduct of banking and financial activities;
- the Autorité des Marchés Financiers’ General Regulation.

The internal control system and procedures can be classified in this way:

- application of instructions and guidance given by the Executive Management;
- a financial performance objective, to ensure effective and proper use of Group assets and resources and protection against the risk of loss;
- access to exhaustive, accurate and timely information for decision-making and risk management purposes;
- a compliance objective, in respect of internal and external rules;
- prevention and detection of fraud and errors.

The supervisory body is the Board of Directors. It defines the group’s strategies and general policies, determining plans, criteria and thresholds of internal procedures. The BOD makes decisions on all matters concerning the governance of the company and it is informed of any significant event of fraud or any other event detected by internal control procedures.

The executive body defines the company’s general organisation and ensures that it is implemented in an efficient way and by competent managers. It also controls if suitable risk measurement procedures are adopted and if they are correctly developed.

Internal credit decisions are determined on the quality of the risk of the counterparty, assessed by an internal rating methods. The credit decision must form part of the formally approved risk strategies. The internal rating system develops all procedures and controls to calculate credit risk, borrower ratings and loss given default for all the group’s exposures.

Second-level controls are developed to test compliance with limits. They consist in processes for monitoring individual risks and portfolio risks, in order to detect any possible deterioration in the quality of the counterparty and Crédit Agricole's commitments.

Summarizing, in accordance with principles in force within the Credit Agricole S.A. Group, Crédit Agricole's Risk and Permanent Control Department implements a qualitative and quantitative system designed to identify, assess, prevent and monitor operational risk (in accordance with the Basel II). Crédit Agricole S.A., as the central body of the group ensures that all of its affiliated members, maintain satisfactory liquidity and solvency levels.

Due to this joint and general guarantee, a default of Crédit Agricole S.A. would be covered by the aggregate capital of the 39 regional banks. In turn, the default of a regional bank would be immediately covered by Crédit Agricole S.A. and therefore there cannot be any individual default of a regional bank unless Crédit Agricole S.A. itself defaults.

This mechanism represents a fundamental pillar of the group's structure. It ensures a high solvency capacity of the bank and financial soundness that individual BCCs would not have if they were on their own.

This is an example of the substantial advantages for all member BCCs and therefore it could be taken into consideration for the development of the Italian reform of mutual banks.

2.3 ANALYSIS OF RABOBANK GROUP

Rabobank is the biggest cooperative banking group in Netherland, consisting of 248 member banks which fully own Rabobank Netherland. The whole group services 9 million clients, 1.55 million of which are members of the 248 local Rabobanks.

Rabobank finds its origins in the local cooperative banks of the rural community. The first cooperative agricultural banks were born in response to the agricultural crisis of the 19th century that brought to the necessity of a new banking system in order to boost the agricultural sector.

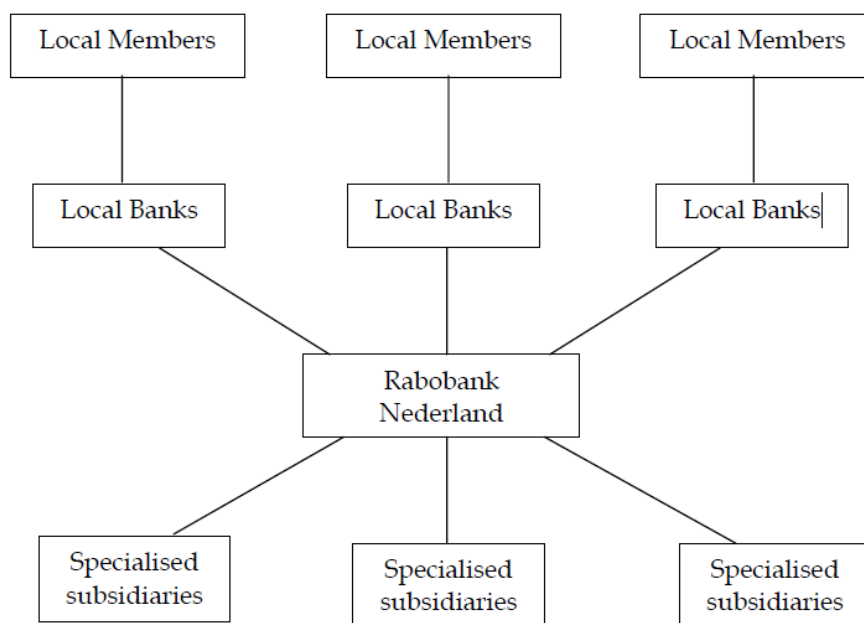
The first suggested solution was proposed by the German mayor, Raiffeisen. In 1864 he founded the first rural cooperative credit society and all the farmers and traders that wanted a loan from this society had to become a member. As the bank had no government funds, the local population had to provide small amounts of savings in order to enable the institution to grant loans to member borrowers.

In the following years, local banks felt the need for a better structured organization for a higher degree of support and coordination. As answer to this situation, two financial institutions were born: “Boerenleenbank” in the south (Eindhoven) and “Raiffeisenbank” in the north (Utrecht) and in 1972 they merged in RA-BO bank (from the abbreviation of both the names of the two previous banks).

Nowadays, Rabobank Group may be defined as a centralised model where member banks have delegated significant supervisory and decision taking power to the central entity. It has a three tier structure including local member banks, the central body Rabobank Nederland (RN) and the various subsidiaries of Rabobank Nederland.

Rabobank is a central network institution. It is fully owned by the 153 local member banks. Within its network there are two levels of membership: the local member banks are members of Rabobank Nederland, and each member bank has members in its territory.

Rabobank's structure may be represented by the following scheme:



Source: Van Dooren and Van Ijperenburg (2009).

The holding Rabobank Nederland has the legal form of a joint stock co-operative society as the local Rabobanks are both its members and shareholders. It advises and supports its member banks, supervises their liquidity and solvency positions and acts as bankers' bank for the whole Group. RN is supported by its subsidiaries to offer services to member banks and their customers. Subsidiaries are not cooperative institutions but they have the form of private or public limited companies.

The group is based on a cross-guarantee system in accordance to which all member banks are liable for the obligations of all other members and the Group itself, granting a full mutual support.

Each member bank is a separate cooperative bank in its own right and is legally independent: they are not to be regarded as branches of Rabobank Nederland.

Rabobank Nederland exercises several functions in favour of the member banks:

- it acts as a central bank of member banks and it intermediates their liquidity requirements making financial resources to flow throughout the group;
- it provides important services to the member banks such as treasury, risk management and product development;

- it exercises a central supervisory role over the member banks on the basis of delegated authority from De Nederlandsche Bank. It also directs the activities of its subsidiaries;
- it is a banks on its own providing wholesale and retail services.

As supervisor, Rabobank Nederland has the power and authority to set rules for member banks. Therefore, there is a two-way relationship between the central institution and the local banks: the member banks own and influence Rabobank Nederland which in turn has supervisory and regulatory powers over the member banks. Furthermore, member banks cannot increase or decrease their operations branches without Rabobank Nederland approval.

Member banks have no entitlement to the equity of their local bank. For the group as a whole, the dominant source of equity capital is retained profits, and a minimum of 75% of profits must be retained as reserves contributing to Tier 1 capital. No dividend distribution can be made to members, though a small proportion of profits can be used for social activities.

The individual member banks pool their equity into the central entity. The capital contribution of each local bank remains traceable and it contributes to determine the number of votes in the new governance. The equity development of each local bank is monitored as a result of annual internal financial reporting.

The group operates with a decentralised organisation of local banks. The relationships between the group's entities are regulated by the internal principles of association, stated below:

“1. local banks give substance to clients' financial needs by providing transparent, honest and logical service across the entire spectrum;

2. each local bank uses the interplay between the local members' council, the management team and the local supervisory board to formulate its own vision on stimulating the development of its geographical region;

3. proceeding from a jointly determined collective framework, the management team bears the administrative responsibility for the local ambitions regarding clients, the market and the geographical region. The management team is inspired by an active local members' council and stimulated by a regionally involved local supervisory board with an all-round perspective on the organisation;

4. by contributing expertise, resources and by establishing connections, Rabobank is economically and socially relevant;

5. *in order to maintain a strong collective position, the local banks collaborate with the supporting organisation in the Rabobank cooperative, which operates as a single powerful unit;*

6. *the Rabobank members are represented indirectly in the highest decision making body, the general members' council." This enables the bank to finance the growth of its activities with its own funds, without being forced to recur to external capital suppliers. Moreover, this strong capital base is also the main reason for its AAA credit ratings, through which the bank is able to obtain the lowest possible funding costs from the professional financial markets.*

Through the years Rabobank has adapted its governance in line with its structural evolution. Governance structures exist at two levels in any network cooperative: at the local member bank and at the central bank. Member banks can choose between two alternative governance models: the Partnership Model and the Executive Model:

- under the Partnership Model, the Board of the local bank is made up of people elected by members and professional managing director appointed by the Supervisory Board. All important strategic decisions are taken by the General Meeting in which all members have voting rights;
- in the Executive Model, each bank has a Board of Management operating under the supervision of the Supervisory Board. None of the board members is elected by the members. However, in this model the bank is required to institute a Members' Counsel which is made of members in order to promote member influence and control. This body is therefore equivalent to the General Meeting.

As regards the evolution of the main bodies of the governance, the Board of Directors has seen to increase their legal authority to issue enforceable instructions to the management. In addition, the figure of a professional banker has been introduced.

Local Supervisory Bodies continue to have important tasks and responsibilities, including a supervisory role to guarantee the local focus. Furthermore, they monitor the execution of the strategy and policy plans by the Management Team Chairman and evaluate whether the bank's services satisfy the needs of customers and members.

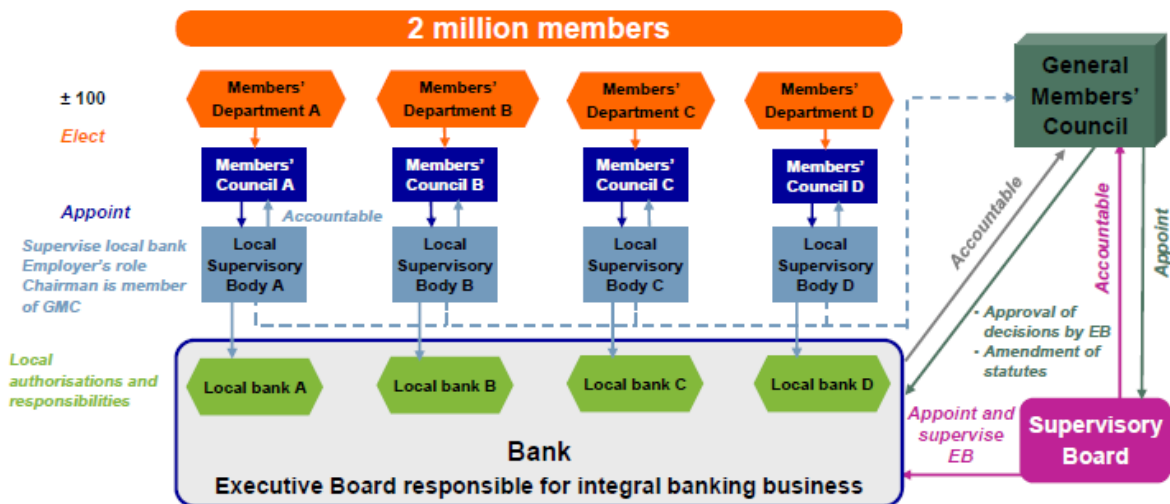
The Local Supervisory Body and Local Management Team are expected to pursue objectives determined at a group level, in line with the values and strategy of Rabobank. In case of conflict of interest, the Executive Board can intervene withdrawing the authorisation recognized to the LSB.

The General Members' Council instead evaluates the governance and the banking business on the basis of commonly agreed strategic principles. It has the power to amend the statutes or change the legal status of the group, other than the right to approve for major decisions of the Executive Board, influencing Rabobank's strategy.

The Executive Board governs Rabobank and it is fully responsible for the whole banking business. It has the power to intervene directly in local banks if necessary and it is responsible for the compliance of local banks with external regulations.

The Executive Board has recognized various authorizations to the Local Management Team Chairmen to execute their functions locally and to take responsibility for their bank. The main reason for that is the preservation of local orientation, local entrepreneurship and of the different features of local banks. The Executive Board may take corrective measures in case of underperformance or in case of financial troubles of the local banks (such as high risk operations or governance issues).

Following, a representation of the connections between local banks and central bodies of the group.



Summarizing, we can say that under Rabobank's view, understanding each entity's background, having a common goal and acting decisively are all factors that determine success.

Due to its decentralised nature, Rabobank is based on a strong collaboration and network, both between the various components of the whole group and through the strengths developed with external parties to pursue economic and social initiatives.

The group does not aim to maximise profits but to maximise the economic benefit for its co-operative members. Profit is only an instrument to serve the continuity of the co-operatives, which is done by demanding the lowest possible price for loans and credits from the member borrowers, and at the same time by creating the most favourable lending conditions. If a member's business is in financial difficulties, a local Rabobank will give support as long as possible.

Through the years, the group has been able to strengthen its cooperative and banking structures bringing the entire group to a great financial stability always maintaining its cooperative principles.

2.4 OVERVIEW OF THE ITALIAN COOPERATIVE BANKING SYSTEM IN THE EUROPEAN CONTEXT

In the previous paragraphs, we have seen that the main European cooperative banking groups, Crédit Agricole and Rabobank, have experienced a development based on second-tier structured banks and other financial departments aimed to safeguard the direct relationship with customers, members and local communities.

Both the systems are characterized by a great integration level and by a central holding that exercises a role of direction and control of the entire group.

Under the financial aspect, these groups are internally unified by cross-guarantee mechanisms that provide a form of patrimonial solidarity toward the BCCs creditors as it allows to move patrimonial resources among the group in order to meet the banking prudential requirements. The main rights and obligations of the member BCCs are provided by the cohesion contract instead of from participation shares of the traditional system.

In the Rabobank Group, the holding has assumed the major responsibility for direction and control on local member banks that maintain a considerable degree of autonomy. The central holding consolidates the capital of all the members through a strict mechanism of “cross guarantees” and meets the capital ratios on a consolidated base.

Instead, in Crédite Agricole the holding bank exercises the function of leadership and control of the group, consolidating assets, liabilities and equity with the S.A. Crédit Agricole.

As regards the current Italian cooperative banking sector, BCCs operate in a decentralised way. Most of the main functions are developed on a voluntary basis as local banks have a high degree of autonomy. BCCs are grouped into separate regional federations, which provide technical assistance and internal auditing procedures of their members. The functions of these regional bodies are overseen by the national association, Federcasse, which is also in charge of the BCCs’ strategic planning functions.

Some steps have been taken through the years toward a more integrated structure. In 2008 the Institutional Guarantee Fund (Fondo di Garanzia Istituzionale – FGI) was founded with the aim to use network resources to safeguard the liquidity and solvency of the member banks.

However, the Banking Law of 1993 (TUB) keeps Italian BCCs very close to their original nature, providing rigid capital and structural constraints³³ that obstacle the growth of the sector.

The cooperative banking sector has represented an important portion of the Italian banking system, growing consistently through the years. However, the financial crisis of 2008-2009 has impacted its financial stability as the sharp increase in non-performing loans has worsened its credit conditions. This has represented a great issue especially for the smaller BCCs that usually have more risky loan portfolios.

The financial crisis has brought in light the weaknesses of the Italian cooperative banks, making urgent the need of a reform to adapt the traditional characteristics of BCCs to the changing financial environment. The main challenge for the cooperative sector consists in countering individual risks and increasing external funding capacities while maintaining the cooperative identity. Another goal is to enforce intra-network mutual support systems. Guarantee schemes of are considered to be one of the main supporting elements of the “safety measures” mechanism of the individual banks, since they are closely interrelated with the ability to practice monitoring actions and ensure the sound and prudent management of the member banks.

Indeed, after the financial crisis of 2008, it has emerged that the most integrated cooperative groups, especially those that consolidate the capital of member banks according to cross guarantee schemes, have been able to better face financial troubles and to promote a progressive strengthening of the capital and dimension. This was specially realized through the greater use of market capital listing central holdings on the stock exchange.

It is clear that the systems of cooperative banks that are still strongly decentralized, such as in the Italian case, will have to converge towards more integrated organizational models, through an overall network enforcement, in order to meet both the re-regulation process and financial needs on the markets. At the same time, it will be necessary to strengthen the constraints within the internal guarantee and solidarity mechanisms, in order to maximize the benefits from the stability of local mutual banks.

The central entities are responsible for the healthy performance of both the banking and the cooperative dimensions of banks, ensuring the economic results and the protection of the cooperative roots. Even though there is no a possible common governance structure for each

³³ In accordance with the TUB, BCCs have to allocate at least 70% of their profits as reserves. Individual participation cannot exceed €50,000 per member. Assets that qualify for a zero risk-weighting under the Capital Requirements Directive (Directive 2006/48/EC) need to represent at least half of the risk-weighted assets. In addition, loans shall be granted primarily to members. Expansions into non-contiguous regions are possible only if the cooperatives have a sufficient number of members in the area.

banking group, the current reforms of the mutual sector in Europe aim to enforce these financial institutions. A major monitoring over risks, an increase of the prudential measures and a more integrated structure would allow to find alternative funding sources and to increase the capitalisation levels giving more stability to the sector. Financial soundness, innovation and higher efficiency would ensure the continuity for the member banks, fostering benefits in the banking industry.

CHAPTER 3 - THE CONTRACT OF COHESION: ON WHAT PRINCIPLES SHOULD IT BE BASED?

3.1 ANALYSIS OF FITD FINANCIAL PRINCIPLES

The 27th May 2016 the National Council of Federcasse issued a working paper that summarizes all the results and reflections developed by a specific study group related to the formation of the cohesion contract. This document represents just a starting point as Federcasse aims to involve further exponents of the BCCs in order to receive a greater contribution and more indications about the formation of the contract.

However, as a final version of the cohesion contract is not available yet, in order to develop my thesis I will take into consideration the financial principles that represent the pillars of the supervisory and management financial institutions. Then, I will try to understand what core financial principles should be considered to constitute the basis of the CBG and I will try to suggest some proposals for the formation of the cohesion contract.

The first financial regulation I will analyse is the one provided by the Fondo Interbancario di Tutela dei Depositi (FITD) and by the Fondo di Garanzia dei Depositanti del Credito Cooperativo (FGDCC). Indeed, these institutions have very relevant roles in the financial sector as deposit insurance is an essential feature of the safety net that underpins the stability of the entire banking system. Deposit insurance supports both the social function of savings and the monetary function of banking intermediation in order to avoid dramatic effects on depositors in case of bank failures. This is the reason why in all the evolved banking systems at the side of indirect protection (provided by vigilance authorities) even direct protection measures are implemented to guarantee deposits.

The first mechanism of deposit insurance was established in the US in 1933 with the Federal Deposit Insurance Corporation. Then other forms of guarantee have been developed through the rest of Europe as a consequence of the development of the banking activity and of the increase of its riskiness linked to the higher presence of potential elements of instability derived from the globalization process³⁴. However, the formation of such guarantee schemes have led to an increase in the risk of moral hazard as they may represent an incentive for managers to undertake riskier activities and to do not develop the necessary controls on the quality of loans.

³⁴ A.M. Tarantola, Ronchi, 1986.

Because of this reason, the protection given by these funds is never for the total sum of money but only for partial amounts. In Italy, such as in the other European states, the guarantee funds require member banks to meet some financial parameters in order to protect the funds themselves and to incentivize the other banks to exercise a healthy and prudent management.

As said before, in Italy, two guarantee Funds are present, the FITD and the FGDC.

The FITD is a private-law mandatory Consortium recognized by the Bank of Italy, established in 1987. In Italy the principle of mandatory membership in a deposit guarantee system has been introduced by the Law 385, 1st September 1993 (TUB). The goal of the FITD is to guarantee depositors of member banks and the financial resources necessary for its interventions are provided by the member banks in proportion to their risk levels.

Instead, the FGDC has been established for BCCs in accordance with the European Directive n. 19/1994. As stated by the Art. 5³⁵ of the FGDC, the financial resources used for the Fund's interventions are provided by the member banks and they are determined through a risk-based approach considering the patrimonial and liquidity levels, profits, exposure to credit risk, diversification level and cost efficiency. As determined by the Art. 25³⁶ of the FGDC's statute, the financial resources are distributed through Iccrea Banca, Cassa Centrale Nord-Est and Cassa Raiffeisen.

In accordance with the Art. 96-ter³⁷ of the Law 385/1993, the Bank of Italy has full powers in supervising and coordinating the activities of the deposit protection schemes of the whole

³⁵ Art. 5 Statuto Fondo di Garanzia dei Depositanti del Credito Cooperativo. "... il Fondo si avvale dei mezzi a tal fine somministrati dalle Banche consorziate, secondo un meccanismo commisurato alla rischiosità di ciascuna Consorziata...il rischio di ogni banca viene valutato sulla base dei seguenti profili gestionali: patrimonializzazione, redditività, liquidità, esposizione al rischio di credito, esposizione al rischio di tasso di interesse, efficienza di costo".

³⁶ Art. 25 Statuto Fondo di Garanzia dei Depositanti del Credito Cooperativo. Misura e modalità di somministrazione dei mezzi. 1. I mezzi richiesti dal Comitato di Gestione, ai sensi del precedente Articolo 24, sono somministrati per il tramite di Iccrea Banca, della Cassa Centrale Nord-Est e della Cassa Centrale Raiffeisen, che fungono da Tesorieri del Fondo.

³⁷ Articolo 96-ter Statuto Fondo di Garanzia dei Depositanti del Credito Cooperativo. Poteri della Banca d'Italia. 1. La Banca d'Italia, avendo riguardo alla tutela dei depositanti e alla capacità dei sistemi di garanzia di effettuare i rimborsi dei depositi protetti:

- a) riconosce i sistemi di garanzia, approvandone gli statuti, a condizione che i sistemi stessi presentino caratteristiche adeguate allo svolgimento delle funzioni disciplinate dalla presente sezione e tali da comportare una ripartizione equilibrata dei rischi di insolvenza sul sistema bancario;
- b) vigila sul rispetto di quanto previsto ai sensi della presente sezione
- c) verifica che la tutela offerta dai sistemi di garanzia esteri cui aderiscono le succursali italiane di banche extracomunitarie sia equivalente a quella offerta dai sistemi di garanzia italiani;
- d) le procedure di coordinamento con le autorità degli Stati membri in ordine all'adesione delle succursali di banche comunitarie a un sistema di garanzia italiano e alla loro esclusione dallo stesso;
- e) transfrontalieri o la fusione fra sistemi di garanzia di Stati membri diversi e partecipa alla vigilanza su di essi;
- f) informa senza indugio i sistemi di garanzia se rileva che una banca aderente presenta criticità tali da poter determinare l'attivazione del sistema;

Italian financial system. The Bank of Italy declares the state of insolvency and starts the controlled administration or the compulsory liquidation of the bank in sufferance. The Bank of Italy also authorizes both the FITD and FGDCC interventions based on an ex-post contribution system. Therefore, the resources for interventions are provided by member banks only after the Funds' requests and for the determined amount. This solution has been preferred to the one of making member banks paying annual quotas (how it happens in the US) in order to avoid to mobilize financial resources when it is not necessary³⁸. The fund consists of an accounting provision and a solidarity pact between the member banks that are committed to intervene to support each other, in the established measures, while there are no real provisions of money made available to the fund. In this way, instead of paying on the basis of their risk profile according to a merit-based system, the healthy banks of the group pay for the crisis of the banks in sufferance.

The FITD and the FGDCC are characterized by some common characteristics as regards their functions and risk measurement methodologies of member banks. Both Funds' interventions can have the form of preventive actions (such as funding operations, granting of guarantees, and participations to capital increases or acquisition of assets) or assurance functions as in cases of banks in liquidation phase the fund concurs to pay deposits³⁹:

The choice of the type of intervention is based on the least cost principle and in the event of intervention the Funds must operate in the interests of their members.

The level of coverage of both the Funds is 100,000 euros per depositor and per bank. For instance, if a depositor has 65,000€ in a bank that enters in a liquidation phase, the FITD/FGD will refund the whole sum of money. Instead, if the deposit amounts to 120,000€ (or to any amount exceeding 100,000€) the refund will be of 100,000€ as the maximum refundable amount is of 100,000€ per depositor. The payout time is presently established at 20 working days from the date the compulsory administrative liquidation takes effect (this time period will reduce to 7 working days with the transposition of Directive 2014/49/EU).

g) puo' emanare disposizioni attuative delle norme contenute nella presente Sezione.

³⁸ A.M. Tarantola, La vigilanza sulle banche e sui gruppi bancari, Il Mulino, 1996.

³⁹ Among the FITD interventions, the main ones have been:

1) Cassa di Risparmio di Prato (1987): the Fund granted to the bank in compulsory liquidation phase fundings for 200 billion L., participating than to a capital increase of 800 billion L. As a consequence of this intervention the Fund become the majority shareholder of the Monte dei Paschi group.

2) Banco di Tricesimo (Udine, 1990): the Fund intervened to refund deposits of the banks in compulsory liquidation phase for an amount equal to 6,5 billion L.

3) Banca di Girgenti (1991): the bank was first subject to extraordinary administration and then it entered into a compulsory liquidation phase. The Fund intervened paying the deficit of sale to the bank that took over the financial institution in liquidation phase.

As stated by the Art. 21⁴⁰ of its statute, the FITD:

- provides financial resources until reaching the objective level equal to the 0,8% of the total of deposits protected by the July, 3rd 2024, through the ordinary contributions of the member banks by the September 30th of each year;
- the available financial resources are allocated to the interventions of the fund;
- the member banks pay annually the ordinary contributions, in proportion to the amount of the protected deposits and of the risk level of each member bank, determined on the base of the management indicators;
- the available financial resources of the fund are invested in low risk activities with a sufficient diversification level. The gains of such activities contribute to achieve the objective level;
- after each intervention (and at least annually) the fund informs the member banks about the accumulation resource plan for the achieving of the objective level, including the additional contributions for the reintegration of the resources used in the interventions.

The interventions of the fund are regulated by the article 29⁴¹ of the FITD statute. The FITD acts in case of compulsory administrative liquidation of the banks part of the group and also in cases of extraordinary administration of the member banks. In both cases, the interventions of the fund have to be authorized by the Bank of Italy and they may be realized through operating companies, whose object is closely related to the institutional purposes of the Fund.

⁴⁰ “Art. 21 FITD Statute. Risorse finanziarie disponibili.

1. Il Fondo costituisce risorse finanziarie disponibili fino al raggiungimento del livello-obiettivo pari allo 0,8% del totale dei depositi protetti entro il 3 luglio 2024, ai sensi della Direttiva 2014/49/UE, attraverso contribuzioni ordinarie delle banche aderenti al 30 settembre di ogni anno.

2. Le risorse finanziarie disponibili sono destinate, al netto degli eventuali impegni assunti ai sensi dell’art. 24, agli interventi di cui all’art. 29.

3. Le consorziate versano annualmente le contribuzioni ordinarie, che sono commisurate alla consistenza dei depositi protetti, nonché al grado di rischio relativo a ciascuna banca aderente, determinato sulla base degli indicatori gestionali, secondo le modalità di cui all’art. 10 dell’Appendice.

4. Le risorse finanziarie disponibili del Fondo sono investite in attività a basso rischio e con sufficiente diversificazione e i frutti concorrono al raggiungimento del livello-obiettivo

6. A seguito di ciascun intervento e comunque almeno annualmente, il Fondo informa le banche consorziate in merito all’attuazione del piano di accumulo delle risorse disponibili per il raggiungimento del livello obiettivo, ivi incluse le contribuzioni aggiuntive per il reintegro delle risorse utilizzate a fronte di interventi.”

⁴¹ “Art. 29 FITD Statute. Interventi. 1. Il Fondo interviene:

a) nei casi di liquidazione coatta amministrativa delle banche consorziate autorizzate in Italia e, per le succursali di banche comunitarie consorziate operanti in Italia, nei casi in cui sia intervenuto il sistema di garanzia dello Stato di appartenenza;

b) nei casi di amministrazione straordinaria delle banche consorziate autorizzate in Italia.

2. Gli interventi del Fondo sono subordinati all'autorizzazione della Banca d'Italia.

3. Gli interventi possono essere effettuati anche attraverso società strumentali, il cui oggetto sia strettamente collegato alle finalità istituzionali del Fondo.”

Similar functions are developed by the FGD. As stated by the Art. 28⁴² of the FGD Statute, the maximum amount that each member BCC may be required to provide to the Fund is equal to the 0.8% of the total of deposits by the 30th June of the previous year. The Fund aims to guarantee the deposits of the member BCCs in accordance with the mutual principles and of the cooperative credit⁴³. As the FITD, the FGD intervenes in case of compulsory administrative liquidation or extraordinary administration or financial difficulties of member banks⁴⁴.

To sum up, it could be said that the interventions of both the Funds aim to:

- assure liquidity to all depositors to ensure their right to full availability of deposits;
- prevent that the regulatory capital of the bank decreases too much (making the bank undercapitalized);
- avoid the closing of the branches, protecting the business continuity of the bank and its employment levels;
- in the interest of the entire system as a whole, to contain and prevent mass phenomena not rational and not justified, that can easily spread to other banks, linked to the fear of losing their savings, with an excess of withdraw requests.

How do the FITD and FDG evaluate the level of riskiness of member banks?

Both the Funds perform their guarantee function through the use of a monitoring system that allows them to control the overall situation of all their member banks through a Balance-Sheet Indicators system that tests four risk profiles:

- Asset Quality;
- Solvency;
- Liquidity;

⁴² Art. 28 FGD Statute. Ammontare dei mezzi. 1. L'ammontare massimo dei mezzi che ciascuna Consorziata può essere chiamata a somministrare complessivamente al Fondo, ai fini degli interventi di cui all'art. 3, è stabilito nella misura dello 0,80% dell'ammontare complessivo dei depositi, alla data del 30 giugno dell'anno precedente, desunto dalle segnalazioni di Vigilanza.

⁴³ Art. 2 FGD Statute. Scopo. 1. Scopo del Fondo è la tutela dei depositanti delle Banche ad esso consorziate ... in osservanza alle previsioni del D. Lgs. 659/96 ed in conformità ai principi della mutualità e nello spirito della cooperazione di credito.

⁴⁴ Art. 3 FGD Statute. Interventi. 1. Il Fondo interviene:

- a) in caso di liquidazione coatta amministrativa delle Banche consorziate autorizzate in Italia, e per le succursali di Banche di Credito Cooperativo comunitarie consorziate operanti in Italia, nei casi in cui sia intervenuto il sistema di garanzia dello Stato di appartenenza;
- b) in caso di amministrazione straordinaria e di gestione provvisoria delle Banche consorziate italiane;
- c) in caso di situazione di difficoltà delle Banche consorziate italiane.

2. Gli interventi del Fondo sono subordinati alla autorizzazione della Banca d'Italia.

- Profitability.

Asset Quality Profile (A1)

The Balance-Sheet ratio A1 measures the capacity of a bank to absorb potential losses without risk of insolvency.

The risk of loss is given by the ratio of Bad Debts to Supervisory Capital. A1 is calculated through the following formula:

$$A1 = \frac{\text{Bad debts (net of adjustments)}}{\text{Supervisory capital}}$$

The numerator is the amount of Bad Debts related to ordinary clients, computed net of all related adjustments.

Solvency Profile (P)

The indicator P provides a measure of the bank's capital. Its formula expresses the excess of capital with respect to risk weighted assets.

The ratio P is calculated as follows:

$$P = \frac{\text{Supervisory capital}}{\text{Risk weighted assets (RWA)}}$$

Liquidity Profile (L)

The liquidity ratio gives a measure of the structural liquidity of the bank.

Its formula is the following:

$$L = \frac{\text{Receivables from clients}}{\text{Payables from clients + Circulating bonds + structured payables from clients and bonds at fair value}}$$

Profitability Profile (D1) (D2)

The profitability profile includes two ratios.

D1 refers to the aspect of the ordinary business of the bank. It highlights both the coverage of costs of the typical banking activity (through gross income) and the ability to meet possible extraordinary expenses.

D2 measures Loan Losses on Profit before Taxes.

These two indicators are calculated as follows:

$$D1 = \frac{\text{Operating expenses}}{\text{Gross Income}}$$

$$D2 = \frac{\text{Loan Losses (net of recoveries)}}{\text{Profit before Tax}}$$

The calculation of Gross Income and Profit before Tax includes interests arising from bad loans. D2 is calculated only if the numerator and the denominator are both positive.

Otherwise, the following coefficient have to be applied for the calculation of the Aggregate Indicator:

Numerator	Denominator	Coefficient
Positive	Positive	Depends on the value of the ratio
Negative	Positive	0
Negative	Negative	0
Positive	Negative	4
Zero	Pos/Neg	0

The five ratios are computed quarterly and they have to be sent to the Fund by all member banks on individual basis. Quarterly ratios are referred to 31st March, 30th June, 30th September and

31st December of each year. The same ratios cannot be calculated on a group basis since currently consolidated prudential returns are mainly reported by banks to the Bank of Italy every six months.

The following thresholds are set for each indicator:

Ratios and Thresholds					
	Low risk	Medium-Low risk	Medium risk	Medium-High risk	High risk
Indicator A1: <i>Bad debts (net of adjustments) / Supervisory Capital</i>	Up to 10%	from 10% to 20%	from 20% to 30%	from 30% to 50%	More than 50%
Indicator P: <i>(Supervisory Capital - Supervisory Capital Requirements) / RWA</i>	More than 6%	between 3% and 6%	between 2% and 3%	between 1% and 2%	inferior to 1%
Indicator L: <i>Receivables from clients / (Payables from clients + Circulating bonds + structured payables from clients and bonds at fair value)</i>	Up to 90%	between 90% and 100%	between 100% and 130%	between 130% and 200%	More than 200%
Indicator D1: <i>Operating Expenses/ Gross income</i>	Up to 60 % or operating expenses = 0	between 60% and 70%	between 70% and 80%	between 80% and 90%	More than 90 % or operating expenses < 0
Indicator D2: <i>Loan Losses, net of recoveries /Profit before tax</i>	Up to 20% or Loan losses <=0	between 20% and 40%	between 40% and 50%	between 50% and 60%	More than 60% or Profit before Tax < 0

Each class has a corresponding coefficient:

	A1	P	L	D1	D2
Low risk	0	0	0	0	0
Medium-Low risk	1	0,5	0,5	0,5	0,5
Medium risk	2	1	1	1	1
Medium-High risk	4	2	2	2	2
High risk	8	4	4	4	4

The sum of the coefficients of each ratio defines the Aggregate Indicator (AI).

The Statute, the Statutory Position is determined according to the following scheme depending on the value of the Aggregate Indicator:

<i>Value of Aggregate Indicator</i>	<i>Statutory Position</i>
from 0 to 3,5	<i>Low risk</i>
from 3,5 to 6,5	<i>Medium-Low risk</i>
from 6,5 to 8	<i>Medium risk</i>
from 8 to 10,5	<i>Medium-High risk</i>
from 10,5 to 14,5	<i>High risk</i>
more than 14,5	<i>Expulsion</i>

In accordance with the article 21 of the FITD statute, the total amount of money that the member banks are committed to make available to the Fund for interventions is between 0.4% and 0.8% of the Reimbursable Funds. However, these resources have a virtual nature as the Fund asks banks for resources only at the moment of the effective disbursement in favour of a member bank in crisis. If this condition does not occur, resources for interventions are just a commitment of the member banks and of the Fund.

The contribution quota is based on the portion of each bank's deposits covered by the Fund. As stated by the Art. 25 of the FITD statute, the Contribution Base is identified as the amount of Reimbursable Funds. The Fund calculates and communicates to the consortium members the contribution quotas for interventions commitments on a yearly basis, calculated on the base of the last available report.

For each member bank, the proportional quota of the contribution is given by the Individual Contribution Base over the Total Reimbursable Funds:

$$\frac{\text{Contribution Base}}{\text{Total Reimbursable Funds}} \cdot 1000 = \text{Proportional quota (in thousands)}$$

Two correction methods are applied to adjust this proportional quota. The regressive mechanism, as provided by the article 14 of the Appendix to the Statute, and the Weighted Average Aggregate Indicator (WAAI) provided by articles 4 and 5 of the Appendix of the statute may increase or decrease the proportional quota.

The Regressive Correction Method uses an increasing/decreasing percentage inversely linked to the size of the bank expressed by the amount of its contribution base. This correction

mechanism decreases the proportional quotas of bigger banks while it increases those of smaller banks. The percentage of increase and decrease of the proportional quotas shall vary from a maximum of +7.5% to a minimum of -7.5%.

The decreasing percentage is calculated through the following formula:

$$-7.5\% : (d - f) = x : (c - f)$$

$$\text{hence, for } c > f \quad x = -7.5\% * (c - f) / (d - f)$$

The increasing percentage is determined as follows:

$$+7.5\% : (f - e) = x : (f - c)$$

$$\text{hence, for } c < f \quad x = +7.5\% * (f - c) / (f - e)$$

where:

c = proportional quota (in thousands) of the bank's contribution base;

d = proportional quota (in thousands) of the highest contribution base recorded in the system on the date record;

e = proportional quota (in thousands) of the lowest contribution base recorded in the system on the date of record;

f = equilibrium quota, that is the proportional quota of contribution base that does not suffer from any increase or decrease.

As regards the Weighted Average Aggregate Indicator is calculated based on the previous three six-monthly balance sheet ratios that the bank submits to the Fund. This mechanism assigns a bigger weight to the closest report (in terms of time).

When the WAAI is:

- greater than 3, the bank's contribution quota shall be increased proportionally to the WAAI value;
- greater than 0 and less or equal to 3, the bank' contribution quota remains unchanged;
- equal to 0, the bank's contribution quota shall benefit from a reduction, commensurate with the total amount of increases.

Therefore we could say that the guarantee mechanisms of both the Funds are very similar as they are based on the same indicators, thresholds and correction methods. The only difference

is that while the FITD operates for the Italian banking sector, the FGD operates specifically for the mutual financial institutions. While the FITD was established in 1987, the FGD was formed earlier in 1978 as it derived from the already existing “Fondo Centrale di Garanzia delle Casse Rurali ed Artigiane”. Its establishment was linked to the wide territorial presence of the BCCs to support local communities that in turn has led to the necessity to provide guarantee to clients through the creation of a specific fund. The FGD guarantees depositors of each BCC from the risk of insolvency⁴⁵. As said before, in case of financial distress of a member bank, the other BCCs intervene to provide financial support to guarantee deposits until a maximum of 100,000€ per depositor. The member BCCs are required to provide financial resources to the Fund only in case of necessity, otherwise the quota they have to pay remains just a commitment. However, as a consequence of this mechanism, if large BCCs or several small BCCs find themselves in financial troubles at the same time, healthy BCCs may risk to do not be able to face these situations compromising their financial stability. To face this problem, in other European States, the Funds to support mutual banks are formed by real financial resources, in this way they are able to ensure a prompt intervention to financial crisis.

In conclusion it could be said that the presence of guarantee mechanisms in the banking system is essential to guarantee financial stability that is considered to be the first protection of savings⁴⁶. Especially the establishment of the FGD has allowed to enforce the capacity of the mutual banking sector improving the analysis of the member BCCs stability and the detection of criticisms through early warning systems. Interventions and recovery plans have been improved and continuously monitored to ensure the efficacy of their effects and developing the cooperative sector.

⁴⁵ Furthermore, the introduction of the Fondo di Garanzia degli Obbligazionisti (FDO) has strengthened the soundness and trustiness offering higher protection to clients. Indeed, it guarantees the refund of bonds in case of the bank's insolvency.

⁴⁶ In the first twenty years of activity, the FGD has provided funding grants for a total amount of 44,8 billions L. and further support interventions for 241 billion L.

3.2 ANALYSIS OF BANKING RATING PRINCIPLES

Other financial principles that may provide a guide for the formation of the cohesion contract are those provided by the Credit Rating for the evaluation of risk factors in assessing the future creditworthiness of financial institutions.

Indeed, Credit Rating Agencies (CRA) are defined as independent providers of credit opinions and they play an important role as their scores are used by investors, borrowers, issuers and governments for a variety of reasons. The main three CRA in the financial landscape are Moody's, Standard & Poor's and Fitch.

The rating score goes to a top level of AAA until a default level of SD/D in accordance to the following table:

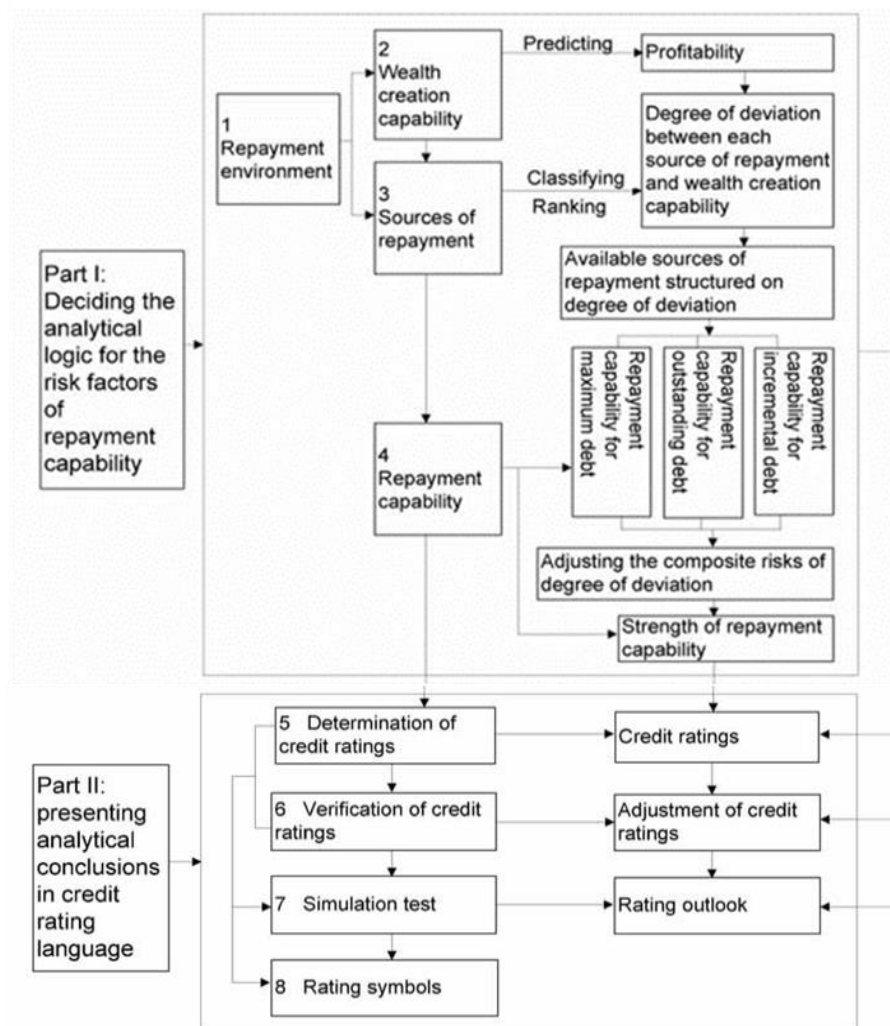
Interpretation	S&P and Fitch	Moody's	Meaning
Highest quality	AAA	Aaa	Extremely strong capacity to meet financial commitments.
High quality	AA+	Aa1	Very strong capacity to meet financial commitments.
	AA	Aa2	
	AA-	Aa3	
Strong capacity of payment	A+	A1	Strong capacity to meet financial commitments, but somewhat susceptible to adverse economic conditions and changes in circumstances.
	A	A2	
	A-	A3	
Adequate capacity of payment	BBB+	Baa1	Adequate capacity to meet financial commitments, but more subject to adverse economic conditions. Considered lowest investment grade by market participants.
	BBB	Baa2	
	BBB-	Baa3	
Uncertainty. Likely to fulfill obligations	BB+	Ba1	Less vulnerable in the near-term but faces major ongoing uncertainties to adverse business, financial and economic conditions.
	BB	Ba2	
	BB-	Ba3	
High-risk obligations	B+	B1	More vulnerable to adverse business, financial and economic conditions but currently has the capacity to meet financial commitments.
	B	B2	
	B-	B3	
Vulnerable to default	CCC+	Caa1	Currently vulnerable and dependent on favorable business, financial and economic conditions to meet financial commitments.
	CCC	Caa2	
	CCC-	Caa3	
Near or in default or bankruptcy	CC	Ca	Currently highly vulnerable.
	C	C	Currently highly vulnerable obligations and other defined circumstances.
	D	D	Payment default on financial commitments.

The credit quality of an enterprise entity or financial institution is not fixed and steady over a period of time, but it tends to undergo change to reflect alteration in creditworthiness.

Credit ratings include the following activities:

- Credit Risk Measurement & Monitoring;
- identify, measure and monitor exposures to market, interest rate, liquidity and asset risks;
- provide historical performance and underlying & cash flow projections based on credit models;
- deliver detailed quantitative and qualitative reports highlighting drivers of performance.

The rating process may be represented by the following scheme:



As regards the rating process of mutual banks, in Europe two categories of cooperative banking groups can be identified:

- cooperative banking groups that have a central authority, combining treasury management with group strategic planning and compliance with European regulations. These groups (such as Rabobank and Crédit Agricole) have usually a strong contractual guarantee system and are viewed as a consolidated group for financial and regulatory purposes. The rating assigned to these highly integrated groups refer to the ability of that particular legal entity to meet its debt obligations reflecting the strength of the group as a whole. Indeed, for well-integrated and consolidated CBGs it is hard to separate the attributes of the single member banks from those of the group as a whole as the shared support mechanisms provide a solid link between the financial resources of each member with the financial health of the entire group making;
- cooperative banking groups where the authority within the group is less centralised and is divided between central banks and powerful associations that claim responsibility in strategic planning, auditing, and the administration of support funds. The national regulator oversees each individual member bank and the groups' support mechanisms are not based on cross-guarantee systems. This is the case of Italian BCCs. For these CBGs, the degree of cohesion and solidarity may vary significantly in comparison to the first group. Because of their characteristics, rating agencies believe that their ratings are driven more by credit quality than by the entity itself. However, even in this case the rating score reflects both the cooperative banks' own strengths and their abilities to distribute financial resources within the group through internal guarantee systems.

To sum up, it could be said that CRA's rating procedures evaluate two main aspects: the integration level, considering the level of benefits that member banks receive being part of the group and if member banks would be supported by the group in case of financial distress.

All the cooperative banking groups in Europe have developed some solidarity mechanisms. However, these mechanisms differ in their extent, nature, depth and coverage levels. Considering the extent and the nature of these guarantee systems, while individual banks benefit from the group rating as the support of the other member banks strengthen their financial flexibility, some entities may be excluded from solidarity agreements. Therefore CRA aim to determine first which entities are covered by the guarantee mechanism and in what measure. Then, it is important to understand how the mechanism works, if member banks are legally bound to provide support to other members or if it just a voluntary commitment, if the financial

resources are already available or if they are paid at the moment of the call. Indeed, by understanding the nature of the fund it is possible to evaluate the efficiency and the speed of the interventions. Regarding the depth and coverage of the agreement, CRA aim to estimate how much money are available to support member banks. To do that, they have to take into consideration the extent to which member banks can contribute without compromising their own financial stability. Furthermore, it has to be evaluated the amount of resources it would be provided as the fund's resources should be enough to meet the needs of member banks in financial distress. Also, it is important to understand if the agreement covers balance sheet and off-balance sheet liabilities and the timelines of its interventions to determine the financial circumstances that would imply the fund's intervention and to evaluate whether they would be covered by the agreement.

It is important to underline that the well-functioning of a guarantee mechanism requires a high level of strategic and managerial cohesiveness, strong business integration, and unified risk management. In order to achieve cohesiveness and solidarity within a group of independent banks, the group requires a transparent and accepted process for making strategic decisions developed by the group's organizational bodies in order to ensure a common and coherent strategy and a homogeneous credit risk management within the whole group. To this purpose it is important for the group to have a monitoring process in place with an adequate level of internal reporting to review the implementation of the strategy. Another relevant aspect is represented by the extent to which the central organisation may intervene in group members, if they depart from group policy in their business (for example removing local executives in case they pursue different goals not aligned with the group's strategy).

Other elements that rating agencies take into consideration to assign their rating score may be classified in three broad categories:

- Macro Profile;
- Financial Profile;
- Qualitative Profile.

Macro Profile

Though the macro profile, CRAs assess the system-wide factors that are likely to affect the propensity of banks to fail. Indeed, from several studies it has emerged that macro variables such as GDP growth, real interest rates and exchange rates significantly affect bank failure

rates. Furthermore, other relevant factors included in this profile are represented by the strength and reliability of a country's institutions, its compliance with the national financial law and avoid corruption, the presence or absence of system-wide liquidity mechanisms or funding vulnerabilities, and structural advantages or deficiencies.

The elements included in the macro profile are the following:

- Economic strength;
- Institutional strength;
- Susceptibility to event risk;
- Credit conditions;
- Funding conditions;
- Industry structure.

Financial Profile

The financial profile aims to determine a bank's financial strength considering its solvency, its liquidity and its ability to generate cash flows. Indeed, a bank's financial strength may be considered as a function of its solvency (indicated by its risk relative over its loss-absorbing capital) and its liquidity. Instead, solvency can be defined as the combination of asset quality, leverage and earnings (the weaker and less predictable the asset quality, the higher the required returns), while liquidity is determined by a bank's funding profile together with its ability to access cash (the less predictable the bank's sources of funding, the larger the buffer of liquid assets required). It is important to highlight that all these variables are related to each other. In fact, a stronger capitalisation increases the capacity to absorb losses, increasing the confidence of counterparties and reducing the risk of liquidity problems. In turn, greater liquidity levels enhance solvency (as a bank disposing of an adequate liquidity is less likely to need to sell illiquid assets in the event of a funding problem).

Therefore, the financial profile is centred on the analysis of two main aspects: solvency and liquidity. The main financial ratios considered by this section are:

- Asset Quality: Problem Loans / Gross Loans
- Capital: Tangible Common Equity / Risk Weighted Assets
- Profitability: Net Income / Tangible Assets
- Funding Structure: Market Funds / Tangible Banking Assets

- Liquid Resources: Liquid Assets / Tangible Banking Assets

Asset risk

Asset risk is the measure of the degree of risk in the bank's asset portfolio both in terms of banking and trading. It implies also the monitoring of assets volume and its evolution. Risk policies of asset management are the most powerful indicators of bank risk. Great relevance is also given to risk concentrations and diversification as these aspects are considered a primary reason for bank failures. Another factor analysed by the asset risk is the complexity of assets that could come by the nature of assets or by their combination.

Capital and Profitability

Capital and profitability consider as first point the regulatory requirements the bank must fulfil.

Secondly, it examines the Bank's Risk Adjusted Capital Level Ratio (RAC) that compares the bank's capital to its Risk-Weighted Assets (RWA). It represents a forward-looking evaluation of a bank's ability to rebuild capital through its retained earnings.

The third step is to consider the earning capacity. This aspect is based on the use of estimations for operating incomes and losses for a certain future period. For this purpose, it is important to understand the key strategic factors likely to support future cash flow, and at the same time to identify critical factors that will inhibit them.

Particular attention has also to be given to the sector-specific analysis, as specific risk factors likely to be weighed in the credit rating vary considerably by sector.

In examining financial data, it is important to take into consideration both the economic reality of the underlying transactions and the differences in accounting conventions that may influence true economic values (for example, asset evaluations should be based on their ability to generate cash, not on the value stated in the balance sheet).

Funding structure

Funding structure aims to compare the bank's funding mix with the domestic industry average. To do this, CRAs evaluate financial ratios such as loan-to-deposit ratio and long-term funding ratio. Rating committees examine a variety of possible scenarios. Their aim is to measure the

issuer's ability to meet debt obligations against economic scenarios reasonably adverse to the issuer's specific circumstances.

Liquidity resources

Liquidity resources refer to the bank's ability to manage its liquidity needs in case of adverse conditions. This aspect focuses on the degree of bank's dependence on central banks liquidity facilities and on bank's degree of access to other possible liquidity resources. The common ratios used to analyse liquidity are liquid-assets, wholesale-funding and liquid assets/core-deposits.

Qualitative Profile

The financial profile also includes the supplementary analysis of other relevant qualitative considerations. Indeed, since ratings are thought to measure long-term risk, the rating process takes into consideration fundamental factors that will drive each issuer's long-term ability to meet debt payments (such as a change in management strategy or regulatory trends). As credit ratings involve a look into the future, it is evident that they are by nature subjective. Because of this reason, they cannot be based exclusively on a defined set of financial ratios and rigid computer models. Rather, they are the product of a comprehensive analysis of each individual issue and issuer by experienced, well-informed, impartial credit analysts. Any attempt to reduce credit rating to a formulaic methodology would be misleading and would lead to serious mistakes. To this purpose, further elements have to be considered into the rating analysis, such as the business diversification level, the extent to which a bank's inherent complexity may increase the risk of strategic errors and the corporate behaviour to evaluate whether a bank's strategy, management or corporate policies may reduce or increase its overall risk profile.

In sum, it could be said that a bank rating score includes an evaluation of the bank's asset quality, its capital adequacy and level of earnings, the appropriateness of its funding structure and its capacity to access to liquid resources. A further quantitative analysis considers the calculation of financial ratios that allow to assess the context of the macro-economic and financial environment in which the bank operates. In the end, further qualitative variables are considered, including the business model, corporate behaviour and the degree of internal complexity to give a complete analysis of the bank's financial scenario.

3.3 ANALYSIS OF BANK RECOVERY PLANS

As a consequence of the financial crisis of 2008, a “core” function of banking supervision is represented by prudential vigilance that aims to increase the monitoring level of banks to allow a fast detection of financial issues and therefore to provide prompt measures to avoid financial crisis that may undermine the global financial system. The prudential rules have been determined by the Basel Committee for the banking vigilance and they have been applied by the European Community in order to develop a homogeneous functioning of the banking sector within Europe. The prudential methodologies are based on patrimonial requirements and on the internal control and monitoring of risks and operations that may affect the soundness of the financial institutions.

The analysis of risks aims to determine the bank capacity to allocate efficiently its credits. Indeed, the risk measurement of a bank is linked to its attitude to select solvent clients, to finance profitable activities and to maintain an adequate diversification level⁴⁷.

The main banking risks to which correspond specific capital and liquidity requirements are:

Credit Risk: the risk that the counterpart fails to fulfil its obligations to repay its debts and interests. The insolvency of a large number of clients may bring to large losses affecting the profitability level of the bank.

Concentration Risk: an adequate diversification level has to be met by the bank’s activities in order to avoid that the concentration of credits toward a low number of clients undermine the soundness of the financial institutions.

Interest Risk: a balance between interest incomes and expenses should be always guaranteed to avoid that a variation of the interest rates may negatively affect the bank profitability.

Liquidity Risk: this risk may incur if a consistent number of clients decide to withdraw their funds at the same time as the bank would not have enough liquidity resources to face its obligations in the short time.

Market Risk: this risk is linked to external factors that may impact the bank functioning, such as a negative trend of prices.

⁴⁷ A.M. Tarantola, F. Parente, P.Rossi, 1996, La vigilanza sulle banche e sui gruppi bancari, Il Mulino.

As regards the capital requirements, in accordance with the Basel III, in addition to the minimum capital requirement equal to the 8% of the risk weighted assets a capital conservation buffer of 2.5% of risk-weighted assets has been established to ensure that banks dispose of a quota of capital promptly available to face situations of financial distress. This means that banks should accumulate capital during phases of economic growth and use this buffer in case of financial difficulties. Furthermore, countercyclical buffers have been introduced to prevent the amplification of cyclicality in the banking sector caused by excessive credit growth. The purpose is to protect the banking sector from losses deriving from the burst of bubbles and to ensure the availability of credit to the economy during times of financial distress.

The liquidity and solvency requirements instead include the Liquidity Coverage Ratio (LCR), and the Net Stable Funding Ratio (NSFR)⁴⁸. The LCR (high-quality liquid assets/total net cash outflows over the next 30 days) aims at ensuring that banks have sufficient high quality liquid resources to face short-term stress scenario. The NSFR (available amount of stable funds/required amount of stable funds) aims at maintaining a more robust structural liquidity profile, by creating further incentives for banks to fund their balance sheets exposures with more stable sources of funding. In practice, the ratio requires a minimum amount of funding that is expected to be stable over a one-year horizon based on liquidity risk factors assigned to assets and off balance sheet liquidity exposures.

Regarding the macro-prudential supervision, the goal is to timely detect areas of systemic risks and potential threats to financial stability and requires appropriate corrective interventions by competent authorities. Indeed, the micro-prudential supervision is not sufficient to ensure systemic stability of large banks that operate in complex interconnected financial landscapes with the consequent risks of propagation of the crisis at a systemic level, as demonstrated by the financial crisis. Therefore, it is important that both the micro and macro prudential supervision systems work together for ensuring a continuous and integrated risk-management approach and an efficient control.

In accordance with the prudential vigilance, control of banking groups has to be exercised at consolidated level, specifying the methodologies used for the consolidation process and also at individual level. It is necessary for banks to dispose of an adequate internal organization and reliable control systems⁴⁹ to ensure a healthy and prudent management. The supervisory functions should be exercised in accordance with the principle of proportionality considering

⁴⁸ Giuseppe Boccuzzi, Quaderni di Ricerca Giuridica, Towards a new framework for banking crisis management. The international debate and the Italian model, Banca d'Italia, 2011.

⁴⁹ Directive 89/646/CEE.

the different types and sizes of financial institutions and to take more focused preventive intervention (for example, larger banks should expect a very intense supervision and they should be prepared at any moment to deal with a distressed situation that could take place both for internal and external problems). An appropriate design and implementation of corporate governance, organisational structure and operational processes as well as internal control system and procedures, plays a key role in detecting weaknesses and identifying effective interventions. Strengthening internal control is the essential for the well-functioning of the banks as no external control can be more effective than a good internal one.

As stated by the Basel II, another key role is represented by stress tests that allow to evaluate the resilience of banks to adverse market conditions. They consist of assessing the effect on the bank's risks of specific events (sensitivity analysis) or of the joint movement of a set of economic and financial variables using adverse scenarios hypotheses (scenario analysis). The choice of risk factors has to be related to the bank's business; the construction of scenarios is also important as it could be too severe or too flexible, with consequent implications in terms of risk management. After the financial crisis of 2008, stress tests have become an ordinary tool of bank management and banking supervision, especially for large and complex financial institutions, determining in advance the degree of severity.

Another important component of a crisis prevention framework is given by the "living wills"⁵⁰ approach consisting in the preparation by banks, (especially by large and complex financial institutions) of specific contingency plans thought to explain how they are supposed to deal with adverse conditions. The plans have to report all the actions that a bank intends to take to recover from weaknesses that affect the technical profiles of the bank (recovery plans) or to start a resolution procedure in the event that it should fail (resolution plans). Contingency plans could be considered a type of preventive planning of crisis resolutions and they have to be continuously updated under the supervision of supervisory authorities. The 'living wills' principle may require banks to reorganise and simplify their corporate structures by separating business lines or activities making a clear distinction of banking operations in order to facilitate their selling to third parties in case of crisis. Critics of living wills claim that it might imply a return to a world of national markets in order to make things simpler for the authorities. Others claim that such wills may prevent a bank from entering into new lines of business or expand its

⁵⁰ C. Goodharth, How should we regulate bank capital and financial products? What role for "living wills", in The Future of Finance, The LSE Report, 2010

operations. However, dealing with the “too-big-to-fail” problem or “too-interconnected-to-fail” problem reducing banks complexity may be an advantage⁵¹.

The contingency plans may take the form of a “recovery liquidity plan” or “recovery capital plan” providing a clear identification of the decision-making process and the execution of the plan also including the timeframe for the plan development.

The recovery liquidity plan could be considered a funding plan, thought to help banks to deal with liquidity distress. The plan should include all information, readily available, about liquidity holdings (such as treasury bonds, and marketable assets) as well as the availability of collaterals for ordinary and emergency liquidity facilities by central banks.

Instead, the recovery capital plan is aimed at “derisking” the banking group⁵². This means that banks have to be prepared to liquidate part of their portfolios as well as selling part of their business lines in emergency situations. Another possibility for banks is to include in their recovery plans how they may be able to raise capital from private investors. This capital must be debt convertible in ordinary loss-absorbing equity when a bank is hit by distress. Furthermore, banks must prepare a resolution plan to ensure that if the bank is failing, or is likely to fail, the situation could be rapidly resolved or liquidated. Supervisory authorities should assess whether the proposed arrangements are credible, realistic and effective to restore the financial stability of the bank. If they are not satisfied by the bank’s proposal they can ask to modify the plans.

Contingency plans are based on early intervention systems that aim to identify the appropriate triggering indicator for interventions. In accordance with the Article 9 of the Directive 2014/59/EU, the European Banking Authority (EBA) has the mandate to issue guidelines to specify the minimum list of quantitative and qualitative indicators for the purposes of banks recovery planning. The proposed guidelines have been developed within the framework established by the Bank Recovery and Resolution Directive (BRRD) for the recovery and resolution of credit institutions and investment firms. In particular, this Directive requires to banks to establish recovery plans which set out measures they would adopt to restore long-term

⁵¹ ESFRC (European Shadow Financial Regulatory Committee), Dealing with problem banks in Europe, 22nd June 1998.

⁵² Giuseppe Boccuzzi, Quaderni di Ricerca Giuridica, Towards a new framework for banking crisis management. The international debate and the Italian model, Banca d’Italia, 2011.

financial stability in case of severe distress and to set up a special banking crisis management and resolution regime dealing with a wide landscape of problem situations⁵³.

The framework of recovery plan indicators provided by EBA⁵⁴ should be:

- adapted to the business model and strategy of an institution and be adequate to its risk profile;
- adequate to the size and complexity of each institution. In particular, the number of indicators should be sufficient to alert the institution of deteriorating conditions in a variety of areas;
- aligned with the overall risk management framework and with the existing liquidity or capital and business continuity plan indicators;
- integrated into the governance of the institution and within the decision-making procedures and include forward looking indicators.

The specific indicators⁵⁵ per category required by the EBA are listed in the following table:

To be included in the minimum list of categories of recovery plan indicators
1. Capital indicators
a) Common Equity Tier 1 ratio
b) Total Capital ratio
c) Leverage ratio
2. Liquidity indicators
a) Liquidity Coverage Ratio
b) Short-term wholesale funding ratio
c) Net outflow of retail and corporate funding
d) Cost of wholesale funding
3. Profitability indicators
a) Return on Assets
b) Return on Equity
c) Significant losses due to administrative/regulatory fine or adverse court ruling
4. Asset quality indicators
a) Impaired and past due loans / Total loans
b) Coverage ratio (loans and debt instruments)
c) Non-performing loans by counterparty sector
5. Market based indicators
a) Rating under review or/rating downgrade
b) CDS spread
c) Stock price variation (daily or weekly)
d) Default of a peer institution
6. Macroeconomic indicators
a) GDP variations
b) CDS of sovereigns
c) Rating downgrades of sovereigns

⁵³ The US Prompt Corrective Action (U.S. Code, Title 12, Chapter 16), operating since 1991, is a useful reference model of a system of mandated corrective action. It is based on five capital thresholds for capitalised, undercapitalised, significantly undercapitalised and critically undercapitalised. Corrective measures include a broad range of requirements and restrictions such as suspension of dividend payments, restriction of asset growth, compulsory recapitalisation and, when a bank is critically undercapitalised, authorities are obliged to close it, and this happens when the bank has not entirely lost its capital.

⁵⁴ EBA Recovery Planning, Comparative Report on Governance Arrangements and Recovery Indicators, 5th July 2016.

⁵⁵ EBA Recovery Planning, Comparative Report on Governance Arrangements and Recovery Indicators, 5th July 2016.

Furthermore, in every supervisory system, supervisory authorities should have enough powers and responsibilities to intervene timely and effectively. Among powers recognized to supervisory authorities the main ones regard requiring banks to take actions to raise their capital, to restrict their business and limit their operations, to restrict distributions to shareholders and to require intra-group financial support according to voluntary agreements reached at group level and taking. Additional powers may regard replacing board members and directors if necessary and imposing frequent reporting requirements.

To conclude we could say that the first objective in banking crisis management is the protection of financial stability maintaining confidence in the banking system. Indeed, in periods of financial crisis a lack of trust may lead to bank runs deepening the crisis and affecting the whole banking system. Therefore, in cases of financial instability restoring confidence is the first goal to pursue for supervisory authorities and the early detection of financial issues becomes of fundamental importance in order to avoid financial troubles and contagion effects on other institutions or on the whole market.

3.4 WHAT PRINCIPLES SHOULD THE CONTRACT OF COHESION INCLUDE?

In light of the financial principles provided by the FITD, by the rating agencies and by the Banking Recovery Plans, I will try to individuate the key elements that the cohesion contract should take into consideration for the well-functioning of the banking group.

So far, a working paper has been provided by Federcasse that should be considered an initial track for the formation of the final cohesion contract. In accordance to this first draft, the cohesion contract should be structured in two main sections. The first part should be dedicated to the duties and responsibilities of the holding company. It is highlighted that the leader of the CBG remains subject to the compliance with the mutual aims and the entrepreneurial autonomy of the individual BCCs, in addition, the management and coordination activities of the parent company must be developed to a service perspective for the member BCCs. At the same time, the holding is required to meet all the necessary capital and control constraints in order to ensure the healthy and prudent management of the whole group. Instead, the second section should focus on the risk assessment of the single BCCs. A set of management indicators should be provided to monitor the main operational areas of the bank, such as: capital and profitability, asset quality, liquidity and mutualistic functions. The evaluation of thresholds and weights and regulations of further specific areas are still under discussion.

Taking into consideration this first track, I will try to deepen the details of these two sections on the base of the information gathered through the previous paragraphs.

As said before, the first part of the cohesion contract has to be focused on the role of the holding, regulating in particular all its coordination and direction functions. From the analysis of the banking groups' regulations a relevant role is recognized to the central institution. Indeed, in accordance with the vigilance dispositions of the Bank of Italy, the holding company plays a role of strategic summit of the group⁵⁶. It can require data and information to the other member banks, it gives an organizational structure to the group and to the execution of its functions and it exercises a strategic control.

As regards the direction functions, the regulation refers to the direction process of the firms, articulated in the following phases: planning and programming, organization, coordination and

⁵⁶ Banca d'Italia, Istruzioni di Vigilanza per le banche, Sezione III, "...La capogruppo deve dare al gruppo una organizzazione che le consenta l'effettivo controllo sia sulle scelte strategiche del gruppo...".

control⁵⁷. This process is applied either to single companies either to groups of firms. In case of groups, in particular of banking groups, the direction activity affects the entire group and it is of competence of the holding.

The planning and programming phase may be defined as the process through which the objectives of the group are determined and how the firm intends to pursue them. The planning function is defined strategic if it is referred to the long period, while operative if it is developed for the short period. Within the banking group two levels of hierarchy are identified: a corporate level in charge of taking the strategic decisions regarding the entire group and a business level that aims to guarantee the competitive advantage of each member bank (that may be identified as Strategic Business Units)⁵⁸. In the banking group, the development of the corporate strategy is developed by the holding that is in charge to issue dispositions and instructions to ensure the homogeneous implementation of the strategic measures throughout the whole organization including the power to select and discharge components of administration bodies of member banks if necessary to safeguard the unity of the group⁵⁹. This aspect opens the issue of coordination between the holding and the subsidiaries. In a group characterized by a high integration level, controlled banks see their managerial and organizational autonomy limited by the constraints required by the holding. However, it is important to underline that the strategy at corporate level is not imposed by the holding but it is based on a contractual regulation determined in accordance with the other member banks (cohesion contract). The planning phase includes also an analysis of the internal and external environment in which the group operates⁶⁰. The internal analysis regards the identification of strengths and weaknesses of the organization itself and it is therefore based on an internal information system. This explains the information requirements of controlled banks to submit continuous data to the central institution. Instead, the external analysis implies an evaluation of the opportunities and threats that the group has to consider on the formation of its strategy. The analysis of the external environment includes also the regulation dimension and its evolution that of course may consistently affect the banking group functioning.

Following, the organization phase has the goal to determine the procedures of decision, control and execution, assigning the respective competences and responsibilities to each area. In

⁵⁷ Pennesi Roberto, *Attività di direzione e poteri della capogruppo nei gruppi bancari*, Giappichelli Editore.

⁵⁸ Pennesi Roberto, *Attività di Direzione e Poteri della Capogruppo nei Gruppi Bancari*, Giappichelli Editore.

⁵⁹A preliminary consultancy phase of the holding is required for the nomination of the components of the internal administrative bodies. A simplification of internal nomination processes of member banks 'components may be required to increase the efficacy and efficiency of the group's functions.

⁶⁰ Porter, "The essence of formulating competitive strategy is relating a company to its environment".

accordance with the vigilance dispositions of the Bank of Italy, the structure of the group is decided by the holding that has to evaluate the most suitable structure for the strategy it intends to pursue, furthermore, the group structure has to be efficient and to meet the regulation requirements imposed by the Bank of Italy⁶¹. The banking groups' structure requires the formation of homogeneous internal bodies to allow the group to benefit from synergies under the operational, technological aspects and scale economies. Common is the establishment of sub-holdings inside the groups in order to follow specific operative units. Therefore, it is important that the contract of cohesion provides a regulation of the relationships among the internal bodies of the different organizational levels.

As regards the coordination phase, it is the one that allows to realize the programs and to put them in place. Hence, it is necessary to guide and coordinate the activities of the different areas in order to ensure a homogeneous implementation of the programs. The coordination phase is strictly linked to the planning one, as it includes the coordination of forces, resources and factors thought to motivate employees. It is clear that this phase requires a large flow of information from the top toward the down of the group (as employees have to be informed of the objectives decided at the top level). In the banking groups, the information are communicated by the top through the issuance of dispositions and instructions that managers of the single areas have to implement. This in turn implies that the efficacy of the coordination at group level is given by the capacity of the holding to direct and influence the member banks⁶². In most of the cases, the direction functions inside the banking groups are developed by administrators however, in some cases specific bodies are formed to deal with the controlled institutions.

The next and last phase of the management process, is the one of control that aims to monitor the progresses that the group is doing toward the fixed objectives. The control function is strongly linked to all the other previous phases as its goal is to ensure the well-functioning of the planning, organizational and coordination activities. The control activity starts fixing some parameters to which the group has to compliance. If the results differ from the parameters, it is necessary to individuate the causes of such divergence promptly detecting financial threats and providing fast interventions. The banking regulation requires to banking groups two types of controls, the strategic one focused on the analysis of the competitive scenario and the control of the group's performances that have to be aligned to the group's objectives.

⁶¹ Banca d'Italia, Istruzioni di Vigilanza per le Banche, Sezione IV, Art. 4.

⁶² Pennisi Roberto, Attività di direzione e poteri della capogruppo nei gruppi bancari, Giappichelli Editore.

The financial stability of the banking group refers to the vigilance of the Bank of Italy that issues specific instructions in the group's interest, limiting the direction powers of the holding. The holding, in turn, has to exercise its functions on the base of the principles of fairness and reasonableness in order to guarantee the financial stability of the group⁶³. In accordance with the fairness principle, the holding is required to provide an equal distribution of duties among the member banks. However, this principle leads to several issues as not always it can be applied (for instance, if the holding has to reduce the exposure of the group toward a specific client and it is individuated a single institution that has to proceed to this reduction, it is impossible to ask to other banks to take these measures). The concept of reasonableness instead regards the coherency among the measures taken by the holding and their alignment with the group's goals. From several doctrines it has emerged that the sacrifices imposed by the holding to member banks may be compensated by the advantages deriving from the group's activity for the controlled banks. However, this assertion is based on the concept that to the sustained sacrifices correspond equal advantages. Therefore, the holding is required to implement strategies that take into consideration that sacrifices asked to controlled banks have to be compensated by adequate advantages. As regards the expenses faced by the holding for the direction of the group, the law defines this activity of competence of the holding and therefore the expenses cannot be spread among the member institutions but they have to be afforded by the central institution⁶⁴.

Another important aspect regards the funding mechanism based on a cross-guarantee system aimed to provide fast access to capital markets to ensure the prompt recapitalization of member banks in financial distress. It is also required to adopt an efficient monitoring system in order to promptly detect financial threats and provide fast interventions. The cross-guarantee system commits all member banks both in a vertical sense (from the holding to the BCCs) and horizontal sense (BCCs among each other's). The guarantee commitment of single banks is commensurate with available capital resources of each bank and limited to the amount of assets exceeding regulatory capital requirements at individual level (free capital). This kind of guarantee has a double function. An external function as it provides a guarantee in favour of creditors in case of breach of obligations of a member bank, and an internal one as it represents a mechanism of inter-group financial support aimed to prevent the insolvency of any member bank. An ex ante constitution of specific buffer of capital at the holding as a measure of intra-group sustain are required in order to guarantee the effective availability of funds (TIER1).

⁶³ Banca d'Italia, Disposizioni di Vigilanza per le Banche, Art. 61.

⁶⁴ G. Scognamiglio "Gruppo" e "Controllo".

Each member BCC has to participate to “promptly available funds” in proportion to its RWA and in the limit of its free capital.

As stated by Federcasse, the second section of the cohesion contract should focus on the risk assessment of each member BCC and to the determination of the main financial indicators that should be taken into consideration. On the base of the financial ratios provided by the financial institutions considered in the previous paragraphs, the main areas and indicators that should be included in the cohesion contract are:

Capital indicators:

- The Tier 1 capital ratio. It compares a banking firm’s core equity capital to total risk-weighted assets. It provides the measure of a bank’s financial strength based on the sum of its equity capital and disclosed reserves. Instead, a firm’s risk-weighted assets includes all assets that the firm holds that are systematically weighted for credit risk. Risk-weighted assets are used to determine the minimum amount of capital that must be held by banks and other institutions to reduce the risk of insolvency. The capital requirement is based on a risk assessment for each type of bank asset. In accordance with the Basel III, a firm must have a Tier 1 capital ratio of 6% or greater to be classified as well-capitalized.
- The Tier 1 leverage ratio: is calculated by dividing Tier 1 capital ratio by the firm’s average total consolidated assets. This ratio helps to determine the capital adequacy and to place constraints on the degree to which a banking firm can leverage its capital base. Holding banks need to have a Tier 1 leverage ratio equal to 3%, while other banks can arrive to 4%.
- The capital adequacy ratio (CAR) is the sum of Tier 1 and Tier 2 capital, divided by the sum of risk-weighted assets. It aims to ensure that banks have enough cushion to absorb a reasonable amount of losses before they become insolvent and consequently lose depositors’ funds.

$$CAR = \frac{\text{Tier One Capital} + \text{Tier Two Capital}}{\text{Risk Weighted Assets}}$$

As regards asset quality indicators a great attention has to be given to Non Performing Loans (NPL) that is the sum of borrowed money upon which the debtor has not made his scheduled payments for at least 90 days. A nonperforming loan is expected to enter default. If a bank

Profitability and liquidity indicators:

- The return on assets (ROA) ratio is the main profitability indicator that illustrates how well management is employing the company's total assets to make a profit.

The higher the return, the more efficient the management of resources. The ROA ratio is calculated by comparing net income to average total assets, and is expressed as a percentage:

$$\text{Return on Assets} = \frac{\text{Net Income}}{\text{Average Total Assets}}$$

- The return on equity ratio (ROE) measures how much the shareholders earned for their investment in the company.

The higher the ratio percentage, the more efficient is the management of the equity of the company and the better return is to investors:

$$\text{Return on Equity} = \frac{\text{Net Income}}{\text{Average Shareholders' Equity}}$$

- The loan-to-deposit ratio (LTD) is used to assess a bank's liquidity by dividing the banks total loans by its total deposits:

$$\text{LTD} = \frac{\text{Loans}}{\text{Deposits}}$$

If the ratio is too high, it means that banks might not have enough liquidity to cover unforeseen fund requirements; if the ratio is too low, banks may not be earning as much as they could be.

Loans in the numerator of the formula are investments or assets of a bank.

Instead, deposits in the denominator can be considered the same as debts as the individual depositors are granting monies to the bank with a return equal to the deposit rates and that can be called upon at any time.

In addition to these key financial indicators, of great relevance are the contributions of the methodologies of risk measurement and assessment of capital adequacy, among which the main

ones are represented by the Internal Capital Adequacy Assessment Process and by the Risk Appetite Framework.

ICAAP

In their activities, banks require to be compensated for the resources that they invest to offer their services. This compensation is linked to the entrepreneurial risk undertaken by them. Therefore management system to identify and take on well-priced risks becomes ever more important in today's competitive banking market. In accordance with the Basel II, banks are asked to implement an Internal Capital Adequacy Assessment Process (ICAAP) that focuses on capital management in order to ensure the capital adequacy of the bank. The Basel Committee defines economic capital as the methods or practices that allow banks to attribute capital to cover the economic effects of risk-taking activities.

As stated by the Basel II, the capital management function has to consider the capital supply side given by the balance-sheet capital (Tier 1, Tier 2, and Tier 3) and the capital demand determined by the regulatory capital for credit risk, market risk, and operational risk accounts. In addition, the capital management function should consider the valuation methods of rating agencies, which base their ratings mostly on Tier 1 capital on the capital supply side. Furthermore, the capital management function has to consider simultaneously the economic view of matching the capital supply (risk-taking capacity) with the capital demand (economic capital)⁶⁵. Capital supply includes mainly planned capital transactions and expected profits whereas capital demand is mainly driven by business plans and by risk-profile forecasts in combination with macro-economic scenarios. Since the requirements for both regulatory and economic capital have to be fulfilled, banks have to define possible solutions in case of conflicting requirements for regulatory and economic capital.

The ICAAP considers: the comprehensive risk assessment of material risks by measuring economic capital (the measurement of economic capital comprises collection of all necessary data), the determination of risk-taking capacity comparing economic capital with its risk-taking capacity (risk-taking capacity is derived from accounting items), the capital adequacy maintenance aligned with frequent and efficient internal controlling and reporting activities thought to continuously monitor and assess the adequacy of management methods and processes to the risk profile of the bank. It is of responsibility of the Board of Directors and of

⁶⁵ KPMG, Internal Capital Adequacy Assessment Policy.

Senior Managers to oversee the ICAAP by establishing well defined risk management strategies and guidelines.

RAF

A fundamental part of the financial profile is determined by the internal controls and information systems that provide a set of early warning indicators to monitor the risk level of the member BCCs. In this section, great relevance is given to the implementation of risk assessment methodologies. As stated by the Bank of Italy, it is of the holding competence the determination of the Risk Appetite Framework (RAF)⁶⁶.

The RAF sets the financial institution's risk profile and contributes to development of the institution's strategy and determination of the risks undertaken in relation to the institution's risk capacity. The Risk Appetite may be defined as the aggregate level and types of risk a financial institution is willing to assume within its risk capacity to achieve its strategic objectives and business plan⁶⁷. It also determines the maximum level of risk the financial institution can assume given its current level of resources before breaching constraints (risk capacity) and the tolerance risk thresholds that fix the maximum allowed deviation for the risk appetite. The risk tolerance thresholds are fixed to levels that would allow banks to exercise their operations within their risk capacity even in stress conditions.

Among the elements considered by the RAF, the main ones are: the business nature, the target market, the number of high-risk clients, the jurisdiction to which it is exposed, the internal audit and the volume size of its transactions. An effective RAF should provide a common framework and comparable measures across the financial institution for managers and the board directors to communicate and assess the types and level of risk that they are willing to accept. RAF explicitly defines the boundaries within which management is expected to operate when pursuing the institution's business strategy. An effective implementation of this procedure requires the incorporation of the RAF into the decision-making process and into the institution-wide risk management framework together with its communication throughout the organisation, starting from the top. The RAF should be continuously monitored and assessed by the internal audit on an institution-wide basis as well as on an individual business line and legal entity basis in order to ensure a constant alignment of the RAF to the institution's strategy

⁶⁶ Circolare n. 263, 27th December 2006.

⁶⁷ Financial Stability Board, Principles for an effective Risk Appetite Framework, 2013.

and to guarantee prompt corrective measures. For this purpose, continuous information flows are required by member BCCs and if necessary, the holding may require them the application of integrative information systems to guarantee the reliability and the correctness of the determined risk levels.

To sum up, it could be said that the contract of cohesion is the tool that allows BCCs to adhere to the CBG, accepting to be subject to the direction and coordination functions of the holding. It also states the responsibilities and duties corresponding to holding's role in charge of the strategic and operative direction of the group, regulating the strategic goals, the valuation principles and the risk measurement procedures to ensure the alignment of the single banks' internal procedures with the overall group's activity. For this purpose, the internal control functions of the member BCCs are externally exercised by the holding that also establishes the criteria for member institutions' activities (with reference to the grant of loans and to the level of risk exposure). The mutual nature of the group is protected by the art. 37-bis TUB in accordance to which the adhesion to the CBG does not compromise the exercise of BCCs mutual functions. Among the main powers of the holding we find the management of the group and of its internal bodies, internal control functions aimed to ensure the respect of the prudential financial requirements and the power of intervention on the affiliates even applying sanctions if necessary. The holding ensures the financial stability of the group through an efficient early warning system including the development of homogenous financial indicators together with valuation and risk assessment methodologies (such as ICAAP and RAF) throughout the whole group. As regards the aspects non-regulated by the cohesion contract, member BCCs maintain their contractual autonomy (the autonomy degree of single BCCs is calculated on a risk based approach and each single BCC maintains its own managerial autonomy in the limit of the operating agreements established with the holding). The agreement among the member banks is based on a system of cross guarantees that aims to mobilize the intra-group financial resources in case of necessity, allowing, in this way, to comply with the prudential rules provided for banks. A high capital disposal and the possibility to recur quickly to the market are preliminary to the ability to maintain and increase the support of the economy, other than to finance the necessary investments that otherwise the single BCCs would not be able to face individually. Moreover, the centralization of the common functions are necessary to realize cost synergies and to increase the offer of products and services improving the ability of self-financing of the whole group.

CHAPTER 4 –THE COOPERATIVE BANKING GROUP MODEL: EVALUATION OF POSSIBLE SCENARIOS

4.1 THE CRITICAL ASPECTS OF THE REFORM

As we have seen in the previous chapters, the current reform aims to develop the Italian cooperative banking sector around the figure of the cooperative banking group. The reform may be developed in two possible ways:

- establishment of two cooperative banking groups, a large one under Iccrea holding and a provincial one under Cassa Centrale Raiffeisen;
- establishment of a further group under Cassa Centrale Banca (that therefore would not join the group of Iccrea holding).

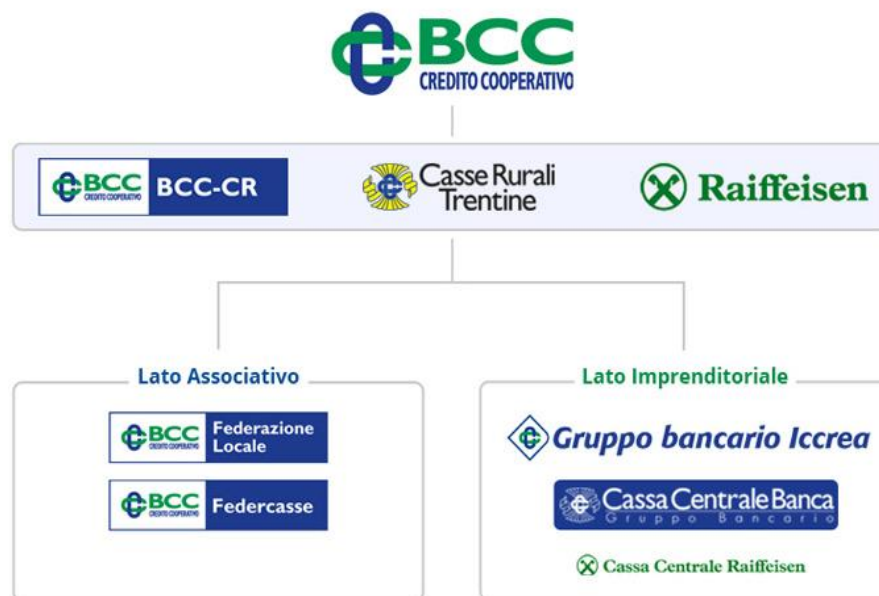
Let's deepen the profiles of these cooperative banks.

Iccrea Holding S.p.A. with 400 BCCs and more than five million clients is the biggest cooperative group in Italy. It is structured in three main areas (Institutional, Corporate and Retail) and it is formed for the 49% by subsidiaries and including a holding, Iccrea, that in turn owns shares in Iccrea Banca and Iccrea Gestione Crediti. Because of its large dimensions and its important network is considered to be the most suitable bank to cover the role of holding company of the Italian cooperative banking group.

Cassa Centrale Raiffeisen, instead, has always been considered a particular financial institution because of its territorial, cultural and linguistic characteristics. It includes 47 BCCs of the Bolzano area. Its activities are developed for the 72,5% within the province of Bolzano while for the 27,5% out of its province (including also its participation in an Austrian bank). The same situation recurs for the BCCs in the Bolzano area located in proximity to the border that, because of their location, have extended their activities out of the province of their competence. Therefore, we can understand that the territorial constraint provided by the reform would negatively affect these institutions leading to the loss of the portion of their activities provided out of the province of Bolzano. The formation of a provincial group would allow to Cassa Raiffeisen to maintain its clients. Indeed, in accordance with the provinciality criteria, the holding of the group is required to have its legal basis and its subsidiaries within the province of its competence but no limits are fixed for the area of exercise of its operations. The objective of this exception is align with the cooperative nature of the institutions as it would allow the group to access to further markets for the benefit of the member BCCs.

As regards Cassa Centrale Banca (CCB), it is the second biggest mutual bank in Italy after Iccrea and it is considered the ‘head’ of the north-east of Italy. It is a banking group established in 2007. It is formed by a holding company Centrale Finanziaria del Nord Est S.p.A. and by Cassa Centrale Banca-Credito Cooperativo del Nord Est that in turn owns shares in other institutions (Centrale Credit & Real Estate Solutions, Centrale Leasing Nord Est and Centrale Soluzioni Immobiliari). The holding, Centrale Finanziaria del Nord Est SpA has been created to maintain the control of Credito Cooperativo del Nord Est in Cassa Centrale Banca. It is owned for the 78% by the Casse Rurali Trentine, for the 20% by the Banche di Credito Cooperativo del Veneto and of Friuli Venezia Giulia and for the 2% by cooperatives of the Cooperazione Trentina. Cassa Centrale Banca instead is owned for the 68% by the holding, for the 25% by DZ Bank AG, and for the 6% from business associates and for the remaining 1% from other BCCs and Casse Rurali.

The structure of BCC is represented as follows:



The initial proposal of the BCC reform argued to include CCB under the group of Iccrea holding. However, CCB has not completely agreed with this deal and it has proposed the creation of its own group. Because of its relevant role covered in the Italian financial sector, CCB’s proposal is linked to the necessity to maintain its full autonomy to continue to ensure the protection of the local communities and to enforce the strong relationships of trust and networks that have been built through the years. CCB has not excluded the option to join Iccrea’s group but it has asked in exchange a large share of the capital of the holding together with a representation in the management and administration bodies (another condition asks to shift the legal basis of the group to Milan but this requirement will not probably be met as Iccrea

is from Rome). Its proposal has been taken into consideration. Federcasse is evaluating this possibility but until an agreement is not signed with Iccrea holding all the scenarios are still open.

To sum up, the new financial landscape would include a main large group under Iccrea holding and a provincial group in Bolzano represented by Cassa Centrale Raiffeisen. What is still under discussion is the position of Cassa Centrale Banca that has expressed its will to create another group, but at the same time the option to join Iccrea holding is not excluded. As a final agreement has not been founded yet, both the streets are still possible.

As we have seen previously, the provincial groups will see their activities limited to their provinces (the activities developed outside of their competence territory cannot exceed the 5% of their total operations) while all the other BCCs (except the three institutions that have opted for the way-out) are thought to join the group of Iccrea holding.

But what do BCCs think about this reform?

BCCs seem to be quite sceptical about the reform. The main critical aspect regards the governance of the holding. Indeed, especially the well-managed BCCs are worried that the administration of the group will be assigned to large BCCs managed by who has not developed a good management of its own BCCs. Even the functioning of the cross-guarantee system is not well defined yet, this makes BCCs sceptical about the efficiency of the new system. The flow of resources throughout the group must be well regulated in a proportional way, even regarding the advantages distribution derived from its activities.

Another risk is to create a cooperative banking group too large that may lead the member BCCs to lose their mutual nature and their territorial feature. It is important to remember that their relevant role in the current financial scenario has been given thanks to their role close to their territory. The relevant influence exercised by their shareholders and clients has allowed BCCs to take key management decisions and to provide always more appropriate services to local communities.

A further aspect that has not to be undervalued regards the negative effects on the employment level of these banks. BCCs will have to go through complex reorganization processes to eliminate bodies that exercise the same functions or structures whose activities have been transferred under the holding competences.

BCCs complain that if the reform is not well developed it will lead to several problems such as a large restriction of the BCCs' autonomy, high coordination and reorganization costs, loss of the territorial feature and decrease of profitability of the individual institutions. The competence and mentality of the governance are considered to be key elements in the group management. Therefore, managers should come from the soundest BCCs and also, they should change periodically in order to ensure a prudent and healthy management of the group. The cooperative banking group should represent an opportunity for each member BCC to enforce itself and to strengthen its role in the territory, guaranteeing higher reliability and higher solvency levels.

The pros and cons of the reform are not visible yet as everything is still being developed. However, we can start to see the first effects as since January 2016 until the end of July 2016 the number of BCCs is decreased from 366 to 337 and it is expected to decrease until 300 by the end of the year. Moreover, since the end of June 2016, the Temporary Compulsory Fund has become operative providing support for mergers between BCCs. In particular, its interventions are thought to provide financial support to BCCs in acquisitions processes so that the acquiring bank does not incur in financial distress as a consequence of the acquisition.

4.2 ONE OR TWO COOPERATIVE BANKING GROUPS?

As said previously, Cassa Centrale Banca has proposed to form a second CBG under the holding Cassa Centrale Banca that will have to meet the 1 billion capital threshold. The objective of CCB is to create a modern banking network able to compete at international level thanks to its levels of profits, its efficiency and its risk management. The level of autonomy of member BCCs would be proportional to their soundness and it would be determined on the base of a rating model developed in accordance with a risk-based approach. It has specified that the majority of its members will be institutions with high ratings and only few BCCs with low creditworthiness will be included. Other proposals of CCB regard the adhesion to the Fondo Interbancario Tutela di Depositi (instead of to the Fondo di Garanzia dei Depositanti) as normal banks and the increase of the limit of the amount of shares that can be owned by single shareholders from 10% to 25-30% in order to attract new shareholders even at international level. At the moment 15 BCCs have expressed the will to join CCB's group, but CCB estimates to reach a minimum of 91 members for a total of 1,187 branches, with a total capital ratio greater than 15%.

But what could be the impact of the creation of a second group in the Italian cooperative sector?

First, let's try to understand why Cassa Centrale Banca is reluctant to join Iccrea holding. The reasons given to justify CCB's resistance about the formation of a unique cooperative banking group are more political than economical. Indeed, in the past Trentino-Alto Adige has always been subject to a strong Austrian influence that has left significant cultural and ideological roots. Because of these reasons, Trentino-Alto Adige has always maintained its autonomy through the years, having also a special statute. Its local communities have a different mentality from the rest of Italy and especially from Rome.

CCB aims that by creating its own group it would see its autonomy more guaranteed without compromising its mutual nature and its networks. The 15 BCCs that argue to join CCB's group are solid and well-managed institutions with 156 branches in the national territory, 1.107 employees, own funds equal to 709 million euro, a total capital of 8,8 billion euro and a patrimonial ratio equal to 17,1%. In their appeal to the Italian Parliament, they have asked an appropriate vigilance over the correct implementation of the reform as they are worried to be deprived of their autonomy and to be transformed in tools of Federcasse.

Another CCB's concern is that the holding's governance located in Rome may be less efficient respect its standards and that it may be influenced by the politic that could be addressed to

pursue different interests from those thought for the prudent and healthy management of the member BCCs. Indeed, often in Italy, the governance of these financial institutions has appeared to be related to political interests that do not secure efficiency in financial markets nor at the level of individual financial intermediaries. Instead, they are likely to lead to a misallocation of funds, impairing the effective functioning of the markets and bringing in second plan the mutual values. This political influence in most of the cases makes BCCs to take on higher risks and a higher financial exposure dramatically increasing the risk to incur in financial distress.

A further aspect regards that belonging to a large network implies that some counterparts may behave opportunistically by applying risky strategies and by appropriating part of the benefits generated within the alliance (as the term “cooperation” is also defined as mutual cooperation between “self-oriented” actors). Therefore, efficient control mechanisms are needed to detect similar problems and timely prevent them from occurring as an opportunistic behaviour of only few members could have negative effects on the entire cooperative credit system.

What would be the advantages of joining Iccrea’s group for Cassa Centrale Banca?

By joining Iccrea holding CCB may have consistent advantages either under the security point of view, either as regards economic opportunities.

As the main goal of the CBG is to use the financial resources of sound BCCs to support the weak ones, CCB and well-managed BCCs do not want to risk to find themselves in an adverse position and to get weakened by a wrong implementation of the cross-guarantee mechanism. However, establishing a unique large-size group would allow to spread financial risks among a larger number of banks, reducing the financial impact on each institution. In a globalized world companies are exposed to high market risks as they have to face global competition that in turn increases BCCs’ risks to incur in financial distress. Therefore, even the soundest BCCs would benefit from operating under a unique CBG as they would be supported by a larger financial network. Large dimensions and high diversification levels are essential characteristics to survive in a globalized economy. Also, the holding would dispose of larger amounts of financial resources and it would be able to better guarantee the respect of prudential thresholds.

Another advantage regards the economic opportunities in terms of know-how, innovative processes, technology and infrastructures at network level. Further benefits would derive also from a decrease in management costs due to the rationalization of internal bodies whose functions have been transferred to the holding. The presence of two groups would imply a

double organization (in terms of internal bodies, control mechanisms, number of employees) and therefore double costs for the financial sector. Furthermore, there would be the risk that the two groups would not develop homogeneous assessment methodologies, internal controls and auditing procedures leading to vigilance and control issues.

A further opportunity for CCB would be represented by the exploitation of possible synergies arising from the cooperative network that would bring to benefits in terms of efficiency, profits, growth and business expansion.

As regards the mutual values and the territoriality issue, the reform provides proportional autonomy constraints on the base of the risk level of each member institution. This means that efficient and well-managed BCCs as in the case of CCB would not see significant restrictions of their autonomy while they would obtain more benefits from the group's activity. Therefore, BCC's local presence is not threaten by the new regulation instead they may be able to run their local activities in autonomy seeing themselves enforced by a sounder structure that in turn would increase clients 'trust.

Another critic has been done about the fact that the unique CBG would represent a case of monopoly. However, as individual BCCs will maintain their autonomy this is not a real risk. The holding would be in charge of the direction and coordination of the group, while the operations at local level would remain under the competence of the local BCCs without altering the current competition.

In conclusion, I would say that coordinating around 300 autonomous BCCs under a unique group would be very delicate and complex especially in absence of previous experiences in this sector. The reform proposed by the Bank of Italy seems to be oriented to the short-run, open to future possible adjustments once that the main changes will be developed in accordance with the new regulation.

The complexity of the reform's implementation requires a gradual process that brings the Italian cooperative banking structure toward a unification path through mergers and acquisitions. Then, the process should lead to the formation of a high integrated cooperative banking group whit member BCCs meeting the constraints provided by the cohesion contract and the prudential requirements stated by the vigilance authorities. The reform is expected to have a first-round effects after which further adjustments will be developed to reach the goals of integration and financial soundness of the group.

It is important to consider that each cooperative banking system is characterized by different features, linked to cultural values and developments. Because of that, the reform has to be implemented step by step considering that every cooperative banking group has a different history and operates in a different economic and banking environment. Therefore, there is no one-size-fits-all solution and the development of each cooperative banking system varies under the influence of historically and contemporary economic and social conditions and it should coherently evolve with the development of the territories in which cooperative banks operate.

A final consideration must be expressed about the wide and complex EU regulation. Indeed, the creation of a CBG of large dimensions implies a high level of regulation with high costs of compliance risking to penalize the activities of the smallest BCCs that would see themselves restricted by too heavy rules. To avoid these negative effects, regulations must be applied in a proportional way in order to respect the different business models and different financial peculiarities of each member bank.

4.3 ANOTHER PROPOSAL OF REFORM

As said before, the formation of a unique large CBG will imply for the holding all the difficulties related to the organization and direction of managing a group of more than 300 BCCs.

An answer to this issue is coming from the BCE on the example of the American banking reforms proposed after the default of the Lehman Brothers to provide a solution to the issues linked to the banks too big to fail. Indeed, the idea that promotes the role of small BCCs over those of large banking groups is changing as a banking system based on few large groups increases the systemic risk that may bring to negative repercussions for the whole national economy.

Since years, in Europe it has emerged the necessity to have larger financial entities as they are thought to lead to greater benefits either in terms of economy either in terms of capital. In fact, larger the companies are, more wealth they are able to produce boosting the local economy. Also, because of their large capital they are considered to be very solid and therefore able to absorb more risks.

However, the financial crisis has highlighted the high risks related to these large institutions. Because of their large dimensions, the default of these financial entities would have drastic consequences on the whole economic system, even at global level. As stated by the President of the Federal Reserve of Minneapolis, Neel Kashkari, the only way to avoid future systemic crisis is to break into pieces the banks that have become “Too big to fail”.

‘There cannot be any risk they default’ as the consequences of their failures would deeply affect the collectivity. Therefore, especially in the banking sector, it is not sufficient to think only about a way to save financial institutions (such as the bail-in) but it has to be evaluated a solution to prevent the default of these banks.

In light of this new American vision, the reform of Italian BCCs is going to the opposite direction, risking to unify lots of weak banks under a unique weak group. Because of this reason, the BCE is showing its scepticism about unifying all Italian BCCs under a unique nation-size CBG, suggesting a different solution that would encourage the formation of more CBGs of adequate proportions.

Since years the global financial landscape has been divided between the ‘Too big to fail’ and ‘Too small to succeed’ banking models. But how is it possible to determine what the right size of a financial system should be?

It is important to underline that the purpose of the financial sector should be to serve the real economy. Indeed, the size of the financial sector of a country not only affects the level of output by allocating productive capital more efficiently but may also contribute to economic growth.

The size of the banking sector may be defined as the total assets of credit institutions including both the domestic assets of local credit institutions and the assets of branches and subsidiaries of foreign credit institutions present in a country.

Among the literature, Goldsmith (1969)⁶⁸ has empirically shown a positive correlation between the size of the financial sector and the long-run economic growth. Moreover, further studies have revealed that the relationship between financial development and economic growth is influenced by several elements such as financial depth, institutional factors and competitiveness of banking systems. As stated by Levine (2005)⁶⁹, a well-developed financial sector is beneficial for growth and better developed financial systems ease external financing constraints that firms face. However, there might be negative effects when the financial sector becomes too large, as it may harm the economy and the society as a whole bringing to a misallocation of resources and to deep crisis (Arcand, Berkes and Panizza, 2012)⁷⁰. Therefore, through the years, several studies have tried to understand whether there is a threshold above which financial development no longer has a positive effect on economic growth and it has emerged that different countries have different thresholds.

In particular two main views emerge about the size of the banking system. The first point of view argues that the size of the banking sector should be related to the capacity of the country. This means that the size of the financial sector should not be too large compared to the size of the country, this in turn implies that small countries cannot have large banking sectors. However, this does not necessarily mean that large banks are more dangerous than small banks as this aspect depends on the riskiness of their assets (Dermine and Schoenmaker, 2010)⁷¹. Instead, the second vision is based on the ‘follow-the-client’ principle, in accordance to which

⁶⁸ Goldsmith R. (1969), *Financial structure and development*.

⁶⁹ Levine R. (2005), *Finance and growth: theory and evidence*.

⁷⁰ Arcand, Berkes and Panizza (2012), *Too much finance?* IMF.

⁷¹ Dermine and Schoenmaker (2010), *In banking, is small beautiful?*

the banking sector should support its clients (Grosse and Goldberg, 1991)⁷² and therefore the size of the banking sector should be in line with the financial needs of households and firms.

Another consideration must be done about the financial needs of a country, indeed as banks are thought to serve the real economy, socio-economic trends determine credit composition within a nation. From the study of Beck, Büyükkarabacak, Rioja and Valjev (2008)⁷³, it has been shown that only banks lending to enterprises have a positive and significant impact on economic growth. As countries differ in their financial needs, and especially with regard to loans provided to non-financial entities, it may be possible that countries with a larger private sector also have larger banks as banks finance both industry and trade.

In light of the analysed literature, it seems clear that the development of a banking system is strictly related to the development of the private sector. As regards the Italian situation, its productive structure appears to be very fragmented, characterized by more than 4 million of small-medium companies. This fragmented structure is reflected by the Italian banking sector, especially by the cooperative financial sector because of its territorial feature. Therefore, it is evident that the Italian financial network cannot be formed by large banks but it is important to respect the dimensions of the local enterprises. This is an important aspect that has to be taken into consideration also for the development of the BCCs reform. The formation of a unique large CBG may do not be adequate to the characteristics of the Italian economic structure that instead is more linked to small local financial institutions able to protect and develop the local territory. Therefore, as final consideration it might be said that the formation of a unique CBG does not seem to be appropriate to the Italian cooperative sector. First of all, as this model may bring the unique CBG to incur into the risks related to large institutions, also including the so called systemic risk exposing the whole national economy to high risks of financial crisis. Because of this reason, even the BCE seems to discourage the unique CBG in favour of the formation of more groups that would allow to better develop management and control functions and to mitigate the effects of possible financial distresses on the national economy. Secondly, a nation-size CBG is considered to imply high challenges at direction and coordination level and to do not match the texture of the Italian economic sector. This aspect may bring to a loss of efficiency and to high costs for the whole system, also threatening the mutual principles and the territorial links representing the foundations of the cooperative financial sector.

⁷² Grosse and Goldberg (1991), *What is the appropriate size of the banking system?*

⁷³ Beck, Büyükkarabacak, Rioja and Valjev (2008), *Who gets the credit? And does it matter?*, Georgia State University.

4.4 FINAL CONSIDERATIONS ABOUT THE FUTURE OF ITALIAN BCCs

The global financial crisis has deeply changed the financial world in which banks operate. The main drivers of this change are represented by the reform of the financial regulations taken always more at supranational level and by the technological progress. After the financial crisis, the aim of the G20 has been to increase the soundness of banks by increasing their disposal of capital of better quality. While the technological aspect is regarding mainly the development of methods of payments and services online, the financial regulation's goal is to increase banks' capacity to resist to external shocks ensuring the stability of the national financial systems.

We have seen that in Italy the financial institutions strongly weakened by the international financial troubles have been the BCCs that are therefore object of a current reform that aims to make their structure more suitable to operate in the current financial conditions.

As final considerations, it could be said that the key element of the BCCs reform is represented by the reorganization of the governance. An effective reform should enforce the cooperative governance framework while preserving the characteristics that identify cooperative banks making their existence essential for the national territory. As seen in the previous chapters, cooperative banks were created to provide financial services to market segments in the local community that otherwise would have had not been able to access credit. Thus, BCCs' business model is based on relationship banking and strong territorial orientation.

To sum up, the Italian cooperative sector is currently evaluating the optimal implementation of the reform. At the moment, the formation of two CBGs seems to prevail on the formation of the unique group. However, a further suggestion of the BCE is proposing the creation of more CBGs.

As analysed previously, a large group would allow to spread the risk among a higher number of members, giving the perception of a sounder network. However, such large dimensions are likely to imply a high risk of "moral hazard" as the perception that creditors of large banks will not be involved by possible financial distresses lowers the cost of capital and encourages managers to engage in risky activities. Secondly, large groups are likely to be complex, non-transparent and difficult to understand and control for outsiders (or even insiders) and they would also imply the need of systemic risk-based regulations. Therefore, I think the formation of a unique group would bring to the creation a very complex entity, very difficult to manage and control. This complexity would be increased by the characteristics of the Italian cooperative

sector that, as based on small-medium banks, has never experienced before the direction of entities of such dimensions.

Regarding the formation of a possible second group, I think that if it will be developed as proposed by CCB, including around 91 BCCs it may have adequate dimensions to provide efficient services to member BCCs and to get enough financial resources in the capital markets. Furthermore, including a lower number of BCCs, the activities of direction and coordination may be better developed also in terms of internal controls. Even with regard to the risk management, the number of member entities (selected on their rating score) seems to be large enough to support financial risks without compromising the financial soundness of member BCCs. However, the final financial landscape would be represented by two non-proportional CBGs (one including around 91 BCCs and another one with more than 200 members) leading to further issues of vigilance and supervision of the sector.

In my opinion, I would say the vision of the BCE seems to be the most appropriate proposal. I think BCCs reform should aim to form more banking groups of similar dimensions in terms of total assets. The groups' dimensions should be adequate to ensure the soundness of the member institutions and of the whole cooperative credit system at the same time without exposing the whole sector to systemic risks. Moreover, sounder and weaker BCCs should be spread equally among the groups, thus creating homogeneous CBGs so that the weaknesses of less stable BCCs may be balanced by the strong ones but without compromising their health. Therefore, the composition of the membership of each group should be regulated by the Bank of Italy on the base of the rating score of each institutions in order to ensure the formation of balanced groups. Otherwise, the free aggregation of BCCs may lead to the risk of creating sound groups of strong financial institutions leaving outside the weaker banks that therefore would form weak networks losing the purpose of the reform.

I think that an optimal proposal may be to create from three to four CBGs. The creation of more groups of similar dimensions among each other and of similar ratings would allow to overcome the difficulties related to the large dimensions of the unique group and also to take a first step toward the direction of the consolidation of BCCs. As this represents an unknown territory for the Italian cooperative credit, I think the reform should be developed gradually to do not make the Italian cooperative sector to pass from a fragmented weak structure to the complex management of a nation-size group. In this way a first-round effects may be assessed on the base of which adjustments and further regulations may be provided improving step by step the groups' functions and structures.

As regards the risk management, in this case the financial risk would be spread among a lower number of BCCs. However, the holding of each group would dispose of 1 billion euro and it would have access to capital markets, therefore each group would have the possibility to raise fresh financial resources in case of necessity. The dimensions of the groups would be not too large so that it may allow to develop efficient controls and at the same time large enough to ensure the soundness of the network without incurring in systemic risks. Indeed, this structure would allow to mitigate the effects of the financial distress or default of a group on the whole national economy.

To conclude, I would say that this reform represents an important evolution of the cooperative sector that allows Italian BCCs to increase their soundness and their competitiveness. As all the possible developments of the reform are still under discussion, we cannot be completely sure about the final effects of the reform but relevant benefits are likely to be reached. For sure, the most key aspect regards the improvement of the governance and the well regulation of the cohesion contract that will have to include all the mutual and financial principles of the new cooperative banking groups to ensure the well-functioning of the Italian cooperative system.

CONCLUSION

The deep financial crisis of 2008 is considered to be the main cause of uncertainty and loss of trust within the cooperative banking system that has brought to an increase in the cost of capital and to the instability of the financial mutual system. The crisis has modified the context as well as the relationships network in which cooperative banks operate. Because of their self-financing mechanisms and their strong presence at local level, these institutions seem to be no more suitable to survive and compete in an always more complex financial scenario.

In this thesis, I have analysed the reform of the Italian BCCs thought to reorganize the Italian mutual sector to overtake its structural limits. In particular, the goal of the reform is to improve the access to funding resources and to allow an adequate diversification level lowering BCCs' exposure to financial risks.

In the first chapter we have seen that the Law 14th February 2016, n.18, TUB introduces in the Italian mutual banking system the model of the Cooperative Banking Group, which pillars are represented by the figure of the holding company, the formation of the cohesion contract and the establishment of a cross-guarantee system. Through this new structure, the reform aims to enforce member BCCs increasing their access to capital markets and providing a sound guarantee mechanism allowing a fast flow of financial resources throughout the institutions part of the group.

In the second chapter, the models of the mutual banking groups Crédit Agricole and Rabobank have been analysed. The main emerged characteristics regard their high-integrated networks based on internal cross-guarantee systems and the roles of the public central holdings that coordinate member banks, ensure a fast access to financial resources and provide an efficient control over the whole group. Because of their sharp growth and their large dimensions, these financial institutions are considered to be the main Cooperative Banking Groups in Europe, representing great examples for the possible development of the Italian BCCs reform.

In the third chapter, we have seen that a guide for the formation of the cohesion contract may be represented by the financial principles and capital thresholds provided by other financial institutions such as the FITD, rating agencies and by those included in the EBA's banks recovery plans. In accordance with the developed analysis, the CBG's financial profile should be based on financial indicators thought to monitor the capital adequacy, liquidity and profitability together with efficient risk assessment procedures of each member BCC in order to timely detect financial threats and provide prompt interventions to safeguard the financial

stability of the whole group. Among the other, the most relevant financial ratios are the Tier 1 capital ratio, the Tier 1 leverage ratio, the Return on Assets ratio together with the ICAAP indicator and the risk measurement methodology RAF. It is important to say that financial and risk assessment procedures have to be homogeneously and correctly developed within the group to satisfy the principle of prudent and healthy management of the CBG. In light of this principle, great relevance is given to the role of the cohesion contract that must adequately regulate the holding's direction and coordination functions together with the development of efficient internal controls to guarantee the well-functioning of the whole organization. Furthermore, the reform has to ensure the respect of BCCs' mutual nature safeguarding their territorial links and their role to serve and boost local economies.

In the fourth chapter instead we have considered the possible ways of the reform development. We have seen that the initial proposal of reform aimed to unify the Italian BCCs in a unique banking group under the direction of Iccrea holding. However, from the recent news, it seems likely that the reform will bring to the formation of a second CBG run by Cassa Centrale Banca and of a further provincial group run by Cassa Raiffeisen. In addition, another proposal of the BCE seems to take place into the financial scenario, suggesting the formation of two or more CBGs in order to protect the national economy from possible systemic risks that would dramatically affect the whole Italian economy. From the analysis of these possibilities, it could be said that this reform may lead to significant benefits for the Italian mutual banking sector increasing the reliability and financial soundness of BCCs boosting a possible growth of the mutual sector itself and of local economies. The final effects of the reform are not observable yet, however in my opinion the optimal solution may be to create more than two CBGs, in accordance with the proposal of the BCE. Indeed, the formation of three or four groups would ease the development of the holding's functions and therefore it would guarantee a better management of the member BCCs ensuring the protection of the mutual principles.

In conclusion, it could be said that in light of this reform, the role of BCCs may be considerably enforced and their local presence would be strengthened by an increase of reliability and clients' trust. However, all these benefits may be reached only through an efficient development of the reform, providing all the necessary measures and regulations to guarantee the protection and the well-working of such important financial institutions in our financial system.

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