



How to apply for the 'Tremonti bonds'

As part of certain anti-crisis measures, hybrid instruments to be subscribed by the state, up to 31 December 2009, that are aimed at increasing the core tier-one capital ratio of the Italian listed banks – the so-called 'Tremonti bonds' – have been provided for by the Italian Ministry of Economics and Finance in its 25 February decree, published in the *Official Gazette* No. 55 of 7 March 2009, implementing article 12 of Legislative Decree No. 185 of 29 November 2008.

Introduction

As part of certain anti-crisis measures, hybrid instruments to be subscribed by the state, up to 31 December 2009, that are aimed at increasing the core tier-one capital ratio of the Italian listed banks – the so-called 'Tremonti bonds', have been provided for by the Italian Ministry of Economics and Finance (MEF) in its 25 February decree, published in the *Official Gazette* No. 55 of 7 March 2009, implementing article 12 of Legislative Decree No. 185 of 29 November 2008. Below is an indicative summary of the main provisions of the ministry decree. The annex summarises the terms and conditions of the prospectus concerning the bonds.

The banks that apply for the measures prescribed by the ministry decree must continue their business without misusing the support that they have received and without undertaking aggressive expansion plans that are not compatible with the objectives of article 12, paragraph 1 of Decree 185 and without taking any unfair advantages from the support.

Procedure for subscribing the bonds

- The application must be submitted by the bank on the same day to the MEF and the Bank of Italy at least 30 days before the envisaged date of subscription of the bonds (in this briefing, references to 'the bank' mean the bank that is applying for the bonds). The application must contain, inter alia, the following:
 - a resolution by the bank's relevant body;

- the amount of the requested subscription;
- the initial nominal value; and
- the expected subscription date.
- The subscription to bonds is subject to the execution of a memorandum of understanding (*protocollo d'intenti*) by the bank and the MEF. This shall be based on a framework agreement executed between the Ministry and the Italian Banking Association (ABI) on 25 March 2009, which provides the necessary guidelines. The bank has six weeks from signature of the framework agreement in which to disclose the initiatives that it is going to undertake to ensure compliance.
- The memorandum of understanding must contain, inter alia, commitments by the bank and its banking group over:
 - the full availability of credit, especially for small and medium-sized businesses, through the preservation, for at least three years, of financial resources for a value of no less than such resources available in 2007 and 2008 to be specified in the memorandum of understanding;
 - contributions, equal to 1.5 per cent of the total amount of the issue, to increase the fund-guaranteeing financing for small and medium-sized businesses provided by article 11, paragraph 5 of Decree 185;
 - the application of credit conditions that take into account the lower risk of the financing, being guaranteed by the state and the fund provided under the second bullet point above, and are

- sufficient to allow for the development and continuance of business initiatives;
- assurance of adequate liquidity level for creditors of state entities;
 - assistance for families that are having difficulties due to the suspension (*Cassa Integrazione Straordinaria*) or loss of their jobs, including the suspension for at least 12 months, without additional costs, of payment of mortgage arrears;
 - a dividend policy that favours bank capitalisation; and
 - the quarterly submission of a report detailing the financing granted, distinguishing between consumer loans, mortgages and loans to different types of businesses.
- The subscription is also subject to the bank's adoption of an ethical code (*codice etico*). This must contain limits on the remuneration of top management and bank staff, including traders. The code shall also set out limits and conditions for severance payments, which shall be disclosed. The bank must establish a remuneration committee.
 - On the basis of the Bank of Italy's evaluation, the Ministry will take a decision on the amount of the bonds to subscribe. The Ministry will inform the Bank of Italy of its decision and the requesting bank of its acceptance; the decision is, however, subject to a prime ministerial decree indicating the resources required to finance the transaction.
- Bank of Italy's evaluation**
- For the purposes of the Ministry's decision, the Bank of Italy will evaluate, inter alia:
 - the bank's capital adequacy, both currently and as expected in the future;
 - the bank's risk profile, taking into account market indicators, where available, including the spread on liquid credit default swap (CDS) relating to subordinated debt, and the bank's rating, which should not be lower than two on the credit quality assessment scale as per Directive 2006/48/CE; and
 - the features of the bonds, their conformity to the Ministry decree and the prospectus attached thereto, their allocation to supervisory capital
- and the ratio of the amount of the requested subscription to the overall value of the bank's risk-weighted assets.
- As to the economic terms and conditions, it is possible to carry out the subscription if the transaction is completed under the terms and conditions set out in the prospectus.
 - The economic terms and conditions of the transaction could also be deemed satisfactory if they lead to an overall expected return lower than that provided for in the prospectus, subject to the following conditions:
 - such return is greater than the average return of 30-year BTPs (long-term treasury bonds) plus at least 200 basis points; and
 - the bonds are subscribed to by private investors (instead of by the Ministry) for at least 30 per cent of their total amount, of which at least 20 per cent is held by investors who are not shareholders holding more than 2 per cent of the issuer's capital since the issue.
 - With the Bank of Italy's assistance, the Ministry assesses whether the transactions that are also subscribed to by private investors, as provided above, are in line with market conditions.
 - For each bank, the amount of the subscription is limited to the minimum required for the goals to be reached and should not exceed 2 per cent of the total value of the bank and its banking group's risk-weighted assets. Furthermore, the amount is established with regard to requests coming from the financial system, taking into account the state of the financial market and the need not to damage the state's fund-raising.
 - If the bank's rating is lower than two on the credit quality assessment scale as per Directive 2006/48/CE, the Ministry will notify the transaction to the European Commission for the purposes of an evaluation of its compliance with the communication to the Commission dated 5 December 2008 (state aid).
 - The bonds subscribed are deposited by the Treasury in a settlement account registered in the name of the Bank of Italy with Monte Titoli. The Bank of Italy keeps the accounting of the bonds subscribed and the related interest.

Transactions monitoring

The transactions, as detailed above, and their effects on the economy are monitored by the Ministry, with the Bank of Italy's assistance, on the basis of data received from each bank.

To this end, the Bank of Italy must send aggregate information on the financing granted by the banks to the regional observer established at the prefect's office (*Prefettura*) by article 12, paragraph 6 of Decree 185.

Annex: the prospectus

The bonds will be issued by the bank at face value and subscribed by the MEF. The bonds will be convertible into the bank's ordinary shares.

Subordination

If the bank goes into voluntary or administrative mandatory liquidation (*liquidazione coatta amministrativa*) or other insolvency proceedings, the outstanding debt (equal to the nominal value of the bonds) will rank after all of the bank's other debts and equally with the ordinary shares in the order of priority upon liquidation.

In a case of business continuity, the bonds will also rank equally with the ordinary shares, as follows. If the bank makes losses that reduce the overall minimum net worth adequacy ratio (*coefficiente patrimoniale di vigilanza complessivo*) to 8 per cent they are to be absorbed by the share capital and reserves. Losses reducing the minimum net worth adequacy ratio to below 8 per cent are to be shared proportionally by the bonds and by the aggregate amount of share capital and the reserves; the nominal value of the bonds is then to be adjusted through a pro rata reduction (ie if the minimum capital adequacy ratio falls to 4 per cent, the nominal value will fall by 50 per cent). The reduced nominal value of the bonds will be increased with any subsequent net profits of the bank in proportion to any increases in the bank's net assets until it reaches the bonds' nominal value at their launch (the initial nominal value).

Maturity

Unless the bonds are converted or redeemed earlier, they will expire and be repaid if the duration of the bank expires or if the bank goes into voluntary or

administrative mandatory liquidation (*liquidazione coatta amministrativa*) or other insolvency proceedings.

Conversion ratio

The 'conversion ratio' represents the number of ordinary shares of the bank that each bond can be converted into if the bank exercises its conversion right. The ratio is equal to the ratio of the initial nominal value to the average reference price (as defined by article 4.1.7 of the Borsa Italiana Markets Regulations) of the bank's ordinary shares in the 10 days preceding the bonds' launch. If Borsa Italiana publishes an adjustment figure for derivatives traded on the IDEM market and having shares of the bank as the underlying asset, the conversion ratio shall be adjusted accordingly.

Interest payments

Annually on 1 July from 2010 (with an adjusted amount of interest payable on 1 July 2009), interest will be payable in arrears on each bond by the bank for a sum equal to the greater of:

(a) (i) 7.5 per cent of the nominal value of the bond for 2009; this percentage will be increased annually by 0.25 per cent from 2010 to 2013; from 2013 it will be increased bi-annually by 0.5 per cent (the first increase of 0.5 per cent, to 9 per cent, taking effect in 2015) until it reaches 15 per cent in 2039; or, alternatively, (ii) 8.5 per cent of the nominal value of the bond from 2009 to 2012, 9 per cent from 2013 to 2016 and then the percentage is to be increased by 0.5 per cent bi-annually until it reaches 15 per cent in 2039; and

(b) an amount equal to a set percentage (105 per cent for 2009, 110 per cent for 2010, 115 per cent from 2011 to 2017 and 125 per cent for 2018 and for the following years) of any form of dividend distributed by the bank for ordinary shares, multiplied by the number of shares that the bonds would be converted into by applying the conversion ratio (the underlying shares), limited to 15 per cent of the bonds' nominal value; and

(c) from 2011 and for the following years, a percentage of the nominal value of the bonds equal to the average return on the issue of 30-year BTPs (long-term treasury bonds), relating to the first quarter of the year in which the interest is payable, increased by 300 basis points for payments in 2011 and 2012 and by 350 basis points for payments in 2013 and for the following years.

The interest is payable if and to the extent that there are distributable profits as indicated in the bank's most recent financial statements available on the interest payment date. If there are no distributable profits and/or the bank has a minimum net worth adequacy ratio equal to or below 8 per cent, interest is not payable (this also applies to the dividends on ordinary shares). Unpaid interest will not accumulate and therefore if interest is not paid it will be lost.

Warranties and undertakings from the bank

While the bonds are outstanding, the bank undertakes not to voluntarily reduce its capital or to delist its shares. If the bank breaches either of these undertakings it must pay a penalty sum to the MEF. It also warrants that nothing has occurred (that has not already been made public or communicated to the MEF) that has had or could have a material adverse effect on its net worth, financial situation or income. The bank undertakes to disclose any changes that occur before the bonds are subscribed to.

Redemption rights (*Riscatto*)

The bank has at any time the right to redeem all or part of the bonds. It must give the MEF notice of 30 to 60 days before the date for redemption. The Bank of Italy must approve any redemption of the bonds.

If condition (a)(i) of the interest provisions applies (see above), the redemption will take effect for the greater of: (i) 110 per cent of the bonds' initial nominal value; and (ii) the market value of the underlying shares calculated as an average of the reference prices over the preceding 30 days (the market value being capped by a set percentage, increasing annually, of the bonds' initial nominal value).

If condition (a)(ii) of the interest provisions applies (see above), redemption will take effect for the bonds' initial nominal value if it occurs before 30 June 2013, for 110 per cent of the initial nominal value between 1 July 2013 and 30 June 2015 and then for the following years for the greater of: (i) 110 per cent of the bonds' initial nominal value; and (ii) the market value of the underlying shares calculated as an average of the reference prices over the preceding 30 days (the market value being capped by a set percentage, increasing annually, of the bonds' initial nominal value).

Conversion rights

From the third anniversary of the bonds' date of issue, the bank may exercise its conversion rights over them. It must give the MEF notice of 30 to 60 days before the date for conversion. The total value of the underlying shares (calculated as the average of the reference price in the preceding 10 business days) must be equal to or greater than 110 per cent of the initial nominal value for conversion to take place. The bank may exercise these rights only if it has prior shareholder approval for the share capital increase.

Other details

The bonds are transferable only with the bank's prior written consent (except if transferred to other public entities or companies controlled by the state). The bonds are in a dematerialised form. They are governed by Italian law and the courts of Rome have jurisdiction over them. The bonds will not be listed on any regulated market and no offer or listing prospectus will be published for them. The costs (including taxes) of issue and subscription procedures will be borne by the bank.

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