FSB FINANCIAL STABILITY BOARD

Peer Review of Italy

Review report

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Foreword

Financial Stability Board (FSB) member jurisdictions have committed, under the FSB Charter and in the *FSB Framework for Strengthening Adherence to International Standards,*[1] to undergo periodic peer reviews. To fulfil this responsibility, the FSB has established a regular programme of country and thematic peer reviews of its member jurisdictions.

Country reviews focus on the implementation and effectiveness of regulatory, supervisory or other financial sector policies in a specific FSB jurisdiction. They examine the steps taken or planned by national/regional authorities to address IMF-World Bank Financial Sector Assessment Program (FSAP) and Reports on the Observance of Standards and Codes recommendations on financial regulation and supervision as well as on institutional and market infrastructure that are deemed most important and relevant to the FSB's core mandate of promoting financial stability. Country reviews can also focus on regulatory, supervisory or other financial sector policy issues not covered in the FSAP that are timely and topical for the jurisdiction and for the broader FSB membership. Unlike the FSAP, a peer review does not comprehensively analyse a jurisdiction's financial system structure or policies, or its compliance with international financial standards.

FSB jurisdictions have committed to undergo an FSAP assessment every five years; peer reviews taking place typically two to three years following an FSAP will complement that cycle. As part of this commitment, Italy volunteered to undergo a peer review in 2022-2023.

This report describes the findings and conclusions of the Italy peer review, including the key elements of the discussion in the FSB's Standing Committee on Standards Implementation (SCSI) in November 2023. It is the second FSB peer review of Italy and is based on the objectives and guidelines for the conduct of peer reviews set forth in the *Handbook for FSB Peer Reviews.*[2]

The analysis and conclusions of this peer review are based on the responses to a questionnaire by authorities in Italy and reflects information on the progress of relevant reforms as of September 2023. The review has also benefited from dialogue with the Italian authorities as well as discussion in the FSB Standing Committee for Standards Implementation.

The draft report for discussion was prepared by a team chaired by Makoto Minegishi (Bank of Japan) and comprising Sarah Delvigne (Banque de France), Vaibhav Chaturvedi (Reserve Bank of India) and Fernando Dancausa (World Bank). Lara Douglas, Michael Januska, Marianne Klumpp and Hans Sassen (FSB Secretariat) provided support to the team and contributed to the preparation of the report.

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1 See the *FSB Framework for Strengthening Adherence to International Standards* (January 2010).

2 See the *Handbook for FSB Peer Reviews* (April 2017).

Abbreviations

BdI	Banca d'Italia
CCR	Central credit register
CN	Composizione Negoziata
CRR	Capital Requirements Regulation
EBA	European Banking Authority
ECB	European Central Bank
EU	European Union
EWS	Early Warning Systems
FSAP	Financial Sector Assessment Program
FSB	Financial Stability Board
GACS	Guarantee on Securitisation of Bank bad loans
GBV	Gross book value
GFC	Global Financial Crisis
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
LSIs	Less Significant Institutions
NBV	Net book value
NPL	Non-performing loan
ROE	Return on Equity
SCSI	Standing Committee on Standards Implementation
SIs	Significant Institutions
SME	Small and Medium Enterprise
SPV	Special Purpose Vehicle
SSM	Single Supervisory Mechanism
UTP	Unlikely to Pay

Executive summary

Background and objectives

The main purpose of this peer review is to examine Italy's progress to date in reducing non-performing loans (NPLs) in the banking sector and any further reform plans, with a view to drawing lessons for the FSB membership. The peer review focuses on three areas: the accounting, regulatory and supervisory measures to reduce NPLs; the development of a secondary market for NPLs; and measures for resolving NPLs, notably through the enforcement, restructuring and insolvency framework. It examines the steps taken by the authorities including by following up on relevant FSAP recommendations and FSB commitments.

Main findings

The Italian authorities have achieved significant success in reducing NPLs on bank balance sheets. From their peak of €360 billion in December 2015, gross NPLs fell to €63 billion by June 2023, with the gross NPL rate declining from 16.5% of total loans to 2.8% over the same period. Close cooperation between domestic authorities, open communication with the private sector and a collective responsiveness significantly contributed to this successful reduction.

Accounting and regulatory steps from the authorities included the adoption of IFRS 9 and the implementation of European Banking Authority (EBA) and European Central Bank (ECB) guidelines and capital directives. These guidelines cover specific expectations of banks' management executives and the competent supervisor in relation to the management of NPLs; the implementation of calendar provisioning; the assessment of Pillar 2 capital requirements and guidance; and detailed reporting requirements. Banca d'Italia (BdI) introduced a regulatory requirement for granular NPL loan reporting that preceded the ECB reporting requirements. This increased completeness of relevant data improved NPL management at banks and led to additional transparency which supported the development of the secondary market. Alongside these regulatory requirements BdI increased supervisory intensity with several publications of best practices.

To support the removal of NPLs from bank balance sheets, the authorities took several steps to facilitate the securitisation and sale of NPLs. The Guarantee on Securitisation of Bank bad loans (GACS), introduced in 2016 by the Italian Ministry of Economy and Finance, has undoubtedly been a success in contributing to the removal of NPLs from banks' balance sheets. GACS has accounted for the largest reduction in NPLs in banks' balance sheets between 2017 and 2022 and so far has not been at a cost to the taxpayer, although the workout of NPL portfolios disposed via GACS remains in progress and therefore still could expose government finances to risk. The securitisation and sale of NPLs supported by the GACS enabled a secondary market for NPLs to develop and attracted new players and capital. It prompted a structural change by increasing the technical capacity of the Italian financial sector to transfer and manage NPLs outside banks. Some other jurisdictions have introduced reforms modelled on this approach.

The authorities have undertaken a dynamic overhaul of in- and out-of-court restructuring and enforcement procedures. The insolvency, debt restructuring, and debt enforcement systems were a key impediment to the resolution of NPLs in 2016, and Italy has made remarkable

progress in improving its legal and institutional framework, although further improvement is necessary. In the broad reform process that started in 2015, insolvency procedures were overhauled, a new focus on out-of-court restructuring was introduced, debt enforcement was streamlined and key institutions, including courts and administrators, were strengthened.

At the same time, further steps can be taken to preserve the success achieved and to improve further the ecosystem for managing NPLs in the banking sector. These include maintaining a robust secondary market for NPL disposal and further improving the efficiency of the insolvency, debt restructuring and debt enforcement framework.

Maintaining a robust secondary market for NPL disposal

GACS has finally expired after several extensions and is not expected to be reactivated as it is not needed in the current environment. With the bad loans legacy stock largely reduced, the focus of bank's balance sheet management is now on the Unlikely to Pay (UTP) portfolio. Compared to bad loans, where debtors are insolvent or in substantially similar circumstances, the sale and workout of UTP loans involves different considerations and skills for banks, investors and servicers for the debt management and, if needed, resolution and enforcement. In the current macro-economic environment, it is imperative that the market mechanisms for NPL sales and securitisation not weaken, and that the authorities continue to monitor and take steps to maintain a robust secondary market for NPLs. Furthermore, the role of servicers continues to be critical. While master servicers are under the supervisory purview of the BdI, their activities are often outsourced to special servicers that operate outside the regulatory perimeter. BdI has tightened its supervisory monitoring of master servicers and issued guidance observing that market practice has drifted in some cases from the regulatory framework and reiterating acceptable practices to meet the regulatory objectives. Further strengthening of the supervisory oversight of the servicers is planned and would be important for effective NPL resolutions and from a broader financial stability perspective.

Improving the efficiency of the insolvency, debt restructuring and debt enforcement framework

Insolvency reform is a lengthy process: the reforms introduced since 2015-16, which culminated with the Insolvency Code in 2022, are only likely to yield results in the medium- to long- term. Despite progress made, substantial legal issues remain outstanding, and the insolvency and debt enforcement framework would remain a bottleneck if NPLs were to surge in the near future. Long durations of enforcement and insolvency procedures are a key challenge that should continue to receive the authorities' attention. To address the persistent long durations, further reforms to simplify and streamline court procedures are necessary. The information systems to track and monitor court proceedings are not apt to monitor their efficiency as the Italian court system does not collect granular information.

The Insolvency Code has made Early Warning Systems (EWS) one of the main pillars of the new system, with an obligation on certain stakeholders to issue an early warning by notifying the debtor of financial difficulties. However, upon receipt of the notification, there is no specific obligation on the debtor to act; this means little formal connection exists between the EWS and debt restructuring procedures, unlike in some other jurisdictions. While indications suggest that

the EWS could be having a positive effect, a stronger connection between the EWS and the restructuring system could be considered.

In Italy, as in other countries, judicial and hybrid restructuring proceedings are costly and there is evidence that firms filing for restructuring are larger than average firms. The Insolvency Code introduced a new out-of-court procedure that features an inexpensive and efficient process, which will encourage small and medium enterprise (SME) restructurings. This is a welcomed development. However, the out-of-court procedure also presents complexities that may prevent SMEs from taking full advantage. Adequate data should be collected to monitor the use and outcomes of the out-of-court restructuring process and assess whether improvements are needed.

The system of insolvency, restructuring and enforcement is complex and could merit some simplification, although its recently completed reform makes it inadvisable to introduce drastic changes at this time. The focus now should be on monitoring the system closely and on ensuring that it meets its intended objectives, including by providing sufficient human resources and adequate training of the experts involved. Once the mechanisms implemented by the 2022 reforms have been well-established, the authorities could explore introducing some degree of simplification.

Recommendations

In response to the aforementioned findings and issues, the peer review has identified the following recommendations to the Italian authorities:

1. The authorities should continue monitoring and fostering the secondary market for NPLs, including by resisting measures that would undermine past success; and BdI should continue to strengthen its supervision of relevant supervised entities, including servicers.

2. To address the persistent long durations of enforcement procedures, the authorities should: (i) increase courts' resources and staff, especially in those courts facing the most severe backlogs, (ii) strengthen court specialisation in commercial matters, and where possible, in insolvency and enforcement matters specifically, and (iii) finalise the ongoing digitalisation of the court system, which will involve the introduction of an e-tracking system that would allow monitoring of courts' performance and setting adequate incentives.

3. The authorities should monitor the system of insolvency, restructuring and enforcement closely and ensure that it meets its intended objectives, including by: providing sufficient human resources and adequate training of the experts involved; and collecting adequate data to monitor the use and outcomes across processes. Once the mechanisms implemented by the 2022 reforms have been well-established, the authorities should evaluate the system and explore further reforms such as (i) improving the possibility for out-of-court 'pre-negotiated plans' to be swiftly confirmed by the court; and (ii) strengthening simplified insolvency proceedings for reorganisation and liquidation of SMEs. The authorities should also monitor the existing EWS and assess its effectiveness to explore the need for further reforms including establishing a stronger connection between EWS and the debt restructuring.

1. Introduction

The first FSB peer review for Italy was completed in 2011,[3] and examined the steps taken or planned by the Italian authorities in response to the 2005-06 IMF FSAP recommendations on financial regulation and supervision as well as on institutional and market infrastructure. The review concluded that the Italian authorities had made good progress in addressing FSAP recommendations, but there was scope for additional steps in some areas covered by those recommendations.

Italy subsequently underwent FSAP Updates in 2013 and 2020.[4] The 2020 FSAP Update concluded that recent prudential measures have played a key role in bolstering the financial system. Nonetheless, it found that the banking sector was still vulnerable as solvency stress tests indicated that banks still faced important challenges and noted that the authorities should adopt measures to further improve banks' capital levels and operational efficiency. The FSAP report noted that banks had made remarkable progress in reducing NPL ratios, but more effort was needed. It also recommended that authorities should consider using prudential policies to moderate the sovereign-bank nexus, with gradual phasing-in to minimise potential disruptions to markets. Finally, it noted that reinforcing the bank crisis management framework is a priority.

The IMF's 2023 Article IV consultation[5] noted that the Italian economy grew robustly in 2022 despite surging energy prices on the post-pandemic recovery and fiscal stimulus. Bank credit had begun to decline although loan quality continued to hold up. The report suggested that supervision and policies should be attuned to risks arising from tighter financial conditions, including adequacy of banks' funding plans, size of capital and liquidity buffers, quality of commercial real estate exposures, implications of heightened funding competition between banks and the government, and consequences for weaker banks of a future narrowing of net interest margins.

Implementation of the core G20 financial regulatory reforms in Italy is progressing well. Annex 1 provides an overview of Italy's implementation status of G20 financial reforms as of September 2023, including the steps taken to date and actions planned by the authorities in core reform areas not covered in this peer review where implementation has not yet been completed.

This peer review assesses Italy's recent experience in reducing NPLs in the Italian banking sector, focusing on the following areas:

- accounting, regulatory and supervisory measures put in place to support the management of NPLs on banks' balance sheets;
- measures to facilitate a robust secondary market for the removal of NPLs from bank balances sheets, notably the GACS mechanism; and

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3 See FSB (2011), *Peer Review of Italy*, February.

4 See IMF (2013), Italy: Financial System Stability Assessment, *IMF Country Report No. 13/300*, September and IMF(2020) Italy: Financial System Stability Assessment, *IMF Country Report No. 20/81*, March.

5 See IMF (2023), Italy: 2023 Article IV Consultation, *IMF Country Report No. 23/273*.

- measures to improve the efficiency of the legal framework for enforcement, debt restructuring and insolvency.

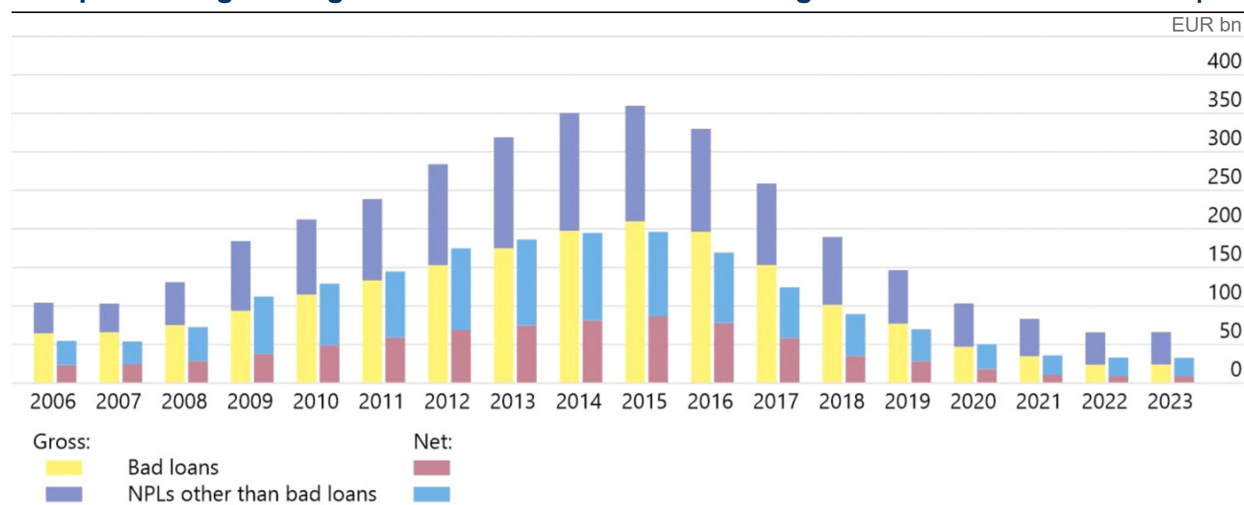
Annex 2 provides an overview table of the reforms and procedures in the Italian enforcement, insolvency and restructuring framework and Annex 3 lists relevant EU and Italian regulatory and supervisory measures.

2. Steps taken and actions planned

Banks dominate the Italian financial system with assets of €3,230 billion (at end June 2023), approximately 80% of which are on the balance sheets of Significant Institutions (SIs). There are 12 SIs in Italy, supervised by the Single Supervisory Mechanism (SSM),[6] and 118 Less Significant Institutions (LSIs). Recent acquisition activity resulted in the addition of one SI and removal of nine LSIs. Capitalisation remains stable with the level of capitalisation of Italian SIs at end June 2023 on average 20 basis points higher than peers in the SSM.

Italy has achieved significant success in reducing NPLs on bank balance sheets from the peak in 2015. Between 2008 and 2014 Italy experienced a deep and prolonged double-dip recession that drove a surge in gross NPLs to €360 billion in 2015, with the gross NPL rate at 16.5% of total loans and the net NPL rate at around 10% of total loans (see Graph 1).[7]

Non-performing loans gross and net: total Italian banking sector **Graph 1**



Source: BdI, based on supervisory reports

This stock level remained persistently high due to the slow pace of debt collection procedures, lengthy procedures in civil justice, and lack of depth in the secondary market for NPL disposals. Whilst more favourable economic conditions have led to lower default rates, the combination of new regulatory requirements; increased supervisory intensity; the deliberate development of the secondary market for NPLs and reforms to the judicial system have also had a significant impact on the NPL reduction over the past years. As at end-June 2023, the stock of NPLs has reduced

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[6] The SSM refers to the system of banking supervision in Europe. It comprises the ECB and the national supervisory authorities of the participating countries.

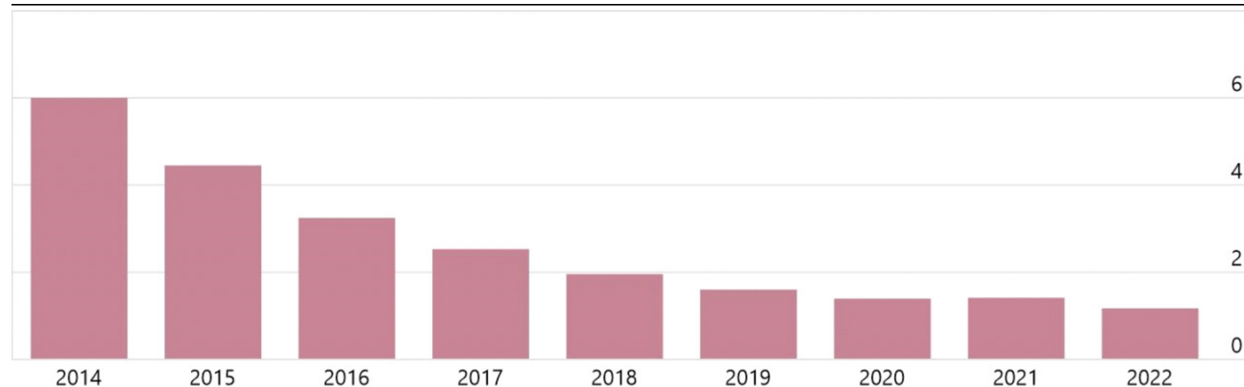
[7] Net amount means the gross amount net of provisions. Total loans include exposures toward central banks, general government, credit institutions, other financial corporations, nonfinancial corporations and households. See *Italian economy in brief*.

materially to €63.4 billion gross (€31.8 billion net), with the gross NPL ratio falling to 2.8% and the net NPL ratio at 1.4% of total loans.

The flow of new NPLs has steadily decreased from the peak in 2014 of 6% of total loans (see Graph 2). Over the period of 2016 to 2023 losses arising from NPL disposals, write-offs and provisions absorbed a large portion of operating profits, impacting Return on Equity (RoE) (see Graph 3).

Default rate

New NPLs as a percentage of total loans — **Graph 2**



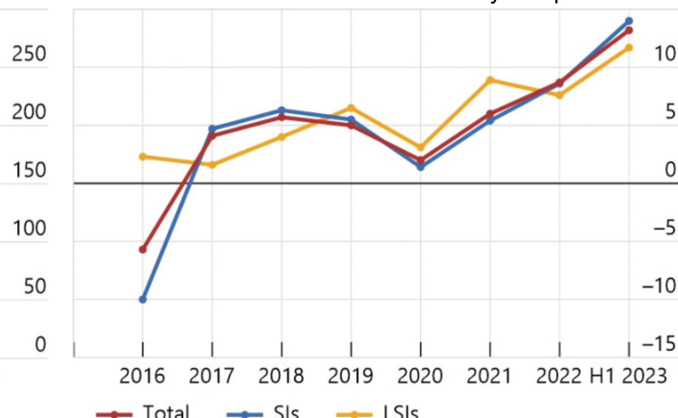
Sources: BdI based on Central Credit Register and supervisory reports.

Evolution of profitability of Italian banks[1]

In per cent — **Graph 3**

Loan loss provisions over operating profits

RoE of Italian banks net of extraordinary components[2]



[1] The perimeter of SIs and LSIs differs between the dates in the figure. The classification of banks (SI or LSI) refers to the situation as of the end-year of the corresponding year. [2] As a ratio to average equity in the year; percentage points.

Source: BdI based on supervisory data

Close cooperation between domestic authorities, open communication with private sector and a collective responsiveness to issues have been critical. The deliberate development of the secondary market with increased expertise and capacity within the financial sector to deal with NPLs, progress on debt workout mechanisms, regulatory requirements and increased supervisory intensity of both banks and master servicers have all worked together to contribute

to the NPL reductions. Table 1 below breaks down the flows for High-NPL SIs to give an overview of the methods used.[8]

Table 1: Drivers of NPLs evolution–Annual results for High-NPL SIs (€ million)

	2022	2021	2020	2019	2018	2017
Opening balance of NPLs	54,855	70,517	100,861	136,747	188,471	222,216
Inflows	12,048	12,923	13,313	16,278	17,928	17,704
Back to bonis[1]	-3,484	-3,901	-3,033	-5,785	-7,778	-7,495
Collections	-5,538	-7,233	-7,219	-10,302	-12,137	-12,513
Collateral liquidation	-1,056	-737	-995	-1,825	-2,798	-3,314
Foreclosure	-81	-244	-382	-802	-982	-675
Disposals and risk transfers	-12,374	-6,914	-22,39	-21,555	-31,025	-12,216
Write-offs	-3,581	-5,100	-6,731	-9,209	-9,046	-10,495
Classification as held for sale	-3,101	-8,074	-8,476	-1,691	-8,045	-23,763
Net Flows due to other reasons	2,992	4,166	5,600	3,407	2,386	4,788
Closing Balance of NPLs	40,679	55,402	70,548	105,262	136,974	174,237

[1] NPLs returning to the performing state. Sources: Italian authorities, based on supervisory data. The universe of SIs has changed through time due to mergers and acquisitions.

2.1. Managing NPLs on banks' balance sheets: accounting, regulatory and supervisory measures to reduce NPLs

In 2015, BdI adopted definitions of NPLs harmonised with the EBA standards published in 2013. BdI, for reporting purposes, divides NPLs into three sub-categories (see Box 1).

Box 1: Classifications of NPLs

Bad loans are exposures to debtors that are insolvent or in substantially similar circumstances. The recovery strategies usually follow a gone-concern approach, involving the liquidation of collateral assets and the enforcement of guarantees.

Unlikely-to-pay are exposures to which banks believe that debtors are unlikely to meet their contractual obligations in full, unless action is taken. The recovery strategy may follow a going-concern approach or a gone-concern approach depending on the probability of success and the limitation of losses. This is a subjective assessment.

Overdrawn and/or past-due are exposures that are overdrawn and/or past-due by more than 90 days and for above a predefined amount. The non-performing status is considered temporary. This is an objective assessment.

[8] The definition of a High NPL institution has evolved over time, with a combination of assessment of the NPL to gross loans ratio relative to peers and qualitative supervisory judgement and most recently it has converged on a ratio of NPLs of 5% or more of gross loans.

2.1.1. *Accounting measures to reduce NPLs*

Write-offs are a key avenue of dealing with NPLs on banks' balance sheets. When credit institutions have no reasonable expectation of recovering an exposure, such determination should lead to a partial or full write-off of the exposure.[9] Write-offs perform a critical role in NPL resolution, as they prevent a potential accumulation of uncollectible NPLs on banks' balance sheets. When write-offs are not implemented in a timely manner, financial institutions may carry the full amount of uncollectible loans in their balance sheet, hoping that the economic conditions will improve and that the collateral may appreciate, thereby elevating the NPL volumes in the system.

In Italy, write-offs have been a key contributing factor to the reduction of NPLs. Loan write-offs were the third most utilised NPL resolution avenue during the period 2017-2022, amounting to 14.5% of total NPL gross reductions in SIs (see Table 2). In absolute terms, High-NPL banks wrote off €44.1 billion of NPLs during the period, i.e. a write-off rate of 6.1%. This rate is aligned with the averages observed in other SSM jurisdictions, which also recorded a rate between 6% and 8% during the same period. No specific data is available on the vintage of written-off loans but following the observed vintages of closed bad loans (as write-offs are usually related to bad loans closure), it can be assumed that in the majority of cases these loans were older than five years and, therefore, originated as a direct result of the Global Financial Crisis (GFC).

Table 2: Write-offs in High-NPL SIs since 2017

	Total NPLs (million €)	Total Outflows (million €)	Outflows due to Write-offs (million €)	Write-off rate
2022	54,855	-29,215	-3,581	-6.5%
2021	70,517	-32,203	-5,100	-7.2%
2020	100,861	-49,226	-6,731	-6.7%
2019	136,747	-51,169	-9,209	-6.7%
2018	188,471	-71,811	-9,046	-4.8%
2017	222,216	-70,471	-10,495	-4.7%

Sources: Italian authorities, based on supervisory data.

Loan write-offs increased after 2018, partially as a result of the adoption of IFRS 9. Before 2018, banks had heterogeneous practices for write-off, due to the absence of a specific definition under IAS 39. The introduction of IFRS 9 and the 'no reasonable expectation of recovery' standard contributed to a higher harmonisation of bank policies. As a result, the write-off rate increased from 4.7% in 2017 to 6.7% in 2019 in High-NPL SIs, a 40% increase (see Table 2 above). Write-off levels have been maintained by SIs in the following years, suggesting a more proactive approach to irrecoverable loans by banks. While the introduction of the new accounting standard made it clear that financial institutions have the obligation to accept write-offs at a certain point, the point when those must take place remains a matter of interpretation: if the bank has even a minimum expectation to recover the exposure, it would apply impairment provisions while in case

[9] See IFRS 9.B3.2.16.r.

of a higher degree of certainty that the exposure will not be recovered, the bank is expected to write the exposure off.[10]

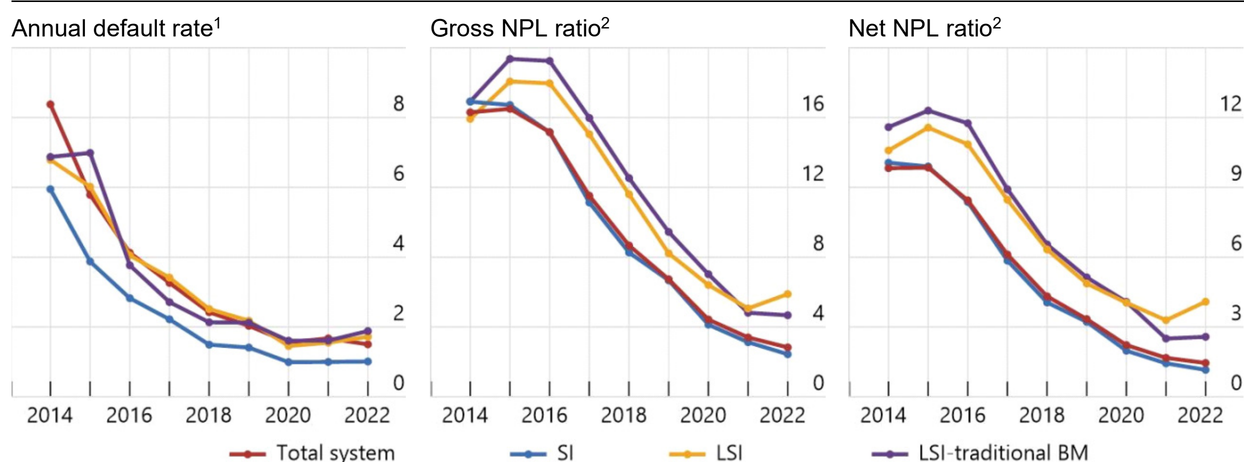
2.1.2. *Regulatory measures to reduce NPLs in the banking sector*

In response to the issue of persistent high NPLs across Europe, a European Council Action Plan was developed. The ECB issued its guidance on NPLs, addressed to SIs, in March 2017, complemented by an addendum issued in March 2018 covering supervisory expectations for the provisioning of NPLs not under the Pillar 1 backstop. As part of the Council Action Plan, the EBA and ECB released a series of guidelines on loan origination, provisioning, capital requirements, disclosure and management of NPLs, with some differences in applicability between SIs and LSIs (see Appendix 3). The Italian authorities promptly implemented these guidelines and directives and, in some cases, extended the guidelines to LSIs earlier than required by the EBA and ECB.

The difficulty of access for LSIs to the securitisation market and the smaller economies of scale in the internal workout capacity of LSIs together result in a higher NPL ratio for LSIs (see Graph 4). BdI has maintained high supervisory intensity across both SIs and LSIs.

Default rate and Gross and net NPL ratio by lender type

In per cent **Graph 4**



[1] Annualised quarterly flows of adjusted NPLs in relation to the stock of loans at the end of the previous quarter net of adjusted NPLs. [2] Gross/Net NPLs as a percentage of total loans.

Sources: BdI based on Central Credit Register and supervisory reports.

Regulatory guidelines for management and supervision

In January 2018 BdI issued a set of guidelines for LSIs aligned with the ECB Guidance to SIs on NPLs issued in 2017. Similar to requirements for SIs, the guidance required LSIs with high levels of NPLs to develop operational plans with a three to five year time-horizon with reduction targets and clear actions. The guidance also provided best practices in terms of management strategies, governance arrangements and operational frameworks, conflict of interest management, forbearance practices, classification of NPL loans, write-off practices, assessment

[10] The IFRS standard states that financial institutions must accept write-offs 'timely' without providing further guidance.

of real-estate collateral and information systems. These guidelines were transposed to provide guidance to off-site supervisors and are the basis of horizontal assessments, which in turn generate further best practice identification.[11]

Between June 2018 and December 2022, the gross NPL stock of high-NPL LSIs fell from €15.1 billion to €5.5 billion. The average gross ratio decreased from 16.6% to 5.4%.

Capital measures

The Capital Requirements Regulation (CRR) Pillar 1 backstop, in the form of calendar provisioning, is applied to both SIs and LSIs for flows of NPLs, limited to loans originated after 26 April 2019. This compulsory minimum prudential coverage for non-performing exposures that increases over a set period of time incentivises disposals of NPLs firstly because the capital consumption increases regardless of recovery expectations and secondly the long duration of the recovery process through the Italian judicial system results in the high capital charge being held over a long period (see section 2.3). As at 30 June 2023, the aggregate Pillar 1 capital deduction resulting from the backstop is negligible, largely to due to loans being at most at Year 2 in the calendar.

For NPLs classified after 1 April 2018 and where the original loan has been granted before 26 April 2019 (stock of NPL), calendar provisioning only applies to SIs in the form of a Pillar 2 specific add-on. The 2020 IMF FSAP recommended that BdI consider extending this approach to LSIs given their high NPL levels; BdI is of the view that the combination of supervisory intensity relating to NPL management strategies, and the Pillar 2 add-ons discussed below negate the need to formally extend calendar provisioning in this way.

Pillar 2 requirements and guidance have been used to increase capital. For LSIs the Supervisory Review and Evaluation Process methodology defines a specific supervisory proxy to calculate a Pillar 2 requirement and Pillar 2 guidance add-on to cover the risk of under-provisioning in normal and stressed conditions respectively, taking into account the severity and vintage of the non-performing status, the IFRS staging for the performing portfolio and the status of secured/unsecured loans. According to the BdI, the application of supervisory Pillar 2 capital add-ons has incentivised LSIs to strengthen capital in the absence of calendar provisioning for the stock of NPLs.

Data collection

BdI introduced reporting requirements that led to improved NPL management at banks and supported the development of the secondary market for NPLs. In 2016 BdI introduced specific granular statistical reporting on bad loans greater than €100,000 for both SIs and LSIs. A key objective was to drive the development of substantive management information databases on these exposures. At that time the secondary market was facing difficulties regarding the supply by banks of prompt, adequate and reliable information on bad loans. This lack of available information resulted in higher risk premiums and therefore significant discounts on the sale price of bad loans. The reporting requirements were designed to address investors' needs when

[11] See Banca d'Italia Circular 269.

assessing NPL transactions. This achieved the dual purpose of better informing management and supervisors as well as improving the banks' ability to rapidly share more complete and relevant information with investors, which expedited due diligence. BdI is of the view that this significantly supported the development of the secondary market.

Supervisory measures

Supervisory oversight of the correct classification of NPLs into bad loans, UTP and overdrawn/past due is important as there are capital, balance sheet and profit and loss implications of the classification.

A regular supervisory exercise is to conduct quantitative assessments to evaluate the credit risk profile of a bank. These assess a representative sample of the bank's credit portfolio to confirm the bank's classifications and valuations are in line with applicable requirements. Supervisory discussions on non-compliance can result in a revised classification and provision adjustment.

Horizontal analyses and bank-specific deep dives have supported best practice identification, particularly in the classification of UTP. National guidelines complementing EBA guidelines define triggers for UTP, but these are qualitative with room for interpretation. The guidelines suggest different sets of UTP triggers depending on the portfolio with some triggers considered 'hard' with little room for interpretation and others as 'soft' with some room. To support industry application of these guidelines, in 2022 BdI completed a horizontal analysis, which led to publication of best practices.[12] This supervisory focus on UTP classification and management is of merit, as following successful disposals of bad loans, UTP at December 2022 is 64% of net NPLs (€21 billion).

2.2. Removing NPLs from banks' balance sheets: development of a secondary market for NPLs

2.2.1. Guarantee on Securitisation of Bank bad loans (GACS)

Design of the GACS

The GACS has been the primary mechanism for NPL reduction in Italy. Introduced by the Italian Ministry of Economy and Finance in 2016,[13] it provided a state guarantee scheme to assist Italian banks in disposing of bad loans from their balance sheets by way of securitisation. GACS started in 2016 with an initial duration of 18 months but was then amended and extended several times until its final closure in June 2022.[14]

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[12] See Banca d'Italia 2022: Financial Stability and Supervisory Notes no28 - Survey on the management of Unlikely-to-Pay Loans (March)

[13] Law Decree No 18 of 14 February 2016 (the "2016 Decree"), subsequently amended vide Law No 49 of 8 April 2016

[14] The 2016 Decree provided for an initial duration of 18 months for GACS, with the possibility for an extension of a further 18 months, subject to approval by the European Commission. GACS was renewed for the first time with MEF Decree of 21 November 2017, until 6 September 2018, and subsequently for a further six months until 6 March 2019. The Law Decree 25 March 2019 No 22 renewed GACS for a further period of 24 months. In July 2021 GACS was extended until 14 June 2022.

The scheme envisaged that an individually managed private securitisation vehicle buy bad loans from the originating bank, pool them, and fund the purchases by selling notes with different risk levels to investors. The lower-risk senior notes benefited from a state guarantee, while the risk-bearing junior and mezzanine notes are sold to investors without any such guarantee. In the event of non-payment of any guaranteed amount, the guarantee may be invoked by the senior note holders. The guarantee's objective was to increase and improve the level of disclosure, reduce the bid-ask price spread between originators (selling banks) and investors and increase the number and the volume of NPL transactions.

The design features of GACS reflected a balance resulting from a coordinated approach between the public and private sector. It entailed an unconditional, irrevocable and first-demand guarantee for senior noteholders under a securitisation structure. This created investor demand in an otherwise subdued securitisation market. To address the risks of moral hazard involved due to the state guarantee, several features were incorporated in the design including:

- Narrow eligibility of underlying assets and participating institutions. The only eligible loans are those classified as bad loans, for which no workout is possible other than the sale of collateral. UTP classified loans are not eligible.
- The loan receivables can be transferred to a Special Purpose Vehicle (SPV) for an amount not higher than their net book value (NPV).
- Payment to the State of market-linked guarantee fee by the securitisation vehicle (calculated on the basis of a basket of CDS prices of Italian-based companies).
- The guarantee is issued only once the senior notes are rated with a rating of BBB or above by an independent rating agency.
- A third-party servicer must be appointed, different from and not belonging to the same group of the originator.
- A monitoring mechanism for the performance of the servicers. The 2019 amendments further strengthened some of the features relating to the servicers, including making the payments to servicers conditional on performance targets, and explicit performance-based binding conditions for replacement of servicers.

Removal of NPLs from banks' balance sheets

GACS has accounted for the largest reduction in NPLs in banks' balance sheets between 2017 and 2022. During this period, about 53% of bad loans were sold through 46 GACS-backed securitisation transactions. The underlying loans of these transactions had an aggregate gross book value (GBV) of €117.8 billion, and a NBV of €28.2 billion.[15] The nominal value of the notes issued under these transactions was €26.5 billion, of which €21.6 billion were senior notes covered by the state guarantee.

[15] Equal to GBV minus the provisioning level.

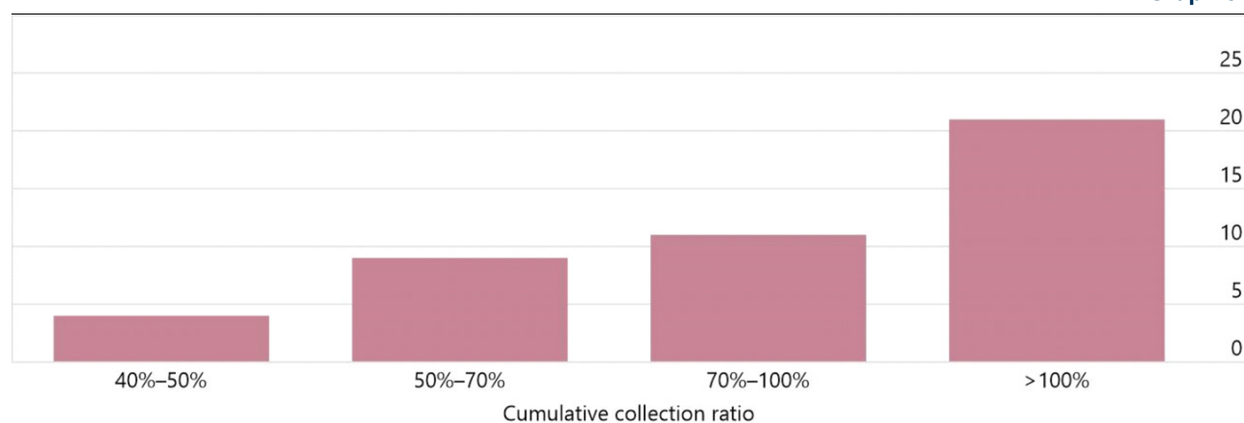
SME NPL loan disposal was an important component of GACS backed securitisations from 2017. SMEs account for 63% of Italian value-added and 76% of employment.[16] Correspondingly, SMEs account for 47% of Italian bank loans and 63% of NPLs, which is consistent with SMEs being riskier, on average, than large firms. The current default rate of SMEs is 1.7% compared to larger corporations at 1.5%. In 2017 and 2018 three large securitisations contained a substantial proportion of SME loans.[17]

Workout of disposed NPLs

While disposal with support of the GACS removes the NPLs from the banks' balance sheets, the performance so far of the NPL workouts for the GACS-supported NPL disposals has been mixed and the use of the guarantee cannot yet be fully excluded. As Graph 5 below shows, as of July 2023 the gross cumulative collections have been higher than the collections estimated by the initial Business Plan in 21 transactions covered under GACS (i.e., the Cumulative Collection Ratio was more than 100 percent).[18] For the remaining transactions with actual collections lower than expected in the original recovery plan, the average collections were 33% lower than those predicted. The authorities attribute the slowdown in the recovery process to the consequences of the pandemic, the temporary shutdown of the courts, and the interruptions in property auctions.

Cumulative collection ratio analysis, July 2023

Number of GACS **Graph 5**



Source: Italian authorities.

Almost all transactions continue to have an adequate degree of coverage for senior tranches relative to the expected future inflows included in the updated recovery plans. The redemptions made so far on senior tranches have reduced the State's exposure by more than 46%, from €21.6 billion at inception to €11.1 billion as of June 2023. To date no calls regarding the Government's guarantee on senior notes have occurred, and for one securitisation the senior notes have been repaid in full. The potential risk for the State in enforcing the guarantee (for a

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16 Data as at 2022. See the European Commission's SME Performance Review 2022/2023 - Italy country sheet

17 SME loans represented 54% and 71% in two of the transactions, and in the third transaction 48% of total GBV is accounted for by exposures below €1 million.

18 The analysis is based on 45 GACS operations (the overall portfolio included 46 operations), for a guaranteed senior notes residual nominal value equal to €11 billion as of July 2023.

limited number of securitisations) is expected to be covered by the GACS endowment, with no need for additional state funding.[19]

2.2.2. Development of the market ecosystem

In addition to reducing NPLs on banks' balance sheets, the GACS has led to the development of a secondary market for NPLs**.** The market activity created by the GACS program developed a market ecosystem which may be beneficial for un-guaranteed securitisations and NPL disposals in the future. The market ecosystem created by the GACS program has been facilitated by several complementary reforms and initiatives:

- granular data collection on bad loans introduced by BdI (see section 2.1.2), which reduced informational asymmetries between banks and investors across the NPL market;
- legislative changes that have rationalised the securitisation regulations; and
- appropriate supervisory controls of the servicers by the competent supervisor.

Key amendments to the securitisation law included allowing SPVs to extend asset-backed securities to all the NPL categories; allowing SPVs to grant new loans to debtors with the objective of improving their current non-performing status; and permitting SPVs to purchase equity or quasi-equity instruments issued by the assignor. Amendments to the law have also permitted Italian and EU Alternative Investment Funds to directly lend to Italian borrowers and to purchase bank debt without the need for a securitisation structure subject to specified procedures.

The servicing industry has emerged as a key facilitator for the development of a broader market. The servicing activities in securitisation transactions are governed by Law 130/1999, which requires that such transactions must be managed by authorised servicers ("master servicers"). Servicers collect the receivables of the transferred loans, provide cash and payment services, and ensure compliance of the transaction with the law and the information contained in the prospectus. Only banks and financial institutions enrolled in BdI's Single Register are allowed to act as servicers. However, servicers may delegate to other entities ("special servicers") the collection and recovery activities.[20] Special servicing activities can be undertaken by a wider set of entities, including outside the regulatory perimeter of BdI. The market of servicers operating in the NPL sector is strongly concentrated, with about 95% of NPL securitisations (with and without GACS) managed by seven servicers – one bank and six non-bank financial intermediaries.

In view of the critical role of servicers, BdI has intensified its supervisory focus towards master servicers. BdI communicated in 2021 to servicers to highlight the sector's risks and formulate

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[19] GACS was also supported by a special Fund set up at the Ministry of Finance, with an initial endowment of €120 million, further incremented by €100 million in 2019.

[20] Details of the entities operating in the financial system, maintained by the Banca d'Italia since 2016 pursuant to amendments to the Consolidated Law on Banking. See Supervisory registers and lists

recommendations on the appropriate controls to be adopted in the servicing industry.[21] Monitoring the performance of NPLs securitisation (i.e. recovery rates vs original business plan) with or without GACS, including the performance of the servicers, was one of the main supervisory priorities of BdI in 2022. Servicers supervision will be fostered also through the implementation of Directive (EU) 2021/2167.[22]

The market has also seen the emergence of private platforms with the objective of purchasing the mezzanine and junior tranches of NPL securitisation transactions, as well as partnerships among banks, servicers and asset management companies. The secondary market was also aided by loan aggregation through multi-originator platforms, which could be particularly helpful for smaller banks for which standalone securitisations of NPLs is difficult.

2.2.3. Secondary market in NPL disposals without benefit of GACS.

Alongside the securitisation transactions with GACS, the volume of securitisations without the benefit of a GACS guarantee and non-securitised disposals has remained steady, aided in large part by the evolving market ecosystem.

From 2017-2022, non-GACS disposals averaged 61% of total disposals. The non-GACS market segment constitutes the following:

- assignment of NPLs classified as bad loans or UTP by originators to specialised entities, including banks;
- originator-led securitisation outside GACS, including through multi-originator platforms; and
- disposal or securitisation of UTP that may need refinancing after acquisition.

The initial NPL disposals without the benefit of GACS were largely concentrated in the bad loan segment. UTP disposals have materially increased since 2018, and in 2022 they represented 50% of the NPL disposals (see Graph 6). Multi-originator platforms and partnerships with banks, servicers and asset management companies are growing as a mechanism to manage UTPs.

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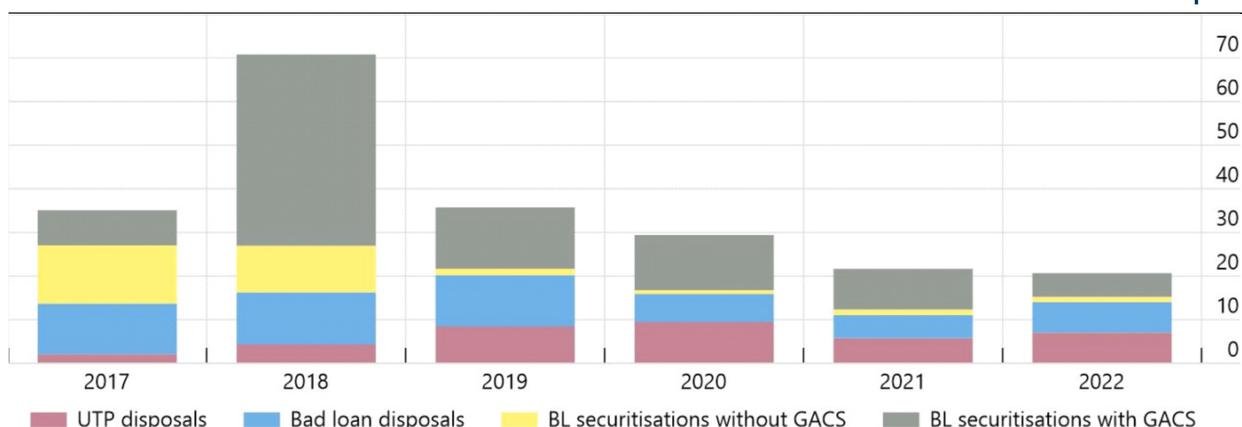
[21] See BdI (2021), *Servicers in securitisation transactions. Risk profiles and supervisory guidelines*, November

[22] In terms of the Directive, credit institutions must periodically provide prospective information, such as credit purchasers' details and aggregate outstanding balance of the transferred credit portfolios, to their national authorities. Credit purchasers transferring a creditor's rights must also give the relevant authorities details of the new purchaser and information such as the aggregate outstanding balance.

NPL disposals by classification

In EUR bn **Graph 6**



Source: Italian authorities.

Given the specific features of UTP loans, the system capacity to undertake deep restructuring of borrower accounts on a going concern basis is limited. UTP loans have different features from bad loans and require specific skills for the proper management of corporate restructuring. The UTPs sold have been highly heterogeneous with single name transactions representing more than 30% of UTP sales. Transactions for high value portfolios were carried out by a limited number of banks and often sold to companies specialised in the management of UTP. Banks are also entering into partnership agreements with external servicers or with funds specialised in the turnaround.

The reforms of in-court and out-of-court restructuring and insolvency procedures generated an improvement to the framework for the workout of UTP loans. While the full effects of the reforms in this area remain to be seen, the procedural enhancements provide tools to debtors and creditors to restructure these loans, irrespective of final ownership of the debt (see section 2.3). These tools may directly or indirectly improve the performance of the portfolios. The management of UTPs by specialised market operators might foster restructuring activity in particular in relation to specific loan segments, such as loans to SMEs.

2.3. Resolving NPLs: enforcement, restructuring and insolvency framework

2.3.1. Credit information

Efficient financial information systems ensure that transparent credit information is available to lenders and other creditors to provide early warning signals before there is a default in debt servicing. This allows early action to be taken.

Different sources are available in Italy to creditors seeking information about the financial situation of debtor corporations. Banks receive monthly information from the Italian Central Credit Register (CCR), managed by BdI, concerning the global risk position of their clients. The services of CCR, which include borrower-specific aggregated data across all lenders, are free of charge for participating creditors. Banks and other financial intermediaries are obliged to periodically transmit to the CCR data referring to the credit risk positions of their clients. Private credit information providers in Italy offer several services including scoring and rating for a fee.

By accessing credit reporting systems, creditors receive information about the debtor's credit quality, the initiation of insolvency proceedings of corporations and the dispute of credit in civil proceedings.

These creditor information systems can be a critical tool to address financial distress at an early stage, thereby preventing an NPL surge. Although they have traditionally been designed to alert creditors and public authorities, the EU Restructuring Directive has shifted their focus to the debtor, so that the latter can be alerted of the existence of financial difficulties and address them in a timely manner. Within this broad definition, EWS have taken many different forms across EU Member States, ranging from purely internal control systems that rely on corporate bodies to external control systems that rely on third parties. (See more detail in Section 2.3.4).

2.3.2. Judicial Enforcement

Lengthy proceedings have been a chronic feature of Italy's enforcement system. As of 2021, the average time for real estate related judicial enforcement was five years, while judicial liquidations took on average longer than seven years.[23] Several factors explain these delays, including an overly formalistic legal framework and, especially, challenges faced by the court system, which lacks adequate resources and faces a significant backlog. The duration of proceedings varies significantly depending on the competent court and region and on the economic and social environment, with real estate foreclosures taking less than four years in some regions and more than seven in others.[24]

Long delays have had a direct impact on banks' NPL resolution strategies. Facing long procedures and uncertain outcomes, banks have shown limited reliance on enforcement procedures: only 4.6% of the gross NPL reduction achieved by SIs since 2017 was attributed to resolution through enforcement (€13.8 billion).[25] Instead, banks have preferred to follow a disposal strategy that outsources collection of bad loans to servicers and investors, who must rely on the same enforcement system as the bank, and therefore, face similar durations.

The focus on resolving NPLs highlighted the excessive duration of enforcement procedures. A wide array of measures was introduced in 2015-16 with the aim of shortening the length and improving the efficiency of credit recovery proceedings for secured and unsecured debt. Among other effects, the reforms shortened the procedural deadline of the pre-sale stage of foreclosure and allowed reductions of up to 50% off the value of assets in real estate auctions to encourage asset sales. Complemented by additional reforms introduced in 2017,[26] the reforms were successful in achieving a reduction in the duration of proceedings, as shown by the percentage of proceedings closed within three years from their start, which almost doubled. More specifically, these improvements were achieved by reductions in the duration of the pre-sale and

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[23] Ministry of Justice data (2023).

[24] See IMF (2020), Italy: Financial System Stability Assessment - Technical Note - Tackling Non-Performing Assets, *IMF Country Report No. 20/234*, August.

[25] Banca d'Italia (2023).

[26] Supreme Judiciary Council Guidelines (2017), which introduced best practices for the foreclosure process.

sale phases.[27] Despite these improvements, data from the Ministry of Justice reveal an increase in the average duration of proceedings reported as closed, which increased from 1,364 days in 2014 to 1,886 in 2021 (see Table 3). This increase was driven by the closing of a significant number of older proceedings, as courts have tried to reduce the backlog. Data on new proceedings point to a reduction of their duration.[28]

Table 3: Duration of real estate foreclosure proceedings

Year	Number of closed proceedings	Average duration (days) for the proceedings closed in the year
2014	64,586	1,364
2015	67,392	1,557
2016	67,827	1,652
2017	75,187	1,705
2018	85,444	1,764
2019	87,799	1,826
2020	65,654	1,928
2021	66,170	1,886

Source: Ministry of Justice data (2023).

The information systems to track and monitor court proceedings are not conducive to the adequate monitoring of efficiency. The Italian court system does not collect granular information on the cost and efficiency of judicial enforcement procedures. In addition, there are no detailed statistics that provide a breakdown of data based on the nature of the claim (secured or unsecured). It is only possible to provide information based on the nature of the assets seized to satisfy the claim (real estate or movable property).

The 2016 reform also introduced a new procedure, the "*patto marciano*". This procedure allows for out-of-court enforcement of commercial loans secured by collateral, enabling the creditor to adjudicate the secured asset in payment of the debt. This represents a novel approach to enforcement that has only rarely been adopted in civil law countries, although it is entirely aligned with a 2018 proposal of the European Commission.[29] One of the limitations of this procedure is that it is only applicable upon the parties' express agreement at loan origination and therefore cannot be used by creditors when addressing the pre-2016 NPL stock. Although on paper this new procedure could allow creditors to avoid lengthy court procedures for loans originated after 2016, it has had virtually no impact in practice. This is due to several factors, including the alleged

[27] See BdI (2019), Notes on Financial Stability and Supervision - Real estate foreclosures: the effects of the 2015-16 reforms on the length of the proceedings, September. The note showed that that the pre-sale phase duration was significantly shortened as a result of the 2015-16 reforms, with the share of proceedings concluding within 12 months increasing from 16% for procedures initiated before 2015, to 30% for procedures initiated after 2015 and 37%, for procedures initiated after 2017. The average duration of the pre-sale phase was also reduced from 23 to 17 months for procedures started after the 2015 reform.

[28] *ibid*.

[29] See the 2018 Proposal of a EU Directive on Accelerated Extrajudicial Collateral Enforcement (AECE).

reputational concerns raised by banks when relying on it, as well as some legal difficulties experienced by investors in its application.[30]

2.3.3. Debt Restructurings and out of court workout

Restructurings have played only a limited role in the resolution of NPLs. Since 2016, Italian SIs reclassified €31 billion of gross NPLs to performing categories following a cure process, which represents 10% of the gross NPL reduction achieved during the period to 2022.[31] Data is not available on the type of procedure used to achieve these cures. Compared with the other NPL resolution avenues (disposals (52%), collections (18%) and write-offs (14%)) restructurings (i.e. return of exposures to bonis categories) have played a limited role in addressing the post-2016 NPL stock.

The relatively low relevance of restructuring is explained by multiple factors.[32] These include (i) long delays observed in formal restructuring procedures, which can take years when relying on court intervention; (ii) the prevalence of bad loans in the 2016 NPL stock, for which restructuring is not the most effective resolution avenue, and (iii) banks' internal capacity constraints, as restructuring activities are time- and resource-intensive and workout units present limitations in the volume of restructured debt that can be processed yearly.

The restructuring legal framework has been amended multiple times since 2005. The reform process culminated in 2022 with the enactment of the Insolvency Code. The result of multiple reforms is a complex system, with sometimes overlapping procedures that try to achieve the same outcome. These include:

- **Moratoria Agreements** (*convenzioni di moratoria*) are a type of debt restructuring mechanism that allow debtors to temporarily suspend their debt payments and are therefore theoretically useful for addressing temporary debtor cashflow issues. There is no data available to evaluate their effectiveness.

- **Certified recovery plans** (*piani attestati di risanamento*, 'PAR') are informal restructuring procedures that allow debtors to negotiate and implement a restructuring plan without any formal judicial control. The plan is certified by a qualified professional and must specify the restructuring measures that will be taken. PARs are flexible and give debtors a considerable degree of initiative, but they lack court confirmation and may be vulnerable to challenge in the future. There is no official data on their effectiveness.

- **Debt restructuring agreements** (*accordi di ristrutturazione dei debiti*, 'ARD') are a hybrid restructuring procedure. Although they allow the debtor to negotiate a plan with their creditors outside of court, they require court confirmation of the plan. ARDs offer

[30] Although the "*patto marciano*" is a purely extrajudicial procedure, the debtor still has the right to raise challenges and convert the procedure into a court-supervised one, undermining the procedure's main benefits.

[31] This is a proxy because the reclassified amount refers to the residual exposure which moves to back to bonis after a period of credit collection during non-performing classification, and is therefore not directly comparable with the original GBV of the exposure at the time of classification as NPL.

[32] Restructuring may also occur on positions which do not return to bonis but are fully recovered within the non-performing status.

debtors a greater level of flexibility to maximise the possibilities of creditors' approval.[33] The judicial phase is generally quick, and they can be implemented rapidly. However, ARDs require the involvement of several professionals for the certification of the plan and an ability to negotiate with creditors. Therefore they are typically used by larger firms. ARDs have not been widely used in Italy.

The Insolvency Code introduced a new out-of-court procedure, the "Composizione Negoziata" (CN). This out-of-court procedure is a negotiated workout system designed to help companies overcome temporary financial difficulties with limited or no court intervention. The CN is voluntary and entirely confidential. As certain stages take place electronically through an online platform, the CN features an inexpensive and efficient process, which should encourage SME restructurings. In Italy, as in other countries, judicial and hybrid restructuring proceedings are costly and there is evidence that firms filing for restructuring are a larger than average size.[34] The introduction of the CN is therefore a welcome development in this respect. However, the CN presents common features generally applicable to out-of-court procedures, including that it is binding only for those creditors participating to the agreement. Another common feature is that it also requires court intervention for the debtor to receive additional financing or stay creditors' enforcement actions, which could raise complexities for SMEs.

The CN consists of a series of steps to facilitate negotiations between debtors and creditors, rather than a procedure through which a specific kind of agreement is reached. Its essential features are that:

- the debtor is assisted by an independent expert who must assess the likelihood that the business can achieve a reorganisation and facilitate negotiations with creditors;
- during negotiations the debtor may apply to the court for the suspension of enforcement actions and for receiving fresh financing, which may receive priority status;
- the debtor continues to manage the firm, but any actions potentially conflicting with the restructuring options must be communicated to the expert;
- the outcome may be either that a formal reorganisation procedure is initiated,[35] or an informal agreement is concluded, which may provide tax reductions and protection from avoidance actions; and
- creditors have a duty to actively take part in the negotiations.

It is too early to assess the impact of the CN, although it has already led to successful restructurings. From November 2022 up to September 2023, the Chambers of Commerce received 951 applications, half of which remain in progress, while the other half have been closed, with 72 approved plans. Despite its early success, some participants have suggested

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[33] Among others, ARDs allow cramming down dissenting creditors, provide of the protection from avoidance actions; new finance is granted super seniority ranking and the court can grant a stay of individual actions.

[34] See BdI (2020), *Business continuity in times of distress: debt restructuring agreements and compositions with creditors in Italy*, July.

[35] If negotiations with creditors do not succeed, the debtor can enter into any formal reorganisation procedures, including a newly introduced restructuring procedure called simplified composition with creditors for the liquidation of the assets (*concordato semplificato per la liquidazione del patrimonio*), which is, however, a fully court-supervised procedure.

that the CN could be used by debtors to benefit from the stay and eventually further delay insolvency procedures. However, legal measures are in place to avoid any dilatory use of the CN. Specifically the independent expert is entitled to end the CN if it becomes apparent that a successful restructuring is not possible. While it might be premature to introduce amendments, a future reform could further simplify the process and explore more efficient interaction among this instrument and judicial procedures.

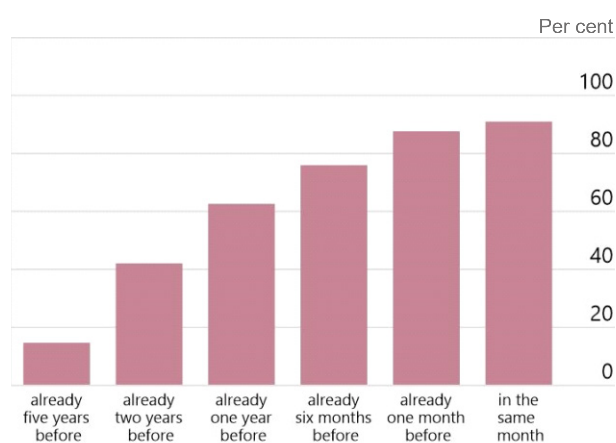
2.3.4. *Insolvency*

Early Warning Systems

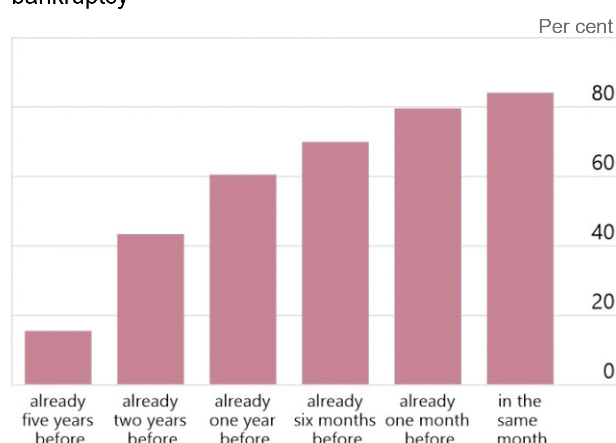
Late filings for insolvency have traditionally been a chronic problem in Italy**.** Debtors tend to postpone the recognition of financial distress and only resort to the insolvency system when it is too late. More than 90% of firms were already inactive by the time they accessed insolvency procedures (see Graph 7 below). This practice leads to a strong prevalence of liquidations, which are widespread when compared to restructurings, and to very low success rates of reorganisations. Aware of this challenge, the Rordorf commission recommended in 2016 that the focus of the reform of the 1942 Insolvency Law be on EWS, suggesting a similar procedure to that available in France.[36]

Inactivity and bad loans before bankruptcy **Graph 7**

Firms' inactivity before bankruptcy



Firms and loans classified as bad loans before bankruptcy



Sources: Banca d'Italia, *Centrale dei Rischi*; INPS; Infocamere (2023).

The Insolvency Code has made EWS one of the main pillars of the new system. The focus on preventive restructurings is clear and includes a range of tools that incentivise early action without relying on court intervention. The most relevant ones include the creation of a national online platform where the debtor can self-assess its financial situation, and the introduction of an obligation on certain stakeholders to issue an early warning by notifying the debtor of the existence of financial difficulties. This latter obligation is imposed on:

[36] The Rordorf commission was established in January 2015 to develop draft legislation to reform the existing Insolvency Act.

- the debtor company supervisory body, which must notify the firm's management as soon as it becomes aware of business difficulties, following which the directors have a short time limit to adopt remedies;
- qualified public creditors (e.g., Tax Agencies and Social Security Authority), which must notify the debtor's management in the event indebtedness exceeding certain thresholds has become more than 90 days past due; and
- banks and other financial institutions, which must notify the debtor's management upon their decision to withdraw, limit or cancel existing credit facilities granted to the borrower.

Upon receipt of the notification, there is no specific obligation on the debtor to act. This means that no formal connection exists between the EWS and debt restructuring procedures, besides the general duty to file for insolvency. This is in stark contrast with the approach adopted in the 2019 draft version of the Insolvency Code.[37] In this respect, it would have been useful if the EWS was expressly connected with restructuring tools, ideally of confidential nature, such as mediation or the out-of-court debt restructuring procedure (CN). Other countries in Europe have adopted an even more interventionist approach and have established the obligation to file for preventive restructuring proceedings upon receipt of the notification unless steps are taken to reduce the effects of insolvency on creditors and other stakeholders. In a future reform, a stronger connection between the EWS and the restructuring system could be considered, which could consist of an obligation on the debtor to perform a self-assessment or to explore initiating an out-of-court restructuring procedure following receipt of the notification.

Early indications suggest that the EWS could be having a positive effect. Notifications remain confidential and therefore there is no official data on their number nor on debtors taking action as a result of notifications. However, the number of out-of-court restructuring procedures opened since the Insolvency Code entered into force (discussed above) are promising and could be explained by the introduction of the obligation to notify. As the introduction of the EWS is relatively recent, the authorities should ensure that creditors are complying in a timely fashion with notification requirements and debtors are taking early action to address financial distress at an early stage.

Duration of procedures

As in enforcement, the main shortcoming of the insolvency system remains the long durations observed. The lack of specialisation of courts and court-appointed professionals in bankruptcy proceedings and the overload of cases and backlog in the courts play an important role in these delays and inefficiencies. The pre-2022 system provided for two main procedures to deal with insolvent companies, which have been retained in the Insolvency Code.[38]

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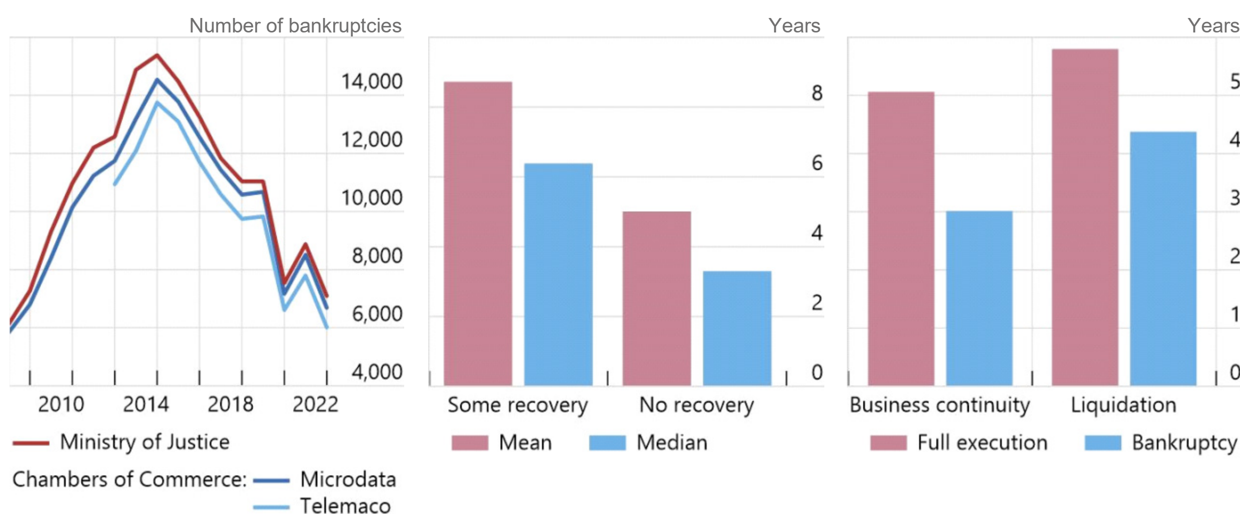
[37] The 2019 version of the Insolvency Code, which never entered into force as it was amended in 2021, foresaw similar obligations to notify the debtor and, in case of failure to address them, stakeholders had an obligation to inform the "*Organismi di Composizione della Crisi (OCRI)*", which were supposed to assist the debtor in attempting a restructuring. In case an agreement was not reached, OCRI had an obligation to report the case to the public prosecutor which could file for insolvency against the debtor.

[38] In addition, there were also other procedures, including the (i) accordi di ristrutturazione dei debiti, (ii) piano attestato di risanamento, and (iii) convenzione di moratoria.

- Judicial liquidation (*liquidazione giudiziale*) is used (solely) to wind up a company and distribute its assets to creditors (although business continuation is allowed when it maximises the return for creditors). In 2022, around 7,000 corporates were declared insolvent in Italy (left panel, Graph 8). The average duration of judicial liquidations is around 7.1 years, although the average duration of procedures with recovery for creditors is actually 8.9 years (centre panel, Graph 8). A study based on court registries found that 45% of judicial liquidations end up with no recovery at all.[39]

- Composition with creditors (*concordato preventivo*) is a procedure that allows a company to both restructure its debt and wind up the business. The confirmation phase takes an average of 1.5 years, while the execution phase takes an average of 5 years for business continuity plans and 5 years and 10 months for asset liquidation plans (right panel, Graph 8). The recovery rate for secured creditors in joint compositions is very high, with full recovery in most cases.[40] The recovery rate for all unsecured creditors is 12%.[41] The low recovery rates for unsecured creditors suggest that the joint composition procedure is not very effective in protecting the interests of these creditors.

Liquidations and duration **Graph 8**



Sources: DWGC, SIECIC registry, Ministry of Justice of Italy, Italian Chambers of Commerce, *Telemaco*.

Changes to the framework

The newly-adopted Insolvency Code is designed to provide a more comprehensive and efficient framework for the resolution of business failures. The reform established general principles for dealing with insolvent firms and created a single, unified procedure that applies regardless of

[39] See BdI (2023) *Questioni di Economia e Finanza: Le caratteristiche e la durata dei fallimenti e dei concordati preventivi*, July (Italian only).

[40] The average recovery rate for the compositions with creditors where the business activity is liquidated is 94%, where the business activity is carried out by the same entrepreneur is 96%, where the business activity is sold as a going concern is 94%. Ministry of Justice data (2023).

[41] Ministry of Justice data (2023).

the option followed by the debtor (reorganisation or liquidation). The overall goal of the reform was to improve legal certainty, predictability, and economic efficiency, making it more competitive internationally.

The liquidation procedure has remained largely unchanged, but in-court restructuring has been strengthened. A key change has been that access to the Composition with Creditors for liquidation purposes *(concordato liquidatorio)* has been restricted, while entering it on a going-concern basis *(concordato con continuità aziendale)* has been simplified. The Code has also introduced other new features that have improved the system significantly, including, among others, (i) the mandatory creation of classes of creditors for voting purposes, (ii) a clear system for the payment of pre-petition claims and claims secured by assets that are essential for the continuation of the business, and (iii) a strengthened super-senior priority for new finance. The Code has also introduced a new in-court restructuring procedure, the "*Certified Restructuring Plan*", which is the "preventive procedure" selected by the authorities to implement the 2019 Restructuring and Insolvency Directive.[42]

The impact of the reform is still too early to assess. To monitor the efficiency of the reform and decide if any changes should be made to the text currently in force, the Company Crisis Observatory was established in November 2022. The Observatory is a (non-profit) association charged with collecting data on insolvency procedures and also researching the legal interpretation and economic-business data involved in insolvency procedures. Judges, insolvency administrators and academics contribute to its activities. The Observatory's first meeting took place in April 2023. A future reform could establish simplified insolvency proceedings for reorganisation and liquidation of SMEs, which should be based on the principles of easy access, minimal formalities, and shorter deadlines. [43] Some reforms to consider could include that the debtor remains in-possession in liquidation proceedings, and the introduction of special voting rules to avoid creditors' passivity.[44]

Information systems

The information systems to track and monitor court proceedings, including enforcement and insolvency cases, are not robust enough to allow monitoring the efficiency of the procedures. The Italian court system does not collect granular information on the cost, efficiency and outcomes of judicial enforcement and insolvency procedures. While some data is collected on the number of cases opened and closed, their duration and whether a plan is confirmed (or not), no granular data is collected on other key indicators that would allow a detailed assessment of the system's performance. This would include, among others, the amount of debt filed by each type of creditor, their respective recovery rates and the costs incurred throughout the

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[42] The Restructuring Plan is an in-Court restructuring proceeding similar to the Composition with Creditors but with a few significant differences, including (i) the Plan can provide for the satisfaction of creditors' claims through the proceeds generated in implementation of the restructuring plan in derogation of the absolute priority rule; (ii) payments of prepetition claims and transfers of assets outside the ordinary course of business are not subject to court authorization; (iii) the plan must be approved by all classes of creditors; and (iv) labour claims cannot be rescheduled or written-off and must be repaid in full within 30 days from court confirmation.

[43] For general guidance on key features of SME Insolvency, see principle C.18 of the World Bank (2021) *Principles for Effective Insolvency and Creditor/Debtor Regimes*.

[44] Creditors silence or lack of negative vote on a duly notified reorganization plan should be considered as acceptance of the plan and counted as an affirmative vote.

procedure.[45] On the critical issue of durations, the system can calculate average durations of all cases currently open but does not allow the calculation of averages by the year in which the case was opened, which would provide confirmation of a reduction in the duration of cases. Moreover, data currently collected is only made available with a significant lag, sometimes exceeding a year.

3. Conclusions and recommendations

The Italian authorities have achieved significant success in reducing NPLs on bank balance sheets from the peak in 2015. Whilst more favourable economic conditions have slowed the flow of new NPLs, close cooperation between domestic authorities, implementation of EBA and ECB guidelines and capital directives, increased supervisory intensity, the deliberate development of the secondary market for NPLs and reforms to the enforcement, restructuring and insolvency frameworks have had a significant impact towards this success. Some other jurisdictions have introduced reforms modelled on this approach.[46] In addition to reducing NPLs in the banking sector, these efforts have increased technical capacity of the Italian financial sector.

At the same time, further steps can be taken to preserve the success achieved and to improve further the ecosystem for managing NPLs in the banking sector. These include maintaining a robust secondary market for NPL disposal and further improving the efficiency of the insolvency, restructuring and debt enforcement framework.

3.1. Maintain robust secondary market for NPL disposal

GACS has undoubtedly been a success in contributing to the removal of NPLs from banks' balance sheets. The state guarantee provided to senior tranche investors created an investor demand in an otherwise subdued securitisation market. While the structure did entail moral hazard concerns, these were mitigated through appropriate design features, including fair transfer pricing, risk-based pricing of the guarantee, reduced informational asymmetries, engagement of expert services and dedicated initial endowment.

GACS has finally expired after several extensions, and while it could be reactivated if needed, the current environment does not call for it as the large legacy stack of bad loans has been reduced and the secondary NPL market appears active. The authorities' preference for not resorting to public support in the current environment is also reflected in the fact that the Decree Law 115/2022, which introduced a Guaranties Loans Active Management scheme aimed at centralised management of receivables arising from performing or UTP loans that benefit from the state guarantee granted under Covid-19, has not been adopted for implementation, although such measures remain part of the potential regulatory toolkit.

The share of UTP exposures on banks' total net NPLs has grown in recent years, rising from 52% in 2014 to 64% in 2022. In 2022 they represented 50% of the overall NPL sales. This portfolio requires different considerations and skills regarding debt resolution and enforcement.

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[45] Collection of these data is suggested as good practice under the EU 2019 Restructuring Directive, article 29.3.

[46] Greece's Hercules asset protection scheme (HAPS) was inspired by and is very similar to the GACS model.

It is critical that the market mechanisms for NPL sales and securitisation not weaken. The authorities should continue monitoring the secondary market and fostering its robust development in the absence of GACS. Proposals that would introduce uncertainty or undermine the NPL secondary market and the past success of GACS should be resisted. The market ecosystem, including the servicers and investors, has developed expertise in niche areas and structures and will need to evolve to accommodate diverse loan types. The role of servicers is critical in this context. While master servicers are under the supervisory purview of the BdI, their activities are often outsourced to special servicers which operate outside the regulatory perimeter. BdI continues to increase supervisory monitoring of master servicers. While a large portion of NPL exposure may have moved out of the banking sector, until the stressed borrower accounts are completely resolved, the risks to financial stability may not be mitigated completely. While the current regulatory, supervisory and market environment, which permits credit purchases only to authorised entities, is considered adequate at the current juncture, it would be important for the authorities to closely monitor and address any potential information gaps.

- **Recommendation 1:** The authorities should continue monitoring and fostering the secondary market for NPLs, including by resisting measures that would undermine past success; and BdI should continue to strengthen its supervision of relevant supervised entities, including servicers.

3.2. Enforcement, debt restructuring and insolvency

The insolvency, restructuring and debt enforcement systems were a key impediment to the resolution of NPLs in 2016, and Italy has made remarkable progress in improving its legal and institutional framework in the broad reform process that followed. Insolvency procedures were overhauled, a new focus on out-of-court restructuring was introduced, debt enforcement was streamlined and key institutions, including courts and administrators, were also strengthened. Insolvency reform is however a lengthy process: the reforms introduced since 2005-2006, which culminated with the Insolvency Code in 2022, are only likely to yield results in the medium- to long-term.

Despite progress made, substantial legal issues remain outstanding, and the insolvency and debt enforcement framework would remain a bottleneck if NPLs were to surge in the near future. Long durations of enforcement and insolvency procedures are a key challenge that should continue to receive the authorities' attention. To address the persistent long durations, further reforms to simplify and streamline court procedures are necessary. The information systems to track and monitor court proceedings are not apt to monitor their efficiency as the Italian court system does not collect granular information.

- **Recommendation 2:** To address the persistent long durations of enforcement procedures, the authorities should: (i) increase courts' resources and staff, especially in those courts facing the most severe backlogs, (ii) strengthen court specialisation in commercial matters, and where possible, in insolvency and enforcement matters specifically, and (iii) finalise the ongoing digitalisation of the court system, which will involve the introduction of an e-tracking system that would allow monitoring of courts' performance and setting adequate incentives.

The Insolvency Code has made EWS one of the main pillars of the new system, with an obligation on certain stakeholders to issue an early warning by notifying the debtor of financial difficulties. However, upon receipt of the notification, there is no specific obligation on the debtor to act; this means little formal connection exists between the EWS and debt restructuring procedures, unlike in some other jurisdictions. While indications suggest that the EWS could be having a positive effect, a stronger connection between the EWS and the restructuring system could be considered.

In Italy, as in other countries, judicial and hybrid restructuring proceedings are costly and there is evidence that firms filing for restructuring are larger than average firms. The Insolvency Code introduced a new out-of-court procedure that features an inexpensive and efficient process, which will encourage SME restructurings. However, the out-of-court procedure also presents complexities that may prevent SMEs from taking full advantage. Adequate data should be collected to monitor the use and outcomes of the out-of-court restructuring processes and assess whether improvements are needed.

The system of insolvency, restructuring and enforcement is complex and could merit some simplification, although its recently completed reform makes it inadvisable to introduce drastic changes at this time. The focus now should be on monitoring the system closely and on ensuring that it meets its intended objectives, including by providing sufficient human resources and adequate training of the experts involved. Once the mechanisms implemented by the 2022 reforms have been well-established, the authorities could explore introducing some degree of simplification.

- **Recommendation 3:** The authorities should monitor the system of insolvency, restructuring and enforcement closely and ensure that it meets its intended objectives, including by: providing sufficient human resources and adequate training of the experts involved; and collecting adequate data to monitor the use and outcomes across processes. Once the mechanisms implemented by the 2022 reforms have been well-established, the authorities should evaluate the system and explore further reforms such as (i) improving the possibility for out-of-court ‘pre-negotiated plans’ to be swiftly confirmed by the court; and (ii) strengthening simplified insolvency proceedings for reorganisation and liquidation of SMEs. The authorities should also monitor the existing EWS and assess its effectiveness to explore the need for further reforms including establishing a stronger connection between EWS and debt restructuring procedures.

Annex 1: Italy's implementation of G20 reforms (as of September 2023)

This table presents the status of implementation of G20 financial regulatory reforms, drawing on information from various sources. The tables below distinguish between priority areas that undergo more intensive monitoring and detailed reporting via progress reports and peer reviews, and other areas of reform whose monitoring is based on annual survey responses by FSB member jurisdictions. See here for further information.

IMPLEMENTATION STATUS OF REFORMS IN PRIORITY AREAS

Reform Area	BASEL III					COMPENSATION	OVER-THE-COUNTER (OTC) DERIVATIVES				RESOLUTION					NON-BANK FINANCIAL INTERMEDIATION		
	Risk-based capital	Requirements for SIBs	Large exposures framework	Leverage ratio	Net Stable Funding Ratio (NSFR)		Trade reporting	Central clearing	Platform trading	Margin	Minimum external TLAC for G-SIBs	Transfer / bail-in / temporary stay powers for banks	Recovery and resolution planning for systemic banks	Transfer / bridge / run-off powers for insurers	Resolution planning for SI>1 CCPs	Money market funds (MMFs)	Securitisation	Securities financing transactions (SFTs)
Agreed phase-in (completed) date	*2023*	*2016 (2019)*	*2019*	*2023*	*2018*		*end-2012*	*end-2012*	*end-2012*	*2016 (2022)*	*2019/2025 (2022/2028)*							*2017/2023*
Status		C	LC		LC													

Legend	Final rule or framework implemented. Final rule published but not implemented, draft regulation published or framework being implemented. Draft regulation not published or no framework in place (dark red colour indicates that deadline has lapsed). Requirements reported as non-applicable. Basel III: **C**=Compliant, **LC**=Largely compliant, **MNC**=Materially non-compliant, **NC**=Non-compliant. Compensation: B,I=Principles and Standards deemed applicable only for banks (B) and/or insurers (I). OTC derivatives: R/F=Further action required to remove barriers to full trade reporting (R) or to access trade repository data by foreign authority (F). Non-bank financial intermediation: */**=Implementation is more advanced in one or more/all elements of at least one reform area (money market funds), or in one or more / all sectors of the market (securitisation). Further information on the legend.
Notes	CCPs=Central counterparties. G-SIBs=Global Systemically Important Banks. TLAC=Total Loss-Absorbing Capacity. SI>1=Systemically important in more than one jurisdiction.
Source	FSB, *Promoting Global Financial Stability: 2022 FSB Annual Report*, November 2022.

IMPLEMENTATION STATUS OF REFORMS IN **OTHER AREAS**

Reform area	**Hedge funds**			**Securitisation**			**Supervision**				**Macroprudential frameworks and tools**	
	Registration, appropriate disclosures and oversight of hedge funds	Establishment of international information sharing framework	Enhancing counterparty risk management	Strengthening of regulatory and capital framework for monolines	Strengthening supervisory requirements or best practices for investment in structured products	Enhanced disclosure of securitised products	Consistent, consolidated supervision and regulation of SIFIs	Establishing supervisory colleges and conducting risk assessments	Supervisory exchange of information and coordination	Strengthening resources and effective supervision	Establishing regulatory framework for macroprudential oversight	Enhancing system-wide monitoring and the use of macroprudential instruments
Status	REF*	REF	REF*	REF*	REF	REF	REF	N/A*	REF	REF	REF	REF

Reform area	**Credit rating agencies**		**Accounting standards**	**Risk management**		**Deposit insurance**	**Integrity and efficiency of financial markets**		**Financial consumer protection**
	Enhancing regulation and supervision of CRAs	Reducing the reliance on ratings	Consistent application of high-quality accounting standards	Enhancing guidance to strengthen banks' risk management practices	Enhanced risk disclosures by financial institutions		Enhancing market integrity and efficiency	Regulation and supervision of commodity markets	
Status	REF*	REF	REF	REF	REF	REF	REF	REF	REF

Legend	REF=Implementation reported as completed. IOG=Implementation reported as ongoing. ABN=Applicable but no action envisaged at the moment. N/A=Not applicable. *=collected in previous year(s) for all members.
Notes	The FSB has not undertaken an evaluation of survey responses to verify the status or assess the effectiveness of implementation. In a number of cases, the complexity of the reforms and the summarised nature of the responses does not allow for straightforward comparisons across jurisdictions or reform areas. In particular, reforms whose status in a particular area is reported as complete should not be interpreted to mean that no further policy steps (or follow-up supervisory work) are anticipated in that area. CRA = Credit Rating Agency, SIFI = Systemically important financial institution.
Source	FSB, *Jurisdictions' Responses to the IMN Survey*.

Other information	Latest IMF-World Bank FSAP: Mar 2020	Latest FSB Country Peer Review: 2011	Home jurisdiction of G-SIBs: yes	Signatory of IOSCO MMoU: yes	Signatory of IAIS MMoU: yes

The following table presents the steps taken to date and actions planned by the Italian authorities in core reform areas (not covered in this peer review) where implementation has not yet been completed. The actions mentioned below have not been examined as part of the peer review and are presented solely for purposes of transparency and completeness.

Reform area	Steps taken to date and actions planned (including timeframes)
Final Basel III framework	
Risk-based capital	In Italy, the implementation of the Final Basel III framework will take place following the and according with the EU legislative process. At the moment, the EU Co-legislators are conducting negotiations to agree on: i) the 3rd Regulation on Capital Requirements (CRR3), which will transpose the Final Basel III reforms in the EU regulatory framework and ii) 6th Directive on Capital Requirement (CRD VI) which will complement provisions under the CRR3. According to the latest available information, EU negotiations have been completed in December 2023 and the publication of the legislative text is expected in the first half of 2024. Once adopted the CRR3 will be directly applicable to all EU Member States (and therefore also to Italy), according to transitional or phase-in period agreed upon by Co-legislators. The CRD VI shall be transposed within the Italian legislative framework according to the timeline agreed (usually 18 months from the publication in the EU Official Journal).
Resolution	
Transfer/bridge/run-off powers for insurers	At present, Italy does not have a resolution regime for insurers; therefore, transfer/bridge/run-off powers are not available for being used in a resolution hypothesis. However, the Code of Private Insurance provides the national supervisory authority with the legal basis to apply the portfolio transfer and the run-off powers (entirely or by individual insurance classes) in the context of: a) going-concern supervision; b) extraordinary administration; c) administrative compulsory winding-up. No provision is set for bridge institutions. The adoption of the EU Directive on the recovery and resolution of insurers, being discussed by the EU legislators, will trigger a comprehensive review of the current Code of Private Insurance provisions concerning extraordinary administration and administrative compulsory winding-up. As the EU negotiation is still ongoing, the implementation date of the EU framework into the national legislation cannot be foreseen for the time being, depending on the regulatory process on the final adoption of the Directive
Non-Bank Financial Intermediation	
Securities financing transactions	The BdI collects granular SFT data and has conducted pilot exercises (as foreseen within the FSB framework) to test technical aspects of the global data reporting process (e.g., including data

	transmission channel, data structure definition and data file format), through the submission of dummy data to the BIS. In cooperation with four EU jurisdictions (i.e. France, Germany, Netherlands, Spain) and the ECB, the BdI also contributes to a range of initiatives (e.g. memorandum of understanding among relevant parties, revision of legal guidelines, changes to legislation) to overcome legal and confidentiality issues that have so far represented an obstacle for the reporting of actual data in Europe. While the timeline for implementation remains open, the projected solution, if successful, would enable to submit granular data in 2023. The same information about the implementation status of EU jurisdictions has been recently shared within the FSB-SFTDEG group (‘Update on the progress of the Global securities financing transactions data collection’).

Annex 2: Enforcement, insolvency and restructuring framework – overview of reforms and procedures

Year	Reform	Main elements
Enforcement Framework		
2015, 2016	Foreclosure reform: two distinct pieces of legislation	Measures to shortening the length and improving the efficiency of credit recovery proceedings for secured and unsecured debt included • the introduction of mandatory use of professional experts • shorter time limits for certain procedural activities • new criteria for accepting bids in auctions • the introduction of the nation-wide online platform for sales of assets. Additionally, an out-of-court mechanism for collateral enforcement was established. Two new legal instruments to strengthen creditor protection: (1) the *patto Marciano;* and (2) the non-possessory pledge.
2017	Supreme Judiciary Council guidelines	
Insolvency and in-court restructuring framework		
2005	Reform of the bankruptcy law dating 1942	Introducing a number of new features including three different schemes for business failures resolution (two of them in court): • winding-up (fallimento) • court-ordered reorganisation based on a restructuring plan that must be approved by creditors *(concordato preventivo)* • rescue through out-of-court debt restructuring agreements (accordi di ristrutturazione; piani attestati di risanamento).
2008, 2009, 2012, 2013, 2015	Several reforms of the bankruptcy law	Reforms included • increased monitoring of the debtor's activities during the reorganisation process • mandatory use of professional experts to carry out the activities related to the disposal of collateral • shorter time limits for certain procedural activities • new criteria for accepting bids in auctions • a dedicated website to advertise forced sales.
2015	Amendments to the bankruptcy law focused on NPLs	Reforms included

		• the mandatory use of professional experts to carry out the activities related to the disposal of the collateral • shorter time limits for certain procedural activities • the immediate full tax deduction for write-offs • write-downs and disposals.
2022	New Italian Code on Business Crisis and Insolvency, *Codice della Crisi d'Impresa e dell'Insolvenza* ('CCII')	The CCII creates a unified procedural model for both liquidation proceedings and crisis resolution to improve legal certainty and predictability. The CCII creates a unified procedural framework for the relationship between enforcement and protective and precautionary measures within insolvency procedures. This relationship is the same for all procedures. To monitor the efficiency of the reform, the Company Crisis Observatory was established in November 2022.
Out-of-court restructuring (OCW) framework		
2005	Reform of the bankruptcy law dating 1942	Introducing three different schemes for business failures resolution (two of them out of court) • certified recovery plans (piani attestati di risanamento) • debt restructuring agreements (*accordi di ristrutturazione*).
2015	D.I. 83/2015	Moratoria Agreements (*convenzioni di moratoria*)
2021	Negotiated workout (*composizione negoziata*	The procedure bears a number of features designed to enhance its chances of success: • stay on creditor enforcement actions • the ability for the debtor to obtain super-senior finance • the appointment of an independent expert to monitor the negotiations • a duty on creditors to take active part in the negotiations.

Annex 3: Regulatory and supervisory measures – overview of reforms

Year	Reform	Applied to	Main elements
			Regulatory and supervisory measures
2016	Italian dedicated reporting on NPL	SI and LSIs	Granular reporting on gross bad loans of more than €100,000. Supported secondary market by improving digitally available detailed data on the credit facility, type of collateral, and guarantees.
2017	ECB Guidance on non-performing loans	SIs	Non-binding guidance that sets supervisory expectations regarding NPL identification, management, measurement and write-offs. High NPL banks to develop time-bound NPL reduction strategies with targets to address NPL stocks and corresponding expectations on governance and operations.
2018	EBA guidelines on the management of non-performing and forborne exposures (EBA/GL/2018/06)	SIs and LSIs	Specified sound risk management practices for credit institutions in the management of NPL and forborne exposures, including requirements for NPL reduction strategies, governance and operations of the NPL workout framework, the monitoring and the internal control framework. Guidelines encouraged credit institutions with gross NPL ratios at a level of 5% or above to establish an NPL strategy, as part of their overall strategy and related governance and operational arrangements.
2018	Addendum to the ECB Guidance to banks on non-performing loans: supervisory expectations for prudential provisioning of non-performing exposures	SIs	The non-binding addendum sets out supervisory expectations for prudential provisioning for new NPLs: • Applies to loans originated before 26 April 2019 classified as NPL after 1 April 2018. • Sets provisioning coverage levels. • Divergence from the expectations is reflected in the Supervisory Review and Evaluation Process. Moreover, ECB communicated supervisory expectations for provisioning of NPL stock of SIs (i.e. exposures classified as NPL on 31 March 2018) in July 2018.
2018	EBA guidelines on disclosure of non-performing and forborne exposures (EBA/GL/2018/10)	SIs and LSIs	To reduce information asymmetry and increase comparability of credit institutions' risk profiles and promote market discipline, they set out: • A common content and uniform disclosure format for the information on

			NPL and forborne exposures for all institutions • Specific templates for credit institutions with a gross NPL ratio of 5% or above.
2018	Italian national guidelines on NPL management	LSIs	Following the 2017 ECB guidance, BdI introduced guidance for LSIs with high levels of NPLs to adopt operational plans (over a three to five years' time horizon) with reduction targets and actions. Specific expectations of the credit institutions' management body involvement in the monitoring of the NPLs strategy were set.
2019	Pillar 1 prudential backstop (EU regulation 2019/630)	SIs and LSIs	Requires a deduction from capital when NPLs are not sufficiently covered by provisions as compared to a uniform pre-defined provisioning calendar. Applies to NPLs arising from loans originated after 26 April 2019.
2020	Italian tax incentives on NPL disposals	SIs and LSIs	Temporary tax incentives for the disposal of impaired loans were introduced, allowing banks and non-financial corporations to convert deferred tax assets in tax credits into an amount proportional to the NPLs sold.
2020	EBA guidelines on loan origination and monitoring (EBA/GL/2020/06)	SIs and LSIs	They aim to ensure that credit institutions have robust and prudent standards for credit risk taking, management and monitoring, and that newly originated loans are of high credit quality.
2021	Banca di Italia revision of the bank's internal governance regulation	SIs and LSIs	Requires credit institutions to take into consideration the monitoring and management of NPLs when defining business strategies.