EMEA DC Meeting Statement 8 August 2017

The EMEA DC met on 4 August 2017 to discuss whether:

(a) for the purposes of trades entered into using the 2014 Definitions, a Governmental Intervention Credit Event has occurred with respect to Banca Monte dei Paschi di Siena S.p.A. (**MPS** or the **Reference Entity**); and

(b) for the purposes of trades entered into using the Updated 2003 Definitions, a Restructuring Credit Event has occurred with respect to MPS,

as a result of the decree (the **Burden Sharing Decree**) of the Ministry of Economy and Finance of Italy (the **MEF**) that was published in the *Gazzetta Ufficiale* of Italy on 28 July 2017 and pursuant to which certain burden sharing measures amongst holders of MPS's subordinated debt were implemented. The Burden Sharing Decree was made pursuant to Law Decree No. 237/2016 (the **Law Decree 237**) and specifically provides for the conversion of MPS's Additional Tier 1 and Tier 2 financial instruments (as listed in the table to MPS's press release of 29 July 2017 (the **MPS Press Release**)[1]) into newly-issued ordinary shares of MPS. The Burden Sharing Decree became effective on 29 July 2017.

The EMEA DC resolved that a Governmental Intervention Credit Event occurred under the 2014 Definitions in relation to the European Financial Corporate and Standard European Financial Corporate Transaction Type (subordinated 2014 Transactions only) and a Restructuring Credit Event occurred under the Updated 2003 Definitions in relation to the European Corporate and Standard European Corporate Transaction Types (senior and subordinated Updated 2003 Transactions), in each case with respect to MPS on 29 July 2017.

Additional Background

Law Decree 237 was an emergency decree passed in December 2016 following the Italian referendum and MPS's failure to meet an ECB deadline to recapitalise following the negative impact for MPS in the 'adverse' scenario that was shown during recent European-wide stress tests. The aim of Law Decree 237, however, is not only to safeguard MPS but also to safeguard the Italian banking sector more generally. Law Decree 237 was converted into Italian law in February 2017. It gives the MEF the ability to support Italian banks during a limited window of time through two principal instruments: (a) state guarantees of newly issued debt of Italian banks; and (b) precautionary recapitalisation measures in respect of Italian banks, in each case in order to avoid or remedy a serious disruption of the Italian economy and preserve financial stability. Precautionary recapitalisation of Italian banks[2] is intended to be achieved by way of the MEF subscribing for shares issued by such banks as well as burden sharing amongst the holders of certain types of such banks' financial instruments, the aim of the latter being to limit the use of public funds. The Burden Sharing Decree was, in fact, accompanied by a precautionary recapitalisation decree also made pursuant to Law Decree 237 pursuant to which the MEF subscribed for ordinary shares of MPS (the **Recapitalisation Decree** and, together with the Burden Sharing Decree, the **Decrees**).

In light of the foregoing, the EMEA DC considered Law Decree 237 in relation to Directive 2014/59/EU on the recovery and resolution of credit institutions (**BRRD**)[3] and EU Regulation 806/1024 for the resolution of credit institutions in the framework of the Single Resolution Mechanism (the **SRM**)[4]. The EMEA DC noted that the circumstances in which the resolution and recovery provisions of the BRRD and SRM would be utilised are significantly different to the circumstances in which the provisions of Law Decree 237 might be utilised. Specifically, the resolution and recovery measures of the BRRD and SRM are triggered, *inter alia*,

[1] The MPS Press Release is available on MPS's website: http://english.mps.it/media-and-news/press-releases/ComunicatiStampaAllegati/2017/CS_decreto%20MEF_28072017_ENG%20RQ.pdf.

[2] The DC understands that these measures are available to Italian banks for which a capital shortfall has been identified in the context of 'adverse' scenario (as opposed to 'baseline' scenario) stress tests conducted by the relevant competent authority.

[3] http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0059&from=EN

[4] http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0806&from=EN

where the relevant financial institution is failing or likely to fail and/or is at the point of non-viability. In contrast, in order to qualify for the state intervention instruments under Law Decree 237, the relevant bank must *not* be failing or likely to fail nor must it be at the point of non-viability (under Law Decree 237, such circumstances are deemed not to exist to the extent that they are not ascertained by means of an inspection by the Bank of Italy or the European Central Bank). However, the EMEA DC noted that Law Decree 237 performs certain similar functions to the powers conferred by the BRRD and SRM (in particular with respect to the ability to impose a bail in of certain financial instruments as part of recapitalisation measures) and therefore, for the purpose of the 2014 Definitions, the EMEA DC was of the view that Law Decree 237 constitutes a "*restructuring and resolution law or regulation (or any similar law or regulation)*".

2014 Definitions

The EMEA DC initially considered whether the Burden Sharing Decree coming into effect constituted a Governmental Intervention Credit Event as described in Section 4.8(a)(iii) of the 2014 Definitions. Section 4.8(a)(iii) of the 2014 Definitions provides that a Governmental Intervention Credit Event occurs with respect to one or more *Obligations* upon "*a mandatory cancellation, conversion or exchange*" resulting from "*action taken or an announcement made by a Governmental Authority pursuant to, or by means of, a restructuring and resolution law or regulation (or any similar law or regulation), in each case, applicable to the Reference Entity in a form which is binding, irrespective of whether such event is provided for under the terms of such Obligation*".

The EMEA DC noted that the Standard Reference Obligation for the Subordinated Level in respect of MPS is one of the Lower Tier 2 financial instruments listed in the table to the MPS Press Release (ISIN Code: XS0236480322) and as such constitutes an Obligation. More generally, the DC was of the view that the other Lower Tier 2 financial instruments were borrowed money obligations of MPS and as such also constituted Obligations. Accordingly, the DC only considered the impact of the Burden Sharing Decree on the Lower Tier 2 financial instruments for the purposes of the present analysis.

The EMEA DC was of the view that the coming into effect of the Burden Sharing Decree satisfied the requirements of Section 4.8(a)(iii), because at that point the mandatory conversion of all of the Lower Tier 2 subordinated debt into newly-issued ordinary shares of MPS became binding on the relevant holders. Specifically, the MEF is a Governmental Authority, being a ministry of the Italian government which oversees economic policy and public investment decisions, and the publication of the Burden Sharing Decree in the *Gazzetta Ufficiale* of Italy on 28 July 2017 was, at the time at which it became effective – 29 July 2017 – binding on the holders of the affected debt instruments of MPS. The EMEA DC was not aware of the terms and conditions of the Lower Tier 2 financial instruments providing for such conversion but in any event a Governmental Intervention Credit Event can arise irrespective of whether the conversion is provided for under the terms of the relevant Obligation and therefore the DC did not analyse such provisions. The EMEA DC was also comfortable with the fact that Law Decree 237, pursuant to which the Burden Sharing Decree was made, constitutes a restructuring and resolution law (or any similar law) applicable to MPS for the reasons outlined above.

In considering whether a Credit Event had occurred in respect of any Senior 2014 Transactions referencing MPS, the EMEA DC noted that under Section 3.6(b) of the 2014 Definitions any Subordinated Obligations are Excluded Obligations for the purpose of determining whether a Governmental Intervention Credit Event has occurred in respect of any Senior 2014 Transactions with Financial Reference Entity Terms specified as being applicable in the related Confirmations, which is the case here. **Accordingly the Governmental Intervention Credit Event determination will only apply to any 2014 Transactions which have a Subordinated Obligation as their Reference Obligation.**

The EMEA DC noted that by virtue of Section 8.9(a) of the 2014 Definitions, this Credit Event will constitute an Asset Package Credit Event and, pursuant to Section 8.8 of the 2014 Definitions, that Asset Package Delivery will apply.

In light of the fact that the EMEA DC had already concluded that the coming into effect of the Burden Sharing Decree constituted a Governmental Intervention Credit Event, the EMEA DC did not consider whether a Restructuring Credit Event under the 2014 Definitions had occurred.

Updated 2003 Definitions

The EMEA DC's discussion then focused on whether the coming into effect of the Burden Sharing Decree constituted a Restructuring Credit Event under Section 4.7(a)(ii) of the Updated 2003 Definitions (as under the Updated 2003 Definitions, there is no equivalent to a Governmental Intervention Credit Event as described under the 2014 Definitions). A Restructuring Credit Event will arise upon the announcement of certain events by a Governmental Authority in a form that binds all holders of the relevant Obligation and where such event is not expressly provided for under the terms of such Obligation. The event described in Section 4.7(a)(ii) is "*a reduction in the amount of principal or premium payable at maturity or at scheduled redemption dates*". The occurrence of the event must directly or indirectly result from a deterioration in the creditworthiness or financial condition of the Reference Entity and the Multiple Holder Obligation must be satisfied.

The question under discussion centred on whether the mandatory conversion of the MPS subordinated debt into equity would be tantamount to a reduction in the principal amount of the subordinated debt, to the extent that the underlying bond documentation does not permit such convertibility. The EMEA DC considered the question with respect to the Lower Tier 2 financial instrument with ISIN Code XS: XS0236480322 on the basis that the EMEA DC had recently reviewed the terms of this subordinated debt obligation for the purposes of selecting the Standard Reference Obligation for the Subordinated Level for subordinated 2014 Transactions and therefore was aware that these terms did not permit any such convertibility.

The EMEA DC was of the view that:

(a) the mandatory conversion of these Lower Tier 2 notes into equity amounted to a reduction in the principal amount of the bonds;

(b) the MEF is a Governmental Authority and the publication of the Burden Sharing Decree on 28 July 2017 was, at the time at which it became effective – 29 July 2017 – binding on all holders of the affected debt instruments of the MPS;

(c) the publication of the Burden Sharing Decree resulted from the deterioration in creditworthiness or financial condition of MPS. For example, the EMEA DC noted that MPS failed to meet an ECB deadline to recapitalise following the very severe impact for MPS in an "adverse" scenario that was shown during European-wide stress tests in the summer of 2016[5]. Law Decree 237 was an emergency decree implemented partially as a response to this and to mitigate the negative impact on MPS's capital resources in such a scenario; and

(d) based on the considerable size (by reference to principal balance) of these Lower Tier 2 notes immediately prior to the publication of the Burden Sharing Decree, the fact that these Lower Tier 2 notes were listed and the fact that the EMEA DC has seen no evidence to suggest that such notes were held by fewer than four holders, the Multiple Holder Obligation requirement was satisfied.

On this basis, the EMEA DC resolved that a Restructuring Credit Event under Section 4.7(a)(ii) of the Updated 2003 Definitions had occurred in respect of MPS and that the date of such event was the 29 July 2017, being the date on which the Burden Sharing Decree became effective and therefore binding on the relevant holders of the Lower Tier 2 subordinated debt. The EMEA DC noted that Mod Mod R would apply to the Updated 2003 Transactions.

Next steps

[5] The press release relating to the results of the EU stress test is available on MPS's website: http://english.mps.it/media-and-news/press-releases/2016/Pages/PR-Stress-Test-29072016.aspx

The EMEA DC resolved to hold an auction in respect of the 2014 Transactions (subordinated transactions only). The EMEA DC resolved potentially to hold one or more auctions in respect of the relevant Updated 2003 Transactions (senior and subordinated transactions).