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WEBINAR
SHADOW BANKING?
NON-BANK SUBJECTS MANAGING CREDIT

(Centro di Ricerca Interdipartimentale sul Diritto Europeo della Banca e della Finanza, Paolo Ferro-Luzzi, Grandangolo, Università Roma Tre, 13 novembre 2020)

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1. The objectives of the webinar

The Centro di Ricerca Interdipartimentale sul Diritto Europeo della Banca e della Finanza, Paolo Ferro-Luzzi, Grandangolo, of Roma Tre University, held the webinar "Shadow banking? La gestione del credito da parte di soggetti non bancari" as part of the "Ciclo di Seminari" (Seminars serie) that took place through October – December 2020.

The webinar was held, organised and moderated by Professor Andrea Zoppini, vice-director of Centro di Ricerca "Grandangolo" and Full Professor of Private Law at the University of Roma Tre.

Opening the event, Professor Zoppini introduced the subject under consideration. He defined "shadow banking" as the activity of credit intermediation performed out of the banking system regulation.

The Professor proceeded illustrating the rationales underlying the study of Centro Ferro-Luzzi. The reasons for the event reside in the necessity to address the multiple issues the "shadow banking" poses. Among the others, whether it is adequately and sufficiently regulated.

According to the speaker, the lack of a harmonized regulation of the phenomenon – and it not amounting to an irregular condition – answers the above question.

Relevant data cited by Professor Zoppini and The Economist evidence the qualitative and quantitative relevance of shadow banking, therefore, the convenience to analyse it. Also because of the strict regulation of banking activity, figures highlight it performs a different, negative and increasingly less profitable trend with respect to the activity provided by non-banking subjects.

In light of the above, Professor Zoppini considered it useful and necessary to assess the perimeter of the phenomenon, the adequacy of the legislative framework and the efficacy of the control systems.

Mutual lending was a helpful example for the speaker to define the scope of shadow banking: it does not qualify as saving collection, as such activity is only performed with respect to members of the mutual company and not investors.

Even because of its quantitative relevance – credit unions collected EUR 11 billion among their members – the phenomenon generated uneasy criticalities. Professor

Zoppini considered those arising from economic crises the ones of major interest. Credit unions bankruptcy reshapes what was perceived as a safe loan as a non-protected loan worsened by the juridical qualification of member of a credit union. Notwithstanding being creditors of the company, they were subject to a worse treatment with respect to other creditors.

The evolution of shadow banking sparked a live debate and proposals aiming to level playing field among mutual lending and bank deposits stemmed; Professor Zoppini branded them unfit.

The possibility provided to credit unions' customers to access a "platform" and open a deposit account caused the interplaying of mutual lending regime and depositors' protection rules. Professor Zoppini qualified the matter in question as an ante litteram case of shadow banking.

Professor Zoppini concluded it was on these grounds an assessment regarding the necessity of a shadow banking specific regulation and its adequacy was deemed useful and noted the overarching issue concerns the banking future.

The floor was then left to guest speakers.

2. The interventions

Professor David Ramos Muñoz, Full Professor of Commercial Law at Universidad Carlos III de Madrid, opened the round of interventions.

He firstly outlined the structure of his speech: distinguishing myth and reality of the shadow banking phenomenon; an investigative effort regarding the proper institutional approach and rationales justifying shadow banking; and, lastly, assessing whether shadow banking may be regarded as an opportunity for FinTech and sustainability investments.

Professor Muñoz followed identifying the first two myths on shadow banking, namely believing it new and considering it shadowy: shadow banking emerged with banking activity and one may argue at the time when banking activity was not regulated it all pertained to shadow banking; the phenomenon shall not be considered suspicious, albeit some cases may qualify as regulatory arbitrages, as per cases where market players avoid the application of mandatory rules, or the State itself grants regulatory aid to entities providing activities it considers socially desirable and worth enhancing.

Professor Muñoz followed pointing out shadow banking is not shadowed by something: contrarily, it often finds itself at the very core of the banking system.

The speaker identified two concepts at the core of shadow banking which also underly the banking system: money and credit.

Considering they are provided by the State activity – acting both as credit and money provider other than lawmaker – banking activity may be considered as an entrepreneurial idea or a State concession.

Bearing the latter perspective in mind, or accepting a hybrid version of the two, the speaker noted one may be led to think it as an activity to be performed under mandatory rules.

A different point of view takes into account privileges such activity enjoys, both in terms of liquidity and solvency – e.g., deposit guarantee schemes – which shall be paid a price.

Professor Muñoz commented the banking system grounds its rules on the abovementioned philosophies and noted State acting ambiguously – one time applying rules based on equality, others using a transactional approach – results in a lack of clarity of the prevailing philosophy.

Once illustrated the above, the speaker proceeded discussing the rationale underlying investment opportunity: in presence of low interest rates it is desirable to enhance investment diversification whereas, from an entrepreneurial perspective, non-financed projects shall be provided credit access.

For this purpose, innovation helpfully lowers transaction costs and enhances functional specification.

Regarding the rationale underlying sustainability investments, the speaker noted some investments are more sustainable and more fit for societies than others. Consequently, the structure of the banking system grants them financing. Instead, subjects who do not have access to credit may obtain it thanks to more flexible rules.

Examining justifications one by one, the speaker explained, convincing arguments justify a more flexible approach allowing shadow banking in specific contexts.

The speaker listed examples which prove useful easing access to more profitable investments when negative interest rates occur.

Professor Muñoz highlighted none of these themes is new: the idea of

combining low interest rates and supplying new products to investors so that they may catch more profitable opportunities was the rationale underlying the setting-up of money market funds in U.S. around 1970.

Professor Muñoz followed recalling the U.S. replied to low interest rates and lack of real estate investments with securitization, and with known results.

The speaker questioned whether the phenomenon presents differences this time and, in order to provide the answer, furtherly addresses the structural issue regarding maturity transformation and its transactional volume.

Professor Muñoz told himself unconvinced by concerns of shadow banking and FinTech ties are concerned as banking has always been a key sector in innovation. FinTech promises to ease disintermediation and make personal data management more efficient were considered justifications to specific regulatory responses in the U.S., higher tolerance in China and other different regulatory proposals.

The speaker drew the path leading from the special charters idea to a charter-based system causing some banking groups ending up under the supervision of a less adequate authority and highlighted how disintermediation led to shadow banking being based on securitisation.

Therefore, Professor summarized that no business model is completely new: smart technologies were used in the past as arguments justifying the tolerance of hedge funds and Wirecard case taught.

The speaker drew to the end and addressed the question of whether "this time is different" from another perspective. He wondered if such question shall be answered with another: whether we are in a moment of disintermediation or re-intermediation, and, thus, it is necessary to assess if value is being created or redistributed among traditional entities who are losing it and new entities who are gaining it as a result from direct contact with the customer.

The Professor told himself convinced by the efficiency deriving from better data management rather than by data management superiority as an argument per se, the former being the fundamental argument with respect to Fintech or Big Tech.

The speaker considered more welcoming regulatory attitude may ease channelling socially desirable investments flows or financial inclusion but, he notes again, this is convincing, not new.

The idea of easing access to credit through demonization of secondary market inspired government sponsored enterprises and social investment.

At last, Professor Muñoz summarized shadow banking is simply not new and it shall not raise suspects at any cost.

Professor Muñoz concluded stating the above illustrated arguments and justifications apply to new shadow banking models but are already known and were previously used, successfully in some cases, failing in others, as sometimes problems reside in shadow banking, other times in rules.

The second speaker to take the floor was Professor Filippo Annunziata, Associate Professor of Economics Law at Bocconi University. His intervention would illustrate a known example of shadow banking – which, he agreed with Professor Muñoz, is not so shadowy – as the undertakings for the collective investments (hereinafter UCIs), as doctrine states, traditionally belong to it. He noted not only in Italy but in many more countries these market players are subject to various regulations. Professor Annunziata underlined the interest of UCIs case as it confirms how regulation may cover shadow banking, which is far less unregulated than it is thought. Plus, it shows the flexibility of the UCIs tool as it evolved significantly with respect to the time it was introduced in Europe and U.S. many decades ago.

Collective investment had been conceived as a tool for savings collection among the public with the view to invest on secondary markets in liquid or easily liquid securities. It then evolved.

Professor Annunziata paused on the historical evolution of UCIs in recent years proving this tool adaptable and polymorphic and took in consideration their role as an alternative to banks or subjects authorized to provide credit. Such evolution came with other undefined schemes, where credit provision by UCIs is performed in more specific contexts.

The speaker also provided examples of rules allowing private equity UCIs to provide financings to target companies. Such features highlight the diversification of said tools and their openness to schemes winking at sustainable finance themes. Regulation EuVECA or UCITS evidence the above allowing investments in determined activities socially oriented or sustainability-coloured start-up.

Professor Annunziata acknowledged UCIs providing credit directly – and not in conjunction or in association with an investment activity – is a new instrument which appeared few years ago in some systems, as in the Italian one.

Nowadays, he followed, the tool is three-folded: those allowed to provide credit directly – so called supplying UCIs – in some systems including the Italian; investment UCIs – credit UCIs buying credits on the secondary market and securitizing them; and, lastly, restructuring UCIs – a hybrid species performing credit buy-out activity functionally to debit restructuration of one or more issuers and which find themselves in the middle of corporate, crisis and insolvency procedures legislative frameworks.

The growing importance of UCIs in various credit systems poses apical and punctual issues, as highlighted by the speaker.

The first matter Professor Annunziata took in consideration regarded the erosion of the reserve of an activity traditionally provided by banks and non-bank authorized subjects, monopolists of credit provision. However, this erosive phenomenon manifests in multiple ways: in the same years when the UCIs providing credit were introduced in Italy and other countries – just like a bank or a financial company referred to in Article 106 of the TUB – a similar faculty was recognized to insurance companies. Professor Annunziata then cited the case of peer-to-peer platforms. With reference to these, a clear regulatory structure has not been reached. These platforms are located in a grey zone in between the reserved activity and the deregulated activity, which poses an intersectoral "regulatory competition" issue. In fact, these entities may provide credit and are subject to more or less pervasive disciplines – depending on the legal system – but are not subject to the same rules banks and financial companies must comply with.

The Professor notes that regulation of credit UCIs has gone further in some countries whereas in others it has fallen behind.

However, the Professor commented, also in countries who firstly regulated credit UCIs a satisfactory balance point between the various types of UCIs that can operate in various capacities has not yet been found.

The speaker continued illustrating the example of UCIs investing in debt securities, such as mini bonds or other bonds issued by corporate entities. In such cases the approach is hybrid: looking at the substance of the transaction, these UCIs generate credit not only when they buy securities on the secondary market but most importantly

when they underwrite issuances of private companies on the primary market. They find themselves subject to the discipline of UCITS – as they are closer to the traditional scheme of the collective investment scheme – instead of being subjected to more specific or simply different rules of credit UCIs.

Professor Annunziata deemed necessary to understand whether substance shall prevail over form and posed following questions. How shall a UCIs with a portfolio represented in its entirety by debt securities both purchased on the primary and subscribed on the secondary be considered? As a UCIs that invests in financial instruments or as a credit UCI?

Professor Annunziata underlined the issue is not uncommon as the regulation of credit UCIs is more specific in countries that have decided to regulate credit UCIs differently from UCIs investing in debt securities.

In an effort to answer the question, Professor Annunziata observed if form shall prevail over substance, the traced path is one, contrarily, if the substance of the economic operation shall prevail, these UCIs should also be progressively subject to the rules and schemes provided for credit UCIs.

Professor Annunziata then briefly dwelled on the choices that have been made in Italy when introducing and regulating credit UCIs.

First of all, he addressed the decision not to limit the discipline of credit UCIs to so-called reserved UCIs. This decision, the speaker emphasized, is also to be considered worthy of consideration on the international scene: in other countries the choice to reserve such UCIs to the public or to professional investors prevailed. In Italy it was imagined that these UCIs could collect resources they use for investment activities with non-reserved investors relying on the classic gradation of the rules that apply to the different types of UCIs, which, as is well known, are very more flexible for reserved UCIs than those applying to non-reserved UCIs.

The above shall be considered a distinctive trait of the Italian system which marks a choice worthy of being highlighted, although it has not had a concrete and significant application on the market because of the lack of non-reserved UCIs in Italy.

He then highlighted another distinctive trait of the Italian system: the inclusion of activities reserved for AIF managers within the scope of collective management activities.

This choice, the speaker stressed, is far from obvious. He observed in many countries UCIs are not subject to specific discipline or it remains uncertain whether the applicable discipline is that of collective asset management. At the EU level, Professor Annunziata explained, the AIFMD does not unequivocally include discipline of credit UCIs in its perimeter unless the principle of prevalence of substance over form applies.

The third element of the Italian discipline Professor Annunziata examined was the mandatory enrolment to central credit registers imposed to credit UCIs. In the opinion of the speaker, this aspect is the closest point between the rules of the banking business and those of UCIs which, otherwise, are not subject to typical rules of prudential supervision applying to banks or other entities providing credit.

The speech followed providing explanation for this. The removal of these tools from a set of rules applying to banks or other entities traditionally providing credit, albeit applied pursuant to a principle of proportionality, certainly creates dystonia.

The reasons are to be found in the onerousness of capital absorption and in terms of limitations set in the provision of credit. Therefore, the rules concerning the concentration of risks, large exposures applying to banks or those related to capital requirements, are not applicable in this context.

Access to the central risk registers, Professor Annunziata considered, is a measure that on the one hand equates or brings closer the regulation of credit UCIs to that of banks. On the other hand, it is an indispensable tool for the management of UCIs itself which have the duty and the obligation to evaluate the credit assignment. Thus, it ensures a more solid and reliable risk management process.

Lastly, the speaker noted credit UCIs can only provide credit to non-retail clients in our country. Rationale for this provision was to not completely erode the reserve of activity of other market players.

Professor Annunziata then continued his intervention by citing ESMA opinion of 2016: the charts composing it mainly referred to EU countries, nonetheless, some referred to non-EU countries such as Switzerland. For each of these, ESMA pictured the applicable regulations. In some cases, such as in Croatia or France, at the time there were no specific rules for credit UCIs and this dystonia within the EU created an obstacle to the integration of the market at EU level for these products or tools.

The speaker stated such obstacle arises from the divergence of regulatory approaches, as many countries have not yet decided whether and how to regulate these products; on the other hand, the fact that these funds are not included in the perimeter of EU directives does not allow them to obtain the European passport.

Professor Annunziata stressed the importance of different regulation of these products and highlighted even when the scheme of credit UCIs is captured by rules applicable to banking activity, it shall still be borne in mind that the risk transformation activity the UCIs carries out is different from that of banks. While the depositor has a credit right to be repaid of the deposited sums in respect of the bank, whoever subscribes to an UCIs does not have a right to repayment but participates in the overall result deriving from the investment activity.

Professor Annunziata remarked and explained the different functions of credit UCIs when considered in their complexity – i.e. not considering the provision of credit as an isolated activity – and considered the regulatory approach not to entail the subjection of these bodies to the full regulation justifiable. The difference stands objective with respect to the typical banking activity, as credit is the object of the investment activity and the position of a depositor of a bank is different with respect to that of a shareholder of a fund.

The future of credit UCIs, Professor Annunziata reflected, seems to be linked to the debate on the future of NPLs due to the pandemic crisis. Also, it is solidly tied to the ongoing discussions on the possibility of establishing a bad bank at European level or many connected bad banks at national level to avoid the apparently unstoppable coming of NPLs resulting from the pandemic crisis. In this context, credit UCIs could actually play a role as securitization instruments for NPLs and support to the management of the crisis being experienced.

Professor Annunziata deemed necessary to proceed to level playing field of these subjects at EU level. In the study of ESMA – although dated – he found it remains the fact that today these bodies are not included within the EU directives. Importantly: since the NPLs market will have to be addressed in a European context, this problem shall be taken in consideration in the just started revision of the AIFM Directive. This might be an opportunity to clarify whether or not these subjects are included in this directive.

In the meantime, while waiting for something to move at the European level, Professor Annunziata hypothesized what could be done in Italy to incentivize the spreading of these subjects.

The Professor noted that there are some points that are already subject to the regulator attention: the improvement of the outsourcing approach for the performance of core functions of the UCIs, a cross-cutting point of both shadow banking and Fintech. The existing UCIs make extensive use of outsourcing, especially with regard to the creditworthiness assessment activity. The issue arising is what discipline shall be applied to outsourcers who are not supervised subjects but often perform truly essential functions in this market segment.

The second issue addressed by Professor Annunziata concerned the relationship between the figure of the credit UCI and the very rigid position that the case law retained with respect to reserve assets and conduit operations. He explained such conflict arose because in UCIs at hand – especially in those reserved for professional entrepreneurs – the level of independence and autonomy of the manager with respect to the UCIs participants may actually be rather reduced and, therefore, revive the problem of possible violation of the reserve of activity that would stem from using a vehicle formally authorized in Italy to provide credit but which obtains the resources for carrying out that activity from subjects operating in countries that are not "passported" in Italy.

The speaker underlined the relevance of the matter, as it was verified that performing securitization transactions of NPLs, the UCIs scheme , posed problems precisely in the light of the jurisprudence of the Court of Cassation on conduit transactions.

Professor Annunziata also addressed the revision of the rules of "derecognition" of banks' bad loans, in cases the UCIs scheme is used – for example to dispose of non-performing loans. In his opinion, this would deserve to be reconsidered in the context of the pandemic situation.

Finally, the speaker wished for a better clarification of the boundaries of the sub-sectors in order to facilitate the distinction between proper UCIs, UCIs that invest in debt securities, and lending activities of closed-end UCIs providing credit in various forms to investee companies or companies in which they intend to take a stake.

The link between the credit UCIs and the secondary market of NPLs is also clearly mentioned in the Report of the High Level Forum on the Capital Markets Union which, Professor Annunziata pointed out, has now been released a few months ago in a completely different context, with respect to the latest proposals from the European Central Bank itself on the creation of the bad bank for the management of NPLs.

3. The debate

As the introductory reports were concluded, and having provided a detailed overview of the phenomenon under examination tracing the scope of the debate, Professor Zoppini focused on a concept emerged during the interventions: the absence of a necessarily negative connotation. The reasons, he followed, must be sought in the fact that the activity under analysis is fully regulated and, consequently, regular. Nonetheless, in his opinion, this does not mean that the underlying question related to the suitability of the rules and their effectiveness shall be considered solved.

Professor Zoppini left the floor to Doctor Tiziana Togna, Deputy General Manager and Head of the Intermediaries Division of Consob. She began her speech investigating the wording "shadow banking" and the development around this concept in terms of preconceptions.

Dr. Togna reported the Financial Stability Board defined shadow banking as "any form of credit intermediation that involves entities or activities that are partially or completely outside the traditional banking system." On these grounds, the problem that arose was to ensure the risks associated with this activity be well known and regulatory arbitrage avoided.

Dr. Togna stated it was felt the necessity to regulate not too strictly some unregulated shadow banking activities and underlined initiatives followed – both at a European level and at a national level – with the two-folded aim of not depriving investors and the system of forms of investments and of reducing the impact deriving from shocks as that generated by the Lehman Brothers case.

The speaker added that there were also risks not deriving from the use of intermediation channels alternative to banking but from the banking system, in particular risks of credit quality deterioration, of NPLs and to the need to support the

banking system in order to reduce NPLs and then later UTPs. Walking this path, Dr. Togna continued, it was possible to identify a range of better delineated and partly regulated opportunities. Uncertainties in the regulation still remain.

With respect to the opportunity to combine traditional and alternative channels, the speaker identified possibilities in the context of mini bonds, of new forms of collective investment organizations, partly encouraged by the European legislator and partly regulated at a domestic level, such as credit UCIs, with consequent mismatches.

All of this was achieved aiming at two objectives: creating forms of collection helpful to disintermediate the banking system; and enhancing retail customers participation in these forms of financing, facing the challenge of keeping the same standards of protection.

Dr. Togna provided data from the Bank of Italy as of 31 December 2019 related to the phenomenon. With reference to mini bonds, data show there are 12 active operators, 18 funds and around 1.5 billion of assets invested in UCIs under Italian law that invest in mini bonds. With regard to investment in credit, figures tell the following: 17 operators, 26 funds and around 2.1 billion of assets. These sums are relevant but not as significant as the speaker wishes would be achieved.

Dr. Togna questioned whether recognition of UCIs – also at a European level – may allow a more generalized and less strict regulation.

The speaker argued specific choices made in Italy, in particular with regard to credit UCIs, enhanced the participation of professional investors. The possibility to involve retail customers is envisaged but only under certain conditions. At the time Doctor Togna gave her speech, Consob was unable to ascertain interest on behalf of the managers in this regard, thus she assessed the necessary maturity is not yet present. That is because, whenever an investor – especially retail – is allowed to participate in liquid investments or is required a holding period not allowing reimbursement at request, the commitment of the person suggesting this fund grows identifying the suitable client and the amount of the tied investment.

The speaker listed very interesting initiatives at national level in this regard: peers and alternative peers tried to bring retail customers closer to the context covered by this webinar, also thanks to the support of taxation.

Dr. Togna commented that the Italian experience poses a major problem regarding the involvement of retail customers, as a high percentage of savings of retail customers that are not held in pension funds, insurance, fund shares, but as assets under administration.

The speaker identified the real challenge for the future: working to ensure that retail customers can also access this world.

Although MEF presented initiatives to reduce constraints on the subscription of these types of funds, Dr. Togna illustrated, the most suitable subjects to subscribe to this type of products are investors with characteristics of professionalism, ability and knowledge of higher risks, rather than retail investors. Especially where these funds are no longer limited to buying and investing in debt securities but also provide credit or debt restructuring.

The speaker explained today's most advanced forms of intervention of alternative funds involve UTPs managers, meaning that the ability of investors and SGRs must focus on creditworthiness and work symmetrically with respect to what it is required in the banking system.

On the other hand, subscribers of these shares are not as protected as depositors and, therefore, if retail customers are to approach these forms of investment, it is necessary to have a clear understanding of the risks.

Doctor Togna concluded recalling the President of the Republic himself in his speech during "Giornata del Risparmio"; he pointed out that saving is a value that must be employed to contribute to investments. At the same time, the President underlined it must be properly used.

From the above it can be inferred that Supervisory Authorities are very sensitive to the opening of these forms of investment towards retail customers, as the proper precautions must be adopted.

The debate continued with Doctor Fabrizio Pagani's intervention, Global Head of Economics and Capital Market Strategy at Muzinich & Co. He clarified his favour for the term "Finance for growth" rather than shadow banking, as in English shadow banking is too close to "shady".

Doctor Pagani anticipated during his intervention he would address the

intersection of three representative lines of fundamental issues in terms of economic policy.

The first issue the speaker addressed regarded the banking sector.

He commented banks are challenged to reduce the impact on equity of loans they provide – especially with regard to SMEs loans – in compliance with new Basel rules.

Doctor Pagani explained this circumstance is not yet as evident in Italy as it is in other European countries and U.S., where reluctance of banks to lend to companies grows, especially medium-small ones.

Dr. Pagani followed considering the borrower side.

The speaker clarified his wish to develop a wider debate with regard to Italy. In his opinion, Italian companies are capable, by offering their products, to find international markets and to deeply root in markets where they are already present. They also have the ability to renew offers and bring innovation.

According to the speaker, two fundamental issues linked to the size and the bank-centred traits of the system affect Italian companies: governance and equity.

Dr. Pagani then recalled some of the initiatives implemented during the time he was Head of the Technical Secretariat of the Minister of Economy and Finance Pier Carlo Padoan. He aimed at pushing the Italian production system towards forms complementary rather than alternative to the Italian banking system: e.g. private equity funds, debt funds.

However, the speaker underlined all the initiatives implemented focused on the professional investor. That is because professional investors provide equity or financings the companies need with peculiarities that the bank is unable to provide. Plus, the professional investor, whether Italian or foreign, performs a more penetrating and robust control over companies, thus more stimulating.

In the opinion of the speaker, a company benefits from having an international investor in equity or as lender instead of turning to the bank. Even though it may have in-depth examination, it is certainly more stimulated in terms of competitiveness and productivity of the company.

The third topic addressed by Doctor Pagani is that of savings.

The speaker recalled the intervention of Dr. Togna and specified that interesting

initiatives have been put in place with the objective to channel retail savings to the real economy.

The speaker also mentioned his attempts through the so-called "Traditional peer 1", even though the result of this initiative has been limited.

Dr. Pagani underlined how the current government introduced "Alternative peers" which, in his opinion, are an excellent tool despite the fact they struggle to expand for various reasons.

Finally, the speaker asked Dr. Togna whether there is an issue of fairness, since more and more often saver protection is discussed. In particular, he asked whether it is correct to allow wealthy ones to access forms of savings characterized by high returns – e.g. private equity – whereas ordinary investors only access limited investments, which substantially have no return.

Dr. Pagani concluded his speech by briefly addressing UCITS. In his opinion it is correct no to include them under all the rules to which banks are subject, and it is also true that credit funds do not have access to financing from the European Central Bank.

The above stands as a fundamental difference because banks have access to money below market cost and can still obtain gaining on loans, which is not possible for credit funds.

Finally, the speaker reported the European Central Bank's important "warnings" regarding the incoming wave of NPLs. According to Dr. Pagani, this could represent a further reason to the use of alternative financing funds, be it credit funds, private equity funds, parallel lending funds together with banks.

Lawyer Patrizio Messina, Partner at Orrick Law Firm, then took the floor. He firstly reviewed three points emerged during the webinar, in particular the reference Professor Zoppini made to the article of the Economist. Lawyer Messina explained that article stemmed from the approval of the Capital Markets Union. At this moment, the words "shadow banking" were differently approached with a new constructive debate.

With reference to mini bonds, addressed by Dr. Togna, Prof. Annunziata and Dr. Pagani, the speaker positively evaluated the Italian law on mini bonds as it allowed to generate about 20 billion in eight years. Certainly, Attorney Messina admitted, it

might work better, but he also noted the fact that it was copied in Spain and Africa with the support of the World Bank prove it a positive legislative effort. In his opinion, the culture of mini bonds and alternative finance would probably need to be developed. The following issue Lawyer Messina addressed regarded "Finance for growth." Lawyer Messina agreed with considering this alternative finance which may also be called "Alternative finance for the growth of SMEs."

Moving on, he addressed Capital Markets Union. He illustrated it was launched by the Commission in 2015, when the Capital Market Union had to be the way and the perspective to provide alternative finance to small and medium-sized enterprises.

In the midst of the pandemic, the Commission focused on a plan to "encourage financial participation and transform the saver into an investor."

In the speaker's view, the issue consists of how to open up to alternative financing using the savings of sophisticated investors and, with due protection, that of retail investors.

Furthermore, he followed, the possibility of investing not only in clusters arises on the Capital Market Union. Lawyer Messina described in Italy a marketplace only means investing in clusters, a set of companies, while it is not yet possible to invest in a single company. Also, the company may not advertise in order to obtain alternative finance.

Secondly, the speaker dealt with "single investments." A few weeks before the webinar, the Crowdfunding Regulation was issued and will come into force the following year. It addresses single investments for the first time allowing crowdfunding, that is to put even the single company in the position to receive funding.

This, Lawyer Messina commented, although limitedly relevant from a quantitative perspective, puts single investments under the spotlight for the first time in a European regulation. The legal significance is relevant as it can ease the interpretation of the TUB with reference to the provision of the financial activity.

He noted the inclusive character of the Crowdfunding Regulation and he hoped that, as it is self-executing, it will boost the market.

The last matter Lawyer Messina dealt with regarded an international practice. The speaker illustrated that both United Kingdom and France provide investors the opportunity to check the detail of the investment, under certain conditions. The former

in a more articulated way, with investments platforms allowing the investor to do so.

The speaker wished this international practice may lead, with the help and support of the Commission, to a wider application of alternative finance which is essential to solve our systemic crisis as well.

The debate continued and Doctor Camilla Cionini Visani, General Manager of ItaliaFintech, intervened. Her speech analysed empirical data collected by ItaliaFintech during the first months of the pandemic, an association gathering main Italian Fintech companies.

Opening her intervention, Dr. Cionini Visani noted the Italian FinTech sector in not distant times lagged behind global trends (see U.S. and UK). The current year, instead, marked a strong dynamism regarding new realities entering the market: both in terms of turnover and companies that have exceeded one million euro revenue.

However, the speaker underlined that the gap in investments is still there, especially in venture capital and in the early stages of start-ups, less so in FinTech companies that are in a more advanced state of development.

The speaker highlighted three trends.

The first took into consideration the lending data provided with respect to association members active in the lending and capital market segment.

The first nine months of the year bond loans issuances grew tremendously. Even more importantly, in the opinion of the speaker: the growth of the number of companies served by FinTech solutions was exponential and many of these companies look to FinTech tools for the first time.

The association's members issued approximately 1,700,000,000 euros, for a total of nearly 6,000 companies served.

The second trend the speaker underlined is that of the appearance of new FinTech players in the SMEs market segment, a segment increasingly less served by traditional financial services. In recent months, an important number of new FinTech players – framed as banks or under Article 106 of the TUB under the Italian law – have turned serving SMEs through FinTech models into their core business.

These new players are characterized by lighter and different distribution models with respect to traditional models. They integrate their creditworthiness and rating

assessment platforms with methods exploiting artificial intelligence systems provided by other FinTech players who work and evaluate creditworthiness in a different, more advanced way.

The Doctor illustrated how this allows them to grant loans in relevant amounts.

The last trend the Doctor took in consideration concerned accelerating collaborations. This developed in recent months between FinTech and incumbents. The imposed digitalization imposed by the pandemic also pushed incumbents to accelerate the request and the need to change their business processes which, in turn, accelerated the contamination.

The speaker considered this an excellent news for both, since the nature of the latter is complementary, and its niche nature works better with a more universal as that of a traditional bank.

In conclusion, FinTech can make a very significant contribution both to end users, because they see new solutions and opportunities, and for others as an innovation accelerator. If adequately supported with measures at an institutional level, it may make an important contribution both to the real economy in terms of digitization and innovation.

Professor Zoppini intervened in the debate and, before introducing the remaining guests and speeches, he reported an article by the Economist that qualified Covid-19 as a significant accelerator of social and economic phenomena, which will produce effects in terms of digital transfer in 2-5 years.

The following guest to take the floor was Professor Valerio Lemma, Full Professor of Economic Law at the University of Guglielmo Marconi. Referring to what Professor Zoppini said, he argued the article of the Economist probably referred to more advanced realities than the Italian one. He noted Italy leapt forward by ten years during the pandemic, also in terms of relations with the Supervisory Authorities. Nevertheless, he commented evolutionary dynamics have not always benefitted from accelerations: the PEPP, the purchase program implemented by the ECB, and the emergency decrees adopted by the Government have pressured banks requiring them to act beyond the original role of private borrowers of credit institutions.

Professor Lemma noted that the pressure on banks seems to be reducing their full operation because of two trends: the first related to monetary policy, which is subject

to parameters of prudential supervision. It seems banks have to deal with safer creditors, offering low-cost credit even when backed by government guarantee. The result is that banks are left with a credit market segment characterized by low risk and yields.

Professor explained shadow banking system expands under these conditions, or the non-bank intermediation market, according to the latest definition of the Financial Stability Board. In fact, goods, risks and returns transit through this system because of the dynamics illustrated by Professor Annunziata in his speech, or as a result of financial platforms conveying subjects lacking credit the offer by subjects who have it in surplus, willing to accept in some high returns in exchange of risks not compatible with the prudential supervision system implemented by the latest Basel Accords.

The speaker noted that as UCIs are concerned, the context of Covid caused the skip of one of the typical phases of shadow banking: warehousing. He illustrated as the stock of credit portfolios originates in the assets of an UCI issuing financial instruments which readily circulate in shadow banking conduits modifying their quality, duration, maturity, and providing leverage in order to seize the unexpressed opportunities of investors by reaching a combination of risks and returns suitable to be offered on international markets.

Professor Lemma considered dynamism marked technologies, regulatory and financial innovation.

In this regard, the role of Big Techs is that of financiers of subjects who access their platforms. The Professor doubted the activity of Big Techs may remain in the scope of the exception under Article 3 of the Ministerial Decree of Ministero dell'Economia e delle Finanze, which illustrates the activity of granting financing and provides the exception for supply chain credit.

The Professor followed addressing the acceleration mentioned by Professor Zoppini which would provide all financial instruments of shadow banking with the possibility of digital quality and, thus, crypto assets that refer directly to underlying credits. In the speaker's opinion, the recent innovation linked to the European Commission's proposal to create a market for crypto asset seems to address what was until now the very opaque market-based financing of shadow banking.

Professor Lemma illustrated credits originating directly in vehicles suitable for issuing financial instruments and considered technological innovation projects these

financial instruments towards new types of markets. He commented if there will be the regulatory innovation of a new market dedicated to crypto assets, it might be said that shadow banking is finding full legitimacy within a European regulatory context leading somehow to legitimize and make visible all operations alternative to those of banks.

Professor Lemma then acknowledged how strong the competitive pressure towards credit institutions seems to be and imagined Covid might accelerate the role of banks.

The speaker concluded there will be more and more shadow banking and less and less banking, due

to the market conditions at which the latter can be exercised.

Doctor Ignazio Rocco di Torrepadula, Founder and CEO of Credimi S.p.A., brought in the experience of a FinTech operator under regulation. He proposed a comparison between Credimi S.p.A. and a similar English company: Funding Circle.

Dr. Rocco di Torrepadula briefly introduced his company: a financial intermediary enrolled in the register providing loans to small and very small companies and financing itself on the capital markets with securitization transactions. The company began operating in 2017, as all of 2016 was spent obtaining authorization.

The speaker specified that the obtaining of the authorization took, throughout the EU, a year of work, and an application of about 500 pages.

Before being able to start operating on the market, and in order to have the first customer, it was necessary to provide a three-year plan, the existence of sufficient capital to start and also for the following three years. The company also had to prepare more than ten different risk control policies, internal auditing, and certified financial statements. A risk appetite framework, a board of auditors with strict requirements and an independent chairman were required to be assessed and appointed.

All of this, explained Dr. Rocco di Torrepadula, happened before starting the business. While the operating capital needed to start would have been 2 or 3 million, he made clear in reality 8 million were raised because in order to cover the two years that followed the beginning of the business.

The speaker said Funding Circle, in the same year in which Credimi entered the market, had been operating for seven years in England. While Credimi's volumes

were zero, Funding Circle's volumes were £ 1.5 billion, it was close to listing and had already served thousands of clients. In particular, it operated without authorization, or rather with a provisional authorization from FCA.

Therefore, Funding Circle had put in place about 10-20% of the initiatives and activities that have been described to obtain authorization in Italy operating in England. In 2017, Funding Circle obtained its definitive license after seven years of activity. The following year it went public.

The speaker then explained that he compared the two companies to draw the attention to the fact that there are two effects of the regulation.

The first effect is controlling risks and safeguarding stability. Dr. Rocco di Torrepadula pointed out regulation has an extremely strong impact on competition and on the possibility of innovation. In these events regulatory arbitrage is often cited and this creates a certain bitterness in those who have truly dedicated gigantic resources to comply with all the rules. In his opinion – at least in the EU – regulatory arbitrage is substantially impossible, it results in a very strong advantage for existing operators, as the same type of legislation and regulatory investments are imposed on operators of very different sizes, disregarding the principle of proportionality.

The speaker followed indicating that very rarely, when dealing with these issues, he does hear about the impact on competition.

He considered Young FinTech companies are actually companies that often operate without any maturity transformation and stated they are owned by the same operators for which none of these would take a liquidity risk. That is not because they are more ethical but because the company is theirs, so almost everyone knows very well that a liquidity risk means a lethal risk.

When built this way, FinTech companies bring into the system an element of diversity and drive competition and growth. They also act as a hare allowing large operators to innovate.

In the speaker's opinion, this function shall be at the centre of the regulator's focus and noted it is interpreted in a more active way in Great Britain, where in fact every year the FinTech industry generates 10,000 jobs in London alone.

The speaker recalled data provided by Dr. Camilla Cionini Visani's importance because proving Italy largely at the top of the rankings compared to the rest of the EU.

This derives from the fact that, according to Dr. Ignazio Rocco di Torrepadula, Italy is a fabric of small businesses. This meant that many initiatives aimed at these companies were born thanks to the spontaneous Italian entrepreneurial sense.

Finally, the speaker went on specifying the risk he feared is that this entrepreneurship and innovation will not be left free to run its course and develop a market in which Italy is at the top, dedicating effort to regulating risks which they are still not there and not considering growth and competition.

Before concluding the webinar, Professor Zoppini again gave the floor to Doctor Togna, in order to allow her to respond to numerous questions she was addressed with during the debate.

Dr. Togna preliminarily focused on Dr. Fabrizio Pagani's observation and explained how, in her opinion too, it is correct to give the opportunity to participate in profitable investments even for individuals who do not have significant assets.

In this regard, the Doctor reminded the audience that this is one of the problems that led Consob, together with the Bank of Italy, to make a proposal to review the limits for the subscription of alternative investments by retail customers. Today this amount has been set at € 500,000. Analysis were carried out on the regulations in the various countries to try to more adequately calibrate protection and opportunities.

On the other hand, the Rapporteur continued, it is important to underline that also at EU level, in the MiFID II discipline, which somehow characterizes the definition of retail customers. An attempt was made to introduce a new category of retail investors – e.g. the retail investor sophisticated – to try to get out of the quantitative mechanism, which, in the opinion of Consob, risks to ignore the aspect of personalization of the investment.

Thus, Dr. Togna pointed out, the issue is sensitive: one must be aware of the fact that, taking into account the current distribution of the assets under administration, there is a pulverization of the funds currently invested in financial instruments.

The speaker noted there is a high number of investors who hold managed assets below 50,000 euros. She clarified that those to which it refers are invested in financial instruments and not the wealth of Italians.

Dr. Togna specified the underlying rationale: to transit these subjects towards these forms of investment, slightly riskier, through those channels that Dr. Pagani

recalled in his speech.

The speaker summarized the goal is to lead retail investors down that path in a less adventurous way and emphasized this is a topic to reflect on to enhance the principle of alternative finance for growth.

Continuing her reflection, she focused on Lawyer Patrizio Messina's considerations on the topic of crowdfunding. The speaker considered also in lending a further step forward has been made at European level following the Italian experience on equity crowdfunding, which our country was the first to discipline, thanks to the help of the Ministero dell'Economia e delle Finanze.

Crowdfunding initially had numerous constraints, but slowly they have been loosened.

Finally, the last point on which she reflected regarded considerations made by Doctor Ignazio Rocco di Torrepadula and, in particular, on how long the investigation was for the company he represents compared to what happens in other jurisdictions.

In this regard, it is necessary to work a lot on another initiative that has already been put on track at national level, the one of sandboxes, already recognized at European level. An experience is well represented in the UK, where an environment has been created for experimenting, before fully applying the rules governing an intermediary. Dr. Togna stated sandboxes became essential, as they provide the chance to have faster investigations and to experiment and she concluded Consob is very interested in these issues, especially because the operators are faster than the regulators and therefore the latter must accelerate the pace.

Professor Zoppini closed the webinar recalling that the regulatory authorities following the evolution of the market is physiological, given that the latter is by its nature qualified as a dynamic fact. Clearly, Professor Zoppini concluded, the regulation of the phenomenon must be aimed at protecting certainty, safety and trust.