

## EXECUTIVE SUMMARY

The Bank of Italy's *Report to Parliament and the Government* describes the Bank's activities in carrying out its functions and administrative duties.

The Bank of Italy conducted monetary policy operations vis-à-vis Italian banks and contributed to the design of market intervention measures by the competent committees and bodies. **Monetary policy**

Between January and May last year, against the backdrop of severe recession and persistent financial market tensions, the Governing Council of the European Central Bank continued the easing of monetary conditions in the euro area begun in 2008, lowering the rate on its main refinancing operations by a cumulative 150 basis points to 1 per cent. In the course of the year, in order to sustain market and banking system liquidity, the Council also took unconventional monetary policy measures. Three 12-month refinancing operations were conducted from June onwards, and in July a programme of purchases of collateralized bank bonds for a face value of €60 billion was begun.

Eurosystem refinancing to banks in the euro area increased sharply in 2009, in terms of both the number and size of operations. The Bank of Italy conducted 241 operations vis-à-vis Italian banks in euros and other currencies, up from 194 in 2008.

In December, given signs that the money market was getting back to normal, the ECB Governing Council announced that it would gradually restore the pre-crisis monetary policy framework, while confirming its commitment to provide all necessary liquidity to the area's banking system. The changes to the Eurosystem refinancing operations in the first few months of 2010 moved in that direction.

In May 2010, in the face of acute strains in some segments of the government securities market in the euro area the Governing Council decided on a series of extraordinary measures to ensure the banking system's access to credit and to foster orderly conditions in the government securities markets of some countries, with the objective of maintaining the channels for the transmission of monetary policy impulses. The Governing Council accordingly began its Securities Markets Programme of outright purchases of bonds on the secondary market, involving all the Eurosystem national central banks and the ECB; the programme also resumed some of the operations and refinancing procedures introduced in 2008 to cope with the market crisis.

In addition to these measures, there were provisions concerning the use of collateral in monetary policy operations. In April the Governing Council decided to keep the minimum rating for eligibility (except for securitized assets) at investment grade even beyond the end of 2010. In early May it suspended the application of the minimum rating requirement for eligibility of securities issued and guaranteed by Greece.

After contracting temporarily in the first half of 2009, bank liquidity regained the high levels of late 2008, exceeding €890 billion after the first 12-month refinancing operation. In the first five months of 2010 liquidity remained abundant, averaging around €740 billion.

#### **The payment system**

TARGET2 – the European real-time gross settlement system in central bank money for interbank transactions, run jointly by the Bank of Italy, Banque de France and Deutsche Bundesbank – had daily turnover of more than 345,000 payments worth €2,150 billion in 2009. This represented a reduction of 6.5 per cent in volume and 19 per cent in value compared with 2008, reflecting the slowdown in economic activity and the contraction in financial market trading in the euro area.

Despite the considerable strains in the distribution of liquidity due to the financial crisis, TARGET2 did not suffer delays either in transaction settlement or in end-day closing; and the system achieved 100 per cent business continuity.

The value of the transactions handled by the Bank of Italy's BI-COMP retail clearing and settlement system amounted to over €3,000 billion, falling 10 per cent compared with 2008. The total number of transactions settled was broadly unchanged. The Bank proceeded with the adaptation of BI-COMP to the Eurosystem's requirements for Single Euro Payments Area (SEPA) infrastructures.

Work proceeded on the TARGET2-Securities project (T2S), which will give central securities depositories a technological platform for settlement of securities trades in central bank money. The ECB Governing Council has assigned the realization and operation of T2S to the central banks of France, Germany, Italy and Spain. The project's Programme Board, entrusted by the Governing Council with ordinary management, began its work in May 2009. The launch of T2S, originally scheduled for June 2013, will be delayed by 15 months because of the added complexity of responding to users' requests for additional functions.

#### **Banknote production**

The Bank of Italy takes part in the production of euro banknotes and handles their issue within Italy. It is participating in the preparations for the creation of the second series of euro notes, and it contributes to the setting of common guidelines for banknote quality and combating counterfeiting. At 31 December 2009, cumulative net issues in Italy came to €143.2 billion, 2.7 per cent more than the stock at the end of 2008.

#### **The State treasury service and public debt management services**

The Bank of Italy performs the State treasury service at national and provincial level, increasingly by electronic means. Last year over 96 per cent of all payments on behalf of general government and other public bodies were made electronically. Since October 2009 the entities belonging to the single treasury system have had an

electronic system for the settlement of their positions vis-à-vis the State Treasury. This improves the quality of the Bank's treasury service and lowers the operating costs for the entities involved. SEPA will benefit from Italian general government bodies' readiness to use the new standard for more than 21 million payments annually starting as early as the second half of 2010.

On behalf of the Ministry for the Economy and Finance, the Bank executes transactions involving the placement, exchange and redemption of government securities and those for public debt servicing. The Bank also collaborates with the Ministry in setting issue policy. Government securities with a face value of €538.6 billion were placed in 2009, of which €530.1 billion represented domestic instruments. In the first five months of 2010 placements of domestic securities amounted to €217.9 billion.

The Bank of Italy holds and manages Italy's official reserves. At the end of 2009 the value of net foreign exchange assets was €24.6 billion, while gold reserves were worth €60.4 billion. In a context of persistent market volatility, the Bank continued its action to mitigate risks on the assets invested and ensure their liquidity.

**Management of official reserves and the Bank's own financial portfolio**

The Bank's portfolio of euro-denominated financial assets not held for monetary policy purposes includes investments of the Bank's own funds and those earmarked for staff severance pay entitlements. At the end of 2009 the value of its financial portfolio was about €103.6 billion, 91 per cent invested in bonds and the rest in equity instruments. The Bank also manages the investment of the supplementary pension fund for staff hired since 28 April 1993, whose assets are separate from those of the Bank administratively and in accounting terms. The Bank does not invest in the equity of banks.

The Consolidated Law on Banking governs supervision of banks, banking groups, financial companies entered in the special register referred to in Article 107, electronic money institutions and payment institutions. Supervision is entrusted to the Bank of Italy. Its objectives are to ensure the stability, efficiency and competitiveness of the financial system as a whole, the sound and prudent management of intermediaries and compliance with credit and financial law and regulations. The Consolidated Law on Finance specifies that the purposes of supervision of intermediaries active in investment services and asset management are to safeguard confidence in the financial system, protect investors and ensure the stability, sound functioning and competitiveness of the system, in compliance with financial law and regulations. The Bank of Italy is assigned powers of prudential supervision.

**Supervision**

Following the incorporation of the Italian Foreign Exchange Office into the Bank of Italy, the Bank took over the management of the lists and registers of financial intermediaries entered in the general register (Banking Law, Article 106) and its special sections (Banking Law, Articles 113 and 115), financial agents (Legislative Decree 374/1999, Article 3), loan brokers (Law 108/1996, Article 16), and gold dealers (Law 7/2000). The Bank's jurisdiction and powers vis-à-vis these operators are less extensive than those over banks and Article 107 intermediaries. They

comprise verification of fulfillment of the requirements for access to the market and compliance with sectoral rules, notably those for transparency and against money laundering.

The Bank's mandate to combat money laundering and terrorist financing is exercised through the Financial Intelligence Unit, whose tasks include information management, regulation, control and sanctions over the institutions supervised. The Bank of Italy issues regulations for customer due diligence, organization, internal procedures and controls, and the recording of transactions. Controls are effected by means of analyses, both in ordinary and in targeted inspections, at intermediaries' headquarters.

The Bank of Italy's duties include promoting the transparency of banking and financial services and transactions and correct relations between intermediaries and their customers. In October 2009 the Banking and Financial Arbitrator (ABF) began operations. Instituted under Article 128-bis of the Consolidated Law on Banking, the ABF is an alternative dispute resolution mechanism for customer complaints. It provides an additional out-of-court forum for resolving disputes, ensuring effective consumer protection, representation of all the interests at stake, and swift and impartial decisions.

At the end of 2009 there were 788 banks in Italy, 115 investment firms, 204 asset management companies and Sicavs and 3 electronic money institutions, plus Cassa Depositi e Prestiti S.p.A and the Bancoposta division of Poste Italiane S.p.A. The number of financial companies entered in the special register under Article 107 of the Banking Law fell from 491 to 172 last year, owing to the deletion of securitization vehicles, which as of October are entered only in the Article 106 general register. The financial system comprises 1,411 financial companies entered only in the Article 106 general register. Further, at the end of 2009 the special sections of the register included: 19,038 persons not operating on a public basis, 753 collective loan guarantee consortiums, 453 money-changers and 127 credit unions (*casse peota*). There were also 67,585 financial agents, 121,542 loan brokers and 216 professional gold dealers.

Last year international supervisory cooperation focused on implementing the recommendations of the Group of 20, the Financial Stability Board and the European Union for strengthening regulation and supervision in response to the international financial market crisis. The Bank of Italy is an active participant in the reform process begun under the guidelines set out by the G20 heads of state and government at their London and Pittsburgh summits in April and September. Among other things, they call for revision of capital and liquidity requirements, measures to reduce risks at systemically important institutions, and crisis management.

In 2009 and the first half of 2010 the Bank of Italy adopted numerous provisions to safeguard the stability of the system by maintaining adequate levels of capital and reserves at the institutions under its supervision. In implementation of a resolution of the Interministerial Committee for Credit and Savings adopted in July 2008, at the end of 2009 the Bank began a public consultation on draft provisions on the

eligible holdings of banks and banking groups, with the objectives of simplifying and updating Italian regulations and harmonizing them with the EU rules. In May 2010 the Bank began a public consultation on draft supervisory provisions concerning banks' and banking groups' risk assets and conflicts of interest in respect of related parties. The Bank has cooperated in the revision of the regulatory framework governing non-bank intermediaries, with the aim of upgrading this sector and reinforcing the system of controls.

Action to improve banking and financial customer protection was wide-ranging and incisive. A comprehensive reform of the secondary legislation on transparency was enacted in July.

Action to promote the recovery of the asset management sector continued, fostering the independence of fund managers and simplifying procedures. In October 2009 supervisory provisions were issued governing parent banks' direction and coordination of asset management companies belonging to their groups. In March 2010 the Bank began a public consultation on a draft amendment to the regulation on asset management activities that would increase the number of cases in which management companies can resort to standing authorization of the rules of funds not intended for retail customers and lay down organizational requirements for closed-end funds.

Supervisory controls were stepped up, in order to guard against the heightening of some risk profiles due to the financial crisis. The approach established in the Guide for Supervisory Activity issued in mid-2008 was applied in full for the first time, featuring the integration of macro- and micro-prudential analysis and off- and on-site supervision. The new approach focuses on consolidated situations, on risks and on proportionality.

The synergies between micro- and macro-prudential analysis make for timely observation of potential factors of systemic vulnerability, thanks to the integrated use of stress testing and ad hoc investigations. Stress testing permits early detection of factors of risk and the potential effects on capital and income, enhancing the ability of the system and of single intermediaries to cope with critical situations. The coordination between off-site supervision and on-site inspection makes it possible to guard against excessive risk exposure.

Actions with respect to banks, in the form of reprimands or interviews with bank officers, numbered more than 900 last year involving more than 300 banks, or over 40 per cent of all supervised institutions. Apart from actions concerning the bank's overall situation, the most common themes were organizational shortcomings and credit risk.

Actions with respect to asset management companies were designed to obtain the information needed to evaluate the impact of the crisis on their strategies and technical ratios, to prevent the deterioration of their operating equilibrium, and to verify their adoption of the measures needed to overcome the most critical situations.

As regards investment firms, the Bank's interventions involved those in difficulty and also those whose technical ratios had worsened.

Supervision of financial intermediaries entered in the special register referred to in Article 107 of the Consolidated Law on Banking concentrated on the sectors where credit quality had already worsened in 2008: leasing and personal credit in the technical forms of loans secured by pledging one fifth of the borrower's salary or pension, and credit cards. Controls on intermediaries entered in the general register referred to in Article 106 focused mainly on the provision of guarantees and on money-changing, sectors with considerable problems also in the field of consumer protection.

The upward trend in the number of bank inspections continued in 2009, rising to 205 (from 175 in 2007 and 190 in 2008). Another 138 were begun between January and May 2010. Inspections were calibrated according to the size and complexity of the intermediary. The number of on-site controls at large and at problem institutions increased, with flexible, targeted modulation of the range of the controls. Priority was given to evaluation of the procedures for credit risk management and control.

There was a significant increase in sanctions levied last year (from 58 to 113 fines) and in the application of crisis procedures (from 4 to 20). Special administration procedures were instituted at 11 banks, one of which ended in forced liquidation. In most cases, these intermediaries were characterized by serious defects in borrower selection and loan management, with severe irregularities in the activities of corporate bodies and major organizational and control shortcomings, and sometimes even large-scale capital losses.

Again in 2009 the Bank of Italy responded to Government requests for collaboration in connection with parliamentary acts of guidance and control. Again there was very close cooperation with the courts, investigative bodies and the Finance Police, while cooperation with Consob and Isvap on matters of common interest also continued.

In the battle against the infiltration of funds of illicit origin into the legitimate economy, at international level the Bank of Italy has taken an active part in the Financial Action Task Force's recent initiatives to defend the integrity of the financial markets. Anti-money-laundering controls, both on- and off-site, were stepped up. The method adopted for inspections proved valuable in calibrating supervisory interventions according to the individual intermediary's degree of risk. Four inspections directed expressly to money laundering were carried out in 2009.

The Bank continued its consumer protection activity. Significant regulations were enacted in 2009, controls were intensified, and the Bank's commitment in the field of financial education was reinforced.

**Market and payment system  
oversight**

The Bank of Italy is responsible for market and payment system oversight, in cooperation with other Italian and foreign authorities. Last year the Bank took part in the Bank for International Settlements' revision of standards for the operation, organization and control of market infrastructures (payment systems, securities

settlement systems and central counterparties). At the suggestion of the Financial Stability Board, the work towards globally shared rules for over-the-counter markets – including the obligation to use standard contracts and to trade through central counterparties – was stepped up. The OTC Derivatives Regulators' Forum was constituted; the Bank of Italy is a member. Within the Eurosystem, the Bank of Italy helped assess the economic impact of the financial crisis, the contraction of trading in non-collateralized money and financial markets and the heightened aversion to counterparty risk. The Bank took part in simulations of operational crises to test the ESCB's ability to cope with extreme emergency situations and contributed to the work on adapting payment infrastructures and instruments to SEPA standards.

Legislative Decree 11/2010, passed on 27 January this year, transposes Directive 2007/64/EC, the Payment Services Directive, into Italian law. The new rules strengthen the protection of users of payment service providers and institute a new class of market operator, "payment institutions". The Decree also reforms Article 146 of the Consolidated Law on Banking, the legislative source governing the Bank of Italy's oversight activity, for consistency with the Eurosystem's Oversight Policy Framework, adopted in 2009. The article now extends the objectives of the oversight function to user protection, redefines its scope, and attributes to the Bank of Italy the instruments for administrative control. The European reform was completed by Regulation 2009/924/EC, passed on 16 September 2009. The regulation extends to all SEPA payments the obligation to charge the same fees as for the corresponding domestic payments and requires the reachability of all payment service providers for SEPA direct debits.

Last year the Bank of Italy gave its opinion on the new rules for wholesale trading in financial instruments and government securities (Decree 216 of 22 December 2009). These adapt Italian provisions to the MIFID Directive, with new organizational and capital requirements for market operating companies, new rules on alternative trading venues outside regulated markets and transparency requirements for wholesale trades in government securities. In cooperation with Consob, the Bank worked on the transposition of the Shareholders' Rights Directive (Directive 2007/36/EC), which modifies the provisions of the Consolidated Law on Finance governing central management and dematerialization of financial instruments.

Oversight action was directed to ensuring orderly trading and settlement. On 2 February 2009 the collateralized interbank market (MIC), developed by the Bank of Italy together with e-MID S.p.A. and the Italian Banking Association, began operations, giving money market participants the opportunity for anonymous, collateralized trading. The Cassa di Compensazione e Garanzia clearing house (CC&G) introduced new services for the partial delivery of financial instruments and made it possible for traders on the IDEX electricity exchange to take physical delivery in lieu of cash settlement. In July 2009 CC&G was granted the status of "recognized overseas clearing house" by the Financial Services Authority, a requisite for performing post-trading services in the United Kingdom. After the merger of Gruppo Borsa Italiana into the London Stock Exchange Group, analysis of the functions and efficiency of

the Italian subsidiaries of the Group proceeded. A memorandum of understanding between the Bank of Italy, Consob and the Financial Services Authority is in course of ratification.

Within the framework of cooperative oversight, the Bank of Italy took part in controls on the multi-currency Continuous Linked Settlement system for foreign exchange trading and on SWIFT, the global provider of financial messaging services. The Bank also contributed to the Eurosystem's assessment of the Mastercard and Visa schemes and contributed to the assessment of TARGET2's compliance with the Core Principles on Systemically Important Payment Systems, analysing the Italian component to trace the operations of system participants during the financial crisis and also conducting stress tests on participants.

The Bank changed its methodology for the oversight of retail payment systems in Italy, in part to facilitate coordination with other European authorities. Analysis and assessment of technical infrastructures focussed on SIA-SSB, the Italian outsourcer of the European Step2 system, and the Central Institute of Italian Cooperative Banks (ICBPI), the partner of the Dutch Equens SE system. The Bank encouraged the more extensive use of SEPA payment instruments in Italy through the National Migration Committee, which it chairs jointly with the Italian Banking Association. It also examined initiatives to encourage the use of innovative payment instruments and electronic money. In response to the July 2009 initiative of the G8 to lower the cost of immigrants' remittances the Bank of Italy, together with the World Bank, promoted the creation of a website for transparency and comparability of the prices charged by various operators, in particular money transfer companies. Work continued on the project for the transmission of cheques by digital image.

#### **Economic research**

The economic research and analysis conducted by the Bank contributes to the preparation of the monetary policy decisions adopted by the Governing Council of the ECB, by providing supporting documents to the Governor for Council meetings and to the Bank's representatives in ESCB committees and working groups. The Economic Research and International Relations Area produces forecasts on the macroeconomic variables of the Italian economy and the euro area, conducts analyses of the current performances of the main countries and economic areas, and addresses specific economic policy issues. It also provides analysis in support of the Bank's institutional activities in international forums such as the European Commission, BIS, IMF, World Bank and OECD. These activities involve interaction and dialogue with the broader academic community. In 2009 and in the first part of 2010, numerous specific studies on the international financial crisis were conducted. Topics included the performance of the money and financial markets, the repercussions for the monetary policy of the Eurosystem and for that of the other main central banks, the interventions to support financial institution and the role of fiscal policies.

A series of studies bore on the transmission of the global financial crisis to the Italian economy and the effectiveness of possible policy interventions, with special attention to monetary policy transmission and the role of fiscal policies. The

channels through which the global crisis was transmitted to the Italian economy were analysed using the Bank of Italy's quarterly model.

On the problems raised by the global financial crisis and the response of the fiscal policy authorities, a joint research project was completed with economists from the BIS. The project weighed the efficiency of the measures adopted by governments to support banks and other financial institutions since September 2008. A second study developed the analysis of the distortions created by government guarantees in the bank bond markets of the various euro-area countries.

Numerous studies examined the effects of the crisis on the Italian economy. Several explored the country's productive system, hit by the economic turmoil in a phase of restructuring, and tried to assess the prospects for recovery and growth. Others were devoted to the labour market and the working of income support schemes. The Bank continued to monitor the financial and credit markets, especially with respect to the quality of intermediaries' portfolios, access to credit for firms and households, and debt trends. Still other studies examined the role of the financial structure in explaining the lending conditions for firms in the various countries. For a better understanding of the causes and effects of the recent crisis, research on past episodes of crisis in Italy and the United States was undertaken.

A conference held on 26 November 2009, attended by the President of the Republic, concluded the research project into the development lag in southern Italy with the presentation of a detailed report on the gaps between the South and rest of the country, and a discussion of economic policies.

The effects of the crisis on the real economy were also taken into consideration, by examining short-term trends and growth prospects in all the main economies, the pattern of global current account imbalances and trends in the prices of oil and other important commodities.

One of the main areas of research centred on the possible triggers of the abrupt and synchronized collapse in international trade at the turn of 2008, which traditional models have difficulty accounting for.

Several studies covered methodological aspects of monetary and financial statistics. Others examined developments in the ratio of bank lending to funding in the Italian regions and the factors determining the lending/GDP ratio at local level and in the OECD countries. The results of the Bank of Italy's surveys on household income and wealth were used to analyse movements of households between income classes and their degree of financial vulnerability; data from the sample survey on international tourism in Italy made it possible to compare flows of foreign tourists into the country before and during the recent crisis.

Local economic conditions were studied at the Bank's branches by economic research and analysis units, working in tandem with the Economic Research and International Relations Area. The units began to conduct periodical surveys of credit demand and supply conditions throughout Italy, using similar methods to those proposed by the ECB for the Bank Lending Survey.

The Bank's research findings are published in the Bank's own series of publications, in specialist reviews or in books by individual researchers. To raise the profile of the economic research activities it conducts in-house, the Bank also publishes an electronic newsletter in English, aimed at readers in the national and international academic community. In addition to posting them on its website, the Bank disseminates its two main series *Temi di discussione (Working papers)* and *Questioni di economia e finanza (Occasional papers)*, on the SSRN and RePEc networks. Statistics on the frequency of their consultation in 2009 ranked the Bank first among the central banks of the ESCB.

During 2009 and in the first months of 2010, the Library and Historical Archives worked on the arrangement and publication of the bibliography of former Governor Paolo Baffi's writings and the guide to his papers, to mark the twentieth anniversary of his death. The two publications were presented at "The Heritage of Paolo Baffi" conference held in Palazzo Koch on 9 December 2009. A second important initiative is the organization of the exhibition on Italian monetary unification, which will be held in the Spring of 2011 in Rome, as part of the celebrations for the 150<sup>th</sup> anniversary of Italian unification.

#### Statistics

During 2009 and in the early months of 2010 the production of statistics was galvanized by European standardization processes and the growing need for information on the unfolding financial crisis. At the same time, a thorough review was begun of the IT platform for data processing.

The reform of the Bank's statistical reports (known as the accounts matrix), which aims to rationalize and reduce the reporting burdens on banks, became fully operational.

The regulations of the Central Credit Register were reviewed with the dual objective of increasing the transparency of bank-customer relations and simplifying the analysis and monitoring of the credit and financial system, making data on non-performing loans easier to correlate with the supervisory reports.

In the international arena, the review of the Memorandum of Understanding for the exchange of data between European central credit registers was concluded.

Work to reform the system for the compilation of balance-of-payments statistics and Italy's external financial position continued. In the second half of 2010 the new approach, based on direct reporting by non-bank corporations, will be fully phased in, permitting the discontinuation of the traditional bank reporting of cross-border settlements.

With the first edition of 2009 (referring to the data for December 2008), the content and layout of the *Statistical Bulletin* changed radically, to respond to the evolving information needs of users and to take account of new developments in supervisory statistical reporting. Significant innovations have also been made to the content and layout of the *Supplements to the Statistical Bulletin*, to make these publications better suited to users' needs.

The Bank of Italy participates in the work of the international community on economic and financial issues and is active in various forums and levels of cooperation, including the IMF, the World Bank, multilateral development banks, the OECD, the FSB, various regulatory and supervisory bodies, the Economic and Financial Committee (EFC) of the European Union, the Eurosystem, and informal groups (G7, G10 and G20). The chief objectives of cooperation in these fields are to identify and prevent risks associated with the performance of the world economy, safeguard the stability of the global financial system, resolve financial crises and combat poverty.

#### International cooperation

The Bank liaises on an ongoing basis with the government authorities to formulate and represent Italy's views in these forums. In the context of European coordination on the key international questions, the Bank takes part in meetings of the International Relations Committee of the Eurosystem and the EFC's sub-committee on IMF-related questions.

In 2009 the units of the Bank abroad continued to monitor real and financial aspects of the short-term economic outlook in their areas of competence, to maintain contacts with national and international authorities, monetary institutions, banks and financial intermediaries, and to act in an advisory capacity to Italian firms, institutes and banks operating abroad.

The Bank's strong commitment to technical cooperation activities in favour of other central banks and supervisory authorities continued.

In 2009 the Bank cooperated with Parliament and the Government with testimony on economic and financial questions of national and international prominence and on specific supervisory issues. Analyses and proposals were submitted to Parliament on the occasion of the Governor's annual testimony on the public finance bill, and in hearings on the banking and financial system and efforts to combat money laundering. Members of the Governing Board intervened as part of fact-finding on Community proposals to restructure the European regulatory and supervisory environment, as well as in relation to fact-finding preliminary to the examination of the budget documents for the period 2010-12. Other representatives of the Bank testified at Parliamentary fact-finding hearings on the determinants of prices and tariffs and the repercussions for consumers, wage levels, the redistribution of wealth in Italy, derivative financial instruments and the reform of the public finance law. Representatives from the Supervision Area contributed to hearings on European supervision, consumer credit and payment services.

#### Cooperation with Parliament

In the first six months of 2010, a member of the Governing Board gave testimony in the framework of fact-finding hearings on the problems relating to the application of the Basel II accords. Other addresses by Bank representatives dealt with the future "EU 2020" strategy, lending to agricultural undertakings, the review of the legislation on corporate crisis management, the reorganization of the administrative process, the Greek debt crisis, and the urgent budgetary provisions of Decree Law 78 of 31 May 2010. Interventions by the Supervision Area focused on

maximum overdraft charges applied by banks, on non-bank intermediaries and on financial education.

**The organization  
of the Bank of Italy**

In 2009 the Bank continued its reorganization, aimed at enhancing its institutional functions and improving operational efficiency.

There was a complete overhaul of the Banknote Printing Department, as part of the industrial plan to adapt output capacity to satisfy demand at European level.

As part of the branch network reorganization, in 2009 the planned closures were completed on schedule, with a total of 39 of the original 97 branches now having ceased operation; six of these were replaced with as many detached supervisory units of the corresponding regional branches; 25 branches became specialized in services to users, with simpler organizational arrangements.

The reorganization is to be completed this year with the specialization of six branches in cash handling, based on a model aimed at improving services for institutional users in conditions of maximum security and functionality.

In response to the earthquake that struck Abruzzo on 6 April 2009, causing the closure of the branch at L'Aquila, organizational and technical measures were taken that enabled it to resume its activities on 9 April in other structures of the Bank. After the necessary repair work, the L'Aquila branch reopened on 27 July.

Interventions to rationalize working processes continued, mainly through regulatory simplifications and more intensive use of technology. In June 2009, the Bank's new digitalized system for handling documents was launched; the new procedure resulted in the dematerialization of practically all internal document transmissions, while the share of outgoing digitalized correspondence now equals 45 per cent of the total.

At 31 December 2009, Bank staff numbered 7,523. The decrease of 232 with respect to end-2008 is due to the increase in the number of terminations of employment, owing partly to early retirement schemes for the staff of the branches affected by reorganization (who accounted for around 40 per cent of the 404 terminations recorded during the year).

Work proceeded on the adaptation of the institutional buildings to the new requirements arising from the restructuring of the Bank's central and branch administrations.

The information technology sector provided support to the central administration and the branch network of the Bank and to the development of institutional and corporate projects, while pursuing more intensive interaction with users.

The Bank's commitment to planning and implementing European initiatives continued; additional functions for TARGET2 were realized; the architecture and functional specifications of the TARGET2-Securities (T2S) platform were also defined.

The channels of communication between the Bank and its counterparts in the handling of the assets pledged as collateral for monetary policy operations were boosted by web technologies. In June 2010 collateral management via pooling was introduced. To support the activity of the Financial Intelligence Unit the technology for data acquisition and processing was updated and steps were taken to facilitate interaction with operators and with the other authorities in the sector.

During 2010 the Bank will continue to take part in the main European projects. The electronic Treasury programme will be completed; the general government transactions information system (SIOPE) will be revised and extended.

The Bank's accounting system, managed by the Accounting Department, comprises structures in the central administration and in the branch network that report and enter the transactions for which they are responsible.

The Bank's Statute assigns responsibility for checking the accounts to the Board of Auditors which was renewed in conjunction with the approval of the 2009 budget. The financial statements are audited by an independent outside auditor, as required by Article 27 of the ESCB Statute; with the 2009 financial statement the mandate for the audit expired and the Bank held a public tender for the conferment of the new assignment for the period 2010-15. Held at Community level, the competition was conducted based on the open tender procedure; the length of the contract, requirements for participating firms and the other requirements for the assignment were based on ECB recommendations.

In 2009, several changes to the Bank's planning processes were introduced, in order to govern expenditure initiatives more effectively and to simplify procedural obligations.

The financial statements, drawn up in conformity with the reporting and compilation criteria adopted by the ECB and its recommendations, are used in determining the Bank's taxable income for the purposes of corporate tax and the regional tax on productive activities. The Bank of Italy also pays VAT and other indirect taxes and is a tax withholding agent. The fiscal obligations are met by the Tax Department, which manages relations with the financial administration, performs internal consultancy activities, provides technical support to general government bodies and international bodies and organizations, and conducts studies and research on fiscal issues. The Department also handles legal disputes on fiscal issues.

For legal questions and legal research, the Bank has its own lawyers, entered in the special list annexed to the professional register. Above all, the tasks of the Legal Department include the handling of legal disputes in civil or administrative courts. The rulings handed down in 2009 in rulings on suits against the measures taken by the Bank in the exercise of its supervisory functions were again largely favourable. In the area of legal consultancy, there was an increase in the number of legal opinions delivered, involving all the major sectors of the Bank's activity. The Legal Department cooperated in especially intense fashion with the departments responsible for expenditure, consulting on public tenders and on the subsequent

phase of contract execution. Cooperation with the Financial Intelligence Unit in examining specific questions concerning legislation to combat money laundering also continued. Papers on issues of major institutional interest have appeared in the Department's *Quaderni di ricerca giuridica* (*Legal Research Papers*).

The mandate for the Internal Audit Department was aligned with the best international auditing practices, among other things formally assigning the Department to assess internal control and risk management systems and work constantly to improve them. It was decided to institute an internal committee with the mandate to advise and support the General Council and the Governor on audit policy. The review paid special attention to the implications of the Bank's reorganization. Forms of monitoring have been introduced for the early detection of potential anomalies in operational processes. Work began on a system for the self-evaluation of risks and controls in the branch network. Work on an integrated operational risk management system, in line with that planned by the Eurosystem, is nearing completion.