IMPORTANT NOVELTIES TO ITALIAN BANKRUPTCY LAW

Law Decree No. 83/2015 dated 27 June 2015 introduced some important novelties to Italian Bankruptcy Law ("IBL"). It is only the last of several reforms that started in 2005 inspired by the same principle: shifting the focus of insolvency law from the liquidation of the insolvent enterprise to its recovery through a financial restructuring and/or turnaround of industrial operations.

Under this perspective, the main changes introduced by the new law are to the bankruptcy procedures known as "court settlements" ("*concordati preventivi*", i.e. settlements approved by the creditors representing the majority of the claims – but binding on all creditors – and confirmed by the court) as well as debt restructuring agreements pursuant to Art. 182 bis IBL (i.e. agreements entered into by the debtor with creditors representing no less than 60% of the aggregate claims and binding only for those creditors).

1. Interim financing (Art. 182 quinquies IBL): This is the ability of the debtor to obtain from banks (or other third parties, including the shareholders) new financing (ranked senior to all other claims) at the time that the application for a court settlement is filed (but before the court approves the application). Recourse to senior interim financing, previously authorized by the court, was already possible prior to the new law, provided that an expert would attest to the fact that interim financing was instrumental to the most effective satisfaction of the interest of the creditors. With the new law, no attestation of an expert is required, as long as the debtor gives evidence that, pending the procedure for the approval of the application, interim financing is urgently needed to prevent serious and non-remediable harm to the company. The court is required to grant (or deny) its authorization within ten days. No such form of interim financing "as a matter of urgency" is possible after the actual court settlement procedure starts (i.e. after the court decides on the application for court settlement filed by the debtor).

2. Competitive bids from third parties (Art. 163 bis IBL): Proposals for court settlements are frequently predicated on the prospective sale of some or all of the debtor's assets to a third party, whereby all terms and conditions of the sale are already agreed and evidenced in an offer (which is usually attached to the application submitted to the court). In such scenarios, the debtor proposes to pay off its creditors from the proceeds of the sale of assets in accordance with the terms of the offer attached to the application. It was customary that, despite the existence of a binding offer for the purchase of the assets, the court would require the debtor to launch a call for tenders. The reason for this was to stimulate competition and elicit better offers from other competitors. The recent law translates this customary practice into law: if an application for court settlement is filed and it provides that creditors are to be paid out of the proceeds of the sale of assets pursuant to a specific offer, the court is required to launch a competitive tender process. The offers are disclosed at a hearing and, if needed, a competitive bid process takes place.

3. Competitive bids from creditors representing no less than 10% of the aggregate claims (Art. 163(4)-(7) IBL): Before this new law, only the debtor had the right to initiate a court settlement proceeding. The new law provides that, when a proceeding is initiated by a debtor, creditors may also present competing plans for court settlement, provided that they represent no less than 10% of the aggregate claims and that, according to the court settlement plan proposed by the debtor, unsecured creditors are paid less than 40% of the face value of their claims (or 30% in cases of court settlement providing for the continuity of the business). This new tool balances the power of the debtor by giving the creditors a more proactive position in planning the solution to the insolvency of the debtor. Again, competition, not only of offers but also plans for court settlement, is seen as a way to reach a higher degree of satisfaction amongst creditors.

4. Pending agreements (Art. 169 bis IBL): The debtor is given the right to ask the court to suspend, for no more than 60 days, or terminate altogether the agreements in force at the time the application is made. Termination will be authorized in cases of agreements whose continuation is likely to worsen the economic conditions of the debtor. The other party is only entitled to compensation for breach of contract.

5. Debt restructuring agreements with banks (Art. 182 septies IBL): The overall discipline of the debt restructuring agreements (Art. 182 bis IBL) has been materially changed in all cases where the claims of the banks and other financial intermediaries account for more than 50% of the aggregate liabilities of the debtor. In summary:
   (a) Cram-down: Creditors may be divided into classes based on homogenous interests: if the agreement is approved by creditors representing 75% of the claims in each class and all other creditors of the same classes have been informed of the proposed agreement and have been given the opportunity to take part in the negotiations, then the agreement, once signed, is binding for all creditors belonging to the same classes (even for those who did not sign it).
   (b) Cram-down of stand still agreements: If a stand still agreement is reached with banks representing 75% of the claims of banks and all other banks have been informed of the proposed terms of the stand still, and have been given the opportunity to take part in the negotiations, then the agreement, once signed, is binding on all banks.

Among the various other changes brought into effect by Law Decree No. 83/2015, it is worth mentioning the last clause added to Art. 160 IBL. According to this new clause, in cases of plans for court settlements where prosecution of the business activity is not contemplated, unsecured creditors are required to be paid no less than 20% of the face value of their claims. This new clause is aimed at eliminating the misuse of court settlement plans that has often occurred in the past, where debtors sometimes would get away with paying unsecured creditors ridiculously small percentages of the claims (such as 2% or 3%), thereby shifting the largest part of the burden of the settlement onto the unsecured creditors.

NEWS ON THE REIMBURSEMENT OF THE SHADEHOLDER LOAN FOR SPAS

According to a recent ruling of the Italian Supreme Court (*sentenza della Corte di Cassazione no. 14056/15*) **the provision according to which the reimbursement of shareholder loans is subordinated to the payment of any other creditors shall apply also to companies incorporated in the form of a "*società per azioni*" or "*SPA*"** and not only to companies incorporated in the form of a "*società a responsabilità*

limitata" or "*SRL*" as currently provided by the Italian civil code. In particular, the Supreme Court clarifies that this principle shall apply to SPAs with a small number of quotaholders or with family-based ownership (*società per azioni chiusa*).

Specifically, according to regulation on SRLs (article 2467 of the Italian civil code), the repayment of quotaholders' loans to the company shall be made only after the repayment of all the other creditors of the company. If a SRL is declared insolvent within one year of the date of reimbursement of a quotaholders' loan, such reimbursement shall be returned to the company. For the purposes of this provision, a quotaholders' loan means any type of cash injection made in any form into the company if one of the following requirements is met: (i) the company's indebtedness is too high with respect to the net assets of the company and in view of its corporate purpose or (ii) it would have been reasonable to make an equity contribution rather than a loan considering the financial status of the company.

Since the Italian civil code does not provide any similar provisions within the regulation of SPAs, such a principle was considered inapplicable to SPAs until the above-mentioned ruling.

However, the Supreme Court clarified that this principle shall apply to companies regardless of their corporate form on the assumption that such companies are similar in terms of their size and structure of ownership. Indeed, the above-mentioned principle is aimed at avoiding an undercapitalization of the company that may be prejudicial to its creditors due to the preference of the stakeholders for financing the company in the form of a loan rather than an equity contribution.

NEW SET OF RULES ON ANNUAL FINANCIAL STATEMENTS, CONSOLIDATED FINANCIAL STATEMENTS AND RELATED REPORTS

The Italian Government has recently enacted a new set of rules relating to "annual financial statements, consolidated financial statements and related reports of certain types of undertakings" by means of Legislative Decree no. 139 of August 18, 2015 (the "Decree"), implementing Directive no. 2013/34/EU (the "Directive").

The measures set out under the Decree concern the following three areas:

A. The introduction of a report on payments to the Italian government applicable to large sized companies and companies of public interest operating in the extractive and forestry industry sectors (Sections 2 – 5)
B. Amendments to the general regulation relating to annual financial statements set forth under the Italian Civil code which, among others, includes the directors' duty to prepare and file "Rendiconto finanziario" (cash flow statements) along with financial statements (Section 6)
C. Amendments to the regulation relating to consolidated financial statements (Section 7)

The abovementioned integrations and amendments, as well as the other provisions set forth under the Decree, will enter into force on January 1, 2016 and will therefore be applicable to financial statements relating to the financial years starting from that date.

A. New rules on the reporting of payments to the Italian government

The directors of the following types of companies must draft a report on payments to the Italian government (the "Report") on a yearly basis: (i) large-sized companies (i.e. companies which at the financial

year end exceed at least two of the following three criteria: (a) a balance sheet total of EUR20,000,000; (b) a net turnover of EUR 40,000,000 and (c) an average number of employees during the financial year equal to 250) and (ii) companies of public interest (e.g. listed companies, insurance companies, banks, etc.) operating in the extractive and forestry industry sectors.

The directors shall prepare the Report in compliance with Section 3 of the Decree and shall file it with the competent Register of Enterprises within six months of the financial year end; where the directors fail to carry out such a filing or the information provided within the Report is untrue, the directors may be subject to imprisonment of up to one year and to a fine of up to EUR120,000.

As provided under the Directive, the Decree sets forth some exclusions (listed under Section 4 of the same Decree) from the duty to draft and file the Report.

B. New rules on the annual financial statements

Section 6 of the Decree introduces some interesting integrations and amendments to the regulation provided under the Italian Civil Code relating to annual financial statements.

The main novelties concern the introduction of (i) the "Rendiconto finanziario" (cash flow statements) and (ii) simplified rules for small-sized companies.

With reference to the first main novelty the draft financial statements will include, along with a balance sheet, a profit and loss account, and the explanatory cash flow statements.

Said cash flow statements will relate to the financial year to which the financial statements refer as well as the preceding financial year, and will provide:

- An indication of the amount and composition of available cash at the beginning and end of the relevant financial year; and
- an indication of the cash flows deriving from operative, investment and financing activities including transactions with shareholders to be indicated separately.

The second interesting novelty set out under the Decree consists of the introduction of simplified rules relating to the financial statements of small-sized companies.

According to these simplified rules companies which are already entitled to draft financial statements in short form pursuant to Section 2435-bis, and that meet particular dimensional conditions (i.e. during their first financial year or subsequently for two consecutive financial years they do not exceed the limits of at least two of the three following criteria: (a) a balance sheet total of EUR 350,000; (b) a net turnover of EUR 700,000; (c) an average number of employees during the financial year equal to five), will not be required to draft:

- The abovementioned cash flow statements
- An integrative notice, subject to the condition that specific information is provided at the end of the balance sheet
- A directors' report, subject to the condition that specific information is provided at the end of the balance sheet

C. New rules on consolidated financial statements

Section 7 of the Decree sets forth several amendments to Legislative Decree no. 127 of 1991 regarding consolidated financial statements.

The most significant amendment from a legal perspective is the increase of the thresholds triggering the duty to draft financial statements in a consolidated form. Specifically, the parent companies which, along with the controlled companies, have exceeded two of the following thresholds for two consecutive financial years shall prepare consolidated financial statements:

- An active balance sheet of EUR20,000,000 (the threshold currently in force is EUR17,500,000)
- Revenues from sales and performances of EUR40,000,000 (the threshold currently in force is EUR35,000,000)
- An average number of employees during the financial year equal to 250

The other amendments relating to consolidated financial statements set out under the Decree concern the composition of single accounting items and are therefore not particularly interesting from a legal perspective.