



21 June 2005

REFORM OF ITALIAN BANKRUPTCY LAW NO. 267 OF 16 MARCH 1942

1. INTRODUCTION

- 1.1 Following several prominent Italian insolvencies (such as Cirio, Parmalat and Volare) on 16 March 2005 the Government issued Law Decree No. 35/2005 which on 14 May 2005 was subsequently converted into law by Law No. 80/2005 ("**Law 80/2005**"). Law 80/2005 introduces important amendments to the Italian Bankruptcy Law, which has remained largely unchanged since 1942.
- 1.2 The most important aspects of Law 80/2005 concern the relaxation in the requirements to be satisfied for a composition with creditors and reductions in the "look back period" within which transactions may be clawed back by the liquidator.
- 1.3 Law 80/2005 also sets out the principles which are to be followed in a further, general reform of the Italian Bankruptcy Law, for which authority has been given to the Government to bring forward legislation by 10 November 2005 (i.e. 180 days from the publishing of Law 80/2005 in the Official Gazette).

2. THE COMPOSITION WITH CREDITORS

- 2.1 One of the main purposes of Law 80/2005 is to try to help any company in financial difficulties (and not just a large company with over 500 employees for example) to recover from the crisis by finding an arrangement with its creditors on a much more flexible basis (such as the debt equity swap proposed in the Parmalat "*concordato*"). Law 80/2005 reflects, to a certain extent, features of the US Chapter 11 regime on this subject.
- 2.2 Under the previous regime, a composition with creditors was available only to a company which was already "insolvent". Following Law 80/2005, even a company which is "merely" in crisis may enter into a composition with creditors. Therefore, this tool will arguably be used more frequently than in the past, before the "crisis" becomes a full-blown insolvency.
- 2.3 Law 80/2005 has also lowered the "approval" requirements for all compositions with creditors (for both companies in crisis as well as those which are insolvent). Indeed previously a company could be admitted to a composition with its creditors if it could prove not only that it was insolvent but also that the company would be capable of paying 40% (by value) of unsecured creditors and 100% of secured creditors. Whilst this latter condition remains (although there is some debate whether it can still be

applicable), it is no longer necessary that the 40% hurdle be satisfied in relation to unsecured creditors.

- 2.4 In the composition with creditors, the company may now propose:
- (a) debt restructuring and satisfaction of creditors' claims by any means, also by way of transfer of assets, assumption of liabilities, or other transactions, including the allocation to creditors or a company controlled by creditors of shares, quotas or bonds, even convertible, issued by that company or of other financial instruments or debentures;
 - (b) the transfer of some or all of the assets of the company to an "*assuntore*" (*assumptor*). (Creditors or even companies controlled by creditors may act as assumptors, whose shares are allocated to creditors as a result of the composition);
 - (c) the division of creditors into classes according their legal status and similar economical claims;
 - (d) different treatment between creditors of different classes;

2.5 The composition with creditors must be approved, on a vote, by creditors representing the majority by value of all "admitted" claims (the list of the claims "admitted" to vote is drafted by the judicial officer based on the accounting documentation of the company). Subsequently, the composition is in any event subject to final approval by the Tribunal ("*omologazione*") which will assess compliance with all legal requirements. When there are more classes of creditors, all such classes must express their vote separately (the vote shall take place in meetings duly called: no written approval is admitted) and each of them shall approve the composition by majority. The composition with creditors can be approved by the Tribunal even if one or more classes of creditors (but not the majority of them) has voted against, provided that the creditors belonging to those classes which have rejected the arrangement cannot be satisfied in a better way ("*cram down*").

2.6 Also, a pre-agreed composition with creditors is now possible. The company (whether in crisis or insolvent) may file a restructuring agreement with the approval of creditors representing 60% by value of claims, together with an expert's report on the feasibility of the restructuring agreement and, in particular, its ability to satisfy the regular payment of those creditors which have not signed the restructuring agreement. Following its publication in the Register of Companies such agreement is subject to challenge by creditors and any other interested party for a period of 30 days. If no challenge has materialised, the Tribunal will then approve the restructuring. Considering this, it seems possible that the company and the creditors may provide that the agreement is subject to the two-fold condition that no challenges have occurred and the Tribunal has approved the same, although this is not expressly provided by the law.

3. THE NEW REGIME FOR CLAW BACK ACTIONS

3.1 In relation to insolvent companies, first of all Law 80/2005 has reduced the "look back" period as set out in the first column overleaf: where the "look back" period was two years under the old regime, it is now one year; where it was one year, it is now six months. In addition the transactions at risk have in some cases been more narrowly defined.

Look back period: if a transaction took place in this period it is at risk of claw back	Transactions	Comment/Burden of proof
1 year before the opening of the insolvency procedure	1. Transactions in which the value of obligations owed by the insolvent company are greater than a quarter of the value of the obligation owed by the counterparty	Clawed back unless creditor can show it had no knowledge of the company's insolvent state
	2. Payments of debts, due and enforceable on the date of insolvency declaration, not performed with money or other normal payment systems	
	3. Giving of security for a debt not due	
6 months the before opening of the insolvency procedure	1. Giving of security for a debt due and enforceable	As above
	2. Payment of a debt due and enforceable	Clawed back if the liquidator can show that the creditor had knowledge of the company's insolvent state
	3. Transaction for a value	
	4. Giving of security for debt originating at the same time as security	

3.2 Another important change introduced by Law 80/2005 is a list of transactions which are exempt from claw back:

- (a) payment for goods or services made in carrying on the ordinary business of the company in accordance with commercial custom;
- (b) banking remittances, except those that substantially and in a sustained manner raised the indebtedness of the company to the bank;
- (c) sales, at market value, of real estate which is used as the purchaser's home, or that of his relatives to the third degree.
- (d) acts, payments and security over the debtor's assets provided that these have been entered pursuant to a plan which appeared to be capable of rescuing the company from its liabilities and ensuring the rebalancing of its financial situation and on which a "reasonableness" opinion was given by an expert;
- (e) acts, payments and security entered into or given pursuant to a composition with creditors (including a pre-insolvency composition), or pursuant to a controlled administration (*Amministrazione Controllata* - this is another pre-insolvency procedure which has not been amended by the Law 80/2005);
- (f) payment of salaries to employees and fees to consultants;
- (g) payments of due and enforceable debts made in order to obtain services necessary to accede to the composition with creditors and controlled administration procedure.

3.3 The exemptions under (d) and (g) represent, without doubt, an encouragement to try to rescue companies in financial difficulties. Whilst under the previous regime such rescue could take place by means of an equity transaction (which could not be unravelled or clawed back), it now appears possible to achieve such a rescue also by means of a debt

transaction which are not at risk of claw back since such acts, payments or security are exempt from claw back if the requirements under (d) above are met. Furthermore, since fees related to services provided in a rescue transaction are also, to a certain extent, exempt it is more likely that advisers and banks will be disposed to studying and negotiating such rescues.

- 3.4 It is worth pointing out that the "exemption" regime applies only to insolvency procedures commencing after the entry into force of Law Decree 35/2005 (that is 15 May 2005). This means that the exemptions do not apply, for instance, to payments made by Parmalat, Cirio or Volare whose insolvency procedures were already pending at that date..

4. **GENERAL REFORM OF ITALIAN BANKRUPTCY LAW**

- 4.1 Law 80/2005 has also vested the Government with the task of bringing forward a new bill for the general reform of the Italian Bankruptcy Law, reconsidering the procedures to be enforced in case of crisis of the entrepreneurs. The deadline by which such reform must be effected is 10 November 2005 (i.e. 180 days from the publishing of Law 80/2005 in the Official Gazette).
- 4.2 Law 80/2005 sets out the principles to be taken into account by the Government in drafting the reform. These include the acceleration and simplification of the insolvency procedures (regarding all the phases: e.g. ascertainment of liabilities, claw back actions, payment of creditors) and the strengthening of the role of the creditors. Also, it is expressly provided that benefits should be granted to the debtor who cooperates with the commissioner to support and accelerate the procedure. Furthermore, creditors' information rights should be accrued in case of temporary continuance of the insolvent company's business.

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