**Recent changes in the Italian bankruptcy law: a work in progress.**

1. In my last year intervention\(^1\) to the International Insolvency Institute Annual Meeting I exposed the main features of the reform of the Italian bankruptcy law. Then only a part of the reform was in force, referred to the discipline of the pre-insolvency procedure of “concordato preventivo” (composition with creditors) and restructuring agreement. The second part directed to the liquidation proceeding (fallimento) went in force in July 2006.

Now we have the first answers of the Courts to the new law and also a Government proposal to change many points of the reform. The Italian Government should approve the draft in the next weeks\(^2\) and then we should wait for the Parliamentary Committees opinion before that the new Act is enacted. But we can say that the changes are focused to solve many problems arisen in the judicial practice. The main features of the reform will not change.

Between the main purposes of the reform I quoted:

a) To increase the possibilities of an agreement between the entrepreneur and creditors to restructure the enterprise or also to settle the insolvency.

b) To facilitate access to the Court and encourage an agreement among creditors.

c) To create procedures for restructuring through a composition with creditors to settle insolvency in the creditors’ interest. The previous system was intended to admit the entrepreneur to the agreement procedures only when his conduct had been fair. Because of this, many times it wasn’t possible to save the enterprise even when an agreement could be useful for the creditors.

d) To reduce the judge’s power in the procedure and to increase the creditors powers.

e) To reduce the number of bankruptcy cases, reserving the procedure to serious insolvency cases, and to avoid the excessive length of proceedings and the resulting lower distribution to creditors.

To reach these objectives the new agreement procedures provide:

2. The “concordato preventivo” (composition with creditors) procedure. The entrepreneur may ask the Court to be admitted in an insolvency case when the enterprise is only in a crisis situation and not technically “insolvent”. The law doesn’t say when there is a crisis situation, but generally we can say that this situation occurs when there are financial or economical difficulties in the enterprise managing which have not yet reached insolvency. That means that is possible to ask to be admitted to the procedure when it’s still possible to reorganise the enterprise and reach an agreement with the creditors.

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\(^1\) L.PANZANI, *The Reform of Italian Bankruptcy Law*, in International Insolvency Institute, Sixth Annual International Insolvency Conference, Fordham University School of Law, New York City, Monday, June 12 – Tuesday, June 13, 2006

\(^2\) This text is updated to May 2007.
The law does not require that the entrepreneur’s previous conduct must have been fair, but the entrepreneur must present a turn-around plan providing for restructuring of the debt. This plan may provide for payment to creditors in different ways, including attributing to the creditors stock options that change their debt capital into risk capital. If this approach is taken, the assets are transferred to a different enterprise (“assuntore”) that will pay the creditors.

Creditors may be divided in classes, according to the legal and economic nature of the debt; classes may then be given different treatment. In any event, secured creditors (in Italy there are many more secured creditors than in U.S.) must be totally paid.

The entrepreneur must always present an expert opinion on the feasibility of the plan. The Court does not have the power to examine if the debtor’s plan is well founded. The Court may only check if the procedure has been fulfilled according the law. But the Court must check if the classes were well formed according to the law and the nature of the debt. In the first few months of experience, some Courts decided they had the power to control the feasibility of the plan, but probably these decisions were suggested by the old law habits. The former discipline provided the Court’s power to control the plan’s feasibility, but now the law is sufficiently clear. Many Courts decided that they had the power to control if the creditors had sufficient information about the feasibility of the plan and if the expert report provided complete data to make a serious judgement to permit the creditors to vote.

The Government draft should confirm that the Court doesn’t have the power to control the feasibility of the plan, as asked by Confindustria, the Italian industrial enterprises association. But we must acknowledge that many bankruptcy judges don’t agree. They think that is dangerous to waste time calling the creditors to decide in cases when the debtor’s proposal is not serious and is aimed to avoid the liquidation proceeding. According to the Italian system only when the liquidation proceeding is open the public attorney will proceed for the bankruptcy crimes. This is a good reason for the debtor to retard the liquidation opening.

According to the law the judgement on the proposal’s merit is reserved to the creditors who vote on the plan. Only the unsecured creditors may vote. The secured creditors do not vote because their credits must be completely paid. The draft provides now that the secured creditors who cannot be entirely paid because the security’s value is less than the credit amount, must be considered like chirographers creditors and may vote.

The plan is approved if the simple majority of the creditors according to the amount of debt is achieved. If the proposal divides the creditors in classes, all classes must approve the plan. The law provides the cram down. The Court may approve the debtor’s proposal also if only the majority of the classes approved the plan. In this

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3 Between these Courts there is also the Rome’s Court, one of the most important in the whole country.
The minority of the classes must be granted not less than in case of liquidation. The Government draft provides that the debtor’s proposal may be approved by the classes’ majority, but each creditor of the classes of the minority may ask the Court to control if creditors who voted against will receive not less than they could receive with other possible crisis solutions, generally with liquidation procedure.

The debtor’s admittance to the procedure stops the enforcement of claims and the administration of the debtor’s assets is controlled by a judicial administrator (“commissario giudiziale”) appointed by the Court. The administrator must prepare his report on the plan before the creditors vote.

After the creditors vote, the Court must approve the agreement. Creditors and also other people who can be affected by the agreement can request the Court to reject the agreement. In this case and also when the proposal divides the creditors in classes, as said before, the Court has the power to examine the plan.

Other relevant question raised by the new law is to decide what the destiny of the enterprise is when the debtor’s proposal is rejected by the creditors or by the Court. For a part of the Courts the judge has the power to verify if there are the conditions to open a liquidation proceeding; for other Courts the judge doesn’t have this power and must wait that a creditor or the public attorney fill a petition. Probably the Government’s draft will say that the Court must wait the creditor’s petition. In the Italian situation this is a problem because the debtor will try to reach an agreement with the creditors or a part of the creditors outside the Court. The opening of the liquidation will be delayed. In the meantime the possibilities for the trustee to sell the enterprise on the market as a going concern may be reduced.

The most serious problem raised by the new proceeding is that in the last twelve months, the period in which the new law was in force, only a small number of petitions were filled to the Courts. There is an obvious explanation linked to the difficulty to deal with a new law and also with so many different opinions in the Courts. Anyways is not nice to see that the provision of a procedure which should be focused to consent to manage insolvency as a restructuring tool, ask a detailed pre-planning, doesn’t put emphasis on guilt/wrong doing of directors and officers, is not well received by practitioners. We must also consider who these practitioners are. The advisors, the administrators and trustees appointed by the Courts, also the Courts’ judges are the same people who were accustomed to deal with the old law and they must change their mind. This is not easy and will require more time.

3. The Reform introduced other procedures to settle the enterprise’s crisis and to avoid liquidation. The Consensual Restructuring Agreement (“Accordi di ristrutturazione dei debiti”) is not a judicial proceeding, because the debtor must reach an agreement with creditors without the legal protections against enforcement of the creditors’ claims, but when the Agreement is fulfilled the debtor may ask to
the Court to approve the Agreement. The only consequence of the Court’s approval is to exempt the payments made according to the Agreement from the avoidable transfers’ discipline.

The Consensual Restructuring Agreement must be approved by 60% by value of claims. The debtor must present an expert opinion on ability to pay 40% of remaining claims when due, on the terms provided by the original contract. These claims are not affected by the Agreement. For this reason the creditors who did not approve the Agreement may challenge before the Court by requiring verification that their claims may be normally paid. Only if this condition is accomplished may the Court grant the exemption from the avoidable transfer’s discipline.

The law says that the Consensual Restructuring Agreement is enforceable when it is published in the Register of Companies, before the Court’s approval. So the Agreement should remain enforceable for those creditors who gave their approval even if the Court rejects it, thereby not granting the avoidable transfer discipline exemption. For this reason, creditors will probably sign the Agreement only conditioned on the Court’s approval.

As said before the Reform is in force from twelve months and in this period the number of Agreement fulfilled is probably not more than ten of fifteen. The main reason is the lack of rules about the Agreement taxes treatment. Now the Government draft tries to implement the new procedure providing that the Court may grant a stay of sixty days to help to fulfil the Agreement. This is a break in the original project of the new procedure. The idea was to give to the debtor the possibility to reach an agreement with a part only of the creditors, outside the Court, provided that he was able to pay the other creditors according to the contract law. And the Court’s role was only to verify that the agreement was real and with the creditor’s majority and to decide the opposition of the creditors not affected by the agreement. These creditors not affected had the right to be paid at the original expiring of their credits, not after. The stay will affect these creditors who will not receive any utilities from the Agreement.

4. Also the Turn Around Plan (“Piani attestati”) is not a judicial procedure; it is a creditors’ agreement founded on the consensual restructuring of the enterprise, without a moratorium provided by the law. The agreement may provide the enterprise reorganization or also the liquidation and the insolvency or crisis settlement.

Also in this case if the debtor provides an expert opinion on “reasonableness” of the plan, the law accords the exemption from the claw back of payments made if bankruptcy is declared.

The expert’s appointment must be done by the Court when the debtor is a corporation or is quoted in the stock exchange market.

After one year of force of the law it’s difficult to understand if the Turn Around Plan is working well. It’s reached in a very private way and generally the entrepreneur
doesn’t like to inform the public of such agreement. Bank’s experts think that there should be a serious number of Turn Around Plans between debtors and banks, but at the moment there isn’t a good research on this subject to verify if this part of the law is working. The Government’s draft doesn’t change the discipline on this subject.

5. The Reform changed also the insolvency procedure (Fallimento). It’s always a proceeding founded on the enterprise insolvency. Italy does know an insolvency procedure outside the enterprise law. To open the procedure always requires a finding of insolvency and, as said before, the proceeding’s opening is required to prosecute the bankruptcy crimes.

The data on the number of proceedings and on the length of them were very discouraging. The proceedings were too long with a modest result for the creditors. So the Reform tried to reduce the number of the bankruptcy proceedings by:

1. Requiring that the debtor is an enterprise which did investments for more than 200,000 euro in capital or had gross earnings in the last three years of more than 300,000 euro for each year;

2. Requiring that a creditor files a bankruptcy petition state that all the creditors’ claims are not less than 25,000 euro;

3. Establishing that the Court can decide not to verify the creditors’ claims after the bankruptcy procedure opening when there are not assets to pay any of the creditors, except for the procedure’s expenses.

This part of the law is in force from July 2006 and the result is a very serious reduction of the proceedings number. The most known Italian financial newspaper did an inquiry. The result is that generally the number of liquidation proceedings is diminished of 50%, but the data are very different from Court to Court. If in the Naples Court the reduction is in the order of 80%, in Milan in the industrial north hearth of the country the proceedings diminished only of 30%. Also the number of liquidation petitions filled to the Court is reduced. According to the Milan bankruptcy Court president opinion the number of petitions filled by the debtor itself is highly increased.

It’s difficult to comment these data, because the Courts gave very different interpretations of the new law and a part of the difference between Court and Court depends from the different jurisprudence. But it’s clear that the legislator accomplished his task reducing the number of proceedings. Many people, and - the most important thing - the politicians, think that this diminution has been to high.

So the Government draft will change the law. Probably to avoid the liquidation debtor should prove to reach both the requirements: to have done investments for not more than 200,000 euro in capital and to have not had gross earnings in the last three
years of more than 300,000 euro for each year. It’s added that the debts must not be more of 500,000 euro.

Probably it was necessary to correct the law. Italy’s industry is made of middle and little enterprises. So it’s necessary to correct the general discipline of insolvency according with our economics.

The Reform introduced in the Italian bankruptcy law the discharge, reserved to physical persons. Legal entities may not receive this benefit. The discharge is admitted only when the debtor, after the bankruptcy procedure, has paid a part of his debts. The law doesn’t establish a minimum percentage of payments to creditors, but it is necessary that creditors receive at least some payment. Further, a discharge is a benefit, so it is not allowed for debtors who were prosecuted for criminal offences against bankruptcy law or did not cooperate with the trustee and other organs of the procedure. The discharge is admitted only for the debtor and not for the obligations of others. The bankruptcy is reserved in Italy to the commercial entrepreneur. There is no insolvency procedure for the civil debtor. So the discharge is not admitted for consumer debts or for the civil debtor also if insolvency is linked to an enterprise crisis, like in the case of the guarantee offered by the owners of the company.

It’s now clear that it’s not possible to give to the debtor the possibility to receive the discharge and to negate such benefit only because the debtor’s dimensions don’t admit the opening of a liquidation proceeding or because the debtor is not a entrepreneur. The debate on this subject is very heated. The Government draft will not solve this problem, but probably in the next future will have a different draft focused in this subject. It’s clear actually that the bankruptcy reform was not the last word on these topics. The Government must deal almost with other two important themes: the bankruptcy crimes law reform and a discipline of insolvency of company groups.

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