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Italy Significantly Amends Debt Restructuring and Bankruptcy Proceedings

Material changes to the Italian bankruptcy law will likely result in increased interest of investors in the distressed market.

The Italian legislators passed significant amendments to the legal framework applicable to debt restructurings and bankruptcy proceedings with law decree No. 82/2015, subsequently converted, with amendments, in law No. 192/2015 (Law 192).

Law 192 introduces several material changes to the Italian bankruptcy law that will likely result in increased chances of success of debt restructuring schemes as well in speeding up the judicial proceedings for the satisfaction of creditors. Below we will briefly introduce some of the newly enacted changes.

New rules on interim financing

Italian bankruptcy law already allowed debtors to request the competent court to authorize new super senior interim financing upon pre-filing of a “blank” request of authorization of a pre-bankruptcy agreement or upon filing of a project of debt restructuring agreement, provided that an independent expert certified that such financing would increase the chances of creditor satisfaction.

Law 192 now introduces a new option available to debtors during the same phases of the process: they can request that the court authorize the undertaking of new super senior interim finance aimed to address urgent needs relating to the continuation of the business, without providing an independent expert’s appraisal, which can be time-consuming to obtain. The debtor must only release an affidavit whereby the debtor specifies the purpose of the financing and certifies a) that the debtor cannot otherwise access the necessary financial resources and b) that in the absence of such financial resources, the business would suffer an imminent and irrecoverable damage. Such interim financing can only be used if the debtor intends to continue to operate its business as a going concern.

The court will decide within 10 days from the filing of the request.

Law 192 also introduces the possibility for debtors to assign receivables as collateral for the new financing, in addition to the already permitted granting of pledges and mortgages. The new option allows the debtor to exclude the amount of the assigned receivables from the scope of application of the par *condicio creditorum*, immediately satisfying creditors.

The following chart summarizes the main differences between the existing interim finance authorization regime and the newly introduced regime under Law 192.

Interim Finance	Existing regime (182- *quinquies* paragraph 1 of the Italian bankruptcy law)	Newly introduced regime (182- *quinquies* paragraph 3 of the Italian bankruptcy law)
Applicability in case of blank petition for pre-bankruptcy agreement	Yes	Yes
Applicability in case of petition for debt restructuring agreement approval (182-bis, first paragraph)	Yes	Yes
Applicability in case of a proposal of a debt restructuring agreement (182-*bis*, sixth paragraph)	Yes	Yes
Applicability in case of loans identified generically, even if not specifically negotiated	Yes	No
Requires continuation of the business	No	Yes
Need to file an expert's appraisal	Yes	No
The court can request additional information	Yes	Yes
Requires delivery of a debtor's affidavit	No	Yes
Allows debtor to assign receivables as collateral for the new financing	Yes	Yes

The cram down of financial creditors in debt restructuring agreements

The large number of creditors, the different and conflicting interests in the restructuring plan and the consequent length of the negotiations all play a significant role in the outcome of debt restructuring agreements. Prolonged negotiations can in fact prevent access to adequate new finance sources and delay the implementation of a restructuring plan, possibly resulting in the worsening of the distressed situation for all stakeholders (such as shareholders, creditors and employees).

Law 192 aims to overcome these obstacles and simplify the negotiation process (in line with similar legal frameworks applicable in other jurisdictions, such as the English law's scheme of arrangements) by introducing the cram down of banking creditors in debt restructuring agreements where, insofar, no creditor could have been affected, unless it adhered to the agreement. This newly introduced cram-down mechanism does not affect creditors that are not financial intermediaries or banks.

The cram down applies when at least 50% of the debtor's overall indebtedness is of a financial nature and at least 75% of the financial indebtedness gathered in a single class of creditors adheres to the debt restructuring agreement. In these circumstances, the remaining 25% of the financial creditors belonging to the same class of creditors are crammed down.

Law 192 sets rules to guarantee that all creditors are duly informed and allowed to participate in negotiations and to ensure that minority financial creditors would not receive less than they would in a bankruptcy scenario. This last provision is particularly relevant as it will limit the parties' ability to define the payment waterfall. Further, courts will be called to make evaluations taking into consideration, *inter alia*, the amounts to be paid, the terms of payment and any possible variation in the order of seniority set forth by article 111 of the Italian bankruptcy law. Courts will also be called to evaluate that the definition of the different classes has been made properly. Crammed-down creditors can indeed challenge the deal and refuse to be forced into it on the basis of the lack of homogeneity of the classes of creditors.

The same principles apply, mutatis mutandis, to standstill agreements — the minority financial creditors can be forced into the agreement when at least 75% of the financial creditors belonging to the same class of creditors enter into the standstill agreement, provided that an independent expert certifies the homogeneity of the classes and all creditors are duly informed and allowed to participate in negotiations.

However, other commercial creditors (*e.g.* trade creditors) cannot be crammed down. If they do not participate in a scheme, they must be paid within 120 days of the court approval of the debt restructuring agreement or by the date on which the relevant payment obligations fall due.

The general rules governing debt restructuring agreements would still apply to the cram down of banking creditors. In particular:

- The agreement has to be reached with debtors that represent at least 60% of the overall receivables (crammed-down creditors are considered in calculating the threshold).
- Payment of non-adhering creditors must take place within 120 days.
- The agreement is subject to publicity requirements.
- Automatic stay would apply.

Competing proposals of pre-bankruptcy agreements

Law 192 introduces a significant change to pre-bankruptcy agreements. Creditors can now submit alternative pre-bankruptcy proposals to compete with the debtor's proposal.

A competing proposal must meet the following conditions to be allowed:

- The debtor's proposal must provide for the payment of less than a) 40% of unsecured debt in case of liquidation or b) 30% of unsecured debt in case of continuation of the business.
- The competing proposal must be submitted by one or more creditors representing at least 10% of the receivables already accrued at the petition filing date for admission to the pre-bankruptcy proceeding.

- In order to prevent possible abuses, the proposal cannot be submitted by individuals or entities controlled, controlling or under common control of the debtor.

The alternative plan may contemplate an investment by third parties in the debtor, also by way of a capital increase. In case of failure by the debtor to enact the actions in compliance with the approved restructuring plan, the court can appoint a judicial officer to step in, call the extraordinary shareholders' meeting to approve the capital increase and exercise the voting rights in lieu of the debtor's shareholder.

These rules potentially create opportunities for more arrangements between the company, creditors and shareholders, also protecting the creditors from possible abuses by the debtor.

Protection of unsecured creditors

In order to provide a stronger degree of protection to unsecured creditors, Law 192 also sets forth that a proposal of a pre-bankruptcy agreement which does not contemplate the continuation of the business must guarantee the payment of at least 20% of the unsecured debt.

Competing offers in case of pre-packaged deals

Law 192 now provides that, in case of pre-packaged deals where the debtor agrees to sell its assets to a third-party investor, pursuant to an agreement entered into prior to the filing of a pre-bankruptcy agreement with the court, the court must launch a competitive procedure for the sale of the debtor's assets.

The competing offers must be irrevocable, unconditional and comparable.

The initial offeror, in the case the sale is awarded to a third party, is freed from all obligations arising out of the original offer and is reimbursed up to 3% of the price indicated in its offer.

Entry into force

Law decree 83/2015 entered into force on June 27, 2015. Some of its provisions, however, are subject to other terms of entry into force.

In particular, the rules on creditors' competing alternative offers of pre-bankruptcy agreements entered into force on August 21, 2015 and are applicable to pre-bankruptcy agreements initiated after that date. The rules on interim finance and cram down of creditors entered into force on June 27, 2015.

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