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The Italian Insolvency Code: New Tools for Managing a Crisis

The Insolvency Code represents a comprehensive reform of the Italian legal framework of business crisis and insolvency.

Key Points:

- The “alert procedure” (*procedura di allerta*) offers out-of-court and confidential proceedings for overcoming a state of crisis of the debtor.
- New provisions regulate the certified recovery plans (formerly called “article 67 plans”).
- A new common judicial procedure aims to ascertain the occurrence of a state of crisis or insolvency and offers *interim* protection of the debtor’s assets.
- New rules apply regarding debt restructuring agreements, the requirements to access *concordato preventivo* proceedings, and the management of a crisis or insolvency of a group of companies.
- New features reorganize and simplify “debtor-in-possession” financing.

On January 12, 2019, the Italian legislator enacted Legislative Decree No. 14, the “Business Crisis and Insolvency Code” (the so-called “Insolvency Code”), for a comprehensive and organic reform of the Italian legal framework of business crisis and insolvency.

The Insolvency Code will come into force 18 months after its publication in the Official Journal of the Republic of Italy (which occurred on February 14, 2019), with the exception of certain provisions that came into force 30 days after publication.[1]

The authors of this *Client Alert* have reviewed the Insolvency Code with the aim of providing a preliminary and high-level overview of its main new features. These features innovate — and deviate from — the insolvency framework outlined by the former Italian bankruptcy law (Royal Decree No. 267 of March 16, 1942, or the Bankruptcy Law), which shall continue to apply until the Insolvency Code comes into full force and effect.

The “Alert Procedure” and the “Assisted Crisis Management Procedure”

One of the main new features of the Insolvency Code is the so-called “alert procedure” (*procedura di allerta*), out-of-court and confidential proceedings the purpose of which is to promptly identify the symptoms of a crisis and the appropriate measures to overcome it. The alert procedure applies to all debtor conducting entrepreneurial activity, excluding big enterprises,[2] groups of relevant dimension (as identified and defined by the Insolvency Code), and listed companies or joint stock companies whose

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The alert procedure is triggered by the company's supervisory bodies, who are under obligation to notify the management body of the existence of crisis symptoms and set a reasonable timeframe for the management to report on potential initiatives and action taken in that regard. Should the management fail to provide an adequate response, the supervisory bodies shall notify such failure to the competent OCRI (*Organismo di Composizione della Crisi di Impresa*), a newly created body for crisis management. OCRI will then appoint a panel of experts before which the debtor shall appear to report on the reported circumstances. If the panel finds a state of crisis, the debtor together with the company's supervisory bodies and the OCRI shall devise viable measures aimed at overcoming the crisis that are to be implemented without the need to inform or involve the creditors.

The Insolvency Code also introduces the "assisted crisis management procedure" (*Procedimento di composizione assistita della crisi*), which aims to overcome the state of crisis through restructuring of the indebtedness by way of an agreement with the creditors to be outlined, negotiated, and executed with the assistance of the OCRI acting as a mediator.

The Certified Recovery Plans (*Piani di Risanamento Attestati*)

The Insolvency Code contains a full set of provisions regulating the certified recovery plans (*piani di risanamento attestati*) aimed at adjusting the debt exposure of the debtor and rebalancing the debtor's financial situation and the agreements executed in performance thereof.

The vast majority of such provisions actually reflects — with limited amends — the principles and rules commonly followed by the market practice, including that:

- The independent expert's report supporting the plan shall cover both its legal and financial feasibility.
- The plan must envisage the solutions to be adopted in case of a mismatch between the goals forecast and the results achieved. This stipulation reflects certain best-practice principles under which the recovery plan should set out in advance adequate mechanisms in order to ensure that its feasibility is preserved in spite of any critical circumstances that may occur in the course of its implementation (the so-called "self-adjusting plan").

New Features for the Phase Preceding the Access to Judicial Insolvency Proceedings

Among the main features of the Insolvency Code is the introduction of a common judicial procedure aimed at ascertaining the occurrence of a state of crisis or insolvency as a preliminary step before the admission of the debtor to a pre-bankruptcy composition with creditors proceedings (*concordato preventivo*), a debt restructuring agreement (*accordo di ristrutturazione dei debiti*), or a judicial liquidation (*liquidazione giudiziale*).

Notably, the Insolvency Code grants the debtor — as previously provided — with the ability to file with the court a petition in order to seek protection from, *inter alia*, potential initiatives from its creditors for the time needed to prepare and file the documentation for the admission to a *concordato preventivo* or the homologation of a debt restructuring agreement. However, the Insolvency Code imposes several limitations on this protective tool, compared with the Bankruptcy Law. More specifically:

- The period that the court may grant for this purpose has been significantly reduced, which means the debtor risks not being able to timely prepare and file all the documentation before its lapse.

- The stay of interim measures (*misure cautelari*) and enforcement proceedings against the debtor does not operate automatically upon the publication in the Companies' Register of the relevant petition, being subject to judicial approval to occur within 30 days of publication. Furthermore, the Insolvency Code appears to discourage such protection, as it prevents the debtor from acceding to "facilitated restructuring agreements" (described below).

The Debt Restructuring Agreements

Articles from 57 to 62 of the Insolvency Code contain certain provisions aimed at facilitating access to debt restructuring agreements (formerly the so-called "182-*bis* agreements"), the main features of which remain untouched. In accordance with the new provisions:

- The debtor has the ability to request and obtain final court approval of a debt restructuring agreement entered into with creditors representing at least 30% of the aggregate indebtedness of the debtor (as opposed to the 60% minimum threshold otherwise required) if (a) the agreement does not provide for a moratorium of the receivables owed to dissenting creditors and (b) the debtor waives its right to request the court to be granted with any temporary protection, including a stay of precautionary and enforcement proceedings against its assets (the so-called "facilitated debt restructuring agreement").

- The cram-down of dissenting creditors has been broadened, allowing the debtor to extend the effects of the agreements to all creditors (both financial and trade claims). More specifically, the debtor may:

  (1) Organize its creditors into "categories" (each of which shall include receivables being homogeneous by their nature and underlying economic interest)

  (2) Ask the court to extend the effects of the debt restructuring agreement to dissenting creditors included in one or more of such categories, provided that:

    (a) The consenting creditors included in the category (which the dissenting ones belong to) represent at least 75% of the overall receivables included in that category.

    (b) The dissenting creditors have been duly informed of, and invited to participate in, the negotiations, and no higher recovery would be obtained by such creditors in the context of a judicial liquidation proceedings.

    (c) The plan underlying the agreement provides for the continuation of the business and the repayment of creditors (in a significant or prevailing measure) from the proceeds arising from the continuation of the business.

  Notably, the requirement under letter (c) does not apply in a case in which at least 50% of the receivables towards the debtor are owned by financial creditors and cram-down is imposed to dissenting financial creditors, as already provided under the current Bankruptcy Law.

The *Concordato Preventivo* (Pre-Bankruptcy Composition With Creditors Proceedings)

The Insolvency Code redefines certain main features of the *concordato preventivo* (which is now intended as an instrument aimed at managing a state of crisis or insolvency on a going-concern basis), through the introduction of certain provisions, including:

- Allowing the debtor access to a *concordato preventivo* on a going-concern basis (*concordato con continuità aziendale*) only if the continuation of the business results in a significant increase of the resources to be utilised for the repayment of the creditors[3]

- Restricting access to a *concordato preventivo* for liquidation purposes (*concordato liquidatorio)* on the assumption of a more tangible cost-effectiveness of the judicial liquidation compared to such form of *concordato preventivo*

The Insolvency Code submits access to a *concordato preventivo* on a going-concern basis to certain additional criteria, namely:

- Maintaining a minimum number of employees (*i.e.*, not less than half of the average of the employees in place in the two financial years before the filing of the *concordato preventivo* petition) for a period of at least one year starting from the homologation of the *concordato preventivo*

- Satisfying creditors mainly using the proceeds arising from the continuation of the business, including the sale of the inventory

In addition, the term for the deferred payment of receivables assisted by pre-emption rights is extended to two years from the homologation (as opposed to the one-year term currently provided for under Article 186-*bis* of the Bankruptcy Law). In addition, voting rights of the relevant creditors are not suppressed (as provided for under the Bankruptcy Law), but can be exercised for an amount to be determined based on an *ad hoc* formula. Based on the wording of the relevant Insolvency Code provisions, it is unclear whether a deferral of the repayment of receivables assisted by pre-emption rights can be extended to a longer term exceeding the two years (previously this was considered legitimate by the academics and certain case law with respect to the corresponding provisions under Article 186-*bis* of the Bankruptcy Law).

The *concordato preventivo* for liquidation purposes (*concordato liquidatorio*), which is likely to play a marginal role among the restructuring tools regulated by the Insolvency Code as an alternative to the judicial liquidation, will be available to the debtor if:

- Third parties provide financial resources that increase the recovery ratio of the creditor by at least 10% more than what they could theoretically recover in the context of a judicial liquidation.

- At least 20% of the aggregate unsecured indebtedness is repaid. In practice, the application of the *concordato liquidatorio* may be hindered by the fact that, reasonably, no third party would be available to invest resources in a distress company just to allow the sale of its assets and the repayment of its creditors.

There are additional provisions provided for the mandatory creation of classes of creditors, *e.g.*, in case of creditors secured by security interests granted by third parties other than the debtors, for which an *ad hoc* class shall be created, and the regulation of situations of conflict of interest among creditors.

With reference to the procedural aspects of the *concordato preventivo*, the following features are new:

- Replacing the creditors' meeting (*adunanza dei creditori*) with an electronic voting procedure
- Granting the judicial liquidator (*liquidatore giudiziale*) appointed after the homologation of the *concordato liquidatorio* the power to exercise actions aimed at repossessing the debtor's assets and recovering its outstanding receivables, as well as the power to file and cultivate lawsuits against the directors and officers
- Giving creditors the right to oppose the transformation, merger, and demerger of the debtor by filing a challenge against the homologation of the *concordato preventivo*
- Granting a judicial commissioner (*commissario giudiziale*) the power to terminate the *concordato preventivo* upon request by a creditor, in case of breach by the debtor of its obligations under the *concordato preventivo*

Under the Insolvency Code, the court shall have powers to assess the feasibility of the *concordato preventivo* from both a legal and economic perspective, thus going beyond the principle enacted by the Bankruptcy Law, pursuant to which the court shall assess the feasibility of the *concordato preventivo* merely from a legal standpoint and defer to an independent expert (*asseveratore*) the assessment (and declaration) that the *concordato preventivo* is feasible from an economic perspective. In the absence of *ad hoc* specialised bankruptcy courts, it is likely that such economic feasibility assessment will require the appointment of experts by the court itself with foreseeable inefficiencies in the process and the risk of non-homogenous approaches.

The *Concordato Preventivo* and Debt Restructuring Agreements for Corporate Groups

Among the main new features of the Insolvency Code is a set of provisions aimed at allowing single management of the crisis or insolvency of a group of companies, in order to avoid several parallel insolvency procedures at the same time.

Multiple companies in state of crisis or insolvency belonging to the same group can accede a *concordato preventivo* or a debt restructuring agreement proceedings by filing a single petition and on the basis of a single plan for all the group companies or different plans mutually linked if this results in a better recovery for the creditors of each company, in comparison with the recovery that they would theoretically get in the scenario in which each company proposes a separate plan. This requirement shall be assessed taking into account the individual interests of the creditors of each company, in accordance with the surviving principle of separation of assets and liabilities, which prevents the creditors of a company to be satisfied with the assets of another company of the same group.

Such principle of separation of assets and liabilities is tempered by certain provisions of the Insolvency Code, which provide that the restructuring plan(s) may envisage contractual and reorganization transactions, including intra-group transfers of resources, provided that an independent expert certifies that such transactions are necessary (1) for the continuation of the business of the companies pursuant to the restructuring plan and (2) are consistent with the aim of optimising recovery for the creditors of all group companies.[4]

The Insolvency Code sets out a number of provisions aimed at simplifying and aggregating the procedures relating to the companies belonging to the same group, among which the appointment of a single judge (*giudice delegato*) and a single judicial commissioner (*commissario giudiziale*), as well as the

inability to terminate or invalidate a *concordato preventivo* for reasons pertaining to one or multiple group companies, save for the case in which the circumstances on which the termination is based would affect in a significant manner the *concordato preventivo* of the other group companies.

New Features Pertaining to "Debtor-in-Possession" Financing

Receivables arising from "debtor-in-possession" financing transactions will be regarded as super-senior (*prededucibili*) claims by the Insolvency Code,[5] namely:

- Financing granted before the homologation of the *concordato preventivo* or debt restructuring agreement
- Financing granted after the homologation of the *concordato preventivo* or debt restructuring agreement

Specific provisions derogate from the legal subordination of such receivables when the financing is extended by shareholders of the debtor.

In addition, the Insolvency Code provides for certain new features with regard to such financing transactions:

- The abrogation of super-senior ranking (*prededuzione*) for loans previously granted to allow access to procedures and before the filing of the petition, as provided for under Article 182-*quater*, paragraph 2, of the Bankruptcy Law
- The introduction of the following conditions to receive any super-senior (*prededucibile*) financing before the homologation, including evidence that: (1) the debtor is not able to otherwise obtain the requested loan; and (2) without the loan, the debtor's business or the insolvency proceedings itself would suffer severe prejudice
- The downgrading of such super-senior receivables to unsecured in case of false statements, omissions, and fraudulent acts against creditors

Judicial Liquidation

Finally, it is worth dedicating a few words on certain new features of judicial liquidation, which replaces the "old" bankruptcy proceedings regulated by the Bankruptcy Law, whilst preserving its general structure, purposes, and conditions. The new features are aimed at implementing the principles of effectiveness and efficiency.

Several provisions have been enacted with the aim of optimizing the results of the judicial liquidation and at simplifying the procedure with the purpose of limiting costs and containing time and safeguarding certain public interests, among which provisions are:

- Telematic tools for a number of procedural steps
- Automatic termination of "personal" agreements (*i.e.*, those agreements that were entered into based on a particular consideration of the identity of the debtor), unless otherwise agreed between the bankruptcy receiver (*curatore*) and the counterparty to the debtor

- General rules according to which the commencement of the judicial liquidation does not cause *per se* the termination of the business activity
- New provisions coordinating the judicial liquidation proceedings and the employment relationships, in order to safeguard workers' rights

In addition, the Insolvency Code introduces several new provisions in order to make the judicial liquidation more efficient:

- Increased powers and responsibilities of the bankruptcy receiver (*curatore*), including through revised requirements for its appointment, including (1) greater powers of access to the databases listing the assets of the debtors and (2) authority to carry out actions to reorganize the corporate structure of the company in a manner appropriate to the procedure and the exercise of the rights at the shareholders' meeting (if envisaged in the liquidation program)
- Specific provisions relating to the continuation of pending legal disputes and authority of the bankruptcy receiver (*curatore*) after closure of the procedure

Conclusion

The Insolvency Code represents a first and significant step that marks the transition to a new chapter for the Italian insolvency framework, the organic reform of which has been encouraged by both professionals and academics so as to better align such framework to those implemented in other jurisdictions and to allow debtors, creditors, and professionals more economic and efficient tools for managing a business crisis.

The authors believe that this is an ambitious but still imperfect intervention. In this perspective, the long interim period before the Insolvency Code will come into force should allow the legislator and professionals to identify some amendments that are recurrently subject to criticism and doubts with respect to their effectiveness and their ability to streamline the relevant proceedings.

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Endnotes

1. Such are minor provisions with limited impacts on the main provisions contained in the Insolvency Code (such as: (1) Articles 356 and 357, relating to the establishment and functioning of the register of subjects in charge of the management and control in the context of the procedures referred to in the Insolvency Code, (2) Article 359, relating to the creation of the reserved web area for notifications relating to access to the procedures, (3) Articles 363, 364 and 366, containing certain provisions relating to the certification of social security debts (debiti contributivi), debts for insurance and tax premiums, as well as certain amendments to the consolidated law on legal expenses, (4) Articles 375, 377, 378 and 379, relating to the certain organisational aspects of the management of companies and liability of directors of limited liability companies, etc).

2. These are enterprises which, based on their last financial statements, exceed at least two of the following thresholds: (1) value of assets for EUR 20,000,000; (2) net revenues for EUR 40,000,000; (3) 250 employees on average during relevant financial year.

3. In the explanatory memorandum relating to the Insolvency Code, the scenario in which the continuation is "*limited to an insignificant branch of the business*" is represented as an example of a case of "apparent continuation of the business activity" where no concordato preventivo on a going concern basis can be entered into.

4. Art. 285 of the Insolvency Code provides that (1) the detrimental effects of such acts and transactions "*may be challenged by dissenting creditors belonging to a dissenting class or, in the event that classes are not created, by dissenting creditors who represent at least twenty per cent of the claims admitted to vote with regard to a single company, by challenging the homologation of the concordato di gruppo*" and (2) "*the shareholders may only make a claim in respect of a loss caused to their respective companies by the transactions referred to in paragraph 1 by challenging the homologation of the concordato di gruppo*", it being understood that "to finally homologate the concordato, the court shall exclude the existence of a prejudice in light of the off-setting benefits accruing to each company pursuant to the group plan".

5. Lenders providing such financing are granted with a special protection of their receivables called "*prededuzione*" aimed at ensuring their full recovery (such receivables being qualified as "*prededucibili*"). By virtue of *prededuzione*, receivables arising from "debtor-in-possession" financing shall be satisfied, in the context of a subsequent insolvency proceedings of the debtor, with absolute priority over other unsecured and secured receivables owing by the same debtor (with the exception of those secured by mortgage or pledge over debtor's assets). Furthermore, *prededuzione* differs from – and operates on a different level than – security interests over assets of the debtor, which may however secure such receivables either by operation of law (e.g., general or special privileges) or because they have been granted by the same debtor (*e.g.,* mortgage, pledge or assignment by way of security of receivables). In such cases, those receivables qualify as both *prededucibili* and secured, and the relevant creditors shall be entitled (1) to enforce the collateral granted as security in case of non-payment of the debtor and (2) to be repaid in the context of a subsequent insolvency proceedings of the debtor (a) not only with absolute priority over other unsecured and secured receivables (other than those secured by mortgage or pledge), as indicated above, (b) but also in accordance with the ranking provided by the relevant security interest (*e.g.,* prior to other *prededucibili* receivables which are either unsecured or secured by lower ranking security interests).