

Italy's Emergency Budget's Provisions Facilitate Restructurings – Updated

BY BRUNO COVA, ANTONIO AZZARÀ AND PAOLO MANGANELLI

This is an updated version of the *StayCurrent* Client Alert published on 1st June 2010 "*Italy's Emergency Budget's Provisions Facilitate Restructurings*", following the conversion of the relevant emergency decree into law on 30 July 2010.¹

In the context of its €24 billion emergency budgetary measures aimed at addressing current market turbulence, Italy has introduced a range of changes to the Bankruptcy Act² that will have the effect of facilitating restructurings and providing investment opportunities in distressed situations.

The new measures have been enacted through an emergency decree issued in June,³ which was converted into law on 30 July 2010.⁴ The law has confirmed most of the measures of the emergency decree but it has also introduced a few amendments and improvements: (i) a more effective automatic stay period for the Article 182-*bis* procedure; (ii) new financing granted during the *Concordato Preventivo* may be treated as a priority claim after the order of the court that admits the petition for *Concordato Preventivo*; (iii) the risk of criminal charges for both debtors and lenders in connection with transactions executed in furtherance of a *Concordato Preventivo*, Article 182-*bis* or Article 67 procedure is significantly reduced.⁵

On the whole, the final provisions contained in the new law impact three critical areas of Italian restructuring procedures: (i) the protection of new financing granted during both Article 182-*bis* and *Concordato Preventivo* procedures; (ii) the automatic stay period for the Article 182-*bis* procedure; and (iii) the harmonization of criminal provisions with the new restructuring procedures introduced by recent reforms of the Bankruptcy Act.

Additional Protections for New Financing

1. Any financing granted to a debtor in the context of (*i.e.*, bridge financing during the procedure) or to implement (*i.e.*, new finance after the procedure has been approved) an Article 182-*bis*⁶ or *Concordato Preventivo*⁷ procedure is treated as a priority claim in case, after the approval of the Article 182-*bis* or the opening or the approval of a *Concordato Preventivo*, the debtor files for bankruptcy.⁸

Such priority status applies if the following requirements are met:

- (i) The lender is a bank or a financial institution registered with the Bank of Italy;
- (ii) For the new finance provided in the context of or to implement the *Concordato Preventivo*, the court grants the priority claim status within the decision that admits the petition for *Concordato Preventivo*, or finally approves the *Concordato Preventivo*;

(iii) for the new finance provided in the context of or to implement the Article 182-*bis* restructuring agreement, the court approves the final agreement.

We believe that these provisions will have several positive effects.

First, in a *Concordato Preventivo* the lenders may provide bridge financing during the procedure, as the court may grant a priority claim status to the bridge financing when admitting the petition for the *Concordato Preventivo* regardless of whether or not the *Concordato Preventivo* is finally approved by the creditors or the same court. In the Article 182-*bis* procedure, on the contrary, the priority status is subject to the court decision that approves the final agreement.

Also, lenders may be more inclined to provide new finance even in those situations in which there are no sufficient assets to secure the new finance, as they may benefit from a priority status of their claims by operation of law.

Furthermore, these provisions may increase the availability of financial resources to distressed companies, by freeing company's assets that can be used as security for additional financing. Typically, the providers of new finance in distressed situations are willing to make available additional cash only if, in the event of insolvency, the new loans enjoy priority over the pre-existing debt of the borrower. This is normally achieved by securing the new loans with any unencumbered asset and/or by entering into appropriate contractual arrangements with the other financial creditors of the debtor and the debtor itself. Following the new measures, the providers of new finance will now be protected by operation of law and may, therefore, allow the debtor to use its unencumbered assets to obtain additional financing from third parties.

Finally, the complex negotiations and arrangements normally used to secure a contractual priority position will, in certain cases, not be necessary. This may streamline the restructuring process, reducing the transaction costs and shortening the amount of time necessary to close a restructuring.

2. The financing granted to a debtor by its shareholders in the context of or for the implementation of a restructuring procedure under Article 182-*bis* or *Concordato Preventivo* will be eligible for priority status for a portion equal to 80% of the amount due, provided that the Article 182-*bis* or *Concordato Preventivo* has been finally confirmed by the court. This is a significant exception to the equitable subordination normally applicable to shareholders' loans in these circumstances.

We believe that the effect of this amendment would be that additional financial resources will become available to address distressed situations by providing an opportunity for shareholders to inject cash with an investment risk similar to that of a debt provider, rather than the higher risk faced by an equity provider.

The new provision is likely to be of particular interest to private equity funds addressing distressed situations in their portfolios.

3. To avoid conflicts of interest, the new legislation states that the holders of priority claims are not allowed to vote on the *Concordato Preventivo* proposal, nor are they considered for the calculation of majorities respectively required for the approval of a *Concordato Preventivo* or the 60% threshold of the Article 182-*bis* proceedings.

This statement will avoid any potential abuse of the position of the providers of new finance against the interest of the pre-existing lenders.

Extension of the Automatic Stay in Article 182-*bis* Procedure

A debtor who carries out a restructuring under Article 182-*bis* is entitled to benefit from the automatic stay for a period of 60 days following the publication in the Companies Register of the agreement that it has reached with its creditors representing 60% of the overall claims along with an expert's assessment. Before the new measures were introduced by the emergency decree, on the contrary, no protection was granted during the negotiation phase.

Pursuant to the new provisions, a debtor is now allowed to benefit from the automatic stay also for the 60-day period preceding the mentioned publication of the final agreement with the creditors, provided that it has followed the specific procedure introduced by the emergency decree. This allows a debtor to seek and obtain protection also during the negotiation phase.⁹

Moreover, the automatic stay prevents third parties from registering judicial mortgages and other preferential rights over the assets of the company unless it is consensual.

This additional remedy should represent a further incentive for debtors to adopt the new restructuring procedures.

Criminal Provisions

The new provision introduced in the final text of the law¹⁰ significantly reduces the risk of criminal charges for both debtors and lenders in connection with transactions executed in furtherance of a *Concordato Preventivo*, Article 182-*bis* or Article 67¹¹ procedure.

Particularly, the new measures exclude the applicability of charges regarding preferential payments and those regarding simple bankruptcy crimes for deepening insolvency to the above-mentioned transactions.

These amendments remove a significant obstacle to the adoption of the recently introduced restructuring procedures and encourage their use by creating a legally less risky environment for debtors, shareholders, lenders and new equity or debt investors.



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

Milano

Bruno Cova
39-02-30414-1
brunocova@paulhastings.com

Antonio Azzara
39-02-30414-1
antonioazzara@paulhastings.com

Paolo Manganelli
39-02-30414-1
paolomanganelli@paulhastings.com

¹ The previous version of the StayCurrent Client Alert is published on our website <http://www.paulhastings.com/FeaturedPublications.aspx>.

² Royal Decree No. 267 of 16 March 1942.

³ Law Decree No. 78 of 31st June 2010 published in the *Gazzetta Ufficiale* No. 125 of 31 May 2010.

⁴ Law No. 122 of 30 July 2010 published in the *Gazzetta Ufficiale* No. 176 of 30 July 2010.

⁵ Article 217-*bis* of the Bankruptcy Act.

⁶ Please refer to our StayCurrent Client Alert of 9 March 2010 for a description of the Article 182-*bis* procedure and the recent case law, which you can find on our website <http://www.paulhastings.com/FeaturedPublications.aspx>. Risanamento is an example of a restructuring conducted through an Article 182-*bis* procedure.

⁷ The *Concordato Preventivo* procedure consists of an arrangement proposal that, if approved by the creditors holding the majority of the debts, binds all the creditors (including the ones who have not approved it). The procedure is supervised by the court. Examples of restructurings conducted through a *Concordato Preventivo* include Sergio Tacchini and Kartogroup.

⁸ The new law gives priority status to the fees of the independent expert appointed to validate the plan for the *Concordato Preventivo* or the agreement for the Article 182-*bis* procedure, provided that such priority is granted by the court in the order that admits the petition for *Concordato Preventivo* or that finally approves it or the Article 182-*bis* procedure.

⁹ The debtor files the relevant petition with the bankruptcy court together with, among others, a personal declaration under oath that he is under negotiation with the creditors holding at least 60% of the claims, and a declaration of an independent expert (who will likely be the same expert that will express its opinion of the final agreement) that the undergoing restructuring proposal is able to ensure the regular payment of the creditors who are not party thereto. The petition is published also with the local Companies Register. The court examines the petition and sets a hearing within 30 days for debating the request and gives notice of such hearing to the creditors. The automatic stay period starts when the petition is published with the Companies Register. The court then may confirm the relevant petition and set the terms, not exceeding 60 days, for the filing of the final and executed agreement along with the opinion of the independent expert.

¹⁰ Article 217-*bis* of the Bankruptcy Act.

¹¹ Pursuant to Article 67(3)(d) of the Bankruptcy Act, acts, payments and securities over the debtor's assets are not subject to claw-back actions if they are carried out in compliance with a plan, which an expert – duly appointed for the purpose – has certified as being adequate to restructure the debts and make a financial recovery possible. Examples of restructurings governed by Article 67 proceedings include Ferretti and Saeco.