



NEWSLETTER NR. 38 - UNLOCKING RESOURCES FOR UNLISTED ITALIAN COMPANIES: THE NEW PROVISIONS OF THE “GROWTH DECREE”

► *Aim of the provisions*

As a part of a systematic broader governmental action directed to prompt Italian economy and stimulate the Country’s undertakings, the provisions set out by the Law Decree No. 83 of 22 June 2012 (the “Growth Decree” or the “Decree”)¹ aim at expanding and strengthening the spectrum of the financing instruments available to unlisted companies and at creating new investment opportunities for institutional investors (Article 32).

By facilitating the access to capital markets for private companies the Italian Government is bringing the Italian system in line with the most advanced European jurisdictions dealing with bond markets.

► *Beneficiaries of the new regime*

The main beneficiaries of the new regime are *unlisted companies* (i.e., any company that does not have financial instruments listed on a regulated market or on a multilateral trading facility) other than banks and “micro-enterprises”, as defined by the EU Commission Recommendation 2003/361/CE of 6 May 2003².

¹ According to Italian law, *Decreto legge n. 83 del 22 giugno 2012* comes into effect immediately and, in order to become law, it shall be ratified by the Parliament within sixty days from its adoption. In the process of conversion of the Decree into law, the Parliament may amend its provisions; the Decree will expire if not ratified by the Parliament within the above mentioned period.

² A “microenterprise” is defined as an enterprise which employs less than 10 persons and whose annual turnover and/or annual balance sheet does not exceed € 2 million.

► *Main Tax advantages*

One of the most significant innovations of the new regime on bonds issuance concerns the extension to unlisted companies of certain favorable tax provisions which so far were applicable only to listed companies. In particular, under the new tax rules private companies:

- will benefit from the exemption on the 20% withholding tax on interest and other payments paid on bonds and similar securities provided that the securities (i) are held by investors resident in “white list” countries³ and (ii) are listed for trading on a regulated market or on a multilateral trading platform. This is an important and long-awaited development, in particular by foreign investors, that will enable unlisted issuers to access international capital markets without having to bear a tax gross-up cost⁴;
- will be able to deduct interest paid on bonds and similar securities within the limit of 30 percent of EBIDTA, provided that such securities are held by “qualified

³ In other words, the beneficial owners of the income received must be established or resident in a jurisdiction with which Italy has concluded a double tax treaty containing an exchange of information clause.

⁴ The rule which provided for the application of a 20% substitutive tax on interest and other proceeds (now being removed with reference to the transactions at issue) is set out in Presidential Decree No. 600 of 29 September 1973; a first step in the direction now confirmed by the Decree was taken by the Italian Government with Article 23 of Law Decree No. 98 of 6 July 2011, which, subject to certain conditions, allowed the application of a 5% withholding tax on interest payments made by Italian companies to foreign non-resident entities in connection with inter-company loans to on-lends funds deriving from the issuance of corporate bonds.



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investors”⁵ that are not (either directly or indirectly) shareholders of the issuer.

► *Removal of the limitation provided for by Article 2412 of the Civil Code on the issuance of notes*

Under the past legislation, Italian unlisted companies could only issue bonds for a sum not exceeding twice the net value of the corporate share capital and reserves (*patrimonio netto*) resulting from the last balance sheet (Article 2412 of the Civil Code). By removing said limitation, the Decree significantly expands the opportunities for the issuance of corporate notes – and thereby access to debt capital markets – by unlisted companies.

Indeed, pursuant to the Decree the limitation above will no longer apply to issuers, *also if they are unlisted*, that issue notes to be listed on a regulated market or on a multilateral trading facility, or notes that incorporate a

⁵ The definition of “qualified investor” includes two broad categories of “professional clients”: (i) professional clients by express provision of law, such as banks, investment firms, other authorized and regulated financial institutions, insurance companies, collective investment undertakings, investment management companies, pension funds and management companies for such funds, financial intermediaries acting for their own account on commodities and commodity-based derivatives, persons whose exclusive activity involves trading on their own account on financial markets with indirect membership of clearing and settlement services [...], other institutional investors, stockbrokers, large-sized companies meeting certain asset/revenue requirements, institutional investors whose principal activity is investing in securities, including companies dedicated to the securitization of assets and other financial transaction; and (ii) professional clients “upon request”, such as individuals meeting certain experience and asset criteria; see, in this regard, Article 26(1) d) and Attachment No. 3 of Regulation No. 16190 of 29 October 2007 of *Consob* (the Italian Securities Exchange Commission).

right to subscribe to or to purchase the issuer’s stock i.e. notes convertible into shares (Article 32, paragraph 26, of the Decree).

► *New financial instruments: profit participation bonds*

One of the most innovative aspects of the Decree is the introduction of an hybrid capital instrument: a bond with a maturity of no less than sixty months that may contain subordination and profit participation clauses (the “profit participation bond”).

On the one side, the subordination clause will establish the priority of the claims of the issuer’s creditors (other than the shareholders) over those of the noteholders.

On the other side, the participation clause will reflect a floating interest rate consisting in a *fixed component*, which cannot be lower than the applicable official rate of reference (*tasso ufficiale di riferimento*), and in a *variable component*, linked to the profits of the issuer, which shall be paid annually within 30 days from the approval of the balance sheet of the issuer⁶.

The Decree sets out some specific tax advantages also for this type of instrument: if the terms and conditions of the bonds include the subordination clause and prevent equity distribution (other than dividends out of profits), the variable component can be deducted for corporate tax purposes⁷.

⁶ The criteria for the calculation of the “variable component” must be determined at the time of the issuance and may not be modified afterwards. Such criteria have to be objective and may not depend on variable corporate resolutions adopted each financial year.

⁷ The general rule, contained in Article 109, paragraph 9, of Presidential Decree No. 917 of 22 December 1986



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Moreover, the variable component of the remuneration will not be subject to the “usury law” provisions of Law No. 108 of 7 March 1996, thereby allowing a significant participation in corporate profits without pre-set quantitative limitations.

The provisions concerning profit participation bonds do not apply to securities listed on a regulated market or traded on a multilateral trading platform (Article 32(4) of the Decree); the effect of this excluding provision is unclear, since it is not specified whether, by effect of the Decree, also listed securities may be issued in the form and with the contents of participating bonds; interpretative efforts will take place on this issue in the first phase of implementation of the new regulations to determine the scope of their application.

► *New regulatory regime of commercial papers*

With the purpose of fostering the development of this relatively unpopular financing tool - at least in the Italian financial markets - the Decree deeply amended the legal framework of commercial papers (“*cambiali finanziarie*”). The main amendments are as follows:

- (i) the reduction of the minimum maturity period down to one month and the extension of the maximum period of maturity up to 18 months⁸;

provided that if the interest rate is linked to the issuer’s financial results no deduction is allowed.

⁸ The previous regulation, set out in Art. 1(1) of Law No. 43 of 13 January 1994 provided for a maturity of at least three months and no more than twelve months.

- (ii) the possibility to issue commercial papers in dematerialized form in order to encourage their circulation;
- (iii) the setting of a quantitative limit: the total amount of outstanding commercial papers cannot exceed the issuer’s “current assets” (“*attivo corrente*”), as indicated in the last financial statements;
- (iv) the application of the same favorable tax treatment now applicable to the bonds, as described above.

► *Issuance of non-listed securities by private companies*

Under the new regulatory regime, unlisted companies may issue bonds, commercial papers or profit participation bonds subject to the following requirements:

- (i) a Sponsor has to be appointed for the issuance and the underwriting stages (an exception is provided for large-sized companies)⁹;
- (ii) the last financial statements are to be audited by a certified auditor;
- (iii) the notes must be issued to, and intended to be traded exclusively among, “qualified investors”¹⁰ that are not, directly or indirectly, shareholders of the issuer.

These requirements *do not* apply to bonds that are offered to the public and are listed on a regulated market or multilateral facility (Article 32(4)).

⁹ Large sized companies are companies meeting or exceeding at least two of the following thresholds: (i) 250 employees; (ii) annual revenues in excess of € 50 million; (iii) annual balance sheet in excess of 43 million.

¹⁰ See footnote No. 6 above.



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► *The Sponsor*

As mentioned above, small and medium-sized enterprises are required to engage a Sponsor if they wish to issue notes.

Pursuant to Art. 32(14), the following entities may act as a Sponsor: banks, investment companies, asset management companies (SGRs), harmonized management companies, open-end investment companies (SICAVs), financial intermediaries registered in the list provided by Article 107 of Legislative Decree No. 385 of 1 September 1993 and banks authorized to provide investment services in Italy, even if their registered seat is outside of EU.

The tasks of the Sponsor are the following:

- i. ensuring the liquidity of the securities and entering into specific undertakings with the issuer;
- ii. holding in its portfolio, until maturity, a certain amount of securities¹¹ (the requirement resembles similar risk-retention requirements brought by EU legislation within securitization transactions pursuant to the so called “retention rule”);
- iii. evaluating, at least every six months, the market value of the bonds;
- iv. classifying the issuer into a risk category, taking into account the EU Commission Communication 2008/C 14/02 concerning

¹¹ Such amount shall be equal to (i) at least 5% of the aggregate value of the bonds issue, if the overall issuance does not exceed € 5 million; (ii) an additional stake equal to 3% of the issuance value in excess of € 5 million, up to €10 million; and (iii) an additional stake equal to 2% of the issuance value in excess of € 10 million.

the revision of the method for setting reference and discount rates¹².

► *Final remarks*

In a period of scarcity of bank credit, the provisions above of the Growth Decree may represent an opportunity for unlisted companies to access capital markets.

As mentioned above, Article 32 poses some interpretative doubts - in particular on the role of the Sponsor and the nature and possible use of profit participation bonds - that will be clarified in the process of conversion of the Decree into Law and by expected implementing regulations.

In the meanwhile, due to the immediate entrance into force of the Decree, all actors of the corporate and financial arena can take advantage of the new provisions.

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¹² The Sponsor will have to publish the background information for the rating and update it as necessary.