



NEWSLETTER NO.39

THE NEW 'COMPOSITION WITH CREDITORS' IN LIGHT OF THE RECENT RULES INTRODUCED BY ARTICLE 33 OF LAW DECREE NO. 83 OF 22 JUNE 2012

► Law Decree No. 83/2012, providing "Urgent Measures for the Country Development"

The Law Decree No. 83 of 22 June 2012 (the "Decree"), effective as from 26 June 2012 and converted into law with amendments¹, has introduced important measures aimed at stimulating the Italian economy (also referred to as "*Decreto Sviluppo*").

The Decree, consisting of seventy articles, provides for a heterogeneous set of rules including, among the others, significant amendments to the Italian Bankruptcy Law².

► The Purpose of Article 33 of the Decree

Article 33 of the Decree plays a central role in supporting the revitalization of a failing business by significantly changing the structure of the 'Composition with Creditors' or 'Business Reorganizations' (*i.e.* the *concordato preventivo*)³.

New provisions, clearly inspired by Chapter 11 of the US Bankruptcy Code, have been added with the aim to solve certain issues that in the past were an obstacle for a successful reorganization of the debtor's business.

Specifically, the new rules try to find an answer to the following concerns:

- The insufficient protection of the debtor during the preparation of the filing and the Plan;
- The debtor's difficulties in obtaining new financing during the phase of its request for the Composition with Creditors (*i.e.* "*interim financing*"); and
- The absence of provisions supporting the conduct of the business during the phase of the filing before the approval of the Plan.

The main purpose of the new provisions is to take care of these concerns in order to facilitate a quick filing with the understanding that the sooner a Petition is filed the easier it is to find solutions allowing for a fresh restart of debtor's business.

► Quicker Access to the Composition with Creditors

One of the most innovative profiles introduced by Article 33 of the Decree relates to the commencement of the case: the debtor is now entitled to simply file a straightforward Petition with the Court, while in the past it was required to file, together with the Petition, the Plan and a support opinion from an independent expert confirming the feasibility of the Plan. As a consequence, the filing required significant time and resources that could not be devoted to the conduct of the business and that exposed the debtor to the risk of harassment by creditors.

Under the new rules, the Plan as well as the supporting documents and opinions⁴ may be filed within a period of time set by the Court of 60 to 120 days from the filing of the Petition, term which can be extended by up to 60 days.

¹ Law No. 134 of 7 August 2012, effective as from 12 August 2012, except for certain rules related to the civil proceedings, which are effective as from 11 September 2012.

² Royal Decree No. 267 of 16 March 1942.

³ *Concordato preventivo* is an Italian bankruptcy procedure available to a debtor in crisis – either an individual, company or other entity – to restore or liquidate its assets avoiding bankruptcy. The discipline prior to the Decree has been recently reformed by three significant interventions: Law No. 80/2005, Legislative Decree No. 169/2007, and Legislative Decree No. 78/2010.

⁴ The documents required by Article 161, paragraphs 2 and 3, of the Italian Bankruptcy Law.



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These set of new rules allow the debtor, on the one hand, to immediately benefit from the protections granted by the commencement of the case, the so called "Automatic Stay", with the effects substantially similar to the ones provided for by §362 of the US Bankruptcy Code⁵ and, on the other hand, to postpone its focusing on the Plan to a time when the business is conducted with the supervision of the Court.

Thus, the Italian Legislator intended to solve the problem, frequently occurred in the practice, of the irreversible worsening of the crisis during the stage of drafting and collection of the aforementioned materials, quite often coupled with the informal negotiations with the main creditors.

Duties of Publicity

Pursuant to new Article 161, paragraph 5, of the Italian Bankruptcy Law, within one day after the filing, the application must be published on the companies' register.

This provision has been coordinated with Article 168, paragraph 1, of the Italian Bankruptcy Law, according to which the date of the publication of the Petition on the companies' register is the trigger date to identify the debtor's creditors (as opposed to the date of the filing of the Petition with the Court, as it was in the past).

⁵ While the application and related documents are being prepared, the operations of the debtor and relationships with the creditors are not protected. Only after filing the application, the debtor and third parties may benefit from the typical protection of the composition with creditors, including (i) a stay of enforcement actions against the debtor's assets, (ii) the prohibition to pay the pre-petition creditors, and (iii) the requirement for the debtor to obtain Court authorization to carry out activities outside the ordinary course.

This form of publicity permits to the third parties negotiating with the debtor to be informed about the filing of the Petition and the consequences thereof.

Composition with Creditors Aimed at Ensuring Business Continuity

The Decree⁶ has introduced the category of Composition with Creditors in an expectation of continuation of the business (going concern), either on a stand-alone basis or through the sales or the contribution of the assets to a new entity (Newco).

If the debtor seeks the approval to continue the business, then the Plan must contain (i) the details of the profits and losses expected from the continuous conduct of the business, together with the required financing and the methods of repayment; (ii) the expert opinion supporting that the conduct of the business is functional to enhance the creditors' recovery; and (iii) the request, if any, to freeze the secured creditors for up to one year.

Furthermore, in the context of this special form of composition with creditors, there are relevant provisions related to the Executory Contracts and the possibility to participate in public tenders.

On the one hand, Executory Contracts may not be terminated because of the composition with creditors proceedings, despite any contractual provision to the contrary⁷.

On the other hand, for contracts with governmental authorities the Decree sets out conditions under which a debtor admitted to the

⁶ Article 33, Letter h) of the Decree has introduced new Article 186-*bis* of the Italian Bankruptcy Law.

⁷ As a result, the typical clauses included in commercial agreements providing for the termination by law in case of bankruptcy of a party have no effects.



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Composition with Creditors proceedings may continue to perform those contracts⁸ or participate in public tenders, as an exception to one of the principles set forth by the Code for Governmental Agreements⁹.

The above provision is softened by the necessity of the company subjected to the special form of Composition with Creditors of the following requirements:

- To provide for the opinion of an independent expert certifying the compliance of the agreement with the plan and the reasonable capability of fulfillment of the plan itself in the context of the tender;
- To recur to the “*avvalimento*” rules under Article 49 of the Code of Governmental Agreements; and
- Not to take the qualification of ‘agent’ company in the event it participates in *A.T.I.* (*i.e.* Temporary Association of Companies).

► Debtor’s Protections

After the commencement of the case and until the Plan is either approved or rejected by the creditors¹⁰, in order to ensure the continuity of the business, the debtor benefits of special protections, as follows:

- the actions in the ordinary course of business can be implemented *autonomously*, while the

⁸ New Article 186-*bis* of the Italian Bankruptcy Law provides that the admission to the composition with creditors proceedings does not prevent the continuance of agreements with the governmental authorities, provided that an independent professional certifies the conformity of the plan and the reasonable capability of fulfillment on behalf of the company in crisis.

⁹ See Article 38, paragraph 1 of the Governmental Agreements Code that expressly prevents the companies subjected to bankruptcy proceedings, including Composition with Creditors, to participate in public bids.

¹⁰ See Article 163 of the Italian Bankruptcy Law.

activities falling outside the ordinary course (*i.e.* the extraordinary transactions) require notice, a hearing and *Court authorization*;

- the financing of the debtor’s operations during the Case is ranked with a “super-priority”¹¹ claims in case of bankruptcy¹², with the further clarification that the relevant payments are not subject to claw-back actions.

The purpose of such amendments – and in particular the “super-priority” rank – is to allow the debtor in crisis to continue its business, overcoming the obstacles that prevented third parties – and particularly suppliers – from contracting with him during the stage of the pre filing.

► The Bridge-Financing

Inspired by the First Day Orders of the US Bankruptcy Code¹³, the Italian Legislator has intervened to solve one of the main criticalities arisen out of the preexisting system, which is the absence of a bridge-financing allowing the debtor to obtain quickly the financial resources needed to continue its business activity and execute the Plan¹⁴.

New Article 182-*quinquies* of the Italian Bankruptcy Law permits to overcome the limits of the past regulations¹⁵, granting the debtor the

¹¹ Super-priority claims have to be satisfied prior to those of unsecured creditors in the event that the debtor is subsequently declared bankrupt.

¹² Court authorization may also be granted for loans identified only by kind or amount, even if the debtor has not yet negotiated the terms. In addition, the Court may authorize the debtor to grant security interests with regard to such loans.

¹³ See Section 364 of the United States Bankruptcy Code.

¹⁴ See Article 182-*quinquies* of the Italian Bankruptcy Law introduced by Article 33, letter f) of the Decree.

¹⁵ Under Article 182-*quater* of the Italian Bankruptcy Law, the credit for super priority are the ones that are expressly authorized by the Court at the time of the admission to the composition with creditors or at the time of approval of the



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opportunity to seek from the Court, simultaneously with the filing of the Petition, the authorization to receive loans¹⁶, provided that an independent expert certifies that such loans are functional to enhance the creditors' recovery.

The Court may authorize the granting of loans identified only by kind and/or amount, which have not been negotiated yet, on the basis of the report of the independent expert, after obtaining further information, if needed.

► Administrative Expenses

A further novelty introduced by Article 182-*quinquies* of the Italian Bankruptcy Law concerns the debtor's possibility to ask to the Court, simultaneously with the filing of the Petition, the authorization to pay selected suppliers of goods or services, provided that an independent expert certifies that the such supplies are essential for the continuation of the business and functional to enhance the creditors' recovery.

It is now clear that Italian Legislator's perspective is directed towards the business continuity, which is not protected as a value itself but only as long as it is functional to enhance the recovery of the creditors as a whole. Particularly, the Italian Legislator would help the debtor in crisis allowing the continuity of the supply of strategic goods or services (such as raw materials or transports) essential to the business, which otherwise would be jeopardized irreparably in case such suppliers' claims were not prioritized.

Plan. Since such approvals come at a later stage from the filing of the Petition there is a period of uncertainty. The new provision aims to cover this period of certainty granting to the Court the possibility to issue early orders, upon request by the debtor.

¹⁶ See Article 111 of the Italian Bankruptcy Law.

Since the allowance of priority claims reduces the amounts of the estate available to prepetition creditors (and is in conflict with the general principle of *par condicio creditorum* (*i.e.* equal treatment of all the creditors), Courts will be very careful in issuing their authorizations and will allow administrative claims only to those suppliers whose supply is essential, according also to the expert opinion, for the continuity of the business.

► The Role of the Expert

Finally, the new provisions have strengthened the role of the independent expert, by broadening the number of cases in which an expert opinion is required to confirm debtor's compliance with relevant matters, such as the compliance with the *par condicio creditorum*, as a basis for the decision of the Court¹⁷.

Under the new rules¹⁸, in the event of material misstatements or omissions of facts, the expert will be personally liable and will be punished under criminal law with jail and other sanctions.

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¹⁷ See Article 33, letter f) of the Decree, which has introduced Article 182-*quinquies* of the Italian Bankruptcy Law.

¹⁸ See Article 33, letter l) of the Decree, which has introduced Article 236-*bis* of the Italian Bankruptcy Law.