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Recent developments in bankruptcy law in Italy

15 September 2020

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The most recent evolution about bakruptcy law in Italy are:

a) The approval of new Crisis Code (D.l: 14/2019)
b) The final implementation of over-indebtedness procedure (law n.3/2016)

Both of the above evolutions are in line with the aim to enhance the possibility to solve the entrapreneurs's crisis as soon as possibile and avoid the worsening of the failure and the risk of penal consequences on their shoulders with a lot of problems for their future .. **It's better to be safe than sorry** !

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Crisis Code (D.l: 14/2019)

The main of those is the new Crisis Code, introduced with Legislative Decree 14/2019 that will be applied only starting from 1.9.2021 (because of COVID 19 consequences ..before the current crisis the d-day was 15.8.2020) requires companies to take appropriate actions to comply with certain parameters and efficiency criteria that certify the company's health.

The main issues of these new Code are :

1.**THE ALERT PROCEDURES**

The Code provides for a series of measures to facilitate the timely emergence of the business crisis before the full-blown insolvency.

The reporting of the difficult situation is entrusted to a double channel, as well as to the autonomous activation of the entrepreneur: one is triggered by the intervention of the internal control bodies and the other by institutional creditors, INPS and tax authorities.

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The alert measures are aimed above all at inducing the company to immediately adopt, **in a completely autonomous way**, the necessary measures to remove the causes of the crisis and, where this does not happen, to identify and implement these measures with the assistance of the **OCRI** , a special body set up **at the Chamber of Commerce**, opening, if necessary, a negotiation with at least the most important creditors destined to lead to an out-of-court agreement **having the value of a recovery plan**.

In the event of a negative outcome of both these phases, the company is invited to make use of one of the bankruptcy procedures envisaged and finally, **but only in the hypothesis of inertia and clear insolvency,** there is a communication to the Public Prosecutor to verify the existence the conditions for requesting the opening of the liquidation procedure guided by the Court.

2. THE COMPOSITION BODY OF THE BUSINESS CRISIS

To manage the alert procedure will be the Corporate Crisis Composition Bodies **(OCRI)**, set up at each Chamber of Commerce.

The first step will be the hearing of the debtor and the corporate control bodies. The OCRI must seek mediation and assist the entrepreneur to seek some kind of agreement with creditors. In this context, at the request of the entrepreneur, protective measures are possible, **for a maximum period of nine month**s (stand still clause), from enforcement actions. In both cases, when insolvency occurs also due to the debtor's responsibility, the procedure can "close" with reporting to the Public Prosecutor for the declaration of opening of the judicial liquidation

3.INTERNAL CHECKS IN THE COMPANY

The reform broadens the obligation of the internal control body, statutory auditor or auditor to adopt, by amending the rules of the Civil Code.

The new control structure is mandatory when, for two consecutive years, one of the following limits has been exceeded: 1) assets in the balance sheet: **four million euros**; 2) revenues from sales and services: **four million euros**; 3) employees employed on average during the year: **twenty units**

The Code imposes on the control bodies (statutory auditors and single auditor) the obligation to report:

as a forecast of non-sustainability of debts with the cash flows that the company is able to generate or of the inability to ensure the going concern in the following six months, in any case noting as an index of the crisis repeated and significant delays in payments already manifested.

When the crisis indices are found, the control body must **formally notify the directors by assigning a deadline of no more than 30 days to report on the solutions identified and the initiatives undertaken**. In the event of an inadequate response or failure to take the necessary measures within the next 60 days, the control bodies must inform OCRI without delay, providing any useful information notwithstanding any duty of secrecy.

The inert auditors are jointly liable with the directors for damages coming from the continuation of activities without the necessary initiatives; the auditor is, therefore, one of the parties responsible for the cases of bankruptcy criminal law focused on the worsening of the failure. There are **three indices** that trigger the official reporting to the OCRI by public bodies:

Tax liabilities: the Tax Office is obliged to report when the VAT payable is equal to at least 30% of the turnover of the last Tax Return .

Social security debts: Inps must communicate when the debtor is over six months late in the payment of social security contributions exceeding the threshold of 50 thousand euros

Tax credits to be collected: The collection agent is activated when the sum of the credits entrusted for collection, self-declared or definitively ascertained and expired for more than 90 days, exceeds the threshold of 500 thousand euros for sole proprietors and, for companies , one million euros

On top of those , some indices set by the National Council of Chartered Accountants and Accounting Experts have been proposed, which have yet to be approved by the legislator but which already provide a clear path .

The mechanism developed provides a fair sequence that sees 7 parameters to be considered.

1. Net worth , in case of negative net worth not covered by shareholders

2. DSCR (Debt service coverage ratio) below 1 . The DSCR is calculated as the ratio between **the free cash flows expected in the following 6 months** that are available for the **repayment of the payables expected in the same period of time**. Values of this index higher than 1 highlight the prospective sustainability of the debts over a 6-month horizon, values lower than 1 the relative inability.

Moreover , If the net worth is positive and if the DSCR is not available or is considered not enough reliable due to the inadequate quality of the forecast, other **5 indices are adopted**, with different thresholds depending on the sector of activity:

1. **index of sustainability of financial charges,** in terms of the ratio between financial charges and turnover;

2. **capital adequacy index**, in terms of the ratio between shareholders' equity and total debt;

3. **liquid return index of assets**, in terms of the relationship between cash flow and assets;

4. **liquidity ratio**, in terms of the ratio between short-term assets and short-term liabilities;

5. **social security and tax debt index**, in terms of the relationship between social security and tax debt and assets.

4. THE ADEQUATE ORGANIZATIONAL STRUCTURE

The new article 2086 of the cod. civ establishes the entrepreneur's duty to: «set up an organizational, administrative and accounting structure appropriate to the nature and size of the company, also based on the timely detection of the crisis of the company and business going concern, as well as to take immediate action for the adoption and implementation of one of the instruments provided for by the law for overcoming the crisis and recovering business continuity ".

The entrepreneur must, therefore, provide his organization with tools to monitor the risk of loss of business continuity: that is, the appropriate organizational structures, defined by the law. The real challenge for the future is verifying the sustainability of business continuity. **The objective is to force companies evolve from an approach in which evaluations are carried out only once a year, on the occasion of the approval of the financial statements, towards a system that instead provides for constant monitoring.**

The link between failure to adopt the structures and liability for damage is often due to the absence of a treasury forecasting system that allows the directors, in the face of prospective indications of a lack of financial flows, to take prompt and adequate action with remedies aimed at addressing and solve the business crisis. This can occur not only in situations of loss of capital but in circumstances that are index of crisis , for example when there are mispayments of taxes and social contribution, overdue suppliers or banks take on significant dimensions. . These are circumstances that can all be monitored preventively through the treasury system.

The lack of a cash flow monitoring system (and therefore the absence of adequate organizational structures) will now be an element to be evaluated among the causes of the crisis also in the context of liability actions for directors and control bodies.

5. THE CRISIS COMPOSITION PROCEDURE

After the first reporting of the indices of the crisis made to the debtor, in the event of his inaction or an inadequate response, the system of alert measures introduced with the Crisis Code **provides for the reporting** by the internal control bodies of the companies and / or by qualified public creditors **to the Corporate Crisis Settlement Body (OCRI),** which is set up at each Chamber of commerce.

Furthermore, the debtor can contact the OCRI directly to start the crisis settlement procedure.

When the report is received by the supervisory bodies or public creditors or when the debtor files the request for the settlement of the crisis, the OCRI representative appoints **three experts.** The board must schedule the hearing of the debtor within **fifteen days** of reporting or submitting the request, also calling the statutory auditors if it is a company with a control body. **This procedural phase is under confidentiality**

If it emerges that the report made by the control body or public creditors is well founded, the body assists the debtor in identifying the necessary measures to remove the crisis situation, then setting a deadline for their implementation. When it does not appear feasible to overcome the crisis situation, without finding a solution agreed with the creditors, with redefinition, for example, of the payment times or partial reduction of credits, the procedure for assisted **settlement of the crisis is opened**. The opening takes place only at the request of the debtor. In this case, the panel of three experts instructs one of them (rapporteur) to follow the negotiations, fixing theirs conclusion of the maximum term **of three months**, which can be extended by a further **three** only in case of initial positive results.

The experts must acquire or prepare an updated report on the equity, economic and financial situation with a complete list of creditors and the causes of pre-emption.

To facilitate the development of negotiations, avoiding unilateral initiatives by individual creditors, following the initiation of the assisted settlement procedure, the **debtor may request the necessary protective measures** from the Court (such as the prohibition to initiate or continue executive and precautionary actions and prohibition of registration of judicial mortgages), the deferral of the obligations connected with the reduction of the capital and the temporary inoperability of the cause of dissolution of the company due to reduction below the legal minimum or loss of capital.

The procedure, in case of a positive outcome of the negotiations, leads to the **written agreement** with the creditors which is filed with OCRI and is not known to third parties, unless the parties agree to register in the business register.

The agreement produces the effects of **a certified recovery plan.**

If an agreement with the creditors is not reached, OCRI invites the debtor to submit an application for access to a procedure for regulating the crisis or insolvency, that is, an application for a homologation of a restructuring agreement or the opening of an arrangement with creditors or liquidation.

To facilitate solutions other than judicial liquidation, the panel of experts, enhancing the preliminary activity carried out during the crisis settlement procedure, certifies the truthfulness of the company data.

The attestation of the feasibility of the plan underlying the restructuring agreements or the arrangement with creditors is, however, **in any case left to another professional chosen by the debtor.**

To encourage the timely emergence of the business crisis, in addition to the reporting mechanism by the control body of the companies and by the Revenue Agency and INPS, the legislator has provided for **reward measures** in favor of the debtor who promptly submits an application to the OCRI for the opening of the procedure for assisted settlement of the crisis or also, alternatively, directly, the request for a homologation of a restructuring agreement or for the opening of an arrangement with creditors or judicial liquidation.

The initiative is timely if adopted **within three months** (for the Ocri application) or **six months** (in other cases) starting from the exceeding of the payables thresholds to employees or suppliers established in the indices prepared by the National Council of Chartered Accountants already for the purposes of the reporting obligation by the statutory auditors or the auditor

The benefits are represented by :

1. a reduction in interest and penalties on tax debts,

2. an increase in the deadlines for proposing the arrangement with creditors as part of the related procedure

3. the limitation of the possibility of competing proposals in the case of an arrangement with business continuity.

But the greatest reward effect concerns criminal responsibility.

For those who, being in office at the moment, have promptly submitted the application to the OCRI or the request for access to one of the procedures for regulating the crisis or insolvency, **the non-punishment is envisaged** with reference to all cases of simple bankruptcy and of fraudulent bankruptcy if the damage is low.

If, on the other hand, the damage is not low, the penalty is reduced by up to half as long as both of the following two conditions exist: the asset inventory is available to creditors ensures the satisfaction of at least 20% of the unsecured debts; the damage resulting from criminal conduct does not **exceed the amount of two million euros**.

Always in order to facilitate the resolution of companies crisis the Code provides important improvements related the measures already outstanding like

THE DEBT RESTRUCTURING AGREEMENTS

The new Code provides for facilitations to access this procedure, because it is expected to extend its effectiveness also to creditors not adhering to the proposed agreement, if the agreement is accepted by at least 75% of the total credits belonging to the same category (eg banks) and provided that the agreement provides for the continuation of the business, even if possible on a reduced size.

The CERTIFIED RECOVERY PLAN

This instrument already exists today and the Code strengthens it in some respects. The Code regulates its effects in two rules, which respectively provide for the exemption from revocatory action of the deeds and payments made in execution of the plan and 'exemption from criminal liability brelating to offenses of preferential bankruptcy and simple bankruptcy that may arise from the performance of such acts and payments

THE TAX TRANSACTION

The Corporate Crisis Code reorganizes the discipline of the tax and social security transaction, in Articles 63 and 88, concerning the implementation of this institute in the context of a debt restructuring agreement and the arrangement with creditors and introduced some changes, in order to overcome the main criticalities that emerged in recent years from the application of the previous provisions .

The new Code provides that the Court can approve the restructuring agreements **even in the absence of the Tax Administration's adherence** to the tax settlement proposals related to these agreements, when:

1) such adhesion, as usually happens, is decisive for the purpose of achieving the percentages of 60% (or 30% in some cases) of the credits established forthe homologation of the agreements themselves;

2) the satisfaction of tax credits offered by the debtor company is, also on the basis of the results of the attestation made by an independent professional, convenient compared to that deriving from the alternative liquidation.

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OVER INDEBTEDNESS PROCEDURE

The procedures for settling the over-indebtedness crisis concern:

- consumer debt structuring plan;
- minor arrangement;
- controlled liquidation.

The over-indebtedness procedures concern a certain category of subjects, in particular:

the consumer, the professional, the agricultural entrepreneur, the minor entrepreneur, the innovative start-ups and any other debtor who is not subject to the judicial liquidation procedure or to the compulsory administrative liquidation or other liquidation procedures provided for by current legislation.

The legislator has established a specific discipline with respect to the general procedure linked to the crisis which is applicable only within the limits of compatibility.

The regulatory provision specifies that the appointment of the attestor is optional and that the functions of the commissioner and liquidators are performed by the OCC (Crisis Settlement Body) regulated by the Ministerial Decree 24 September 2014 n. 202.

An innovative discipline was also introduced with respect to the current one with regard to family procedures involving cohabiting family members or a family group. In the aforementioned cases, unitary management is mandatory, in which the legislation allows for the submission of a single project for resolution of the over-indebtedness crisis and the judge is required to adopt the appropriate measures to ensure the coordination of related procedures in the event that non-contextual requests are received.

The OCC plays, in particular, a fundamental role , appointing a professional (Manager of the crisis) , that assits the debtor to presents the request, prepares the plan and the proposal for a minor arrangement (but also takes care of the execution of the procedure as an auxiliary to the judge (Article . 78). The minor arrangement is approved by the creditors who represent the majority of the credits admitted to the vote. Therefore, an absolute majority of credits calculated on the basis of the list of creditors and credits is required. It is no longer necessary to reach 60% as established in the current legislation pursuant to art. 11 of Law no. 3/2012. .

The Court is obliged to approve the minor arrangement with a specific sentence, if a check has been made on the suitability of the plan and a majority has been reached. it is possible to file complaints and the Court could examine them and approve the arrangement when it believes that the opponent's credit can receive a satisfaction no less than that which it would obtain in the event of judicial liquidation as a result of the execution of the plan. In any case, the creditor is excluded from the right to present objections or possible disputes, if the subject has knowingly determined or aggravated the debt situation, even if dissenting, or to assert causes of inadmissibility that do not derive from the debtor's malicious behavior (art. 74)

- Thanks for your kind attention

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