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Essay on Covid-19 and Insolvency measures in Italy

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Italy's national lockdown in response to the Covid-19 health emergency has been adopted from March 9th, 2020.
Several contingency rules aimed at containing the economic and financial impact of the related lockdown have been unceasingly adopted, affecting various area of law related to business activity, as company and insolvency law.
This short essay means to point out the most relevant changes involving insolvency law, on the premise that these provisions could be further modified or integrated due to the general uncertainty of the length (and aftereffects) of the emergency situation.
Indeed, the first sets of remedies to the health contingency involving judicial and procedural measures dates back to **Law Decree, March 17th 2020, no. 18**, so called "**Cura Italia**", providing that:

- except for few specific judgments (mainly in the field of criminal law), all the hearings fixed between 9th March to 15th April will not be held and are intended as postponed accordingly to the Court office schedule;

- The expiry of the deadlines related to any act of civil and criminal proceedings (safe the above exception) is likewise suspended.

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Moreover, the recent **Law Decree, April 8th, 2020, no. 23**, so called "**Decreto liquidità**", stated that the final deadline of the aforesaid suspension is extended to May 11th.
Although the previous Decree was already able to generally affect some aspects of insolvency proceedings - as the suspension of the 60/120 day-term for filing the restructuring proceedings ("concordato preventivo") or agreements with creditors ("accordi di ristrutturazione" - after the pre-petition file) -, more specific measures have been adopted by the latter decree (no. 23/2020), laying down a set of temporary (and contingent) measures for businesses affecting pivotal aspects of insolvency regime.

The intervention aims to safeguard and preserve the continuity and going concern of businesses by several "suspension mechanisms" described below.

Postponement of entry into force of the Insolvency Law Reform (so called *Codice della crisi e dell'insolvenza d'impresa*).

Art. 5 of *"Decreto liquidità"* postpones until the September 1st, 2021 the enforcement of the new bankruptcy regime (originally scheduled for August 20th, 2020 and already deferred, for certain aspects, to February 15th, 2021) in its entirety, with the exception of several provisions mainly related to corporate governance and adequate organizational

structures to be adopted by the firms, already entered into force in 2019. This delay – as specified in the accompanying Report – is due to several related reasons. An early enforcement (i.e., by August 2020) of such a massive reform would have led to operational concerns and uncertainty, causing further damages in a period of symmetric crisis. Moreover, the same purposes of the new Code consist in the duty of early warnings and diagnosis of imminent crisis (with the introduction of *procédure d'alerte*), assigning duties of reporting and intervention to internal and external supervisory bodies (as the Italian Revenue Agency or the Italian social security Institution). The introduction of such measures, conceived in a regular economic framework, would now be ineffective in selecting companies required to open a virtuous recovery out-of-Court proceedings, and counterproductive since it may affect adversely the prospect of business continuity in many firms.
Thus, a deferral of the Insolvency reform may also lead the introduction of amendments for a better compliance with the EU Directive (2019/1023) on preventive restructuring frameworks, to be adopted by July 2021, and a rethinking of the efficiency and effectiveness of the internal management of certain bodies (as the Chamber of Commerce) required to play a pivotal role in the early warning procedures.

Temporary deferment for bankruptcy filing or request.

Relating with the aforementioned aims at protecting companies that experience financial difficulties as a result of the COVID-19 pandemic and coherently with temporary suspension of obligation to file for bankruptcy (winding-up) and consequent liabilities, art. 10 states that petitions for winding-up proceedings (as well as admittance to "*Liquidazione coatta amministrativa*" and "*Amministrazione Straordinaria"* of Large Enterprises) filed in the period between March 9th, 2020 and June 30th, 2020 are not admissible. The said provision also applies (quite surprisingly) for voluntary cases petition; while is not applicable whereas the filing is made by the Public Prosecutor who also requested the granting of precautionary measures, in order to avoid or interrupt suspected acts of fraud or misconduct by the debtor.
It is also provided, in order to protect creditors, that in case of future winding up, the period of suspension from March to June of this year will not be counted for the purpose of calculating the terms set forth by:
- art. 10 of the Insolvency Law, IL, (*i.e.* winding up within 1 year from the cancellation from the Register of Companies), and
- art. 69-bis IL (forfeiture of claw-back petitions – so called *azioni revocatorie* – after 3 years from the declaration of winding-up and after a certain period from the completion of the operation). In this latter case, the variability (6 months to 5 years) depends on the specific issues and types of claw back (according to art. 64, 65, 67 and 69 IL).

Extension of terms provided for restructuring proceedings (*Concordato Preventivo*) and agreements with creditors (*Accordi di ristrutturazione*).

With the aim of supporting companies and debtors within the exceptional COVID-19 phase, the Italian Government introduced measures for the postponement of terms within restructuring plans. In particular, art. 9 of "*Decreto Liquidità*" provides the extension of six more months for all deadlines expiring between February 23rd, 2020 and December 31st, 2021 for the fulfilment of restructuring plans formed under judicial restructuring proceedings and agreement with creditors already approved by creditors and Courts. With regard to restructuring proceedings pending at the date of February 23rd, 2020 not yet submitted to the approval of the Court, the Decree provides that the debtor can file, until the hearing fixed for the approval of the plan by the Court, a specific motion in order to obtain a new non-extendable term (for maximum 90 days, starting from the decision of the Court) for the filing of a new restructuring plan or a new proposal to creditors. With this regard, the Decree excludes the possibility to file the motion for extension in those proceedings where voting operations have been already executed and the majorities provided by law have not been reached. The term extension for maximum 90-days period can be granted by the Court, even if pending an insolvency motion against the debtor and also in case the debtor already obtained an extension for the filing of the plan or the proposal during the period precedent to the COVID 19 emergency. In this specific case, the debtor shall give specific evidences and demonstrate the need of the term extension. The Court decides on this specific motion, also hearing the Commissioner supervising the procedure and the public prosecutor.
It is also provided that if the debtor intends to file a motion in order to revise and obtain an extension of deadlines regarding the execution and fulfilment of the obligations provided in a plan already submitted to creditors, but not yet approved by the Court, the extension can be granted by the Court for a maximum period of six months. In this specific case the Court approves the plan, highlighting in the approval the new deadlines granted.

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The same decree suspends some provisions of the civil code concerning company law with a (in)direct effect also on insolvency law. More specifically, the suspensions involve the reduction – even below the legal minimum – of capital pursuant to losses (art. 6 "Decreto liquidità"), the recognition of the going concern principle (art. 7) and the subordination of new financing (art. 8).

Reduction of capital pursuant to losses.

The current emergency situation is likely to increase the number of companies that will incur great losses in their balance sheets, despite the support measures envisaged in the decree. In this perspective the same decree provides for the suspension of some specific provisions of the civil code regulating the cases of reduction of capital pursuant to losses for more than one third of its and even when it falls below the legal minimum. This sits on a prompt response of directors, who should call the shareholders meeting without delay in order to resolve the reduction of capital. In principle Italian company law allows shareholders to wait until the end of the following financial year to see whether or not the loss could be recovered. This one-year waiting-period is granted insofar the loss does not affect the legal minimum. In all the other cases shareholders have to choose between the reduction and simultaneous increase of capital to an amount not lower than the minimum set by the law, the conversion of the company, and the termination of it.

Art. 6 of "Decreto liquidità" takes over the provisions regulating the reduction of capital below the legal minimum, the year suspension, and the consequent cause of termination of the company from the day of its entry into force until December 31st, 2020.

Going concern principle.

In this particular situation the going concern assessment of companies shall be affected by the economic downturn from the Covid-19 pandemic. Its consequences will be shown in the financial statements of financial year 2020, which could lack the going concern and require the application of winding-up criteria. In order to neutralize the impact of this situation the "*Decreto liquidità*" sets a *de jure* assumption of presence of business continuity in the 2020 financial statement in case of positive assessment of going concern in the previous financial year, closed before February 23rd, 2020. The application of the going concern principle has to be clearly illustrated in the explanatory notes of the financial statement. Moreover, proper reference to the findings of the balance sheet of the previous financial year is required by art. 7 of the said Decree. This temporary rule can be applied even to the financial statements of a financial year closed before February 23rd, 2020, but not yet approved by the shareholders' meeting.

The provision recalls another measure of (previous) Law Decree no. 18/2020, art. 106, in light of the restrictions enforced for in-person meetings with direct impact on the functioning of companies' bodies: for all companies has been set an automatic postponement of the ordinary deadline for the approval of the 2019 financial statement to 180 days from the end of the financial year, instead of just 120 days.

New financing.

In order to ensure adequate protection to new financing coming from shareholders, art. 2467 and art. 2497-quinquies of the civil code have been suspended for funding provided by shareholders (or those who carry out direction and coordination activity towards the company) in the period between the entry into force of the liquidity decree and December 31st, 2020. This suspension avoids the treatment of the new financing granted as subordinated to the claims of the other creditors of the company, a rule of the civil code intended to sanction those exercising direction and coordination activity who put fresh resources to the company by way of debt capital instead of risk capital in a moment in which the second would have been more reasonable for the financial situation of the company or in presence of an excessive unbalance of debt compared to net capital.

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Conclusions

All measures adopted by the Italian Government with the above-mentioned Law Decrees essentially aim to face this particular emergency period and to support the current stasis of commercial transactions, mostly paralyzed by the lockdown imposed by the majority of National Authorities.

In this particular framework it is necessary to permit companies and entrepreneurs to "take a deep breath" and re-organize their business also with different visions on how the "next life " of business transactions and commercial relationships will be handled, influenced by the COVID-19 emergency.

These are measures of contingency, necessary to prepare the Italian Country for the next worldwide bet: the new "fresh start" of the economic system.