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**Covid-19 and Insolvency Developments in Italy**

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*Introduction*

Italy’s national lockdown in response to the Covid-19 health emergency has been in place since 9 March 2020. Several contingency rules aimed at containing the economic and financial impact of the related lockdown were quickly adopted, affecting various area of law related to business activity, as company and insolvency law.

This Inside Story 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 after effects) of the emergency situation.

*Rapid Remedies Introduced*

Indeed, the first set of remedies for the health contingency involving judicial and procedural measures date back to the **Law Decree of 17 March 2020, no.** **18**, the so-called “**Cura Italia**”, providing that:

* except for few specific judgments (mainly in the field of criminal law), all hearings fixed between 9 March and 15 April will not take held and are postponed accordingly in the Court office schedule; and
* the expiry of deadlines related to any act of civil and criminal proceedings (saving the above exception) is likewise suspended.

Moreover, the recent **Law Decree of 8 April 2020, no. 23**, the so-called “**Decreto liquidità**”, stated that the final deadline of the aforesaid suspension is extended to 11 May. Although the previous Decree was already able to generally affect some aspects of insolvency proceedings, such as the suspension of the 60/120 day-term for filing the restructuring proceedings (“concordato preventivo”) or agreements with creditors (“accordi di ristrutturazione” after pre-petition filings), 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 the insolvency regime.

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

*Postponement of Entry into Force of the Upcoming Insolvency Law Reform*

Article 5 of the “Decreto liquidità” postpones until 1 September 2021 the enforcement of the new bankruptcy regime (the so-called Codice della crisi e dell’insolvenza d’impresa) (originally scheduled for 20 August 2020 and already deferred, for certain aspects, to 15 February 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, which have 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 (virtuous) recovery through out-of-Court proceedings. It could also be counterproductive since it might adversely affect the prospect of business continuity in many firms.

As a result, a deferral of the insolvency reform could also lead to the introduction of amendments for better compliance with the EU Directive (2019/1023) on preventive restructuring frameworks, due 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 of Bankruptcy Filings or Requests*

Related to the aforementioned aims at protecting companies that experience financial difficulties as a result of the COVID-19 pandemic and coherent with the temporary suspension of obligation to file for bankruptcy (winding-up) and consequent liabilities, Article 10 states that petitions for winding-up proceedings (as well as admission to “Liquidazione coatta amministrativa” and the “Amministrazione Straordinaria” of Large Enterprises) filed in the period between 9 March 2020 and 30 June 2020 are not admissible.

This provision also applies (quite surprisingly) to voluntary petitions; while it is not applicable where the filing is made by a Public Prosecutor who has also requested the granting of precautionary measures, in order to avoid or interrupt suspected acts of fraud or misconduct by the debtor. In order to protect creditors, it is also provided that, in case of a 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:

 - Article 10 of the Insolvency Law (IL), (i.e. winding up within 1 year from the cancellation from the Register of Companies); or

 - Article 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 the latter case, the variability of the period (6 months to 5 years) depends on the specific issues and types of claw-back (according to Articles 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 has introduced measures for the postponement of terms within restructuring plans. In particular, Article 9 of the “Decreto Liquidità” provides for an extension of six further months for all deadlines expiring between 23 February 2020 and 31 December 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 23 February 2020 not yet submitted for 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 a maximum of 90 days starting with the decision of the Court) for the filing of a new restructuring plan or a new proposal to creditors. In 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 extension for the maximum 90-day period can be granted by the Court, even an insolvency motion against the debtor is pending and also in cases where the debtor has 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 is required to present specific evidence and demonstrate the need for the extension. The Court will decide 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 will approve a plan and highlight within the approval the new deadlines granted.

The same decree also suspends some provisions of the Civil Code concerning company law with an (in)direct effect also on insolvency law. More specifically, the suspensions involve the reduction, even to below the legal minimum, of capital consequent on losses (Article 6, “Decreto liquidità”), the recognition of the going-concern principle (Article 7) and the subordination of new financing (Article 8).

*Reduction of Capital pursuant to Losses*

The current emergency situation is likely to increase the number of companies that will incur large losses in their balance sheets, despite the support measures envisaged in the decree. In this light, 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 is predicated on a prompt response by directors, who are required to summon a 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 as the loss does not affect the legal minimum. In all 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, or the termination of the company.

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

*Going Concern Principle*

In this particular situation, the going concern assessment of companies will be affected by the economic downturn from the Covid-19 pandemic. Its consequences will be shown in the financial statements for the 2020 financial year, which could reveal the lack of compliance with the going concern principle 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 (provided the financial year ended before 23 February 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 Article 7 of the said Decree. This temporary rule can be applied even to the financial statements of a financial year closed before 23 February 2020, but not yet approved by the shareholders’ meeting.

The provision recalls another measure of (previous) Law Decree no. 18/2020, Article 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, Articles 2467 and 2497-quinquies of the Civil Code have been suspended for funding provided by shareholders (or those who carry out direction and coordination activity in the case of the company) in the period between the entry into force of the liquidity decree and 31 December 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 contribute fresh resources to the company by way of debt capital instead of risk capital at a time where the second would have been more reasonable for the financial situation of the company or in presence of an excessive imbalance of debt compared to net capital.

*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 contingency measures that are necessary to prepare Italy for the next worldwide gamble: the new “fresh start” of the economic system.