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Subject: Law-Decree 23 dated April 8, 2020 (the "Liquidity" Law-Decree): Urgent measures to guarantee that enterprises affected by the Covid-19 emergency can continue to do business

In this issue of our newsletter, we shall continue to explain the measures of support to enterprises introduces by the Liquidity Decree, i.e., Law-Decree 23 dated April 8, 2020, that went into effect on April 9, 2020. In particular, we shall describe the various measures aimed at guaranteeing business continuity.

1. Temporary disapplication of the provisions regarding the reduction of company capital due to losses

To avoid that the loss of capital due to the Covid-19 crisis, in the presence of a consequent rapid reduction of sales, place company directors in the difficult position of having to find financial means to recapitalize their companies or, alternatively, to have to liquidate even well-performing companies, art. 6 of the Decree provides that, **starting on April 9, 2020 (when the Decree went into effect) and until December 31, 2020, for the cases** that may occur during the **fiscal years ended up to the aforesaid date of December 31, 2020**, **the obligations to reduce and/or increase capital due to losses exceeding one third and/or below the minimum legal limit shall not apply**.

The Decree also established that, **for the same period, the cause for dissolution of the companies with share capital** referred to in art 2484.4 of the Italian Civil Code, **established for when capital is reduced to below the minimum legal limit** in absence of its restoration to the minimum value or of the transformation of the company, as per articles 2447 and 2482-ter, **shall not apply.** In the same way, the Decree established that, for the same period, the cause for dissolution due to the **loss of the entire amount of share capital** (as per art. 2545-duodecies of the Civil Code) shall **likewise not apply to cooperative companies.**

In particular, **the following articles of the Civil Code may be disapplied**:

a) art. 2446, paragraphs 2 and 3 (concerning **stock companies**), and art. 2482-bis, paragraphs 4, 5 and 6 (concerning **limited-liability companies**), whereby, when a company's capital has been reduced by more than one third due to losses and therefore, as per the law, its shareholders' meeting has been called promptly to take the appropriate measures, **if by the end of the next corporate year** the loss has not been reduced to less than one third, the shareholders' meeting that approves the annual financial statements has to reduce the capital in proportion to the ascertained losses (and if need be proceed with the recapitalization). Otherwise, the directors or the statutory auditors must ask the court to establish the aforesaid reduction of capital;

b) art. 2447 (concerning **stock companies**) and art. 2482-ter (concerning **limited-liability companies**), whereby, if, due to losses exceeding a third of a company's capital, the capital has fallen to below the legal minimum limit, the directors must without delay call a shareholders' meeting to decide whether to reduce the capital and at the same time increase it to an amount no lower than the minimum limit, or to transform the company or to wind it up.

It should be noted that, considering that the disapplication of the rules concerning capital losses shall apply to cases that will have occurred during the fiscal years ended up to December 31, 2020, this provision of the Decree shall also be applicable to any losses due to **impairments resulting from the Covid-19 emergency that had to be recognized**

in the financial statements relative to the corporate years that preceded the current one and that as of April 9, 2020 (when the Decree went into effect), had not yet been approved.

In any case, since the first paragraph of art. 2446 of the Civil Code has not been suspended, stock companies **are still required** to inform their shareholders if the company's capital has diminished by more than one third due to losses, and to promptly call a shareholders' meeting to adopt appropriate measures.

As regards the aforesaid suspension of the cause for dissolution of companies with share capital, if losses reduce the capital to below the legal limit, this suspension enables the directors to keep on managing the company as a going concern despite the presence of substantial losses, thus avoiding the obligation of limiting their management to merely preserving the integrity of the company's assets.

2. Temporary provisions regarding the principle of business continuity in drawing up the financial statements

Art. 7 of the Liquidity Decree establishes that, when drawing the financial statements for the FY in course at December 31, 2020, as well as those that were closed by February 23, 2020, but have not yet been approved, it is possible to evaluate items in the perspective of the business continuity referred to in art. 2423-bis.1, no. 1, of the Civil Code, provided that said continuity was present in the last financial statements closed at a date preceding February 23, 2020. The new rule requires company directors to specifically illustrate this evaluation criterion in the notes to the financial statements, including making reference to the results of the financial statements for the previous year.

It appears that, in any case, in their notes to the annual financial statements, the directors must set forth their considerations concerning the factors that cause uncertainty regarding the company's continuity, even if the Decree allows them to continue to draw up the financial statements according to the principle of continuity, consistently with the provision (described in the above section 1) that suspends the recapitalization obligations and the cause for dissolution due to losses that reduce the company's capital to less that the minimum legal limit.

It should be recalled that based on the OIC accounting standard no. 11, **business continuity** exists in presence of a perspective assessment of the enterprise's ability to continue to be a functioning economic complex that will produce income **for at least 12 months after the date at which the financial statements were closed**. If the lack of business continuity is identified, in the sense that in this reference period of time company management believes that there are no alternatives to closing the business, but causes for the company's dissolution have not yet been ascertained as per art. 2484 of the Civil Code, the evaluation of the items in the financial statements still has to be made in the perspective that the activity will continue, but applying the accounting standards that are relevant as need be in order to take into account the **limited residual temporal horizon** that influences, for example, the evaluation of the useful life of the corporate assets and of their recoverable value.

Hence, when it is not possible to ascertain business continuity, this provision allows directors to adopt the criterion of continuity (and therefore not to adopt liquidation criteria in evaluating the items in the financial statements) even if, because of the Covid-19 pandemic, the company faces considerable uncertainties as regards its ability to continue to operate continuously for at least the next 12 months.

It should be noted that this rule can be applied only if the last financial statements closed before February 23, 2020, contained the prerequisites for applying the continuity criterion. On the other hand, this rule may be also applied with reference to financial statements that were closed before February 23, 2020, but have not yet been approved. Hence, it appears that, if in the financial statements for fiscal years preceding the current one there was business continuity, which then ceased due to events connected with Covid-19, it is legitimately possible to proceed to approve the financial statements prepared according to criteria of business continuity.

3. Temporary disapplication of the principle of subordination of shareholder and intragroup loans

As regards **loans made up through December 31, 2020,** art. 8 of the Liquidity Decree allows the disapplication of the principle of subordination of shareholder and intragroup loans made by parties who perform directing and coordination activities for the company or by other parties subjected to it, as referred to in articles 2467 and 2497-quinquies of the Civil Code.

In this connection, it should be noted that the aforesaid articles of the Civil Code punish undercapitalization of companies. In all cases in which there is an excessive imbalance of indebtedness compared to net equity, i.e., in all those cases where it would have been reasonable to make a transfer rather than a loan to the company, the repayment (in any form) of loans made by shareholders or by parties who perform directing and coordination activities within a group of companies is subordinated to the repayment of other creditors; moreover, it must be returned if it was made during the year that preceded the declaration of bankruptcy. On the other hand, the rule introduced by the Decree allows the aforesaid company's financers to make a loan to the same company

without there being any risk that its repayment would be subordinate to that of other creditors.

4. Arrangement with creditors and restructuring agreements: facilitations and extension of some deadlines for fulfilment of obligations

In brief, art. 9 of the Liquidity Decree establishes the following:

a) **a six-month extension of the deadlines for fulfilling the obligations set forth in the arrangement with creditors and/or in the debt restructuring agreement** when such arrangement and/or agreement was **approved by a court** and falls due between February 23, 2020, and December 31, 2021.
This rule grants more time for fulfilling procedures that had already been approved by a court and whose possibilities of success before the crisis were therefore good.

b) that, in the case of proceedings for court approval of arrangements with creditors or restructuring agreements pending at February 23, 2020, the debtor can, up to the date of the hearing for the court approval of the arrangement with creditors and the restructuring agreements, ask the court for **a new deadline not longer that ninety days for filing a new debt restructuring agreement and a new proposal for an arrangement with creditors.**
In this way, the debtor is allowed to take into account the economic factors that may have occurred by effect of the Covid-19 crisis, and present a new restructuring agreement and a new arrangement with creditors. The rule specifies that this possibility is not open to debtors whose original proposal has already been submitted to the creditors' vote, without obtaining the majority needed for approval.
The new deadline cannot exceed 90 days from the date when the court grants it, and, because of the exceptional nature of the provision, cannot be extended.

c) the possibility (until the date set for the court-approval hearing) of **changing the deadlines for fulfilling** the arrangement with creditors or the debt restructuring agreement.
This provision enables the debtor to unilaterally modify the original deadlines for fulfilment of the obligations set forth in the proposed arrangement with creditors and in the debt restructuring agreement. The request has to be submitted together with a statement containing the new deadlines – no longer than six months from the original ones – and documentation proving the need to modify the deadlines in question. The provision establishes that in the proceeding for approval of arrangements with creditors, the court shall also obtain the relevant opinion of the court-appointed receiver. In the presence of such a unilateral modification, the court shall approve it, subject to verification of the persistent existence of the conditions referred to in articles 180 or 182-bis of the Bankruptcy Law, and shall expressly acknowledge the new deadlines in its approval decree.

d) the possibility of obtaining extension for up to 90 days:
- if the deadline referred to in art. 161.6 of the Bankruptcy Law has been granted, if it has already been extended by the court, and also if a claim of bankruptcy has been filed;
- if the deadline referred to in art. 182-bis.7 of the Bankruptcy Law has been granted.

This provision enables debtors to benefit of another extension, up to 90 days of the automatic stay (i.e, the **protection of assets from judicial actions**) established for the so-called pre-arrangement with creditors and for the restructuring agreement proposal, referred to respectively in art. 161.6 and 182-bis.7 of the Bankruptcy Law, including for debtors to whom the same deadlines have been already granted and said deadlines are about to expire and cannot be extended further.

5. Temporary procedural immunity of applications for declaration of bankruptcy and of state of insolvency

Art. 10 of the Liquidity Decree establishes procedural immunity for the following applications, if filed between March 9, 2020, and June 30, 2020:
- declaration of bankruptcy under art. 15 of the Bankruptcy Law;
- declaration of insolvency filed before the compulsory administrative liquidation pursuant to art. 195 of the Bankruptcy Law;
- declaration of insolvency filed before being placed under extraordinary administration pursuant to Legislative Decree 270/1999.

This provision cannot be applied when the application is submitted by a public prosecutor and contains a request for the issuance of the precautionary and protective measures referred to in art. 15.8 of the Bankruptcy Law.
The rule also established the sterilization of the period of suspension of the said applications in calculating the deadlines referred to in articles 10 and 69-bis of the Bankruptcy Law. This measure was introduced to avoid that the halting of such applications preclude irreversibly the filing of bankruptcy requests against deleted enterprises (the deadline is one year from the date of their deletion) or adversely affect the filing of revocatory actions.

6. Postponement of the entry in force of the Enterprise Crisis and Insolvency Code

Art. 5 of the Liquidity Decree **postpones** the entry in force of all of Legislative Decree 14, dated January 12, 2019 (the so-called **Enterprise Crisis and Insolvency Code**, hereinafter "ECIC") **to September 1, 2021.** This postponement also includes the reporting obligations established in articles 14 and 15 of the ECIC, which will likewise become operative on September 1, 2021, and not on February 15, 2021, as had been established by art. 11 of Law-Decree 9 dated March 2, 2020.

The aim of the ECIC and its connected alert measures and reporting obligations is to make an enterprise's crisis be revealed in a timely manner.

If the ECIC and its aforesaid measures had not been suspended, a great many well-performing and essentially healthy enterprises would be considered in crisis, due to the current situation of general crisis of all of Italy's economic sectors, whereas in the absence of the economic and financial consequences of the spread of Covid-19 they would have been considered *in bonis*.
In any case, during this emergency, enterprises and operators will be able to continue to use existing well-established crisis management instruments and to avoid applying the new rules established by the ECIC, and all the relative interpretative uncertainties, when at the moment what are needed are rapid and tested crisis management procedures. It should be noted that the postponement of the ECIC's entry in force is appropriate also in order to ensure that it is consistent with the soon-to-be-issued regulation for the implementation of EU Directive 1023/2019.

Our firm will be happy to provide any clarification and assistance its customers may need.

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