Inside Story – Italy

This month's Inside Story is brought to you by Dr. Giulia Pusterla of Studio Pusterla, Como, Italy, email: giulia@giuliapusterla.it

To change a law is one thing, but how to change a culture?

Until 2005, Italian insolvency law was "liquidation-oriented", in the sense that the main objective being pursued was the liquidation of the distressed company. Our old law focused on creditors' rights and disregarded the chances for the debtor company to be rescued as a going concern.

Starting from 2005, thanks to many interventions of the Parliament, Italian insolvency law was deeply modernized and we now have a legal framework that is more "rescue-oriented".

I think that Italian companies and insolvency practitioners should appreciate the effort put by our legislator into improving our insolvency system, especially in such a difficult economic and financial period.

Everything is fine, then? Yes, but…but it's easier and quicker to change a law than an attitude. The issue, here, is cultural.

The cause of the scandal is a new proceeding, introduced in Italy starting from 11 September 2012 (law decree n. 83/2012). According to this procedure the debtor company files the case and is granted by the Court an automatic stay period of maximum 180 days. If reorganization is not feasible, the company can be liquidated. But if the rescue is viable, the debtor will use the period of 180 days to try to reach agreements with its creditors, to prepare a plan to reorganize the business and to borrow the liquidity needed for restructuring. And, as usual, this is the hardest problem: the debtor in possession financing. Another hot issue is the payment of critical suppliers. Of course, we must divide pre-petition creditors from post-petition ones. Post-petition creditors (including lenders) are considered administrative creditors, which means that they have a super-priority in payments.

If you really want to try to save the value of a going concern, if you really want to rescue companies, you should be happy to have provisions like those I shortly described above. Instead, an unexpected reaction happened. A very strong feeling of dislike arose, especially from the Italian Employers' Association.

The competitors of distressed companies consider unfair competition the fact that the new law allows to have such a long period (180 days) to prepare a plan, during which all post-petition creditors will get the right of a super-priority in payments, while pre-petition (unsecured) creditors will receive only very low percentage of their credits.

I have to recognize that in some cases unsecured creditors received a very low percentage of their credit (10%, also 5% sometimes). But creditors, of course, have the right to vote the proposal: if the majority of credits (not creditors) approves, the minority will have to accept.

My personal thinking is that the advantage of an automatic stay period of 180 days should be allowed only to debtors who are trying to reorganize their business. If no rescue is realistically feasible, and the company can only prepare a liquidation plan, it shouldn't receive such a "gift", because it is not only useless, but also harmful, since the procedure can be the source of very relevant administrative credits. And, of course, this reduces the chances for unsecured creditors to see their credits repaid. Therefore, there is still room for improvement and the Parliament should intervene again on the law.

On the other hand, I would never change the law if, in some specific cases, during restructuring plans some debtors adopted fraudulent behaviours against their creditors. In these cases, in my opinion what is needed is not a change in the law (which would bring Italian insolvency law back to the old liquidation approach) but severe punishments of guilty debtors. The issue is debatable and the discussion is hot at the moment in Italy.

There is a bill, which is under discussion in the Parliament, which proposes to continue to allow any debtor to have the automatic stay but introduces a new clause: if the rescue doesn't succeed, the lenders and the suppliers that dealt with the debtor relying on their super-priority in payments, would lose it and would be considered like unsecured creditors. I think this the worst possible solution to adopt. Certainty is a value itself: if such a bill were to become law, no lender or no supplier would ever take such a risk after the debtor has filed the case. Why should they with no a priori guarantee of being paid? But without financing, no restructuring will ever succeed. I don't even want to believe that such a U-turn may occur to our insolvency law. In Italy we have to continue this long and winding road that we started in 2005, learning how to use the new toolbox in a correct way and on a bona fide basis.

If we want Italy to remain (to become?) an attractive country for foreign companies, we must – among many other actions – not destroy our new insolvency law.

Dr. Giulia Pusterla

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