



•ALERT•

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The European Commission expanded the Temporary Framework to provide recapitalization aids to further support companies in the context of the Covid-19 outbreak

The European Commission issued on 8 May 2020 a **second amendment** (Communication C(2020) 3156 final) to **extend the scope of the State aid Temporary Framework** (Communication 2020/C 91 I/O)) as of 19 March 2020. The primary aim of this new amendment is to expand the Temporary Framework to allow **well-targeted public interventions through recapitalization aids** by providing equity and/or hybrid capital instruments to non-financial companies in need (the *Recapitalization Aids*). Under this framework, Covid-19 Recapitalization Aids can be granted until 30 June 2021.

The Communication sets up a number of **criteria** that must be met in terms of eligibility, types of measures, amount of the recapitalization, information undertakings, remuneration, governance rules, cross-subsidization and acquisition restrictions and exit strategy, for the purposes of allowing a Member State to grant the Recapitalization Aids.

Based on the information available, it is expected that the "*Decreto Rilancio*", the Decree in process to be released in the next hours by the Italian Government, will include – amongst others – a Recapitalization Aids scheme that will need to receive the Commission's prior approval in order to become effective.



ELIGIBILITY

Recapitalization Aids can be granted to companies which face the risk to go out of business if no Member State intervention is granted such as (i) companies which are not able to obtain financing on the markets, or (ii) companies located in a Member State where the existing horizontal measures to cover liquidity requests do not ensure the company's viability, provided that the company was not already in financial difficulty as of 31 December 2019 (according to the General Block Exemption Regulation definition).

TYPES OF INSTRUMENTS

Member States can provide Recapitalization Aids through **two distinct sets of instruments**: (i) by subscribing equity instruments, such as newly issued common or preferred shares; and/or (ii) by subscribing hybrid capital instruments having an equity component, such as instruments providing profit participation rights, silent participations and convertible secured or unsecured bonds. A combination of equity and hybrid capital instruments is also possible. For **equity instruments**, the capital injection must be conducted at market value, i.e. in case of listed companies at a price that does not exceed the average share price over the fifteen days preceding the request for Recapitalization Aid. For non-listed companies, the market value must be estimated by an independent expert or by other appropriate means.



AMOUNT OF RECAPITALIZATIONS

The amount of the Recapitalization Aid granted by the relevant Member State cannot exceed the minimum necessary to ensure the viability of the company, nor can go beyond restoring its capital structure to the one predating the Covid-19 outbreak.

SPECIFIC PROCEDURAL REQUIREMENTS

Recapitalization Aids in amount exceeding Euro 250 million require a separate **notification**. In order to benefit from the Recapitalization Aid, a company must file a **written request** for the Member State's intervention.

Furthermore, beneficiaries other than SMEs have to provide **information** on the use of the Recapitalization Aids received, including on how the use of the aid has supported the company's activities in line with EU and national obligations linked to the green and digital transformation.

REMUNERATION

Member States must receive **appropriate remuneration** for granting of Recapitalization Aids. The closer the remuneration is to market standards, the lower is the potential competition distortion caused by the Member State intervention. Any Recapitalization Aid instrument must provide for step-up mechanisms that increase the remuneration of the Member State over the time, with the purpose of incentivizing the company to redeem the Recapitalization Aid instrument as soon as possible when the economy stabilizes.

This increase in remuneration can take the form of additional shares granted to the Member State or other mechanisms. For **equity instruments**, the increase in the remuneration required by the step-up mechanism must

provide a minimum 10% increase on the Member State's remaining stake for each of the following steps: (i) four years after the Member State Recapitalization Aid (or five years for a not-listed company), if the Member State has not sold at least 40% of its Recapitalization Aid equity and (ii) six years after the Member State Recapitalization Aid (or seven years for a non-listed company), if the Member State has not sold its entire Recapitalization Aid equity.

For the remuneration of hybrid capital instruments, it must be considered the level of subordination, the instrument's risk and all terms of payment, incentives for exit, such as step-up and redemption clauses, as well as an appropriate benchmark interest rate. The remuneration of **hybrid capital instruments** must at least equal the 1-year IBOR plus a premium ranging from 225 bps to 950 bps, depending on the company's size and the redemption date. The conversion of hybrid capital instruments into equity must be conducted at 5% or more below TERP (Theoretical Ex-Rights Price) at the time of the conversion. In the same vein as equity instruments, hybrid capital injections must include a step-up mechanism after conversion into equity to increase the remuneration of the State. If two years after the conversion into equity the Member State has not sold its stake, it must receive an additional share of at least 10% of its remaining participation.

GOVERNANCE RESTRICTIONS

Until the Member State's equity stake has been fully redeemed, companies are subject to **restrictions on dividends distribution and share buybacks**. In addition, until at least 75% of the equity stake has been redeemed, a **strict limitation of the management remuneration policy**, including a prohibition on bonus payments, is applied.

PROHIBITION OF CROSS-SUBSIDIZATION AND ACQUISITION

In order to avoid detriment to fair competition in the Single Market, a **prohibition of cross-subsidization and acquisition** is established. Beneficiaries cannot use the Recapitalization Aids to cross-subsidize of the business of their affiliates that were in financial difficulty before the Covid-19 outbreak. Moreover, until at least 75% of the Member State's equity stake has been redeemed, non-SME company are prevented from acquiring more than 10% of the shares of competitors.

EXIT

Companies must have the right **to buy back the equity stake** that the **Member State** has acquired at any time. Similarly, a Member State must be able to **sell** its equity stake at market prices to purchasers other than the beneficiary at any time. Such a latter sale requires, in principle, an open and non-discriminatory consultation with potential purchasers or a sale on the stock exchange market. The Member State may grant to existing shareholders priority rights to buy at the price resulting from the public consultation. Beneficiaries other than SMEs who have received a Recapitalization Aids accounting for more than 25% of their equity must submit a credible exit strategy for the participation of the Member State, unless the Member State's intervention is reduced below the level of 25% of equity within twelve months from the date of the Recapitalization Aid granting. Where the Member State's participation is not reduced below 15% of the company's equity within six years of the Recapitalization Aid (seven years for a not-listed company or an SME), a restructuring plan must be notified to the Commission for approval.

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