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# Insolvency

**Italy**

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# 2020

## Trends and Developments

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### **The Condition of the Italian Business System after COVID-19: Some Indications to Face the Crisis**

In a year that will be remembered mainly for the COVID-19 health emergency, “crisis” is almost certainly the most recurrent word: the effects of the pandemic have indeed permeated across every possible context, both in the public and private sphere.

“The crisis consists precisely in the fact that the old is dying and the new cannot arise” said Antonio Gramsci, an Italian philosopher, writer and politician living at the beginning of the last century. We are all again in this transitional phase: it is now a matter of understanding how to deal with it, because crisis can be an opportunity for change: obviously, for those who want to seize it.

It is certainly not the first global crisis the world has been through. Interestingly, during 2020 the world slowly reacted to the pandemic using a method dating back to the 14th century: the quarantine, an isolation measure to which vessels arriving from areas affected by the plague were subjected. Despite the belated and patchy response, the health sector has therefore been able to make use of past experience to deal with the current emergency because those remedies are still applicable today.

The economic-financial sector has also been through several serious crises. The Dutch tulip crisis in the 17th century or the scandal of the Mississippi Company in the 18th century in France, up to the recent major crises, the first of which was the fall of Wall Street following the 2008 Lehman Brothers’ bankruptcy.

Yet, all these crises had in common the fact that they were “purely” financial and could therefore be dealt with “only” by the use of financial instruments that guarantee the injection of liquidity into the economic system, until companies were able to resume their activities and stand on their own feet again.

The world’s economic and financial systems have clearly learned from the past; thus, in facing a crisis such as the one in which we are currently involved, they have promptly made available large amounts of money to guarantee liquidity to companies.

However, in the 21st century, we turned out to be still unable to react in a structured manner. Providing for liquidity is not sufficient without a strategy that tries to look beyond the emergency. The current economic-financial crisis is, in fact, profoundly different from all those already faced because it follows a pandemic that has had an impact not comparable to any other.

The pandemic will radically change (and has already changed) the world in which we live, redesigning consumers’ behaviours and, consequently, the guidelines required to manage companies.

Nothing will be the same: habits, needs, necessities and the ways of satisfying them have irreversibly changed. In essence, the structure of demand has changed. It is therefore unthinkable that the structure and the modalities on offer will remain unchanged, leading to a necessary adaptation to the changes in demand in order to reconstitute a balanced and functioning system.

What awaits us will not be a simple restart, but the beginning of a new era for business. The rules have changed, and so have the behaviours of all the business players.

This will create new opportunities for organisations that have the courage and foresight to seize on the changes taking place, imagine new possible scenarios and remodel, with speed and efficiency, their business activity, with a vision that goes well beyond the current contingency.

This is why the financial aids – granted in Italy by the emergency legislation based on Decree Law 8 April 2020, No 23, and converted with amendments in the Law 5 June 2020, No 40 – are not sufficient, nor resolute to overcome the current crisis. The business system must be rethought in accordance with the new reality. Any resistance to change will probably delay this path in an irreparable way.

Companies will have to change their strategies radically, because this crisis cannot be won with isolated or spot interventions. The solution is a global vision considering the company for what it is: an entity aimed at the long-lasting exercise of the business.

# ITALY TRENDS AND DEVELOPMENTS

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The reaction to the crisis, in the business world, can be articulated in three macro phases:

- phase of the immediate response, which concerns the period of time in which companies face daily challenges and manage normal operations immediately after the onset of the emergency;
- discovery phase, during which changes to the daily operation must be identified and chosen with care, taking into consideration the wider industry business and the possibilities of creating synergies with other entities;
- development phase, the stage in which the company prepares to face the new normality by capitalising on the experience gained in the two previous phases. In this respect, business leaders have the responsibility to consider the three phases simultaneously, planning and allocating resources accordingly.

The transition from one phase to another depends on exogenous and endogenous factors that involve the company.

In the face of a pandemic, it is indisputable that the role of exogenous factors is predominant.

In cases of emergencies such as the one resulting from the spread of COVID-19, the response is mainly attributable to institutional interventions by governments and international organisations that, evaluating the emergency scenarios, provide protection, treatment and rehabilitation for the population and, at the same time, define the monetary and fiscal policy instruments on which the rescue and stabilisation of the economy are based.

Equally indisputable, however, is the role of endogenous factors – both at territorial and corporate level – that can influence the effectiveness of the measures taken.

Monetary and fiscal policy interventions taken to deal with a health emergency in a given economic context have indeed concrete effectiveness only where the company is able to use the aid with the aim of surviving in order to seize opportunities, to consolidate and grow and, finally, to prosper.

Therefore, companies – in order to ride the change and not be caught unprepared – should implement innovative strategies that take into account both the existing shortcomings (the negative effect of which has widely increased in the present situation) and the needs that have emerged in the last eight months.

First and foremost, we have to recognise that our supply chains show up as extremely weak, since, especially with regard to SMEs (which are mostly family-owned and family-run) the

supply-chain management is not considered as a strategic and competitive element.

Indeed, the system currently in use is uneven, unco-operative, low-tech and essentially anachronistic.

Furthermore, this system entails many risks for the future, such as:

- limitations or interruptions of the supply and productive chains' operativity;
- a lack of availability of raw materials, semi-finished and finished products;
- a direct and indirect labour shortage;
- default of the suppliers and difficulty in finding new ones.

The deficiency of infrastructures which could spread and facilitate the access to e-commerce systems and/or cashless payments represents a further shortcoming.

An adequate corporate strategy, which could avert those issues, should be based on the following guidelines.

## **Risk Analysis**

Strengthening the risk-management systems represents a key element for dealing with crises properly: specifically, a more responsible approach should be applied, by taking into account the concrete perspective of a new pandemic lockdown and assessing its impact on the companies' financial flows, as well as the related consequences regarding their ability to maintain business continuity.

It will then be necessary to provide for continuous monitoring of arising risks and to review promptly the political procedures for risks' management, in order to mitigate their negative effects. Predicting possible future scenarios, although potentially extremely changeable, becomes crucial, always with a view to guaranteeing adequate support for management decisions and/or to the revision of contingency plans.

Such risk assessments should extend to various aspects, including, but not limited to, the management of employment contracts, court trials, supply chain and communication with clients, as well as guaranteeing personnel safety and the security of technological and IT platforms.

## **Safeguarding Employees' Health**

Companies should be facilitated in implementing smart working instruments, with a focus on the well-being conditions of their employees.

In general, companies should guarantee the safety of work environments by rigorously sanitising the relevant areas, in compliance with the hygiene management requirements set up by the national and regional public health authorities. Therefore, employees' health conditions should be constantly monitored, keeping the relevant information confidential. Strengthening safety education, by establishing guidelines for the self-protection of employees and increasing awareness of risk prevention, is also a key element.

## **Supply Chain Risk Management**

Focusing on the supply chain could represent a fundamental measure in the first phase of emergency response as well as in view of the return to normality.

A full optimisation of the supply chain can only be accomplished by a broad understanding of how - and to what extent - the company's business could react to the current emergency: to this end, companies should assess any possible risk related to the supplies' management cycle, caused by interruptions within the supply and distribution chains. In the case of generally long production cycles, companies should be prepared for possible rebounds in demand for goods, which could occur as the epidemic subsides.

In order to maintain business continuity, notwithstanding the emergency, entrepreneurs should focus on contingent needs that may not have been foreseen in the continuity plans.

## **Markets' Monitoring and Customer Relationships**

A constant communication channel with their customers allows companies to understand and predict market trends, consumers' orientation and fluctuations in demand for goods and services.

It is crucial for the companies to share with their stakeholders the contingent condition of mutual difficulty, promptly informing them of ways to mitigate any losses and, at the same time, evaluating the opportunities to amend existing agreements, especially those that could be affected by the emergency, providing evidence of the unforeseen conditions and the objective difficulty of fulfilling the commitments originally undertaken.

## **Communication Plan**

Companies should set up specific communication channels with employees, suppliers and customers, in order to prevent the spreading of unofficial news that could prove harmful to the management of the crisis itself and to the external perception of the company's response. In order to prevent or manage those risks, it would be useful to implement smart communication tools to exchange information and instructions.

It is also important to liaise with the relevant public authorities, both in order to keep up to date with the emergency and to benefit from any support and facilities made available by ministerial and regional decrees to companies affected by the emergency.

## **Cybersecurity**

Companies should evaluate the implementation of new and specific instruments to ensure the security of their data, including those concerning suppliers, partners and customers, in order to prevent any cyber threat.

Particularly, in the context of smart working, it will be necessary to provide adequate security support and define guidelines for employees' self-protection, increasing their awareness of cyber-risk prevention.

## **The Adjustment of Cash-Flow Projections**

Given the emergency conditions, companies should carefully review their cash-flow projections, as liquidity planning is essential to ensure a continuous and balanced business.

In addition, due attention should be paid to import-export flows related to unpredicted changes in both internal and external market conditions: companies should therefore prepare adequate responses to emergency scenarios involving the foreign markets in which they operate.

The context outlined so far leads to the conclusion that, in a globalised world, a much more sophisticated ability to perceive the changes and predict future trends, whatever they may be, is required to implement promptly the most efficient reactions.

The COVID-19 crisis obliged the Italian Government to defer the entry into force of the Code of the Crisis and Insolvency (*Codice della crisi e della insolvenza*) to 1 September 2021, and it is currently being discussed whether it is appropriate to extend the deferral further, taking into account the ferocity of the economic crisis.

No one believes that a new legal provision may provide a definitive solution to all the problems that we are facing. Nevertheless, it should be noted that legislative reform concerning companies' crisis and insolvency was adopted in 2019 (some provisions entered into force in March 2019) and has provided relevant measures to ensure the protection of Italian companies. The legislative reform, indeed, has significantly enhanced the duty, for every company, to define an organisational, administrative and accounting business structure, which must be suitable in light of the nature and size of the business activity carried out. The Code of the Crisis and Insolvency focuses, in particular, on the timely detection of the company's crisis, which will become the main measure in the pursuit of surmounting it.

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**LCA Studio Legale** is an independent law firm with offices in Italy (Milan, Genoa and Treviso) and in the UAE, where it operates in international partnership with IAA Law Firm. It is active in all the main areas of commercial, corporate, banking, finance, restructuring, tax, criminal, real estate and labour law, and, more generally, in all aspects of business law – including IP, new technologies, transportation, art and food law – as well as in the protection of family assets. LCA's over 120 professionals mainly deliver their services to corporate and financial clients and work for industrial, finance and insurance groups, inves-

tors, banks, as well as SMEs, family businesses and individual entrepreneurs. The firm has always adopted an international approach, advising Italian companies in their internationalisation processes, and foreign corporations interested in investing or expanding in Italy, as well as multinational corporations involved in multi-jurisdictional transactions. LCA advises clients in all matters related to business crisis and insolvency: turnaround plans, implementation of insolvency procedures, debt renegotiations and assistance to investors willing to buy businesses or assets in insolvency procedures.

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