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COMMENTARY

Italian Parliament Confirms June Measures Introduced by Government to Boost Italian Lending Market

As reported in our July *Commentary*, "The Italian Government Introduces Measures to Boost the Italian Lending Market,"[1] the Italian Government Law Decree No. 91 of June 24, 2014 (the "Law Decree") introduced certain measures aimed at facilitating the access to financing by Italian companies. Parliament converted the Law Decree into law on August 7, 2014, with only limited changes.[2]

This *Commentary* describes the main rules introduced by the Law Decree. In particular, the first section discusses the measures affecting the lending market, while the second and third sections concern, respectively, securitization transactions and the debt market.

LENDING IN ITALY

The main measures introduced by the Law Decree affecting the lending market can be summarized as follows:

- Securitization vehicles incorporated under the Italian Securitization Law[3] as well as Italian insurance companies (i.e., insurance companies incorporated under Italian law or authorized branches of an insurance company incorporated under the law of a non-EU Member state)[4] are now allowed to lend in Italy;[5]
- The list of assets eligible for investment by undertakings for collective investment (*organismi di investimento collettivo del risparmio*) has been extended so as to include receivables arising from financings granted out of their assets; and
- The scope of certain favorable domestic tax regimes already applicable to loan transactions has been broadened, and a withholding tax exemption applicable to payments of interest to certain nonresidents lenders has been introduced.

Lending License

As a rule, lending in Italy on a professional basis vis-à-vis the public is reserved to licensed banks and financial institutions.[6]

Italian Insurance Companies and Securitization Vehicles. The Law Decree permits Italian insurance companies and Italian securitization vehicles to lend to businesses,[7] to the extent that:

- The borrower is identified by a bank or a financial intermediary enrolled with the register kept by the Bank of Italy pursuant to Article 106 of the Italian Banking Law;[8] and
- The bank or the financial intermediary indentifying the borrower retains a "significant interest" in the financing transaction. As regards loans made by insurance companies, "significant interest" means an interest equal to at least five percent of the loan granted by the relevant insurance company. Banks and financial intermediaries will keep the significant interest for the entire life of the loan; however, they may transfer the significant interest to other banks or financial intermediaries during the same life of the loan. Conversely, the law does not state which is the threshold for loans made by securitization vehicles.[9]

In the case of securitization vehicles, the notes issued to fund the financings to be granted by the securitization vehicle must be addressed to "qualified investors" only.[10]

In the case of Italian insurance companies, such entities must also (i) have an adequate internal control and risk management system; and (ii) be adequately capitalized.

The Bank of Italy and IVASS (the Italian authority supervising the insurance market), each within their respective powers, will issue implementing regulations setting forth the operational limits and the other details applicable to lending by, respectively, securitization vehicles and Italian insurance companies.[11]

To further support lending by insurance companies, the Law Decree has provided that financings granted by insurance companies fall within the assets that insurance companies may hold as investments for the purpose of complying with their technical provisions (*riserve tecniche*) requirements.

Finally, SACE S.p.A., which is an export finance company directly owned by Cassa Depositi e Prestiti S.p.A. and indirectly owned by the Italian Ministry of Economy and Finance, is now allowed to lend to Italian businesses.

Undertakings for Collective Investment. The notion of undertakings for collective investment set out by the Italian Unified Financial Act,[12] has been revised by the Law Decree. As a result, undertakings for collective investment can now grant financings out of their own assets (literally, they may invest in "receivables," including those receivables arising from financings granted out of their assets).

Tax

Broadened Scope of Substitute Tax Regime on Medium- and Long-Term Loans. As a rule, certain qualifying lenders may elect to subject medium- and long-term loans to a 0.25 percent (two percent in some cases) lump-sum tax (so-called substitute tax, or *imposta sostitutiva*) that replaces the indirect taxes generally applicable to the loan and the loan documents. The election is available only if the loan has a maturity exceeding 18 months and is made in Italy. The *imposta sostitutiva* is levied on the amount made available.

If the lender makes this election, the loan and the loan documents are exempt from any registration tax, cadastral tax, mortgage tax, or stamp duty that would otherwise apply. The exemption applies not just to the loan itself but also to all deeds, documents, agreements, and formalities incident to the medium- or long-term loan, its execution, amendment, and redemption, as well as to any guarantees of whatever nature granted by anyone at any time and their subrogation, substitution, postponement, and cancellation.

This elective regime is very favorable if the loan is secured by mortgage because, absent the election, a two percent mortgage tax would apply on the maximum amount secured by the mortgage. Other than for very limited statutory exceptions and "scattered" court decisions, banks were basically the only lenders that could qualify for, and thus elect to apply, *imposta sostitutiva*. In addition, the Italian tax authorities have often taken the position that the *imposta sostitutiva* regime does not cover the subsequent transfers or assignments of the loan and of the related security package. These transfers and assignments were therefore subjected to the ordinary indirect taxes.

The Law Decree broadened the scope of application of the *imposta sostitutiva* regime in two important ways:

- The pool of qualifying lenders now also includes (i) Italian securitization vehicles; (ii) insurance companies that are incorporated and licensed under the laws of a

European Union ("EU") Member State; and (iii) undertakings for collective investment (e.g., investment funds) that are set up in a EU Member State or in a European Economic Area ("EEA") country allowing for an adequate exchange of information with Italy (currently, only Iceland and Norway); and

- The exemption from indirect taxes now also covers any subsequent transfer or assignment of the loan, of the receivables therefrom, and of any related security package.

Repeal of Interest Withholding Tax on Certain Cross-Border Loans. As a rule, if a nonresident lender grants a loan to an Italian resident borrower, interest paid on the loan is subject to a 26 percent withholding tax in Italy,[13] unless the lender is eligible for the exemption under the Italian laws that implemented the EU Interest and Royalties Directive. The withholding tax may be reduced (usually to 10 percent) or, in very few cases, zeroed under the double-tax treaties entered into by Italy, where applicable.

The Law Decree repealed the interest withholding tax in cases of cross-border loans that meet certain requirements. As a result, no withholding tax is now levied on the interest if (i) the loan is a medium- or long-term loan; (ii) the borrower is an enterprise (e.g., an Italian commercial partnership, a resident company, or the Italian permanent establishment of a nonresident enterprise); and (iii) the lender is any of the following:

- A bank established under the laws of a EU Member State;
- An insurance company established and licensed under the laws of a EU Member State; or
- An unleveraged undertaking for collective investment (e.g., an investment fund) that is set up in a EU Member State or in a EEA country allowing for an adequate exchange of information with Italy (i.e., Iceland and Norway).

Because the new rules state that the borrower must be an enterprise, the withholding tax exemption should not apply when the borrower is an Italian undertaking for collective investment (e.g., an Italian investment fund). Moreover, it will have to be clarified in due course whether the withholding tax exemption is available if the borrower is an Italian static holding company.

SECURITIZATION TRANSACTIONS

Granting of Financing by Securitization Vehicles

In light of the Law Decree, securitization transactions can be also implemented through the granting of one or more financings by securitization vehicles to the originator-borrower.

Segregation Regime

The segregation regime (or "remoteness") applicable by operation of law to securitization transactions carried out under the Italian Securitization Law has been broadened. In particular, third-party creditors, other than the noteholders, cannot bring any legal action in order to seize or attach the amounts collected and deposited from time to time by the securitization vehicle or by the servicer on bank accounts dedicated to securitization transactions held with a depository bank.[14]

As a result, in a bankruptcy scenario involving the depository bank, the sums deposited on a segregated bank account opened with the depository bank (i) are not subject to the suspensions of payment otherwise provided by the Italian Bankruptcy Law;[15] and (ii) are automatically transferred back to the securitization vehicle without the need to file any petition with the bankruptcy receiver. The redemption of the amounts owed to the securitization vehicle takes place out of any distribution plan prepared by the bankruptcy receiver and includes also any amounts due to the securitization vehicle following the bankruptcy.

Moreover, no legal actions can be brought by third-party creditors, other than the noteholders, to seize or attach the receivables arising from the securitization transaction and/or any amount paid by the borrower to the securitization vehicle in the case of a securitization transaction carried out by a securitization vehicle through financing and starting from the date upon which the financing is granted.

Servicer

The fairness of the financing transaction as well as its compliance with the applicable laws must be assessed by the securitization servicer.

DEBT MARKET

Withholding Tax Exemption on Bond Interest Broadened

The Law Decree has broadened the scope of Legislative Decree No. 239 of April 1, 1996, which already provided that interest paid to eligible nonresident investors on certain debt-like securities is exempt from tax in Italy. In particular, no withholding tax is levied if the beneficial owner of the interest is resident in a white-listed country and has no permanent establishment in Italy. White-listed countries are countries or territories that allow for an adequate exchange of information with Italy. They are listed in a regulation issued by the Ministry of Finance and periodically updated.

Before the enactment of the Law Decree, nonresident holders could benefit from a withholding tax exemption on interest paid on the following securities:

- Bonds, bond-like securities, and commercial papers that were issued by Italian-resident banks, regardless of whether these securities were listed on a regulated market;
- Bonds, bond-like securities, and commercial papers, whether listed or not, that were issued by resident companies whose shares were traded on regulated markets or multilateral trading facilities of a EU Member State or a EEA country included in the Italian white list (i.e., Iceland and Norway); and
- Bonds, bond-like securities, and commercial papers that, although issued by non-listed resident companies, were listed on a regulated market or a multilateral trading facility of a EU Member State or a EEA country included in the Italian white list (i.e., Iceland and Norway).

The Law Decree has added a new item to the list of exemptions: interest on bonds, bond-like securities, and commercial papers issued by nonlisted resident companies will be exempt from Italian withholding tax if the security holder is a "qualified investor" under article 100 of the Italian Unified Financial Act (e.g., banks, broker-dealers, investment funds, pension funds, etc.), regardless of whether the security is listed. It is not clear, at this stage, whether the exemption is available only in the event the entire bond issuance is subscribed to by "qualified investors."

Finally, the Law Decree has introduced a blanket withholding tax exemption that applies to interest deriving from any type of bond, bond-like security, and commercial paper and paid to:

- Undertakings for collective investment, whether set up in Italy or in another EU Member State, if: (i) their units are entirely held by "qualified investors" under article 100 of the Italian Unified Financial Act; and (ii) more than 50 percent of their assets are the aforesaid debt securities and commercial papers; and
- Italian securitization vehicles, if: (i) their notes are entirely held by "qualified investors" under article 100 of the Italian Unified Financial Act; and (ii) more than 50 percent of their assets are the aforesaid debt securities and commercial papers.

The exact interaction between these two new withholding tax exemptions is not completely clear at this stage and will need to be further assessed.

These measures aim at facilitating private placements by Italian private companies. The goal is to make Italian private companies less reliant on bank debt and lift some of the obstacles that they typically face when seeking to fund their operations.

CONCLUSIONS

Even after the enhancement of the Law Decree, Italian-based and operating banking institutions will still play a crucial role in the Italian lending market, given that they are vested with the task of identifying the potential borrower and are required to keep a significant interest in the financing transaction.

Nevertheless, the Law Decree introduces significant changes resulting in the opening of the Italian lending market to additional qualifying lenders. As a consequence, subject to the eligibility requirements set out by law, investors will be able to grant financing in Italy through securitization transactions or through the setup of undertakings for collective investment, thus without the need to apply in advance for a banking license. Moreover, the Law Decree may foster synergic relationships between banks and new qualifying lenders to the benefit of the Italian lending market. Finally, foreign investors also may be attracted to invest in Italy by the significantly favorable tax and segregation regimes introduced by the Law Decree.

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ENDNOTES

1 Please refer to http://www.jonesday.com/the-italian-government-introduces-measures-to-boost-the-italian-lending-market-07-09-2014/.

2 The Law Decree was published in the Italian Official Gazette No. 144 of June 24, 2014, and has been in force since the day immediately following its publication (i.e., June 25, 2014). The conversion law was published in the Italian Official Gazette No. 192 of August 20, 2014 and entered into force the day immediately following its publication. As a consequence of the above, any reference in this *Commentary* to the Law Decree means a reference to the Law Decree as converted into law, including amendments, by Parliament.

3 Law No. 130 of April 30, 1999, as amended and restated from time to time.

4 The definition of "Italian insurance companies" is set out under Article 1 letter (u) of Legislative Decree No. 209 of September 7, 2005, as amended and restated from time to time.

5 In this respect, please note that article 114 of the Italian Banking Law—as defined below and as amended by the Law Decree—seems to limit to Italian insurance companies only the possibility of carrying out lending activity in Italy vis-à-vis the public.

6 Lending in breach of the lending license is a criminal offense under Italian law.

7 Lending vis-à-vis consumers and micro-enterprises continues to be reserved to licensed banks and financial institutions.

8 Legislative Decree No. 385 of September 1, 1993, as amended and restated from time to time.

9 In this respect, please refer to note 11 below.

10 The definition of "qualified investors" set forth under CONSOB Regulation October 29, 2007, No. 16190—which implements the provisions on intermediaries under the Italian Unified Financial Act (as defined below)—includes among others, (i) Italian and foreign entities authorized and regulated to operate on financial markets (e.g., banks, investment firms, other authorized or regulated financial institutions, insurance companies, and pension funds); (ii) large enterprises (i.e., enterprises satisfying at least two of the following requirements: (a) total assets of at least €20 million, (b) net revenues of at least €40 million, and (c) own capital resources of at least €2 million); (iii) institutional investors whose principal activity is investment in financial instruments, including securitization entities; and (iv) other investors who request to be treated as professional clients, provided that certain requirements set forth by the Italian Unified Financial Act are met.

11 Such implementing regulations should establish, among others: (i) the minimum capital requirements, as far as insurance companies are concerned; and (ii) the applicable retention thresholds as far as securitization vehicles are concerned. As a matter of fact, the retention thresholds applicable to securitization vehicles have not been specified by the conversion law of the Law Decree although the conversion law dossier pointed out that securitization vehicles could lend on the same terms and conditions applicable to insurance companies. The retention threshold issue shall be, therefore, handled by the Bank of Italy.

12 Legislative Decree No. 58 of February 24, 1998, as amended and restated from time to time.

13 Until June 30, 2014, the withholding tax rate was 20 percent.

14 In case of a bank account opened by the servicer, the segregation regime applies only up to those amount credited on the issuer's bank account to be transferred to the relevant securitization vehicles under the securitization transactions managed by the servicer.

15 Royal Decree No. 267 of March 16, 1942, as amended and restated from time to time.