

Italy: New Rules on Financial Leases Provide Clarity

IN SHORT

The Situation: The Italian Parliament has enacted new rules on financial leases.

The Result: A statutory definition of "financial lease" and rules in the case of breach by the lessee have been introduced.

Looking Ahead: The new rules provide more clarity, and the market for leasing portfolios acquisitions will benefit.

Law no. 124 of August 4, 2017 ("Law 124") provides important new rules on financial leases in Italy. It introduces a statutory definition of "financial lease" and deals with the event of serious breach (*grave inadempimento*) by the lessee.

Definition of "Financial Lease"

Italian law already had various provisions governing financial leases (for regulatory, accounting, tax, and bankruptcy purposes), but it did not contain a general definition of "financial lease." Law 124 defines "financial lease" as:

the agreement whereby [a] registered bank or [b] financial intermediary enrolled with the register set forth by Article 106 of [the Italian Banking Law] undertakes [as Lessor] with the Lessee to buy or build an asset according to the Lessee's choice and instructions and, while the Lessee takes the risks relating to the loss/deterioration of the asset, [the Lessor] makes the asset available to the Lessee for a given period of time for consideration which takes into account the purchase or construction price and duration of the agreement. Upon expiry of the lease agreement, the Lessee has the option to purchase the asset at a pre-determined price; or, in case of not exercise of such option, must return the asset to the Lessor.

This definition basically reproduces the one typically used in the market and in the statutes in relation to financial leases of first-dwelling/abode real estate properties.

The reference to a bank or intermediary registered pursuant to Italian Banking Law raises the question whether Law 124 restricts the possibility to act as lessor under a financial lease only to banks and financial intermediaries, thereby excluding other intermediaries (funds and insurance companies) that are otherwise permitted to carry out a lending activity in Italy.



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Serious Breach by the Lessee

In the case of a serious breach by the lessee, the lessor is entitled to terminate the lease. A serious breach occurs if the lessee fails to pay six monthly rentals or two quarterly rentals for real estate assets, or four monthly rentals for other assets.

In the case of termination of the agreement, the lessor is entitled to have the asset returned to it and sell the asset and be paid with the proceeds of the sale. The lessor is obliged to remit to the lessee the proceeds from the sale of the asset at market value, less the aggregate of: (i) the rentals due and still unpaid at the date of termination of the lease; (ii) the rentals not yet due and payable (but only with respect to the principal amount, not interest); (iii) the price payable under the lease agreement for the exercise of the purchase option by the lessee; and (iv) any costs and expenses borne by the lessor for the recovery of the asset, its evaluation, and its custody for the period prior to the sale. This is without prejudice to the rights of the lessor if the price obtained from the sale of the asset is lower than the amounts due by the lessee to the lessor.

These rules are similar to those already provided for in a bankruptcy situation and for first-dwelling/abode real estate properties, both of which continue to apply. They imply the invalidity of penalty clauses, which are typically included in financial leases and which require the lessee to pay to the lessor, in any event, the full amount due for both principal and interest.

The lessor may sell the asset on the basis of the value resulting from publicly available market surveys prepared by professional appraisers. When these are not available, the lessor must obtain a valuation made by an expert appointed jointly by the parties or by an expert independently chosen by the lessor among three professional appraisers. The sale procedure must meet efficiency, transparency, and publicity criteria.

Entry Into Force

The new rules enter into force on August 29, 2017. It is a moot point whether they are wholly or partly applicable to existing financial leases. If they are, it is a further moot point whether leases for which a termination event has already occurred at the time of entering into force of Law 124 are covered by the new provisions.

FOUR KEY TAKEAWAYS

1. A new statutory definition of "financial lease" has been introduced in Italy.
2. In the case of a serious breach by the lessee, the lessor is entitled to terminate the agreement and sell the asset.
3. In the case of sale of the asset, the lessor can retain an amount equal to the rentals due and still unpaid, the principal amount of rentals not yet due and payable, the purchase option price payable by the lessees at the end of lease, and any costs and expenses incurred.
4. The exact impact of the new rules on existing leases needs to be carefully assessed.

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