
Italy

Negotiated M&A Guide

Corporate and M&A Law Committee

Contact

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1. Introduction

This guide provides an overview of mergers and acquisitions of unlisted joint stock companies (*società per azioni*), limited liability companies (*società a responsabilità limitata*) and/or businesses or assets (*azienda* or *ramo d'azienda*) under Italian law.

As a preliminary remark it is worth noting that the contractual/legal practice in share and asset deals is largely similar to those of most other continental European countries, even if it has been largely influenced, as far as contractual standards are concerned, by common law experience.

(a) Legal Framework

The legal framework governing mergers and acquisitions of unlisted joint stock companies, limited liability companies and/or businesses, is primarily set forth in the Italian Civil Code. Unlike the civil codes of other European countries, the Italian Civil Code also governs many of the principal aspects of corporate law.

As from its reform of 2004, the portion of the Italian Civil Code governing joint stock companies, limited liability companies and limited partnerships (*società in accomandita per azioni*) sets forth provisions aimed at facilitating the carrying out of mergers and acquisitions in Italy. In particular, the 2004 reform:

- expressly addressed leveraged buy-outs and provided a specific regulation thereof in the Civil Code, thereby erasing any doubt with regard to their validity under Italian Law;
- provided greater flexibility for limited liability companies by granting the holders of interests in such companies (the so-called “quotaholders”) with the power to adopt articles of association that meet their specific needs on matters such as governance of the company or the exit therefrom;
- introduced greater flexibility with respect to the governance of joint stock companies by allowing shareholders to implement, in lieu of the traditional Italian system, the so-called “dualistic system” (based on the governance usually applied by German companies), and the so-called “monistic system” (similar to the governance applied by US or UK companies);
- increased the limits for the issuance of bonds by unlisted joint stock companies, and further provided for the possibility to exceed such limits upon the occurrence of certain conditions, the most relevant of which is the subscription of the bonds by financial institutions;^y and
- granted the limited liability companies the power to issue bonds, which can be underwritten only by financial institutions.

In recent years, additional measures have been enacted in order to ensure new methods of finance and stimulate investors to seek funding on the risk capital market, as well as to improve the competitiveness of Italian companies. In particular, the following measures could be relevant in the framework of mergers and acquisitions transactions:

- Law Decree No. 83/2012, converted into Law No. 134/2012, set forth that the limits normally provided for under the Civil Code for the issuance of bonds by unlisted joint stock corporations (*i.e.*, amount of bonds not exceeding the double of the concerned company’s overall amount of corporate capital, legal reserves and available reserves) no longer apply to bonds convertible into equity or bonds to be listed on regulated markets or multilateral trading facilities;
- Law Decree No. 91/2014, converted into Law No. 116/2014, provided considerable amendments to voting rights in joint stock corporations. Article 2351, Paragraph 4 of the Italian Civil Code now sets forth the possibility for unlisted joint stock companies to issue shares with up to three votes each. According to what is set forth in the By-laws of the concerned company, such multiple voting can be exercised at all shareholders’ meetings or only at shareholders’ meetings resolving upon specific

matters. For listed companies, the Law Decree No. 91/2014 provided the possibility of issuing multiple voting shares, though subject to certain restrictions, and loyalty shares (*i.e.*, shares with an increased voting right, up to a maximum of two votes per shares as “loyalty bonus” to long-terms shareholders). As a result, the principle of “one share, one vote”, which has always been a cornerstone of Italian corporate law, has been definitely overcome;

- Law Decree No. 3/2015, converted into Law No. 33/2015 – with regard to the so-called “innovative small and medium-size enterprises” – and Law Decree No. 179/2012, converted into Law No. 221/2012 – with regard to the so-called “innovative start-up enterprises” (*start-up innovative*) and “certified incubators” (*incubatori certificati*) – provided specific corporate and tax benefits for Italian companies performing innovative business activities.

2. Structure of the Transaction

(a) Alternative Structures

Similar to other European countries, M&A transactions in Italy may be categorized as follows:

(1) share/quota deals;

(2) asset deals, which can be further sub-divided into the following main two deal structures

(A) purchase and sale of assets;

(B) contribution of assets;

(3) mergers and de-mergers.

Structures may vary depending on the specific characteristics of any single deal and it may also be the case that different structures are combined within the same transaction. A key consideration in the choice of acquisition structure will be the immediate and long-term tax consequences of the transaction. Some basic notions of tax principles applicable to Italian M&A transactions are thus of essence in this respect.

(b) Tax Issues

The tax treatments of the most common structures are briefly described below:

(1) Sale/Purchase of Shares and/or Quotas

- For income tax purposes, the sale of shares or quotas may imply a taxation (tax deduction) of capital gains (capital losses) achieved by the seller in connection with the sale. Capital gains/losses are determined as the difference between the sale price of the shares/quotas and the cost incurred by the seller to purchase such shares/quotas. Income taxes are levied by applying 24% (when the seller is an Italian joint stock company or an Italian limited liability company), or progressive income tax rates from 23% up to 43% (when the seller is an Italian individual or an Italian partnership) on the capital gains. However, if the seller is an individual a 26% tax applies on the capital gains if the shares or quotas that are sold represent less than 20% of the voting rights of the underlying Italian company (2% of the voting rights in case shares of a listed company are sold) or less than 25% of the share capital (5% of the share capital in case shares of a listed company are sold). If the seller is a joint stock company or a limited liability company and certain requirements are met (*i.e.*, shares/quotas have been held by the seller for a period exceeding 12 months; the company to which such shares/quotas are referred to is an “operative” company and it is not resident in a black-listed country), the *Participation Exemption* rule (“PEX”) is applicable. PEX implies that capital gains are taxable up to 5% of their amount. On the other hand, PEX implies that any capital loss incurred with the sale of the shares/quotas is not tax deductible for the seller. When the seller is a foreign entity,

capital gains arising from the sale of shares or quotas of an Italian resident company are generally taxable in Italy unless a treaty against double taxation is in force between Italy and the country where the seller is resident. Indeed, most tax treaties signed by Italy provide that capital gains arising in connection with the sale of shares/quotas are taxable only in the country where the seller is resident. The buyer is not taxable in connection with the purchase of shares or quotas.

- For Value Added Tax ("VAT") purposes, sale of shares or quotas are exempted from the application of VAT.
- For Registration tax purposes, sale of shares or quotas may imply the application of Registration tax up to Euro 200.00.
- Tobin Tax, a 0.2% so-called Tobin Tax applies on the transfer of shares of an Italian SpA or Sapa (it does not apply on the transfer of quotas). The tax is reduced to 0.1% if listed shares are sold.

(2) (A) Sale/Purchase of Assets (Going Concern)

- For income tax purposes, the sale of a business as a going concern implies a taxation of capital gains achieved by the seller in connection with the sale. Capital gains are determined as the difference between the sale price and the net assets value of the going concern, *i.e.*, cost of assets net of liabilities transferred with the business. Income taxes are levied by applying 24% (when the seller is an Italian joint stock company or an Italian limited liability company) or progressive income tax rates from 23% up to 43% (when the seller is an Italian individual or an Italian partnership) on the capital gains. However, the seller (if a joint stock company or a limited liability company) may opt to tax the capital gain by 5 yearly equal installments if the business has been carried on by the seller for over 3 years. The buyer is not taxable in connection with the purchase of a going concern.
- For VAT purposes, the sale of a going concern is excluded from the application of VAT.
- For Registration tax purposes, the sale of a going concern is subject to Registration tax by applying different tax rates depending upon the type of assets transferred, including goodwill (if any). For example, real estate is subject to 9% Registration tax, whereas other assets (including goodwill) are subject to 3% Registration tax. The taxable base is represented by the market value of the assets net of the transferred liabilities resulting from the seller's statutory accounts. The seller and the buyer are jointly liable for the payment of Registration tax. The parties may agree, however, to charge the payment of the Registration tax to the buyer only. Nevertheless, such agreement would not have any effect vis-à-vis the Italian tax administration.
- For cadastral and mortgage tax purposes, real estate transferred with the going concern is subject to cadastral and mortgage taxes of Euro 100.00.

(2) (B) Contribution of a Going Concern

- For income tax purposes, if the seller is an individual, a contribution in kind implies a taxation of the capital gains achieved by the transferor. Capital gains are determined as the difference between the market value of the assets which are contributed and the cost incurred by the transferor to purchase such assets. Income taxes are levied by applying progressive income tax rates from 23% up to 43% (when the seller is an Italian individual or an Italian partnership) on the capital gains. If the seller is a joint stock company or a limited liability company, the contribution of a business as a going concern between companies resident in Italy, or between foreign entities provided that the going concern is located in Italy, may be effectuated without any taxation for the transferor ("tax neutral contribution" or "TNC"). In the case of TNC, the transferee may opt to increase the value of the received asset, up to their market value, by paying a lump-sum tax from 12% up to 16% on the increased asset values. Furthermore, in the case of TNC, the transferor may avail itself of PEX in connection with the subsequent sale, if any, of the participation held in the transferee. In such a case, the 12-month

period needed to apply PEX can be computed by including the period along which the going concern was carried on by the transferor.

- For VAT purposes, a contribution of a going concern is excluded from the application of VAT.
- For Registration tax purposes, a contribution of a going concern is subject to a Registration tax equal to Euro 200.00.
- For cadastral and mortgage tax purposes, real estate transferred with the going concern is subject to the application of cadastral and mortgage taxes equal to Euro 400.00.

(3) Mergers and De-mergers

- For income tax purposes, mergers and de-mergers are completely tax neutral. This implies that any capital gains (capital losses) arising in consequence of a merger and de-merger are not taxable (tax deductible) in the hands of the merging or de-merged company. However, the merging company (in case of a merger) or the beneficiary company (in case of a de-merger) may opt to increase the value of the received assets, up to their market value, by paying a lump-sum tax from 12% up to 16% on the increased assets values. Note that tax losses carried forward may be limited as a consequence of a merger or de-merger. In particular, tax losses carried forward by the companies participating in a merger or a de-merger may be used by the company resulting from the merger or de-merger to offset its taxable profits, but only to the extent of the net equity recorded in the last approved statutory financial statements of the company originating the losses, and only if such company meets a “vitality test”.
- For VAT purposes, mergers and de-mergers are excluded from the application of VAT.
- For Registration tax purposes, mergers and de-mergers are subject to Registration tax equal to Euro 200.00.
- For cadastral and mortgage tax purposes, real estate transferred as a consequence of a merger or de-merger is subject to the application of cadastral and mortgage taxes equal to Euro 400.00.

With a sale of a business as a going concern, it is very common to structure the transaction by: (i) contributing the going concern to a newly formed entity (preferably a joint stock company or a limited liability company) by means of a TNC and (ii) selling the participation into such newly formed entity under the *PEX* rule. Such structure will allow the seller to minimize the overall tax burden since it is not subject to the Italian anti-avoidance tax rule and, therefore, the Italian tax administration should not be able to disallow the relevant (tax) effects. However, in the last year the Supreme Court ruled in the sense of applying to this kind of structure for registration tax purposes the same taxation provided for the sale of the going concern (i.e. basically 3% tax or 9% if real properties are involved). In addition, it is important that a going concern (and not single assets) be contributed, otherwise the capital gains, if any, arising from the contribution in kind would be fully taxable.

The sale of a going concern may be tax efficient if the seller has tax losses carried forward to be offset against the capital gains arising from the sale. However, it is worth noting that the Registration tax burden may be heavy and the risk of a tax assessment on the value of the goodwill could be high.

Mergers and de-mergers do not usually imply tax savings since they are neutral from a tax perspective, even if, in certain circumstances, the merging company or the beneficiary (in case of a de-merger) are allowed to increase the value of the assets received as a consequence of the merger or de-merger. Such increase implies the payment of a lump-sum tax from 12% to 16% of the increased value, which possibility is also permitted under a TNC. An increased value of assets implies higher depreciation or lower taxable capital gains at the time of a subsequent sale, which would be respectively tax deductible

and taxable by applying a 27.90% overall tax rate. However, in such cases, the assets cannot be sold before the end of the following fourth fiscal year.

(c) Principal Legal Aspects of Share/Quota Deals

While in most instances the choice between a share/quota deal and an asset deal will be driven by tax-related considerations, there are several purely legal implications to be taken into account in structuring a transaction and which need to be carefully addressed while drafting the relevant agreements.

(1) Shares and Quotas

As a preliminary remark, it is important to note that the most common forms of Italian corporate vehicles are the joint stock company ("*Società per Azioni*" or "*SpA*") and the limited liability companies ("*Società a responsabilità limitata*" or "*Srl*"), both of which have the benefit of limited liability. There are, however, several important differences between these two types of companies. Leaving aside the analysis of the implications related to the relationship among shareholders when the subject matter of the acquisition is less than 100% of the corporate capital, the principal difference between an SpA and an Srl in this context relates to how ownership is transferred:

- The corporate capital of an SpA is represented by share certificates, which are most often transferred before a notary public or bank officer. Such transfer must be recorded in the company's "Shareholders Ledger" in order for it to be enforceable vis-à-vis the target company, *i.e.*, the company whose shares are being sold or transferred. In case of uncertificated shares, the transfer is formalized by registration in a centralized system;
- The corporate capital of an Srl is divided into "quotas", which are not securities. It is therefore necessary to execute an agreement before a public notary (or a tax consultant), and to file such agreement with the "Companies Register" in order to have the transfer of the ownership enforceable even vis-à-vis the target company and third parties.

As noted, the aforementioned formalities are required to have the transaction enforceable vis-à-vis the target company and third parties. Such formalities are not, however, required in order to effectuate the transfer of ownership rights of the shares and/or quotas as among the parties.

Under Italian law, for both Srl's and SpA's, an analysis of the company's by-laws is advisable, since such documents may set forth restrictions on the transfer of ownership of shares and quotas. It is not unusual, for example, to find restrictions in a company's by-laws such as lock-ups, rights of first refusal, or board of directors approval, all of which must be taken into account during negotiations and drafting.

(2) Seller and Buyer Preferences for Share and/or Quota Deals

As compared to an asset deal, the main benefit of a share/quota deal is that a share/quota deal requires fewer formalities and provides greater certainty in respect of the continuity on the underlying business, with the notable exception of the effects of any change of control provisions contained in agreements entered into by the target company.

Additionally, the change of controlling interest in the target company does not determine a formal change of employer, and there are no express legal obligations to notify, or consult with, trade unions in advance of the quota/share purchase, as is the case for the transfer of a business ("*trasferimento ramo d'azienda*").

From the seller's perspective, another major advantage to a share/quota deal is that all liabilities remain with the company and therefore pass to the buyer upon transfer of ownership. In addition, there is no implied/automatic seller's warranty with respect to the assets of the target company. For this reason,

buyers will usually request specific representations and warranties and indemnity provisions in the purchase and sale agreement (*see more in depth below*).

(d) Principal Legal Aspects of Asset Deals

Asset deals are typically negotiated when the subject matter of the sale is a business division/branch of the seller or one of the businesses of the seller. Asset deals, *i.e.*, purchases of a business as a going concern, are relatively common in the Italian market, particularly in small size deals.

The Italian Civil Code provides specific rules setting forth the definition of the business, or business division/branch (“*azienda*” and “*ramo d’azienda*”) and their transfers (art. 2555 - 2562 of the Italian Civil Code). These rules are essentially designed to:

- enhance continuity of the business,
- protect both creditors and employees of the business.

The transfer of the business requires the entering into of a notarial deed, which sets forth the assets and liabilities, as well as the goodwill for tax purposes, to be transferred. The deed must be filed with Companies Registry.

(1) Seller and Buyer Preferences for Asset Deals

The transfer of a business is subject to certain formalities, including certain pre-closing formalities, such as prior notice to trade unions in the event that more than 15 employees work for the transferred business, as well as certain post-closing formalities, such as endorsement of authorizations/licenses.

Under Italian law, the continuity of the business is only guaranteed to a certain extent. Article 2558 of the Italian Civil Code provides that agreements related to the business existing at the time of the transfer are automatically assigned/novated to the buyer if they are not of a personal nature. However, the other contracting party is entitled to terminate any such agreements with the company for a “justified reason” within three months from the transfer. In the case of termination, the buyer may recover damages from the seller.

From the seller’s perspective, an asset deal may be less advantageous than a share/quota deal since, by operation of law, the seller:

- remains jointly and severally liable with the buyer for liabilities existing before the transfer (art. 2560 of the Italian Civil Code);
- assumes a 5-year non-competition obligation (art. 2557 of the Italian Civil Code); and
- grants an implied warranty on title to the assets and the absence of defects.

The buyer of a business becomes jointly and severally liable with the seller for all liabilities of the business recorded on the books of the company at the time of the transfer, as well as any tax liabilities of the seller in respect of the business up to the value of the business. The buyer may limit its tax liability by requesting a certificate from the competent tax offices. The issuance of a certificate stating that no tax is due, or the non-issuance of the certificate within 40 days as from the filing of the petition, releases the buyer from such joint and severally liability.

(e) Principal Legal Aspects of Mergers and De-mergers

(1) Mergers

Mergers are regulated pursuant to Articles 2501 - 2505 *quater* of the Italian Civil Code, which cover two types of mergers:

- mergers by acquisition, whereby a company merges with and into another existing company, with all assets and liabilities transferring to the surviving company;
- mergers by incorporation of a new company, whereby two or more companies merge with and into a newly created company, with all assets and liabilities transferring to the newly incorporated company.

(2) De-mergers

Another legal mechanism that may be utilized in order to segregate a business for subsequent resale to a prospective buyer is the “de-merger”. The procedure for de-mergers is set forth by Articles 2506 - 2506 *quater* of the Italian Civil Code.

A de-merger may take place by transfer of all of a company’s assets and liabilities to a plurality of companies, which may be either pre-existing or newly incorporated (“complete de-merger”). In this case, the de-merged company can be automatically dissolved without any liquidation or winding up procedure.

Alternatively, a de-merger may be carried out by a transfer of only portion of a company’s assets and liabilities to one or more other companies, which, again, may be either pre-existing or newly incorporated (“partial de-merger”). In this case, the de-merged company will continue to exist.

In both total and partial de-mergers, shares and/or quotas of the beneficiary companies are attributed to the shareholders of the de-merged company.

(3) Seller and Buyer Preferences for Mergers and De-mergers

For not listed companies, mergers and de-mergers are not frequently used in the Italian market due primarily to the considerable time frame required for completing a merger and/or de-merger.

Indeed, the Italian Civil Code sets forth a lengthy procedure for carrying out mergers and/or de-mergers, which involves certain compulsory steps, including approving of financial statements, drafting and approving a merger or de-merger plan, obtaining experts’ appraisals, filing with Companies Registry, elapsing of certain time periods for the opposition of creditors, preparing a merger or de-merger deed, etc.

3 Pre-Agreements – Letter of Intent

Consistent with commercial practice worldwide, the entering into of a letter of intent in the initial stages of negotiations has become rather common in Italy.

(a) Purpose and Content of the Letter of Intent

Through the execution of a letter of intent, the parties to a potential transaction for the acquisition of an Italian company or business usually pursue two different aims:

- on the one hand, in the light of the complexity of the acquisition agreement and the significant number of contractual elements to be agreed upon therein, the parties to a letter of intent intend to settle and memorialize the terms and conditions of the potential transaction on which they have

already reached an agreement. In particular, by means of the letter of intent, the parties will typically agree that, in the event the parties are able to reach an agreement on all outstanding contractual terms and expressly state their mutual intention to enter into definitive agreements, such definitive agreements shall also contain the terms and conditions already agreed to and provided for in the letter of intent. The precise terms and conditions agreed to by the parties in the letter of intent will vary according to specifics of the potential transaction;

- on the other hand, the parties will often also seek to define the modalities through which they will perform the negotiations aimed at executing definitive agreements. The provisions that are typically set forth in such section of a letter of intent include the following:

- definition of the timetable and the procedures pursuant to which the potential buyer will perform its due diligence activities on the target company. In the event that such activities entail the access to an actual or virtual data room, the letter of intent may also set forth the data room regulations. The letter of intent may subordinate the continuance of the negotiations between the parties to a satisfactory outcome of the due diligence activities by the potential buyer;
- confidentiality undertakings by both parties in relation to the existence and content of the letter of intent, the potential transaction and any information that a party may obtain in connection therewith;
- exclusivity undertakings, pursuant to which the potential seller agrees for a certain term not to (a) solicit or encourage the submission of proposals or offers from any person other than the potential buyer in relation to the sale, transfer, encumbrance or disposal of any interest in the target company or in any entity of its group or any of their respective assets; (b) enter into or participate in any discussion or negotiation or to otherwise communicate with any person other than the potential buyer and its advisers in relation to the possible sale, transfer, encumbrance or disposal of any interest in the target company or in any other entity of its group, or any of their respective assets; and
- an agreement as to governing law and dispute resolution.

(b) General Non-Binding Nature of the Letter of Intent

According to Italian case law, the qualification of a document as “letter of intent” is not sufficient to rule out that the sections thereof that settle the terms and conditions of the potential transaction will give rise to a binding contractual relationship between the parties. This is particularly so when the parties have reached an agreement on all the essential elements of a purchase and sale agreement. Indeed, Italian judges do not base their assessment of the letter of intent as a binding or a non-binding document on the qualification of the document as “letter of intent”, but rather on the evaluation of the mutual intent expressed by the parties thereto, through the interpretation of the relevant clauses and the analysis of the behavior observed by the parties prior to and after the entering into the letter of intent.

As a consequence, in Italian practice, the letter of intent will expressly state the parties’ intention that the letter of intent is a non-binding agreement that does not give rise to any obligation to execute any definitive documentation or otherwise consummate the transaction contemplated therein. The typical exceptions to the non-binding nature of the letter of intent include the parties’ obligations with respect to confidentiality and exclusivity, and the parties’ agreement as to governing law and dispute resolution.

The insertion of a clause aimed at excluding from the letter of intent any binding commitment on the part of the parties to consummate the transaction contemplated thereby does not exclude, however, the duty of the parties, pursuant to Section 1337 of the Italian Civil Code, to act in good faith during the negotiations and, as a result, does not prevent a party from being liable vis-à-vis the other party in case of its unjustified withdrawal from the negotiations.

According to Italian case law, such pre-contractual liability arises in the event that the non-withdrawing party had, on the basis of the agreement already reached on the principal terms and conditions of the potential transaction, reasonably relied on the entering into of the potential transaction and that such reliance is thereafter frustrated by the withdrawal by the other party, without just cause, from the negotiations. In such a case, the withdrawing party is bound to compensate the other party for the damages that the latter suffered due to the negotiations, such as the relevant expenses and legal fees and, more significantly, the profits that the non-withdrawing party is able to prove that it would have gained had it accepted an alternative proposal received during the negotiations with the party exercising the unjustified withdrawal. In the light of this possible liability, the wording of letters of intent requires under Italian law careful assessment.

4. Acquisition Agreement

(a) Holdback and Escrows

In the Italian market the most common form of consideration is cash. The terms and conditions of payment may vary greatly depending upon several factors, including the financial strength of the parties, the industries in which the target company conducts its business, etc. It is not unusual to have such terms and conditions defined by the parties at an early stage, including in any pre-agreements.

While it is impossible to define a typical payment arrangement in M&A deals in Italy, some of the most common alternatives observed in the Italian market include:

(1) Down Payments

In case of significant time delay between signing and closing, a seller may be able to obtain a down payment from the buyer at the time of signing. Clauses relating to down payments must be carefully drafted since, depending on the wording and to references to relevant articles of Italian Civil Code, the down payment may be regarded as a termination fee. For example:

- when reference is made to art. 1386 of the Italian Civil Code (the so-called “*caparra penitenziale*”), should a buyer elect to abandon the preliminary purchase and sale agreement, the down payment may be retained by the seller in lieu of damages. This termination fee may also, by agreement, run in favor of the buyer; and
- when reference is made to art. 1385 of the Italian Civil Code (the so-called “*caparra confirmatoria*”), should a buyer fails to fulfill its closing obligations, the seller may retain the advance payment or seek compensation for damages.

(2) Bank Guarantee or Escrows between Signing and Closing

If the seller is concerned about the buyer's ability to pay the consideration when due (usually at closing) it may require the buyer:

- to deposit the amount due in a joint bank account (an escrow account) or an account in the name of a third party, such as a notary, during the interim period. In this case, the parties should enter into an escrow agreement (*i.e.*, a deposit in the seller's interest pursuant to art. 1773 of the Italian Civil Code) setting forth the circumstances, terms and conditions in which the money is released. In the Italian market, escrow agents are typically only willing to enter into escrow agreements to the extent that their obligations are clearly stated and the trigger mechanisms for the release of the relevant funds are clearly defined; or
- to deliver a bank guarantee (or parent company guarantee)

(3) Escrow Agreements as Closing Mechanism

As mentioned in section 2 (“Structure of the Transaction”) above, the formalities to have a transfer of shares, quotas or businesses from a buyer to a seller enforceable vis-à-vis third parties are fairly straightforward. Once again, the following actions are required:

- share deal: endorsement of share certificates before a public notary or bank officers and annotation of the transfer on the Shareholders' Ledger;
- quota deal: execution of a public deed before a notary (or tax consultant) and filing with Companies Registry;
- asset deal: execution of a public deed and filing with Companies Registry.

However, considering the time needed for completing payment in case of payment by wire transfer, or in the case of complex closing obligations involving, for example, several target companies or partial business re-organization and/or carve-outs, the parties may agree to enter into an escrow agreement in order to avoid uncertainty during the closing.

(4) Holdbacks and Escrows after Closing

In the Italian market, the consideration is quite often paid in full upon closing. However, it is not uncommon for the parties to agree to have part of the consideration:

- withheld against breaches of representation and warranty (indemnity escrow);
- deferred and conditional upon the future performance of the target company (earn-out mechanism);
- withheld while the closing accounts for any price adjustment mechanisms are being drafted.

When the buyer's financial strength is uncertain, the seller may seek some form of guarantee from the buyer for the payment of any consideration that has been deferred and/or withheld. In addition to the bank guarantees and escrow mechanisms discussed above in sub-section (2), the seller may request that the buyer grant a pledge on the shares and/or quotas of the target company.

(b) Representations and Warranties

(1) Representation and Warranty Clauses

As mentioned in section 2 (“Structure of the Transaction”) above, asset deals and share and/quota deals differ in terms of the scope of the “implied” representations and warranties automatically granted by the seller to the buyer pursuant to Italian law provisions. In share and quota deals, the implied/automatic seller's warranty is limited to the ownership of the shares and quotas, and it is not extended to the assets of the target company, as it is in assets deals. In share/quota deals, representation and warranty provisions are therefore essential in order to allow the buyer to shift some of the liabilities of the target company back to the seller.

This difference between deal structures, however, has become less relevant in practice as a result of the use of more sophisticated and detailed agreements. In both asset deals and share/quota deals, it is a standard practice, even in small size deals, to include extensive representation and warranty provisions in the purchase and sale agreement, whose wording must be carefully tailored and assessed on the basis of the nature of the target company's business.

(2) Typical Qualifications

In Italian practice, representation and warranty provisions are often subject to certain qualifications, which are extensively negotiated between buyer and seller. The discussions between the parties typically center on materiality and disclosure/knowledge qualifications.

Negotiations on materiality qualifications are generally more straightforward, and are usually linked to the negotiations on indemnity baskets/thresholds.

A greater negotiation effort is usually devoted to disclosure/knowledge qualifications. Although it is quite common for buyers to require the sellers to give full and unqualified representations and warranties, the typical outcome of the negotiation, in particular in cases wherein extensive due diligence has been carried out by buyer, is to have the representations and warranties qualified by disclosures made by the seller. The scope of “disclosure” qualifications may vary significantly, and their implications are largely dependent upon the wording of the relevant clauses.

As in common law jurisdictions, parties may agree on general disclosures provisions covering matters the buyer should be aware of as a result of its due diligence activities (or from public records). Depending on the size and type of the business, the specific exceptions/disclosures may be inserted directly in the representation and warranty clauses. More frequently, however, they are set out in exhibits to the main agreement.

(3) Relevant Law Principles

Certain Italian law principles deserve mention in connection with the interpretation and enforcement of representation and warranties clauses and on seller's liability.

Regardless of the wording of the purchase and sale agreement and the disclosure/knowledge qualifications to the representations and warranties, buyer's knowledge of certain matters, even independent of seller's disclosure, must be carefully considered. Since, by operation of law, the parties are required to act in good faith in the performance of the agreement (art. 1375 of the Italian Civil Code), if the buyer were to bring an action in circumstances in which it was aware, before signing, that certain representations and warranties of seller were not true and accurate, the seller may be able to defend against such actions by arguing that the buyer has acted in bad faith.

Sellers, on the other hand, must be mindful that in cases wherein fraudulent misrepresentations induce the buyer to enter into a purchase and sale agreement, the agreement can be declared void at the request of the other party (art. 1427 ff of the Italian Civil Code). In the case of a fraudulent misrepresentation made by a third party, the contract can only be declared void if the fraudulent behavior was known by the seller and such seller took advantage of the misrepresentation (art. 1439 of the Italian Civil Code).

Additionally, both the seller and its advisers can, in principle, be liable for pre-contractual damages under the general provision of article 1337 of the Italian Civil Code requiring the parties to act in good faith during contractual negotiations.

(4) Renewal of Representations and Warranties and Survival

The representations and warranties given by the parties are to be true and accurate on the date of signing, and are typically “renewed” on the closing date. Between signing and closing the parties may agree to allow the seller to update its disclosure, though this update is usually limited to new events and circumstances arising after the signing. The impact of significant updates of representations and warranties before closing on indemnity obligations is typically heavily negotiated.

In most cases, representation and warranties will “survive” closing, which means that they will continue to serve as a basis for indemnification provisions. The time limitations on the survival of representations and warranties are specified in the indemnification clauses (see sub section (e) below)

(c) Covenants

Acquisition agreements concerning Italian companies will usually set forth both pre-closing covenants and post-closing covenants.

(1) Pre-closing Covenants

Typical pre-closing covenants include the following:

- seller’s covenants on the management of the target company in the period between the execution of the acquisition agreement and the closing. Such clauses on the interim management of the target company typically provide for the seller’s obligation to cause the directors of the target company to manage such entity in the ordinary course of business and in strict accordance with past practices, and to adopt any extra-ordinary resolutions only with the prior written consent of the buyer. In the Italian practice, it is uncommon to set forth a seller’s obligation to cause the resignation of a member of the board of directors and the replacement of such director with an individual designated by the buyer, as such a provision could be deemed by the competent anti-trust authorities to unduly bring about the effects of the concentration prior to receipt of the required clearance;
- in the event that the target company is a party to a contract which contains a “change of control” clause that is triggered by the transaction, seller’s covenant to cause the other party to the contract to grant a waiver to the target company with respect to such clause. Since the granting of such a waiver is often provided for as a condition precedent to the closing, the parties will typically list all the contracts that contain such “change of control” clauses in a schedule to the acquisition agreement;
- seller’s covenant to cause the resignations of all the members of the board of directors and the board of statutory auditors or the sole statutory auditor, as the case may be², and the issuance, by the resigning directors and auditors, of a declaration acknowledging that they have no right or claim to any payment for compensation, indemnity or reimbursement arising from, or in connection with, their services to the target company and that they irrevocably waive any such right or claim;
- buyer’s covenant to timely carry out all activities necessary for the filing of the petition for anti-trust clearance, if such clearance is required. This covenant is frequently combined with the seller’s obligation to provide reasonable cooperation to the buyer and with the buyer’s obligation to promptly notify the seller upon the granting or denying of the anti-trust clearance;
- in an asset deal, covenants of both parties to perform the required consultation procedure with the trade unions, which, according to Section 47 of the Law 29th December 1990, No. 428, must be commenced at least 25 days prior to entering into any binding agreement or the completion of any transaction which gives rise to the transfer of a going concern. In this regard, according to a communication by the Italian Welfare Minister dated 31st May 2001, the entering into of a preliminary agreement concerning the transfer of a going concern does not require the prior performance of the

² Under Italian corporate law, Statutory Auditors are independent professionals who have the duty to verify the director’s compliance with laws and the company’s By-laws; the appointment of such a Board of Statutory Auditors composes of at least three standing members and two deputy members is compulsory for joint stock companies which adopt the traditional Italian governance system. Limited liability companies which exceed certain thresholds with respect to their corporate capital, value of their business assets, yearly revenues or number of employees must appoint either a Board of Statutory Auditors or a sole Statutory Auditor. The Statutory Auditors can also be entrusted with the task of auditing the accounts of limited liability companies and, upon occurrence of certain conditions, also of joint stock companies.

consultation procedure with the trade unions. Such consultation is therefore only mandatory prior to the execution of the definitive agreement through which the closing will occur;

- in an asset deal, seller's covenant to either file a petition for the issuance by the competent tax agency of a document certifying all unpaid taxes related to the transferred going concern, or to provide its consent to the filing of the such petition by the buyer. The filing of such petition is advisable in light of the fact that, according to Italian law, the buyer of a going concern is jointly and severally liable with the seller, up to the value of the concerned business assets, for all taxes related to the transferred going concern. The issuance of a certificate stating that no tax is due, or the non-issuance of the certificate within 40 days as from the filing of the petition, releases the buyer from such joint and several liability;

(2) Post-closing Covenants

Typical post-closing covenants include:

- in the event that the acquisition contract sets forth a price adjustment, covenant of both parties to cooperate in good faith for the performance of all related activities;
- seller's covenant to treat as strictly confidential any information related to the target company or, in an asset deal, the transferred going concern;
- covenant with regard to publicity, press release or announcements concerning the acquisition agreement or the transactions contemplated therein;
- buyer's covenant to approve a resolution at the shareholders' meeting whereby the target company waives any possible liability actions against the former directors and statutory auditors;
- in a share/quota deal, seller's covenant not to commence, continue or join any activities which may be in competition or conflict with the business activities performed by the target company. In an asset deal, the non-competition undertaking by the seller automatically arises from Section 2557 of the Italian Civil Code. Section 2557 of the same code, as interpreted by related case law, also provides that any non-competition undertaking, whether arising by contractual agreement or automatically at law, may not exceed a 5-year period.
- seller's covenant not to solicit for hire any manager or employee of the target company or solicit any such person to terminate their relationship with the target company;
- in the event that the transaction concerns a company which is managed by the seller, covenant of such party or parties to hold the office as director/manager of the target company for a certain period of time following the completion of the transaction;
- in an asset deal, seller's covenant to provide reasonable cooperation for the endorsement to the buyer of all licenses, permits and authorizations necessary for carrying out the business activities of the transferred going concern;
- seller's covenant to cooperate with the buyer for the collection of the receivables of the target company existing on the closing date, or the credits which are part of the transferred going concern. See also section (e) ("Indemnification Provisions") below regarding the potential consequences resulting from the non-collection of such receivables.

(d) Conditions to Closing

Acquisition agreements concerning Italian companies will typically state that the closing and the obligations to sell and purchase are subject to the following conditions, as at the date of the closing:

(1) Granting of Anti-trust Clearance

Merger and acquisition transactions in Italy are governed by the merger control rules set forth in Law 10th October 1990, No. 287 and are subject to the supervision of a specific authority, the “*Autorità Garante della Concorrenza e del Mercato*”. In its capacity as an independent authority, this *Autorità* carries out its supervisory and regulatory activity merely on the basis of the provisions of law, with no interference by the Italian government.

Law 10th October 1990, No. 287 requires prior notification to the Italian anti-trust authority of all mergers and acquisitions exceeding specific turnover thresholds, which are updated every year based on the gross domestic product price deflator index. According to the authority’s resolution No. 26471, dated 14th March 2017, such prior notification is presently required for mergers and acquisitions which involve companies whose combined turnover in Italy exceeds Euro 499 million and that concern target companies with an aggregate domestic turnover exceeding Euro 50 million. The Italian anti-trust authority is entitled to prohibit the implementation of any proposed merger or acquisition that, in its opinion, gives rise to or strengthens a dominant position in the national market and, in such a way, eliminates or restricts competition in a material and lasting manner. This authority also has the power to impose amendments to its structure aimed at avoiding the occurrence of any anti-competitive impact, which amendments thereby permit the implementation of the transaction.

Law 10th October 1990, No. 287 contemplates significant fines in the event of a failure to provide the required advance notification. In addition to these fines, in the event that a transaction having an adverse impact on competition is implemented either without the prior notification or in disregard of an express prohibition, the authority is entitled to order the concerned companies to restore the situation which existed prior to the performance of the transaction.

In contrast with the European Union anti-trust legislation, Law 10th October 1990, No. 287 provides that the parties are entitled to implement a concentration immediately following the filing of the prior notification, without the need to suspend such implementation until the issuance by the anti-trust authority of its decision. Pursuant to Section 17 of such Law, however, the Italian authority is entitled to require the suspension of the implementation of the concentration, upon issuance of the decision to initiate proceedings aimed at verifying its compatibility with the anti-trust provisions. Notwithstanding the above, it is customary in Italy to set forth the issuance of the anti-trust clearance as a condition precedent to the closing and, as a result, not to implement the concentration until the issuance by the anti-trust authority of its decision.

(2) Issuance of Tax Certificate (Asset Deals Only)

In an asset deal, the issuance by the competent tax agency of a document certifying that no tax is due with regard to the going concern to be transferred or, alternatively, no issuance of any such document within 40 days as from the filing of the relevant petition, may be a condition to closing.

(3) Change of Control Waiver

In the event that the target company is a party to a contract setting forth a “change of control” clause that is triggered by the transaction, the closing may be conditioned upon the granting by the other party of a waiver with regard to the transfer of control of the target company to the buyer.

(4) Financing

In the event that the buyer has not yet raised the necessary funds at the time of execution of the acquisition agreement, the closing may be conditioned upon the obtaining of the funds necessary to carry out of the transaction.

(5) Events Dependant Merely on the Will of One of the Parties

Section 1355 of the Italian Civil Code expressly qualifies any clause which subjects the effectiveness of the obligations undertaken by a party to an event dependant merely on the will of the same party as null and void. As a result, acquisition agreements governed by Italian law do not set forth events of this nature (e.g., the approval of the transaction by a special corporate body) as a condition precedent to the closing.

Notwithstanding Section 1355 of the Italian Civil Code, the leading opinion in Italian case-law provides that a party is entitled to prescribe an event which is dependent on its will (e.g., a board approval) as a condition subsequent, giving rise to the automatic termination of the agreement if not satisfied by a certain date.

(e) Indemnification Provisions

(1) Purpose and Scope of Indemnification Clauses

As mentioned in section 2 (“Structure of the Transaction”) above, without specific indemnification provisions, buyer remedies in a share/quota deal would be limited to:

- the right to be indemnified should any third party prove itself to be the lawful owner of the shares (so-called *evizione*); and
- the right to have the agreement declared null and void (*azione di annullamento*) in case of fraud.

Considering the limited automatic protections in favor of the buyer in share/quota deals, in the Italian practice it is common to include explicit indemnification provisions in the purchase and sale agreement to achieve greater protections for the buyer than those existing by operation of Italian law.

Explicit indemnification provisions are often also included in the context of an asset deal, even though a greater degree of protection is already guaranteed to the buyer by operation of Italian law.

Typically, an indemnification clause will require the seller to indemnify and hold the buyer harmless for damages incurred as a consequence of any breach of the obligations undertaken by the seller, including any breach, untruthfulness or inaccuracy of its representations and warranties, and for supervening or unexpected liabilities not reflected in a specified balance sheet.

In both share/quota and asset deals, any amount to be paid by a seller to the buyer pursuant to an indemnification may, by agreement, be paid directly to the target company.

Additionally, a specific remedy may be agreed to in connection with the representations and warranties made with respect to the collection of receivables. In this regard, the seller may undertake to buy from the buyer (if the transaction was an asset deal) or from the target company (if the transaction was a share/quota deal) the “bad receivables” (i.e., credits which the buyer is not able to collect within a specified term after the date of their due payment) if certain conditions are met.

(2) Limitations

In Italy, negotiations between buyer and seller regarding the limitations of the indemnification obligation follows a pattern similar to other European countries.

In addition to the seller’s right to qualify its representation and warranties (see section 4(b) on “Representations and Warranties”), parties may agree on the following additional limitations:

- baskets/thresholds: the amount of loss the buyer must incur before being able to make a claim against the seller may vary significantly on the basis of several factors, but is seldom set higher than 2% of the consideration. The discussion on this limitation may be linked to negotiations on materiality thresholds in representation and warranties;
- caps: the maximum aggregate amount for which the seller may be held liable depends significantly on the bargaining position of the parties, and may vary from 30% to 100% of the consideration;
- survival periods: indemnification claims will typically be permitted to be brought only during the first one to two years from closing. A longer period is usually agreed upon for tax representations and warranties in order to cover the period during which the relevant tax authorities can re-open tax assessments, and for labor and environmental claims.
- prevention of double recovery under warranties, indemnities and insurance policies.

5. Dispute Resolution

Similar to other European countries, parties to M&A transactions in Italy commonly choose between two options with respect to the resolution of disputes arising out of their contracts.

The first available option is to agree to empower an ordinary court, either in Italy or in a foreign country, to settle all disputes. Unless otherwise agreed by the parties, Italian courts normally have jurisdiction over litigation between Italian individuals or entities, and may also have jurisdiction over foreign individuals or entities (pursuant to Article 7 of the Regulation (EU) no. 1215/2012 in relation to persons domiciled in a EU Member State other than Italy or, in accordance with what set forth under Section 3 of the Italian law on conflict of laws, pursuant to article 5 of the Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters of 1968 in relation to persons domiciled in a foreign country that is not an EU Member State), in a wide range of “matters relating to a contract” when Italy is “the place of performance of the obligation in question”. Forum shopping is possible under Italian law and the contracting parties may decide to entrust the settlement of a dispute to a specific Italian court. There are, for example, courts in Italy that have particular expertise in M&A transactions.

In addition to ordinary civil courts, the most popular option for parties wishing to settle M&A disputes in Italy is one of several forms of alternative dispute resolution (“ADR”), such as mediation and arbitration. In practice, arbitration is the ADR procedure most commonly used in Italian M&A agreements.

(1) Pros and Cons of Arbitration in Italy vs. Ordinary Court Litigation

The Italian legal framework is generally very favorable to arbitration and there are many arbitration institutions in Italy. The cost of the procedure and the reliability of the arbitration panelists, however, may vary significantly from institution to institution. The choice of institution, therefore, must be carefully considered. In this respect, the size of the transaction may also play a significant role in the choice of the arbitration institution. In addition, an important element in deciding whether to arbitrate a case often lies in considering the nature of the dispute and the quality of the relationship between the parties.

In Italy, as is undoubtedly the case in other European jurisdictions, arbitration may offer significant advantages over traditional court litigation. The principal advantages and disadvantages of arbitration compared with court litigation may be summarized as follows:

- Procedural Efficiency: The parties may control the process by agreeing in advance to certain arbitration processes and procedures.
- Specific Competence of Arbitrators: The parties may appoint arbitrators who have specific experience and expertise in the subject matter of the dispute, which may result in a faster and

more predictable resolution to the dispute than may be achieved by a presiding judge without similar experience in a particular area of law.

- Freedom of Choice: The parties have the ability to select the arbitrator. In Italy, if the parties are unable to agree on an arbitrator, the court or the arbitration institution selected by the parties may be asked to assist in the selection process.
- Language: Italian language is the mandatory language used in court during ordinary litigation. Arbitration proceedings, on the other hand, may be handled in different languages.
- Costs: Arbitration costs may be substantial, particularly in complex cases, while the cost of litigation in Italian courts is relatively insignificant. Lawyers' fees, of course, will be dependent upon the complexity of the case irrespective of the dispute resolution selected, although the litigation process itself is typically longer than arbitration and may therefore have an impact on the legal fees of the parties.
- Duration: Arbitration often ensures a fairly rapid resolution of a dispute. Timing is often of the essence in M&A cases and Italian courts are generally significantly slower than an average arbitration proceeding.
- Recourse: Arbitration lacks the regular system of appeals found in litigation proceedings. A final decision in arbitration may be difficult to challenge before an Italian court and is generally only possible in limited circumstances.

(2) Peculiarities of Italian Arbitration Law

When the parties decide to resort to arbitration, they may opt for an arbitration proceeding governed by the rules set forth in articles 806 and following of the Italian code of civil procedure (the "C.p.c."). In connection with an administered arbitration, such rules may be enhanced by the rules of the arbitration institution. The new General Arbitration Law introduced by Legislative Decree 40/2006 improved arbitration rules in the C.p.c., granting greater flexibility to the parties for the management of the arbitration proceeding.

It is a well-established principle that the parties may resort to arbitration either by inserting an arbitration clause (*clausola compromissoria*) into the contract or in a separate document at the time of execution of the contract or at any other time prior to the occurrence of the dispute. In the absence of such a clause, the parties may execute a specific arbitration agreement (*compromesso*) in which the nature and subject matter of disputes to be submitted to arbitration are outlined and submitted to arbitrators even after a dispute has already arisen. Both *clausola compromissoria* and *compromesso* are only valid if reduced to writing.

The parties may choose between arbitration "*rituale*" and arbitration "*irrituale*". The Arbitration *rituale* is more commonly used, and results in an award (*lodo arbitrale*) having the effectiveness of a judgment pursuant to the new article 824 *bis* of the C.p.c.

The Legislative Decree 40/2006 introduced in Italy a number of provisions to facilitate the conduct of an arbitration, which are also applicable to arbitration proceedings involving foreign parties, including:

- Trial and Procedural Rules: Arbitrators are granted considerably wide powers in connection with the trial of a case. In this respect, differences between the powers of Italian courts and arbitration bodies have been reduced. Hearings and other formalities may take place anywhere the arbitrators deem appropriate, including outside of Italy. Unless otherwise agreed by the parties, the arbitration decision can also be rendered outside Italy. The arbitrators are entitled to conduct the proceeding in a language other than Italian.

- Timing: Unless otherwise agreed by the parties in their arbitration clause or in the arbitration contract, the arbitration award must be rendered within 240 days from the date of acceptance of the appointment by the arbitrator or the arbitration panel. This deadline ensures certainty as to the duration of an arbitration proceeding. An arbitration proceeding may only be extended upon the agreement of the parties or for justified reasons through an order of an ordinary Italian court (article 820 of the C.p.c.).
- Enforceability of the Arbitration Award: In the most common of the arbitration proceedings, that is, the *rituale* proceeding, the award issued at the end of the proceedings has the same effectiveness as a judgment rendered by an Italian court. However, in order to be enforced, the award must be filed with the competent Italian court. This is typically a rather quick procedure aimed at verifying that the award does not violate any mandatory rule of Italian law.
- Limited Recourse: An award is subject to recourse only in the following very limited circumstances: nullity, revocation (in the specific cases set forth in article 395 of the C.p.c. number 1,2,3 and 6) and third party opposition (article 827 of the C.p.c.). None of the available means of recourse against an arbitration award can be waived by the parties.

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