COUNTRY COMPARATIVE GUIDES 2024

The Legal 500 Country Comparative Guides

Italy

PRIVATE EQUITY

Contributor

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This country-specific Q&A provides an overview of private equity laws and regulations applicable in Italy.

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ITALY
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1. What proportion of transactions have involved a financial sponsor as a buyer or seller in the jurisdiction over the last 24 months?

Financial sponsors have been very active in the Italian M&A market in the last couple of years in keeping with a trend started a decade ago. Based on available data, in more than 30% of Italian M&A transactions the bidders were financial sponsors. The percentage is even greater if one considers also transactions where financial sponsors acted as sellers and add-ons transactions carried out by sponsor-back portfolio companies. Overall, transactions involving a financial sponsor have consistently been in excess of 400 over the last three years, with 2022 being a record year for the industry with 441 deals, followed by 2023 with 406 deals.

Most deals where financial sponsors were involved were mid-market transactions, with a value ranging between 50 million and 300 million. Some multi-billion transactions were closed by big US funds.

Most of the financial sponsors active in the Italian market are Italian, followed by US, UK, and French financial sponsors.

2. What are the main differences in M&A transaction terms between acquiring a business from a trade seller and financial sponsor backed company in your jurisdiction?

Like in most jurisdictions, also in Italy the goal of a clean break with a speedy distribution of the sale proceeds to financial sponsors' investors drives the main differences in the terms of a sale from a financial sponsor compared to the terms of a sale from a trade seller. Broadly, these differences can be outlined as follows:

(a) scope of warranties and specific indemnities: financial sponsors tend to give fundamental warranties only (and not business warranties which are sometimes given by managers) and are very reluctant to provide specific indemnities. Trade sellers normally provide both sets of warranties and are in principle more prepared to give specific indemnities;

(b) pricing structure: financial sponsors favor the locked box mechanism with a view to achieving pricing certainty at signing, avoiding post-closing adjustments (and potentially related holdbacks, escrows, and similar arrangements) and facilitating comparability of offers in auction processes. Trade sellers might make recourse to a locked box mechanism when the sale does not involve carve-outs, separations or complex reorganization;

(c) recourse to W&I insurance policy: the need to avoid post-closing exposure makes the recourse to W&I insurance policy a normal feature of financial sponsors' sales (it is often the case that a staple W&I policy is part of the documentation prepared by the financial sellers in auction processes). The use of W&I insurance policies has become more frequent in trade sales without however being a distinctive element of such sales;

(d) lack of non-compete/non-solicit undertakings: financial sponsors do not generally provide any such undertakings in order to avoid constraints on future investments. Trade sellers are normally expected to provide such undertakings;

(e) seller's indebtedness: the indebtedness incurred by financial sellers for the previous acquisition of a target is normally repaid at closing and the related mechanics are normally embedded in the sale documentation.

3. On an acquisition of shares, what is the process for effecting the transfer of the shares and are transfer taxes payable?

The process for effecting the transfer of shares depends on the nature of the target company, i.e. whether it is a limited liability company (*società a responsabilità limitata*) or a joint stock company (*società per azioni*).

(a) Società a responsabilità limitata: the transfer of the

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quotas (the capital of such type of company is not made out of shares but rather of quotas) requires the execution in front of a notary of a deed of transfer between the buyer and the seller. Such deed of transfer only contains very limited provisions and does not novate the terms of the sale which remains governed by the sale and purchase agreement (normally, a draft deed of transfer in agreed form is an attachment of the sale and purchase agreement). Once executed, the deed of transfer is registered with the Italian Register of Enterprises and the quotaholders' ledger (when issued by the target) is updated by the director(s) with the details of the buyer. Stamp duty in a fixed amount (currently, 200 Euro) is payable and no VAT is levied on the transfer. Sellers have to pay capital gain taxation;

(b) Società per azioni: when shares are physically issued, the actual transfer occurs through an endorsement of the share certificate executed by the seller in favor of the buyer in front of a notary (so called *girata*). The buyer can then obtain the registration in the shareholders' ledger by showing to a director of the target the duly endorsed share certificate. If share certificates are not physically issued, the buyer and the seller must execute a deed of transfer in front of a notary which is then used by the buyer to be registered in the shareholders' ledger. Lastly, for companies whose shares are in dematerialized form (mostly public companies), the transfer is effected through registrations in the financial intermediaries' accounts. Stamp duty in a fixed amount (currently, 200 Euro) is payable and no VAT is levied on the transfer. Sellers must pay capital gain taxation and buyers have to pay a tax on financial transactions (so called Tobin tax) that is, in general, equal to 0.20% of the purchase price (or 0.10% if the shares are listed on a regulated market or on a multilateral trading facility). The Tobin tax does not apply to certain types of transfer, nor to certain institutional entities, such as the ECB or the European Union.

4. How do financial sponsors provide comfort to sellers where the purchasing entity is a special purpose vehicle?

In the Italian market, it is rather common to use a special purpose vehicle to complete the acquisition of targets. To provide sellers with the required level of comfort, at signing financial sponsors normally issue equity commitment letters and guarantees from group entities with funding capacity.

In addition, to achieve "certainty of funds", lenders appointed by the buyer to provide acquisition finance are often required to issue debt commitment letters. In recent times though, due to the conditions of the debt market, lenders are often more inclined to provide soft commitments at signing and sometimes financial sponsors are prepared to front the entire amount of the purchase price under their commitment letter.

Finally, share purchase agreements contain buyers' representations to confirm the availability of funds.

5. How prevalent is the use of locked box pricing mechanisms in your jurisdiction and in what circumstances are these ordinarily seen?

Locked box mechanisms are most prevalent in the Italian market, especially when financial sponsors are involved. The usual advantages of this pricing mechanism (i.e., certainty of price at signing, no post-completion price adjustments with the elimination of lengthy closing accounts process and ensuing risk of litigation, clean exit and swift and full distribution of sale proceeds without holdbacks, escrow or similar arrangements) are most suited to financial sponsors but increasingly enjoyed also by trade sellers. Under a locked box mechanism, economic risks and rewards are transferred to the buyer as of the locked box accounts date. However, it is very common that sellers require that the purchase price agreed bears an interest rate (so called ticking fee) from such date until the closing date. Whether buyers agree on the ticking fee is very much dependent on the balance of bargaining power of the parties.

Completion accounts mechanisms are still used when a locked box mechanism is not suitable (for example, for transactions that require pre-closing business reorganisations or carve-outs, in the absence of recent reliable financial statements, or when the target's performance is seasonal or is expected to be volatile due to market conditions or other factors).

6. What are the typical methods and constructs of how risk is allocated between a buyer and seller?

In the Italian M&A market, the methods for allocating risks are those commonly used in most European jurisdictions, namely:

(a) Pricing risks: as mentioned, the most prevalent pricing mechanism is the locked box mechanism which allows the parties to achieve price certainty at signing. From a buyer's perspective, a thorough due diligence on the locked box accounts and water-tight rules for leakages are the normal protection tools. When the

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performance of the target is volatile for whatever reason, then completion accounts mechanism tends to be preferred by buyers. When there is a valuation gap between the seller and the buyer, earn out mechanisms are also used;

(b) Risks associated with interim period between signing and closing: a robust set of interim covenants is always used by buyers to put constraints on the way sellers manage targets in the interim period. Specific interim covenants can only be used to address issues discovered by buyers during the due diligence process. Recourse to MAC is naturally resisted by sellers and in recent times is less often seen since generally sellers can impose seller friendly terms. Conditions precedent are used to deal with clearance or regulatory matters or specific risks that can be eliminated prior to closing;

(c) Risks associated with the financial, economic and operational condition of targets: these are normally dealt with a set of representations and warranties and related indemnification obligations on the seller. The scope of the representations and warranties and related obligations vary depending on the nature of the seller. Trade sellers are generally expected to provide a full set of warranties and more inclined to do so also because they are normally better placed to assess the associated risks. Financial sellers tend to give only fundamental warranties and business warranties (often from managers) are only given for the purposes of allowing a buyer to obtain W&I insurance cover. In this case, the construct most used in practice (whose enforceability however has not yet been tested in court) is to cap the liability of a seller at one Euro, except in the event of fraud. Although recourse to W&I insurance policies has become more common also for trade sellers, such policies are consistently used when the seller is a financial sponsor seeking a clean break exit. Trade sellers' indemnification obligations in relation to business warranties are normally subject to time limits (for tax, employment and environmental warranties, it is normally the statute of limitations, whereas for the other warranties the average duration is from eighteen to twenty-four months), financial limits (de minimis, tipping baskets – normally ranging from 0.5% to 1% of the equity value – or deductibles – normally ranging from 0.15% to 0.6% of the equity value -, caps – normally ranging from 10% to 30% of the equity value -) and a set of exceptions. The actual terms of such limits and exceptions depend on the bargaining powers of the parties and tend to be deal specific, although over time they have become standard. Specific indemnities for contingent liabilities are very reluctantly given by financial sellers and, when they do so, the duration tends to be rather short, and the amount always capped.

7. How prevalent is the use of W&I insurance in your transactions?

Recourse by buyers to W&I insurance policies has become a common feature of Italian M&A transactions and the process and timing for taking up such policies are now well tested, with several brokers and insurers fairly active in Italy. The use of W&I policies is the norm when the seller is a financial sponsor in that it allows the clean exit sought by it. In auction processes, it is often the case that the seller starts a soft-stapled W&I process where a broker appointed by the seller seeks non-binding indications of interests from several insurers based on the info memo, auction draft SPA and vendor due diligence report and the subsequent underwriting process is then handled by the buyer.

Although over the last few years W&I insurance policies have become more flexible, typically they do not cover certain risks (for example, bribery and money laundering, statutory sanctions, IT risks, forward looking warranties, transfer pricing) and provide for a policy retention (or attachment point) which works as a deductible. Other features of W&I policies depend on the industry of the target, the jurisdictions of subsidiaries, due diligence gaps, etc.

When first introduced in the Italian market years ago, the W&I policies were perceived as rather expensive with a cost normally equal to 5% of the insured amount. Nowadays, their cost in Italy is normally between 1% and 3% of the insured amount, thus more in line with the cost of W&I policies in other European jurisdictions as a result of a significant increase of competition between underwriters.

8. How active have financial sponsors been in acquiring publicly listed companies?

In recent times, we have witnessed a certain increase in take-private transactions by financial sponsors mainly due to the decrease of public market valuations.

Based on publicly available data, in the period between 2021 and 2023 approximately 50 tender offers were launched over companies listed on Euronext Milan and in approximately half of them financial sponsors were involved.

Like in many other European jurisdictions, take-private transactions are governed by rather detailed tender offer rules and are subject to the supervision of Consob.

9. Outside of anti-trust and heavily

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regulated sectors, are there any foreign investment controls or other governmental consents which are typically required to be made by financial sponsors?

Yes. Foreign investments in business sectors deemed strategic must be notified to the Italian Presidency of the Council of Ministries which has the power, to veto a transaction or impose certain conditions or recommendations (so called Golden Power Regime).

Such powers can be exercised when an investment is likely to be prejudicial generally to national security and public order, as well as to the security of the operation of networks and infrastructures and to the continuity of the supply, depending on the sector involved. In assessing notified transactions, the government also evaluates the adequacy of the financial and industrial plan underlying the acquisition, the technical and financial capacity of the investor and the existence of objective reasons which lead to consider that an investor maintains any ties with countries which do not recognize democratic rules and rule of law principles.

The Italian legislation on the control of foreign investments, originally aimed at safeguarding mainly sectors related to public services (defense, transport, energy, communications), has been subject to various amendments during the last years. The list of the sectors (and specific relationships, assets or technologies) which fall within the scope of the Golden Power Regime has been widely enlarged, covering, for example, artificial intelligence and emerging technologies, health and biotechnologies, financial and credit sector, food security, data processing, civil aerospace and other technologies.

Both asset deals and share deals, as well as certain corporate transactions, are subject to notification requirements. The relevant threshold triggering the notification requirement varies depending on whether the investment is carried out by investors within the European Union (in such case, only acquisitions of a controlling stake trigger the requirement) or investors outside the European Union (from 10% or even lower in the defense sector). Green-field investments and the mere incorporation of companies might need to be notified as well.

Despite the increasing number of notifications made and the increase of the scope of Golden Power Regime, only in very few cases the veto rights have been exercised by the Italian government. Authorities are generally reactive and requests for information and clarifications are quite frequent (with suspensions of the relevant term proceeding, which remains nevertheless quite reasonable compared to other EU countries).

This is also why the scrutiny related to the Golden Power Regime is often conducted at an early stage in the deal process and financial sponsors have become quite familiar with this screening mechanism, irrespectively of the value of the transaction. Normally, clearance under the Golden Power Regime is provided as a condition precedent to closing in the form of negative condition (i.e., as the lapse of time without any veto power being exercised or conditions imposed).

10. How is the risk of merger clearance normally dealt with where a financial sponsor is the acquirer?

The merger clearance is usually included as a condition precedent in sale and purchase agreements. Generally, merger clearance concerning financial sponsors is not problematic from a competition law standpoint, unless there are significant overlaps between the target and one of the portfolio companies of the financial sponsor.

Typically, merger control analysis is carried out by the buyer in cooperation with target counsels. The sell-side and buy-side exchange relevant information, as needed, on a counsel-to-counsel basis in order to reach a mutual understanding of the filing requirements.

In order to address any antitrust risk uncertainty, sellers usually request a “hell or high water” clause, which includes the obligation on the buyer to adopt any measure or remedies to ensure the merger clearance. The scope and content of the ‘hell or high water’ clause may differ based on the bargain powers of the parties, and structure and scope of a transaction.

Responsibility for the notification of transactions to the Italian competition authority lies with the buyer.

11. Have you seen an increase in (A) the number of minority investments undertaken by financial sponsors and are they typically structured as equity investments with certain minority protections or as debt-like investments with rights to participate in the equity upside; and (B) ‘continuation fund’ transactions where a financial sponsor divests one or more portfolio companies to funds managed by the same sponsor?

(A) Minority investments by financial sponsors have been

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quite steady over the last couple of years but tend to be a rather small percentage of the overall private equity market (being more frequent in the growth capital space). They are normally structured as equity investments with the usual minority protections: (i) tag-along; (ii) IPO right; (iii) drag-along over all or part of the residual stakes as to allow the financial sponsor to trigger the sale of a majority stake; and, often alternatively, (iv) a put option right to ensure a clear path to exit, especially when the target is not meeting certain performance targets).

(B) Continuation fund transactions have not been frequent in the Italian market although we have recently started seeing some examples.

12. How are management incentive schemes typically structured?

Management incentive schemes aim at aligning the interest of the management of a company with those of the financial sponsor.

The choice of the scheme is usually driven by tax consideration/company cost impact (which may also be determined by the impact of social contribution costs) and may be divided between those that require an investment by the key managers or those that are based on free shares based or cash based.

Most of the schemes have as common factor that they are subject to vesting conditions (e.g. time of the vesting which is usually four/five years) and that the pay-out for the key manager is associated with the continuous employment/collaboration in the vesting period. Indeed, leaver conditions are very common.

When the key managers access the scheme by investing (or reinvesting), the investment is either directly in the target company or most commonly through a management pooling vehicle, in which the financial sponsor is usually a co-shareholder. Amounts as well as conditions associated may vary according to the role and sector. The beneficiaries subscribe for new shares of the company incorporating the right to receive an extra return (the carried interest), typically conditional on the occurrence of a change of the control of the company (i.e., an exit), as well as the achievement of a certain minimum return on the investment by the other shareholders (hurdle rate). This scheme has specific tax advantages for the beneficiaries as outlined in section 13. below and is widely used in the context of private equity transactions in Italy.

Conversely, when an investment is not required, key managers are often included in stock option plans or stock grant plans, which are based on the assignment to specified categories of employees or managers (on a gratuitous basis) of, as the case may be, an option right to purchase or subscribe for a certain number of company's shares, or of a certain number of company's shares, for a certain price (strike price).

As regards stock option plans, typically the exercise of the option rights is subjected to the continuation of the employment relationship for a certain period of time (vesting period), and the occurrence of certain conditions, such as the achievement of targets by the company and/or of individual targets. If, at the end of the vesting period, the value of the shares subject to the option right is higher than the strike price, the beneficiary of the right, by exercising the option, will realise a gain equal to the difference between the value of the shares on the market and the strike price.

As regards stock grant plans, typically the free allocation to the beneficiaries of the company's shares is subject to the expiration of a term, the continuation of the employment relationship during such term, and the achievement of targets by the company and/or of individual targets.

13. Are there any specific tax rules which commonly feature in the structuring of management's incentive schemes?

Yes. As a general rule, article 51 of decree of the of the Republic of Italy n. 917 of 22 December 1986 (the Italian Tax Code) provides that all sums or values in general, howsoever perceived, including in the form of donations, in connection with the employment relationship, received by employees of a company, generate an employment or quasi-employment income subject to the progressive personal income tax (IRPEF) rates – ranging from 23% to 43% plus additional taxes, for an overall maximum tax burden of approximately 46% – and subject to withholding taxes operated by the employer/payer.

Article 60 of decree no. 50/2017 has subsequently introduced the carried interest tax regime into the Italian jurisdiction. The provision in question provides that income from shares, units or financial instruments with enhanced equity-base rights, referred to as "carried interest", in the presence of specific requirements, is qualified as capital income (subject to a flat rate of 26%), as it qualifies as a profit deriving from participation in the capital or assets of companies.

Financial instruments with enhanced equity-base rights constitute forms of incentive which can be granted to

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managers and directors upon achieving certain results. These instruments aim to align the interests and the risks of the management with those of the investors as much as possible, by linking a portion of the remuneration to economic and financial parameters that reflect an increase in value of the shares or in the profitability of the target.

Therefore, upon fulfilment of the conditions outlined below, the remuneration to management is qualified as capital income or other income of a financial nature and, thus, is subject to a substitute flat tax of 26% (instead of the progressive rates mentioned above).

For managers and employees, carried interest is considered as capital income or other income of a financial nature if:

(a) the total investment commitment of all employees and managers eligible for the incentive results in an actual disbursement of at least 1% of the total investment made by a collective investment scheme (undertakings for collective investment, so called UCI or, in Italy, OICR) or of the equity in case of companies or other entities;

(b) the income from the relevant shares, units or financial instruments accrues to the beneficiaries only after all shareholders or participants have reached full repayment of the invested capital and a certain threshold return as set out in the relevant articles or regulations or, in case of disposal, the condition is referred to all other members or participants in the investment having realised upon disposal at least their invested capital and the said threshold return (hurdle rate); and

(c) the relevant shares, units or financial instruments are held for a minimum period of 5 years or, if earlier, until the date of change of control of the relevant company or entity or change of the management company of the collective investment scheme (holding period).

14. Are senior managers subject to non-competes and if so what is the general duration?

Non-competes and non-solicitation undertakings are customary provisions in management investment agreements. Even if the maximum duration of the non-compete for an executive can be, according to the law, up to 5 years, tipically non-compete clause do not include period longer than 12-24 months starting from the termination of collaboration.

Non-compete clauses entered with key-manager that are employees need to include a specific compensation, that has to be assessed based on the scope and duration of the clause and the territory in which it shall apply.

There is an established case law that gives guidance on how to structure a non-compete clause, on the amount to be paid and modalities of payment. Non-compete clauses usually include liquidated damages in the case of breach that are linked to the remuneration paid during the employment.

15. How does a financial sponsor typically ensure it has control over material business decisions made by the portfolio company and what are the typical documents used to regulate the governance of the portfolio company?

Typically, financial sponsors tend to leave the day-to-day business of their portfolio companies to their management. In many cases in Italian private equity deals, which are predominantly mid-market oriented, individual entrepreneurs who have founded or have developed the portfolio company remain involved in the management of targets. Their interests are aligned to those of financial sponsors through management incentive schemes and minority reinvestments of the sale proceeds.

The control over a portfolio company is ensured differently depending on whether the investment of the financial sponsor is of a minority or a majority nature.

In the case of minority investments, financial sponsors retain control over their portfolio companies through:

(a) veto rights within the portfolio company’s shareholders’ meetings (especially in relation to extraordinary transactions, such as mergers, demergers, acquisitions, winding-up, material amendments to the company’s corporate purpose or core activity);

(b) reserving the right to appoint at least one director or, more frequently, two directors, who will typically be granted veto rights in relation to material business decisions (which can be identified in various ways, based on their subject matters, on monetary thresholds, etc.);

(c) reserving the right to appoint at least one standing statutory auditor (and an alternate one), in order to ensure its representativeness within the body entrusted with supervising the management of the company.

These rights are most commonly provided for in the company’s bylaws. Indeed, under Italian law, the

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enforceability of a clause provided in bylaws is greater than that of clauses provided in shareholders' agreements. In the event of a breach of a clause in the bylaws, the remedy is immediate and consists in the invalidity and annulment of the breaching resolutions or actions. Conversely, the breach of a clause in a shareholders' agreement only entitles to seek compensation of the damages suffered (which, moreover, must be proven both in existence and in amount).

On the other hand, bylaws are publicly available documents. Therefore, confidentiality reasons might lead a financial sponsor to include the relevant rules in a shareholders' agreement.

In the case of majority investments, the control is already guaranteed by operation of law (as the financial sponsors, having the majority of the voting rights in the general meeting, will be able to determine any corporate resolutions, including the appointment of the majority of the management body and supervisory body). Typically, as the day-to-day management is often left to the minority shareholders/entrepreneurs, financial sponsors put in place articulated directorship agreements setting out clearly the perimeter of the key managers powers, requesting joint signature or an authorisation from the board of directors for all material business decisions (such limits are also reflected in board resolutions which are filed with the Italian Register of Enterprises).

In the event of qualified minority investments, minority shareholders are typically granted (for the reasons outlined above, under the company's bylaws) certain veto rights within the company's general meeting (in respect of the same material extraordinary transactions listed above) and by reserving the right to appoint at least one director, who will be granted with veto rights on particularly material business decisions.

16. Is it common to use management pooling vehicles where there are a large number of employee shareholders?

As mentioned in Section 12., it is often the case that management pooling vehicles are deployed for the investments/reinvestments by employee shareholders with aligning interests.

17. What are the most commonly used debt finance capital structures across small, medium and large financings?

The Italian market is mainly a market of small and medium enterprises. Bank financing is still the most common source for funding acquisition, but credit funds are increasingly active in the market due to raise of the interest rates offered by banks.

Funding structures often see a combination of secured term loan facilities, both for acquisition and refinancing of existing debt, with bridge to cash facilities to be repaid upon merger of the acquisition vehicle into the target. It is often the case that revolving credit facilities (RCF) are made available to target in the context of the acquisition.

Frequently, vendor loans are also part of the funding sources, especially when vendors are re-investing in the deal.

When credit funds are involved, it is not rare to see unitranche financings, with the banks involved only for RCF. Credit funds mainly operate via issuance of notes due to Italian banking monopoly rules.

Sponsors might also seek for an higher leverage using more sophisticated structures involving mezzanine financing from credit funds (possibly including an equity kicker) and senior debt from banks.

18. Is financial assistance legislation applicable to debt financing arrangements? If so, how is that normally dealt with?

Yes, Italian law prohibits financial assistance by the target both in the form of financing and providing guarantee or collateral. The approach taken by the courts is of substance over form, therefore the financial assistance prohibition is applied as to include indirect financing and refinancing of existing loans granted for acquisition purposes.

As an exemption from the financial assistance prohibition:

(a) a whitewash procedure is available for joint stock companies, but not for limited liability companies. Such procedure requires the shareholders' approval and a report by the directors of the company which, among others, must substantiate the corporate benefit, contain a risks and benefits analysis, and confirm that the transactions is at arms' length. Whitewash procedures are rarely used due to the fact that the amount of the financing, guarantee or collateral is capped at the payable profits and distributable reserves based on the latest financial statements approved by the company (and a non-distributable provision for the same amount must then be included in the liabilities of the balance sheet); or

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(b) a specific merger leverage-buyout structure is followed whereby, among others, a merger plan by the directors and a report by an authorized expert attest that entity resulting from the merger of the investment vehicle into the target can sustain the debt incurred for the acquisition (so called MLBO). The debt push-down through a MLBO structure is the solution commonly adopted for acquisition financings.

19. For a typical financing, is there a standard form of credit agreement used which is then negotiated and typically how material is the level of negotiation?

No standard form of credit agreement is used, although law firms developed their forms looking both at the standards of the Loan Market Association (LMA) and those of competitors, thus having similar templates and clauses in the market.

Lenders (typically foreign ones) might ask to use LMA standards as a starting point for negotiation, which then needs to be amended for consistency with Italian mandatory provisions of law, but such amendments are made individually by each law firm without coordination with the LMA and without a common approach and outcome. This results in a significant level of negotiation compared to a negotiation based on LMA standard, especially in case of bilateral financings.

Market practice has reached a high level of uniformity for security documents among law firms.

20. What have been the key areas of negotiation between borrowers and lenders in the last two years?

Borrowers focus on gaining some room to allow the growth of target, especially in buy-and-build acquisition structures, so to avoid the need of waivers with related costs and timing issues. This also led to an increase of transactions financed by credit funds, which may be more flexible than traditional lenders.

Cure mechanisms have been increasingly negotiated also in light of the number of waivers that the whole system had to face due to the effect on the Italian economy of Covid-19 first, and subsequently of war in Ukraine.

Environmental, social and governance matters (ESG) are also a relevant factor in the financing market now and related key performance indicators (KPIs) are constantly negotiated in connection with margin ratchet.

21. Have you seen an increase or use of private equity credit funds as sources of debt capital?

Yes, the raise of the interest rates in bank financings has made private credit funds a more competitive alternative compared to the past.

In addition, sponsors avail themselves of lending from credit funds in deals with higher complexity, in deals where banks cannot step in due to risk allocation constraints or where a mezzanine financing is required.

Also, paid-in-kind (PIK) interests are generally prohibited for banks in Italy giving room for credit funds in those structures that need to initially limit the cash out from the acquisition vehicle.

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