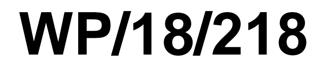

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IMF Working Paper

The Insolvency Regime for Large Enterprises in Italy: An Economic and Legal Assessment

by Nazim Belhocine, Daniel Garcia-Macia, and José Garrido

***IMF Working Papers* describe research in progress by the author(s) and are published to elicit comments and to encourage debate.** The views expressed in IMF Working Papers are those of the author(s) and do not necessarily represent the views of the IMF, its Executive Board, or IMF management.

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The Insolvency Regime for Large Enterprises in Italy: An Economic and Legal Assessment[1]

Prepared by Nazim Belhocine, Daniel Garcia-Macia, and José Garrido

Authorized for distribution by Rishi Goyal and Yan Liu

September 2018

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Abstract

The modernization of Italy's insolvency framework has been the subject of much interest in recent years, related not least to its role in potentially facilitating an efficient allocation of resources. A unique feature of Italy's insolvency framework is a special regime for large enterprises known as "extraordinary administration". This paper evaluates the merits of this special regime by assessing its efficacy and success in achieving its stated goals and comparing its features to international standards and best practices. It finds that the special regime tends to impose large costs on creditors and the state. The regime results, in most cases, in the sale of parts of the group, followed by a liquidation phase of the remaining assets which can take longer than the general regime, hindering legal certainty for creditors and more generally economic efficiency, investment and job creation. Based on international best practices and experience, consideration should be given to folding the special regime into the general insolvency regime, possibly with provisions to allow for state intervention in specific well-defined circumstances.

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I. INTRODUCTION

Italy is unique in the Euro Area for having a special insolvency regime for large enterprises. Known as the "extraordinary administration" (*amministrazione straordinaria*) for large enterprises, the stated goal of this regime is to ensure the continuation of the firm's productive activity and the preservation of the operational unity of businesses. As a result, distressed large companies can maintain employment and production levels during the insolvency procedure while designing a plan for restructuring or sale of the business as a going concern. In this way, the harmony with social partners can be preserved.

The special insolvency regime was originally introduced in response to the industrial crisis of the 1970s. It was aimed at addressing the inadequacies of the old insolvency law, which focused on the liquidation of debtors' assets. It introduced many technical innovations, including the treatment of the insolvency of enterprise *groups*. Over time, the special regime has been used in all major corporate insolvency cases, with legal amendments introduced along the way to adapt to regulatory concerns or address individual cases (e.g., Parmalat in 2003 and Alitalia in 2008).

Extraordinary administration continues to play an important role in the Italian insolvency system despite processing much fewer cases than the general regime. Ordinary insolvency cases in 2017 included 12,009 bankruptcy liquidations (*fallimenti*) and 589 bankruptcy reorganizations (*concordati preventive*). In contrast, there were only 10 cases of special insolvency regime in the same year. The dominance of small and medium enterprises in the Italian economy compared to other EU countries (see Bugamelli et al., 2018) could perhaps explain part of this contrast. That said, even though the special regime is not often used, it has a very important signaling effect regarding the authorities' willingness to intervene in saving large enterprises and corporate groups, given the high-profile cases brought forth and the attending concerns over employment.

Several criticisms have been levelled off against this special regime. First, the regime reduces the role of the judiciary vis-à-vis the Ministry of Economic Development (MED), in charge of administering the procedure. Second, creditors play a passive role in the insolvency process while bearing most of losses from the forced continuation of the business activity, even when prospects of returning to viability may be negligible. Finally, the special proceedings maintain employment, albeit temporarily, at the expense of private and public creditors and, more generally, of investment and competitiveness.

This paper analyses the desirability of the special regime from a legal and empirical perspective. It finds that the special regime is rarely successful in achieving its stated aim of restructuring companies and instead leads in most cases to the sale of the business after 2–3 years of administration. Once the parts of the group that are viable are sold, the remaining assets are disposed during a liquidation phase which is lengthier, than the general regime. Throughout this process, creditors' rights are sidelined and their investment is eroded. The lack of public information on credit recoveries and the direct costs involved makes it difficult to assess empirically the cost of the procedure; tracking recovery rates and the direct costs incurred in these procedures would help to assess the economic trade-offs involved, identify the costs to all stakeholders and increase transparency. The paper,

nonetheless, attempts to estimate such cost and finds that the combined loss to creditors and the state could translate to a cost per transferred employee of about 14 times GDP per capita.

The shortcomings of the special regime suggest grounds for its repeal. Extraordinary administration, with its focus on preserving employment of failed entities at a high cost to creditors and the state, likely hinders more generally economic efficiency and could weigh on investment and job creation. Based on international best practice and experience, the paper concludes that consideration should be given to folding the special regime into the general insolvency regime, with added provisions to allow for state intervention in specific well-defined circumstances.

This paper makes several contributions compared to similar work. The closest paper to this study is the work of Danovi (2010), which looks at the characteristics of the special regimes up to 2008. This paper takes a more holistic view by analyzing the regime both from a legal and empirical perspective. It also uses a longer data set with coverage extending to 2016. Finally, it makes use of a full set of financial metrics of Italian companies to draw comparisons between companies involved in the special insolvency regime and those that are healthy and infers the extent of the procedure's cost. The rest of the paper is organized as follows. Section II describes the special insolvency regime. Section III explains the data sources and Section IV presents the main empirical findings. Section V discusses the findings and identifies the features of the special regime that deviate from international standards and best practices, and their economic effects. Section VI concludes by providing policy recommendations.

II. Overview of the Regime

A. Origins and Evolution

The first extraordinary administration procedure—known as the *Prodi law*—was enacted in the wake of the 1970s industrial crisis. With its almost exclusive focus on liquidation, the old bankruptcy regime, the *legge fallimentare* of 1942, was ill-equipped to address the challenges of the continuity of businesses as going concerns. A decree was adopted in January 1979 on "urgent rules for the administration of large enterprises in crisis", which became known as the "*Prodi law*" when adopted in April 1979.[2] The law was primarily aimed at protecting enterprises and employment through the continuity of business activities and their restructuring. In practice, many of the enterprises subject to extraordinary administration ended up being liquidated, and the main effect of the procedure was to cushion the impact of insolvency on workers by delaying layoffs. The special procedure attracted criticism because of the discretion in admitting companies into the procedure, including cases where companies were deeply insolvent, delays in processing cases, and the excessive powers conferred upon the administration.[3]

[2] Decree Law n.26, of 30 January 1979 converted into law n. 95 of 3 April 1979. Romano Prodi was the Minister of Industry and Commerce at the time of the enactment of this law. Today, the Ministry of Industry and Commerce is known as the Ministry of Economic Development.

[3] See Oppo (1981), Tarzia (2000), and Bianca (2001).

The Prodi law was amended in 1999—henceforth called the *Prodi-bis law*—after it was found to be incompatible with European law. Following the enactment of the Prodi law, the European Commission (EC) and the European Court of Justice (ECJ) reacted in several instances against the results of the application of the extraordinary administration procedure given its anti-competitive features. The landmark decision of the ECJ in the *Piaggio* case[4] established that the Prodi law was incompatible with the state aid rules under European law, since it created a regime where enterprises had automatic access to state aid, without distinguishing between those that deserved or did not deserve receiving state support. As a result, a revised version of the law was adopted and a new procedure, known as "*Prodi-bis*", was regulated in the legislative decree of 8 July 1999, n. 270. The changes sought to address the issues raised by the EC and the ECJ in their analysis of the incompatibility of the Italian law with European state aid rules (see Box 1).

A new special regime for very large enterprises was created in 2003—dubbed the *Marzano law*—to address some of the inadequacies of the Prodi-bis law. The insolvency of the Parmalat group in 2003 prompted the authorities to enact special legislation to address the complex issues raised by this case. The new procedure is based on the Prodi-bis law, but with special rules for very large enterprises by allowing for more flexible and less cumbersome procedures, reducing the possibilities of liquidation, and assigning more powers to the administration at the expense of the judiciary.[5]

B. Standard Versus Extraordinary Insolvency

Extraordinary administration procedures present very different features from those of standard insolvency procedures. There are three major differences:

- **Minimum group size.** The special procedure is aimed at large enterprises, defined mostly by the number of employees and the size of debt.[6]
    - In the Prodi-bis procedure, large enterprises are defined as those employing at least 200 workers, a level considered as a medium-size enterprise elsewhere in Europe.[7] In addition, debt must represent at least 2/3 of the value of the groups' assets or income.[8]

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[4] ECJ judgment of 17 June 1999, in Case C-295/97, *Industrie Aeronautiche e Meccaniche Rinaldo Piaggio SpA and International Factors Italia SpA (Ifitalia), Dornier Luftfahrt GmbH, Ministero della Difesa*.

[5] First included in the decree-law of 23 December 2003, n. 347 and subsequently converted into the law of 18 February 2004, n. 39, known as the "Marzano law". Alberto Marzano was the Minister of Industry (or Minister of Economic Development) at the time.

[6] See art. 2 D. Leg. n. 270 and art. 1 D. Leg. n. 347.

[7] In European law, an enterprise with 200 workers is still a medium enterprise; EU Recommendation 2003/361 sets the threshold between medium and large enterprises at 250 employees.

[8] This commencement criterion has been the object of intense criticism: it is not easy to evidence that the debt levels reach the required 2/3 of the value of the assets and, in any event, that would mean that the enterprise is deeply insolvent in a balance-sheet sense, which may contradict the objective of restructuring viable companies. Connecting the amount of debt with the income of the enterprise is not justified as it does not provide a valid indicator of crisis. Some commentators have even confused the concept of "income" with that of "profit".

  - In the Marzano procedure, large enterprises are defined as employing a minimum of 500 people and having at least €300 million in debt. Initially, the thresholds were set at 1,000 employees and €1 billion in debt but were found too strict following the airline *Volareweb* case.[9]

- **Objectives**. The explicit goal is to preserve the enterprise, despite its state of insolvency, through restructuring or reconversion of the economic activity of the group, typically via a sale.[10] The procedure admits companies which "present concrete prospects for the recovery of the business activity".[11] More than often, this goal is accompanied with the preservation of jobs during the procedure and even more so following the sale of the company, where "the purchaser must undertake to pursue the business activity [of the company] for at least two years and to maintain the employment levels established at the time of the sale for the same period."[12]

- **Structure of the procedure and role of stakeholders.** The procedure has been defined as a "quasi-administrative" or "quasi-judicial" procedure since it is a hybrid of a judicial and an administrative procedure. It assigns a prominent role to the MED and the commissioners appointed by the Ministry who have to liaise with the courts. Creditor protection and participation is minimized, as their interests are merely "*taken into account"*, in contrast to a normal insolvency process where the interest of the creditors determine the envisaged solutions to the insolvency.[13]

The special procedure presents significant differences in its two versions. For this reason, it is necessary to have a separate description of the extraordinary administration regime (Prodi-bis) and the special regime for very large enterprises (Marzano).

C. Extraordinary Administration for Large Groups (Prodi-bis)

Access criteria. Beyond the quantitative criteria on workers and debt noted above, the enterprise must be declared insolvent, meaning unable to meet its obligations to creditors, and there must be specific prospects for the economic recovery of the enterprise. The procedure affects all the enterprises within the group.

Judicial phase. The process starts with a judicial phase, also known as "observation period", where insolvency is ascertained.

- First, the court must declare insolvency, at the request of the debtor or the creditors or the public prosecutor or even *ex officio* by the court, as extraordinary administration cannot be initiated if another insolvency procedure is already in train. Before

[9] Decree Law 29 November 2004, n. 281, converted into the law of 28 January 2005 n. 6.

[10] Literally, "*extraordinary administration is the insolvency proceeding of the large insolvent commercial enterprises, with the objective of preserving the productive estate, through the continuation, reactivation or reconversion of the entrepreneurial activities.*" (art. 1, D. Leg. n. 270).

[11] See Art. 27, D. Leg. n. 270.

[12] See Art. 63, D. Leg. n.270.

[13] See Art. 55.2, D. Leg. n. 270.

declaring insolvency, the court gives the MED a hearing, including an invitation to indicate the names of one or three judicial commissioners,[14] to be appointed by the court in case the enterprise is declared insolvent.

- Once insolvency is declared, the court appoints a judge to oversee the procedure, and one or three judicial commissioners as indicated by the MED. The court sets a deadline for the submission of claims by the creditors and may decide to allow the debtor to continue managing the business or, instead, assigns the judicial commissioner to manage the business.

- Within the judicial phase, and within a deadline of thirty days from the date of the insolvency declaration, the judicial commissioner must deliver a report on the causes of the insolvency and the prospects for economic recovery. The report also assesses the value of the enterprise and describes and assesses its liabilities. A copy of the report is delivered to the MED.[15] The MED submits its own opinion regarding the admission of the enterprise to the procedure.[16] After examining the report, and all relevant opinions and comments, the court declares the commencement of the extraordinary administration. If the court finds that the requirements for extraordinary administration are not met, it will instead declare the bankruptcy of the enterprise.[17]

Operational phase. In the second phase of the procedure, the administration has a leading role. The admission to the extraordinary administration requires good economic recovery prospects achieved through two different programs[18]: a) a restructuring plan, which should not last more than two years[19]; or b) a transfer plan, based on the sale of the enterprise as a going concern, after continuing the business activities for a period no longer than one year.[20] Once extraordinary administration starts, the court establishes measures for the continuation of the enterprise by the judicial commissioner, until the appointment of an extraordinary commissioner.[21] Subsequently, the MED appoints one or three extraordinary commissioners

[14] The possibility of appointing three judicial commissioners, instead of one, is reserved to the cases of extraordinary complexity (Art. 8.3, D. Leg. n. 270). The same principle applies to the appointment of extraordinary commissioners in the administrative phase of the procedure (Art. 38, D. Leg. n. 270).

[15] The debtor, the creditors, and other parties with a legitimate interest may access a copy of the report (Art. 28, D. Leg. n. 270).

[16] See Art. 29, D. Leg. n. 270. The debtor, creditors and other interested parties can also submit comments to the court.

[17] See Art. 30, D. Leg. n. 270. The literal wording is "specific perspectives of recovery of the economic equilibrium of the entrepreneurial activities"—Art. 27.1, D. Leg. n. 270.

[18] This distinction is consistent with the difference between rescue of the entity (restructuring plan) and rescue of the business (the sale allows the continuation of the business, even if another entity acquires it). See Graham (2014). In practice, the sale of the business is the most frequent solution (see section IV).

[19] Once this period expires, the MED may grant a one-year extension (with the possibility of an additional one-year extension after the first one).

[20] This period can also be extended by an additional one-year period, whenever the continuity of business activities is confirmed to be useful by the commissioner (amendment introduced by decree-law n. 145 of December 23, 2013, converted into Law n. 9/2014).

[21] See Art. 32, D. Leg. n. 270.

to take over the management of the enterprise and perform the critical roles of the procedure. The MED also appoints a surveillance committee, which has a consultative function.[22]

Even though the extraordinary commissioner, assisted by experts, manages the business, there are special actions that require the opinion of the surveillance committee and the authorization of the MED. These include: 1) the sale and lease of enterprises or of economic units; and 2) sales, leases and encumbrances of real estate assets; block sales of movable assets; pledges or transactions of indeterminate value or for a value higher than €2,065,682.[23]

The continuation of the enterprise is protected by the legal effects of the procedure. First, there is a stay of creditor actions without any exceptions, allowing continuation of the business without the disruption of enforcement lawsuits.[24] Second, avoidance actions are restricted to cases where there is a program of sale of the business, and only the extraordinary commissioner can undertake these legal actions. Third, the extraordinary commissioner can interfere with executory contracts, but not with labor contracts, or lease contracts where the debtor is the lessor.[25] Finally, the claims related to the continuation of the business represent expenses of the procedure and have priority over the existing creditor claims.[26]

The extraordinary commissioner must present a program within 60 days after the commencement of the procedure.[27] The program is drafted under the supervision of the MED, in conformity with the industrial policy guidelines adopted by the MED aiming to safeguard the operational unity of the enterprise while "taking into account the interests of the creditors".[28] If the implementation of the program requires guarantees from the Treasury, or any other facilitating measures, it would need to abide by EU state aid rules.[29]

The program must include the following: (i) the business activities that will be continued and those that will be discontinued; (ii) a plan for the liquidation of the assets that are not essential for the continuation of the enterprise; (iii) financial and economic projections for the continuation of the business; (iv) mechanisms to cover the financial needs of the business, including possible financial assistance by the state; (v) if the program contemplates the sale of the business, it must indicate whether offers have already been received and the

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[22] The committee must have three or five members: one or two of them must be selected among the unsecured creditors; and two or three will be selected among experts identified by the MED. The committee provides its opinion over key aspects of the process. The committee can inspect the financial statements and documents of the procedure at any time and can also request information or clarifications from the extraordinary commissioner or the insolvent debtor.

[23] See art. 42, D. Leg. n. 270. The amounts reflect the conversion of lire into euros.

[24] See Art. 48, D. Leg. n. 270.

[25] See Art. 50, D. Leg. n. 270.

[26] See Art. 52, D. Leg. n. 270.

[27] The MED can grant an extension for an additional 60 days (Art. 54 D. Leg. n. 270). If the program is not drafted in time, the MED will dismiss the commissioner and appoint a new one.

[28]See Art. 55, D. Leg. n. 270.

[29] See Art. 55.2, D. Leg. n. 270—this article was drafted to address the objections of the ECJ and the EC. See Box 1.

expected recovery for creditors; and (vi) if the program contemplates the restructuring of the business, it must include the eventual recapitalization of the enterprise, changes to the structure of the enterprise, and the timeline and modalities for the satisfaction of the creditors' claims, which can also be based on a composition with the creditors.[30]

The MED authorizes the execution of the program after hearing the surveillance committee.[31] If the program includes state aid, it would require a decision from the EC. If the EC denies it, the commissioner will have to present a new program which does not involve state aid.[32]

Subsequently, the extraordinary commissioner implements the program and presents a progress report to the MED every three months.[33] After completion of the program, the extraordinary commissioner presents a final report. The reports are also delivered to the surveillance committee, which adds its opinion. The reports and opinions are deposited with the court and accessible to all interested parties.

The implementation of the program of sale requires a prior valuation of the business. The acquirer must commit to continue the activity for two years at least, maintaining the employment levels agreed at the time of the sale. The selection of the acquirer considers the offer price and the reliability of the bidder and its business plan, including the preservation of jobs.[34] It is possible to agree on a partial transfer of employees and modify subsequently the employment conditions.[35] After the sale, the commissioner distributes the proceeds among creditors.

At any point, the process can be transformed into bankruptcy if the programs fail or the chances of success become low. The procedure can be closed if: 1) the enterprise recovers its solvency before the end of the program; or 2) if there is a composition agreed by the creditors, which must be authorized by the MED after receiving the opinion of the extraordinary commissioner and after a hearing with the surveillance committee. The composition must remain in line with preserving the enterprise.[36]

D. Extraordinary Administration for Very Large Groups (Marzano)

Access criteria. Although access is limited to very large enterprises, other requirements are looser than under Prodi-bis. Insolvency is a requirement, but it is not assessed at the commencement of the procedure. There is also *no express requirement* of "specific prospects of economic recovery" of the enterprise. When the law was enacted in 2004, it only covered enterprises with at least 1,000 workers and €1 billion of debt. However, in 2005, the thresholds were lowered to 500 workers and €300 million of debt.

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[30] A composition ("*concordato*") is a consensual agreement between the debtor and its creditors whereby the creditors reschedule or reduce debt against the debtor to resolve the insolvency situation.

[31] See Art. 57, D. Leg. n. 270. Parts of the program may be kept confidential.

[32] See Art. 58, D. Leg. n. 270.

[33] Art. 61, D. Leg. n. 270.

[34] See Art. 63, D. Leg. n. 270.

[35] Workers that are not transferred with the enterprise can receive the support of the state through the *Cassa Integrazione Guadagni Straordinaria* (CIGS) (see Box 3).

[36] See Art. 78, D. Leg. n. 270.

Initiation of the procedure: In contrast to the Prodi-bis procedure, the initiation of Marzano procedure is entirely administrative. Under the Marzano law, the debtor applies directly to the MED and, at the same time, submits an insolvency application to the court. The Minister initiates the extraordinary administration procedure by decree, without waiting for the resolution of the court.[37] The court issues the insolvency declaration within five days of the communication of the decree by the Minister.

Role of the extraordinary commissioner. As under the Prodi-bis procedure, the MED appoints one or three extraordinary commissioners. But the extraordinary commissioner has also the function of the judicial commissioner and manages the company until the declaration of insolvency. Within sixty days from the appointment, the extraordinary commissioner must produce a report similar to the report of the judicial commissioner under the Prodi-bis proceedings.[38] The commissioner can also ask the extension of the procedure to other enterprises in the group.

Program for the extraordinary administration. Within 180 days following his or her appointment, the extraordinary commissioner must present a program together with a report on the causes of the insolvency and the valuation and analysis of the enterprise assets, business activities and liabilities.[39] Under the original Marzano procedure, the program could only be a *restructuring* program, and the sale of the enterprise could only be attempted if the restructuring program was not approved. However, after the Alitalia amendments in 2008, it is possible to implement a sale of business program under this proceeding. The restructuring program can include a composition with creditors which could foresee the division of creditors in classes.[40, 41] The composition proposal must be authorized by the MED after assessing the correctness in the formation of creditor's classes. The composition requires the approval of a majority of creditors representing the majority of claims in every class.[42] If one or several classes vote against the composition, the MED can disregard the negative vote if a majority of classes voted in favor. In this case, the dissenting classes will be treated at least as they would have been under other *practicable alternatives*.[43] If creditors do not approve the composition, the extraordinary commissioner will introduce variations to the plan. The extraordinary commissioner can present to the MED a plan for the sale of the enterprise.[44]

[37] See Art. 2, Decree-law n. 347.

[38] The sixty-day period to produce the report can only be extended once, for an additional sixty days (art. 3.2, Decree-law n. 347).

[39] See Art. 4.2, Decree-law n. 347. The deadline to present the program can be extended by the Minister for an additional 90-day period.

[40] See Art. 4 bis, Decree-law n. 347.

[41] The only requirement to create classes is that the creditors share "homogenous economic interests" (Art. 4 bis, Decree-law n. 347). For instance, it is possible to create a class for small creditors, or a class for bond creditors.

[42] However, abstention by creditors is deemed equivalent to a positive vote to the composition.

[43] The usual alternative would be the liquidation of the enterprise. This interesting provision shows the influence of U.S. law (*cram-down* under Chapter 11, §1129).

[44] If the plan is authorized, the one-year term for the sale of the enterprise can be extended for another year, to allow for the continuation of the enterprise activities.

Other special rules. The Marzano procedure incorporates other special rules, some of which have been introduced by successive reforms targeted at specific insolvency cases:

- *Enterprises providing essential public services and strategic enterprises*. A series of legislative changes were introduced to address the 2008 crisis of Alitalia.[45] These changes allow the sale of the enterprise at market value in private negotiations, with the goal of maintaining the delivery of essential public services.[46] An advantageous treatment regarding anti-trust and licensing requirements is also included in these amendments. Similar provisions have been introduced for strategic enterprises.[47]

- *Transactions during the process*. The MED can authorize transactions during the process, such as the sale or lease of assets, businesses or economic units, as long as the goal is the restructuring of the enterprise or group of enterprises.[48] Until the authorization of the restructuring program is granted, the MED can authorize transactions necessary for the continuation of the business. This does not include acts of ordinary administration or acts below €250,000, which do not require authorization.

- *Avoidance actions*. In contrast to the general procedure, the extraordinary commissioner under the Marzano law can undertake avoidance actions even after the authorization of the restructuring program, as long as the avoidance actions are conducive to the objectives of the program.[49]

III. DATA SOURCES

To study the effectiveness of the procedure, data were collected for the two special regimes starting in 1999, when the amendments to abide by EU recommendations were introduced. The main source for this data is the MED and covers the period from 2000 until 2017. The data contain information on the 120 groups intervened under the Prodi-bis procedure (representing a total of 329 companies) and the 25 groups intervened under the Marzano procedure (representing a total of 231 companies). The total number of observations is 145 groups, representing 560 companies.

To obtain balance sheet and income statement information, firms undergoing the procedure were matched with information from the Orbis database. This database is proprietary of the Bureau van Dijk, which sources its information for the universe of Italian companies from the Cerved Group in Italy. Every Italian company with a tax ID that files at the Chamber of Commerce is included in the database. The total number of active and inactive Italian companies in the database is close to 7 million. Orbis provides also non-

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[45] See decree-law “Alitalia”, of August 28, 2008, n. 134, converted into the Law of 27 October 2008, n. 166.

[46] Market value is determined by an expert appointed by the MED, marking a floor for the sale of the enterprise.

[47] See Decree-law n.1, of 5 January 2015, converted into law n. 20, of 4 March 2015.

[48] See Art. 5, Decree-law n. 347.

[49] This feature has been criticized by lawyers and academics in Italy, since it creates a difference with the Prodi-bis procedure: under the Marzano law, it is possible to restructure the enterprise and undertake avoidance actions that can undo transactions done by the company, to the detriment of third parties. Therefore, the company can potentially benefit from its own fraudulent actions.

financial information, such as the number of employees, the region of operation, shareholder structure, etc. Prodi-bis and Marzano firms are compared against the universe of Italian firms—excluding financial firms—with more than 200 employees. Statistics are considered at the company group level, as some companies within groups are not financially independent.[50]

The focus of the empirical approach is somewhat restrained by the limitations of the database. For instance, financial data are only available up to one or two years before the application for extraordinary administration, precluding an analysis of the financial performance of firms once they are admitted into extraordinary administration. In addition, due to issues related to the identification of insolvent firms in Orbis, it is not possible to compare the financial performance of firms undergoing extraordinary administration with those under the general insolvency regime.

It is also important to note that recovery rates for creditors following the application of the procedures are not publicly available. Such data would allow for a more complete assessment of the efficiency of the procedures. For standard reorganization procedures, Danovi et al. (2018) show that repayment of creditors takes less than a year and usually results in full recovery for secured creditors.[51] If, for instance, extraordinary administration recovery rates are lower and take longer to accrue even for secured creditors, then the procedures would necessarily be highly inefficient compared to the standard regime. Given their importance, publication of these data would be very useful. In any case, even without them, useful inferences can be drawn.

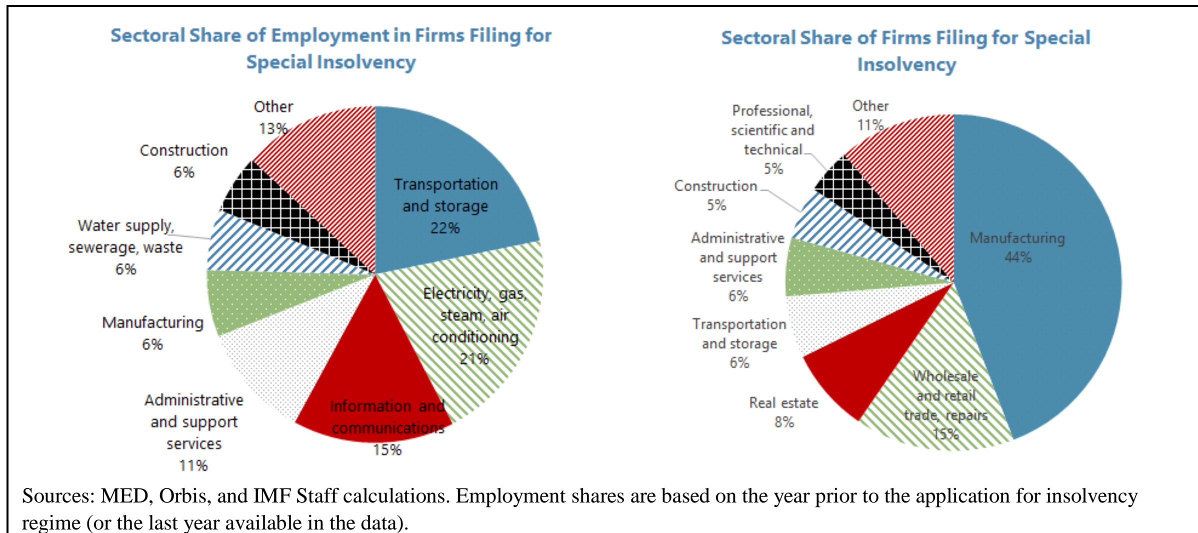
IV. Empirical Analysis

A. Non-Financial Characteristics of Companies Undergoing Special Insolvency

The manufacturing sector is predominant among companies applying for special administration, but other sectors—some appearing to be non-strategic—feature a larger employment share. A combination of large size and exposure to shocks likely explains the predominance of the manufacturing sector in extraordinary administration. However, as a share of employment, among the top sectors accounting for almost 60 percent of the population are transportation and storage, utilities, and administrative support. Many of these companies do not perform strategic roles in the economy, belonging to sectors such as publishing, textile, and private security services (see Annex I).

[50] To obtain group-level data for the control group, the Orbis sample is restricted to the union of firms with consolidated accounts (categories C1 and C2 in Orbis) and firms with unconsolidated accounts which are not part of a larger group (Orbis independence indicators A+, A, A-, B+, B, B- and U). Any duplicated entries at the group-year level are resolved selecting the account with the highest degree of consolidation.

[51] Danovi et al. (2018) analyze a sample of 3,000 reorganization cases in the period 2008–2015 (corresponding to about one third of the reorganization procedures (*concordato preventive*) in that period). However, information on effective recovery rates is only available for a limited number of cases; for those cases, secured creditors recover almost all the value of their loans, while the recovery rate for unsecured creditors ranges between 1 and 25 percent.

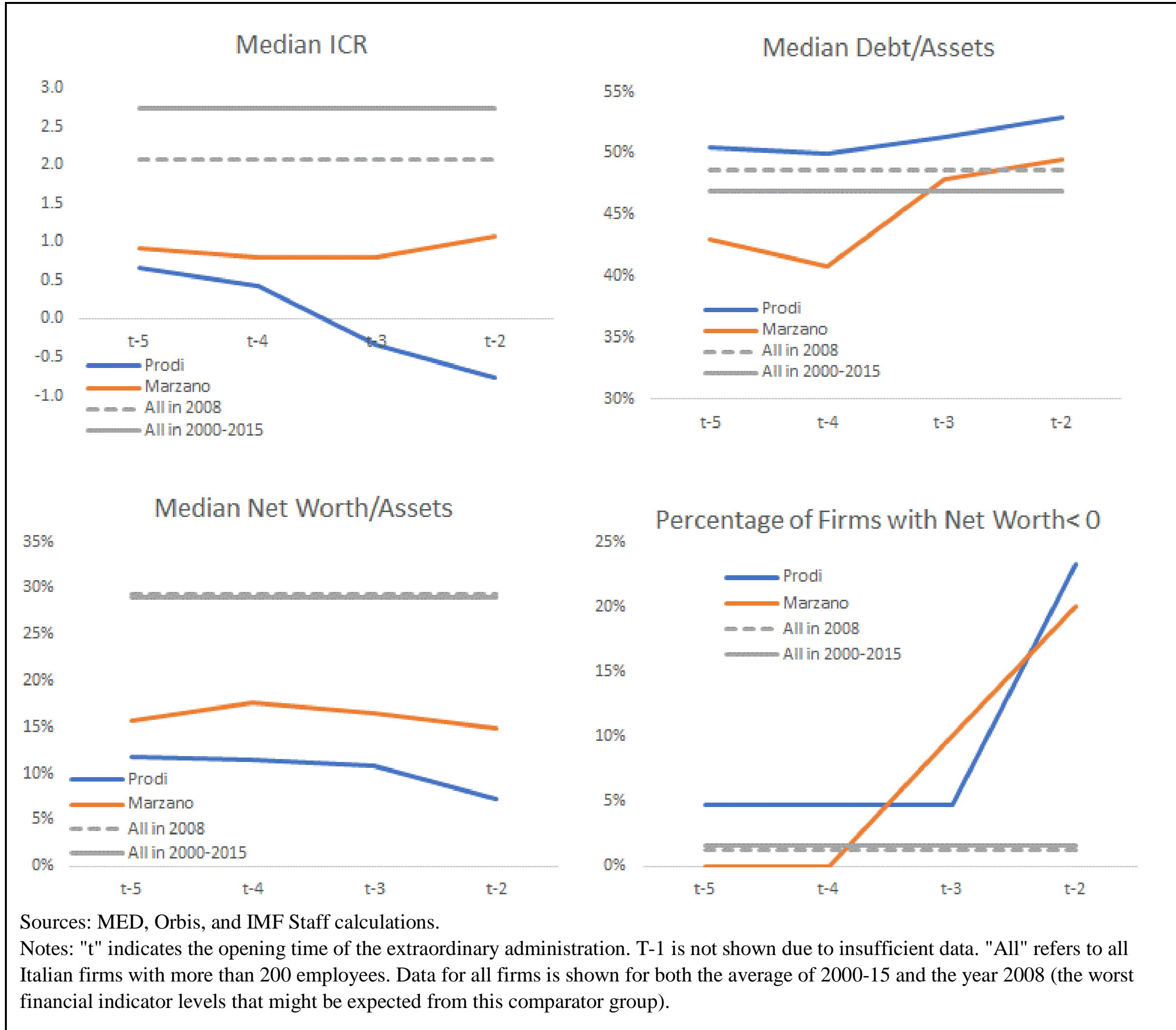


Sources: MED, Orbis, and IMF Staff calculations. Employment shares are based on the year prior to the application for insolvency regime (or the last year available in the data).

B. Financial Characteristics of Companies Undergoing Special Insolvency

Companies are overall deeply illiquid by the time they apply for the special regime. Companies tend to file for the special insolvency regime after experiencing 2–3 years of negative earnings. As shown in the text table and charts below, the group median interest-coverage-ratio (ICR) under the Prodi-bis regime is close to -0.5 percent 2–3 years before the start of the procedure, compared to a median ICR above 2 for the population of firms with more than 200 employees.

Moreover, these companies are characterized by poor balance sheets. In general, two years before the start of the insolvency procedure, groups that are admitted have 10–15 percentage points less net worth-to-assets than the population of Italian firms with more than 200 employees. About 25 percent of groups in the Prodi-bis regime and 20 percent of groups in the Marzano regime are already insolvent two years before the start of the procedure. This compares to only 2 percent in the comparison group.



Sources: MED, Orbis, and IMF Staff calculations.

Notes: "t" indicates the opening time of the extraordinary administration. T-1 is not shown due to insufficient data. "All" refers to all Italian firms with more than 200 employees. Data for all firms is shown for both the average of 2000-15 and the year 2008 (the worst financial indicator levels that might be expected from this comparator group).

Summary Statistics of Each Group of Companies

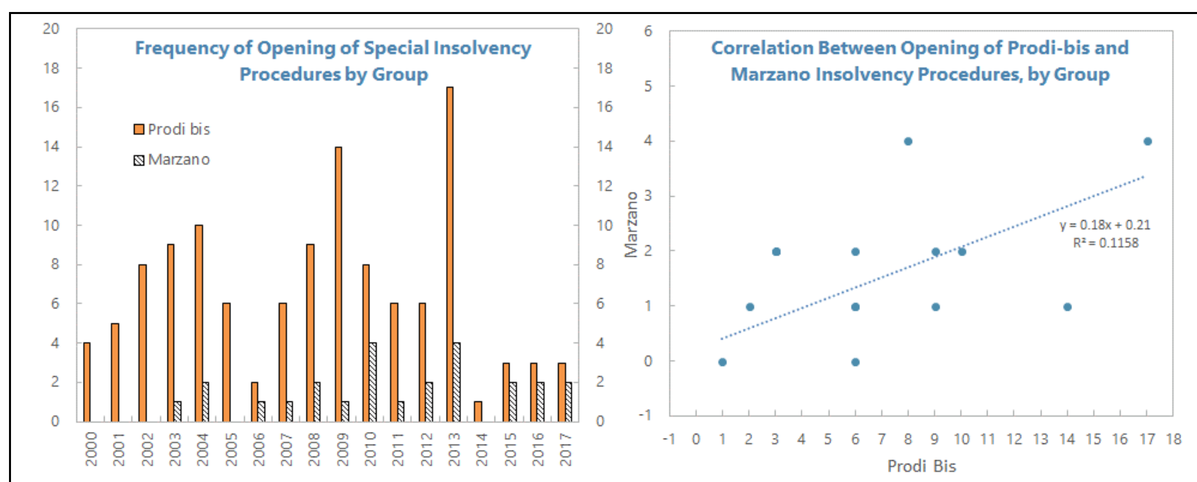
Prodi-bis				
Variable	**No. of Obs.**	**Median**	**Mean**	**Std. Dev.**
Employees	111	338	508	725
Net worth (€ thousand)	111	1188	2298	138,000
Total assets (€ thousand)	111	108,000	207,000	469,000
Operating revenue (€ thousand)	111	71,500	121,000	203,000
Interest Coverage Ratio	101	-1.31	-3.21	28.82
Profit margin (%)	103	-6%	-11%	22%
Debt/Assets (%)	103	53%	58%	42%
Debt/Equity>4 or <0 (% of firms)	111	NA	79%	41%
Debt/EBIT>4 or <0 (% of firms)	111	NA	95%	23%
Net Worth/Assets (%)	103	2%	-14%	52%
Net Worth/Assets< 0 (% of firms)	111	NA	39%	49%
Interest/Debt (%)	100	5%	18%	96%
Marzano				
Variable	**No. of Obs.**	**Median**	**Mean**	**Std. Dev.**
Employees	22	611	2096	4597
Net worth (€ thousand)	22	39,400	241,000	664,000
Total assets (€ thousand)	22	335,000	1,630,000	409,000
Operating revenue (€ thousand)	22	134,000	880,000	2,090,000
Interest Coverage Ratio	22	-0.25	-1.17	9.22
Profit margin (%)	22	-1%	-9%	29%
Debt/Assets (%)	22	54%	91%	195%
Debt/Equity>4 or <0 (% of firms)	22	NA	50%	51%
Debt/EBIT>4 or <0 (% of firms)	22	NA	95%	21%
Net Worth/Assets (%)	22	11%	-42%	198%
Net Worth/Assets< 0 (% of firms)	22	NA	23%	43%
Interest/Debt (%)	22	4%	5%	4%
All >200 employees (in 2008)	**No. of Obs.**	**Median**	**Mean**	**Std. Dev.**
Employees	1889	533	1894	7513
Net worth (€ thousand)	1889	62,900	402,000	3,010,000
Total assets (€ thousand)	1889	206,000	1,620,000	16,200,000
Operating revenue (€ thousand)	1889	192,000	903,000	5,460,000
Interest Coverage Ratio	1869	2.08	9.275045	48.95304
Profit margin (%)	1884	3%	3%	9%
Debt/Assets (%)	1884	49%	46%	20%
Debt/Equity>4 or <0 (% of firms)	1889	NA	18%	39%
Debt/EBIT>4 or <0 (% of firms)	1889	NA	83%	37%
Net Worth/Assets (%)	1889	29%	32%	19%
Net Worth/Assets< 0 (% of firms)	1889	NA	1%	11%
Interest/Debt (%)	1879	4%	5%	5%
All >200 employees (average 2000-2015)	**No. of Obs.**	**Median**	**Mean**	**Std. Dev.**
Employees	26519	493	1762	7285
Net worth (€ thousand)	26475	51,100	406,000	3,230,000
Total assets (€ thousand)	26519	175,000	2,160,000	26,600,000
Operating revenue (€ thousand)	26519	155,000	724,000	4,560,000
Interest Coverage Ratio	25842	3	12	50
Profit margin (%)	26430	3%	4%	10%
Debt/Assets (%)	26118	47%	45%	20%
Debt/Equity>4 or <0 (% of firms)	26519	NA	20%	40%
Debt/EBIT>4 or <0 (% of firms)	26519	NA	82%	39%
Net Worth/Assets (%)	26474	29%	31%	20%
Net Worth/Assets< 0 (% of firms)	26519	NA	2%	12%
Interest/Debt (%)	26021	3%	4%	7%

Sources: MED, Orbis, Haver Analytics, and IMF Staff calculations.

Notes: Values expressed the year before the start of insolvency (or last year available) at group level. NA: Not showing the mean of dummy variables. Measures in euros are deflated to 2015.

C. Uses of the Special Regime and Its Efficiency

Unsurprisingly, admissions to the two special regimes peaked after the global financial crisis and the Euro zone debt crisis. This is evident by looking at the number of admitted companies by group, which peaked in 2009 and 2013. The frequency of utilization of both procedures is positively correlated, indicating that macro shocks are affecting both medium and large companies.



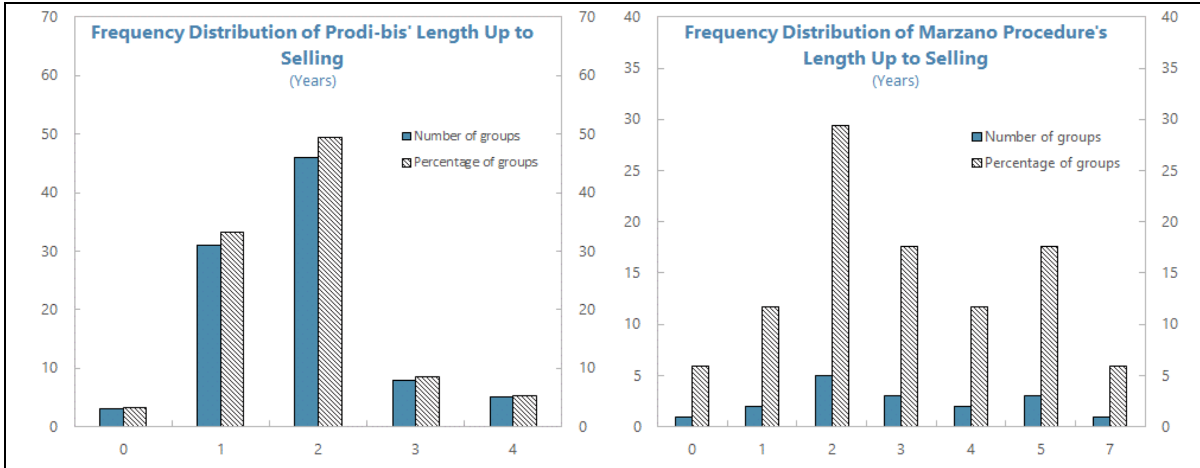
The most likely outcome of the special procedure is the sale of the company, rather than restructuring. In about 95 percent of cases, the special insolvency procedure leads to the sale of the company, or its divisions, instead of a stand-alone restructuring. This suggests that the procedure serves to foster sales rather than carrying out the restructuring or internal recovery of enterprises.

Performance of the Procedures, 2000-15		
	Prodi bis	Marzano
Group cases opened	113	21
Companies in the groups	301	143
Companies still in special administration in 2016	240	126
in percent of companies involved	80	88
Restructured companies	11	17
Converted to bankruptcy	50	0

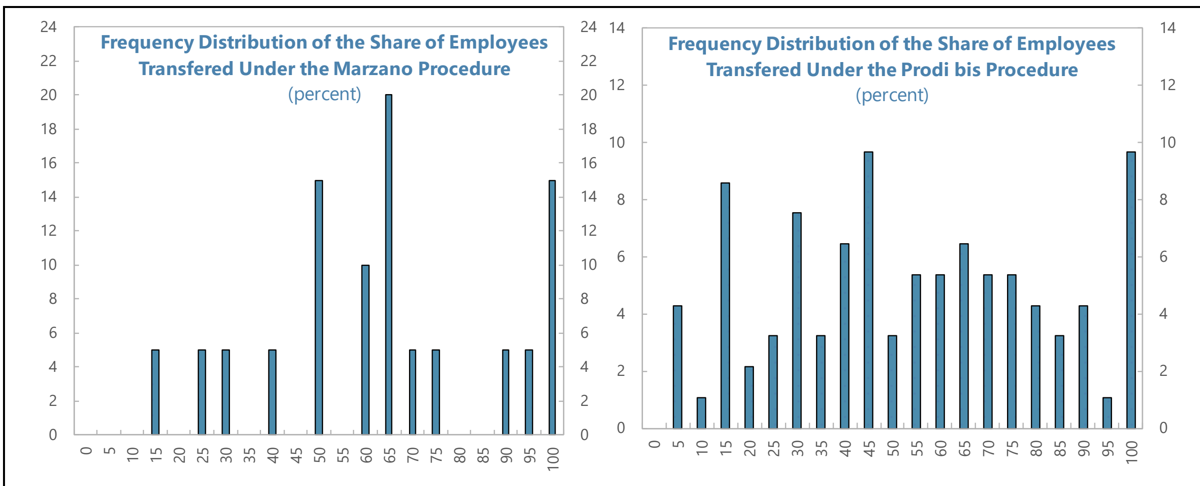
The length of the restructuring or selling phase varies significantly. In most cases, the procedure abides by the deadlines set for the execution of the restructuring or selling program and produces the envisaged outcome (sale, in most cases) within a period of about two years on average for Prodi-bis and about three years for Marzano. However, extensions and changes in programs along the way can lengthen the procedure significantly. For instance, in the case of the Marzano procedure, one third of groups undergo the selling phase for longer than three years.

The subsequent liquidation phase is very lengthy. Following the sale of the companies, the remaining assets must be disposed, which usually takes longer than 8 years, above the average length of the ordinary bankruptcy procedure (*fallimento*). This is likely related to the

organizational complexity and the illiquidity of assets of many of the companies admitted into the special regime. In fact, 80 percent of companies under Prodi-bis and 88 percent of companies under Marzano are still undergoing the procedure. Annex I shows the range of years and length of the liquidation phase for each group involved.



Slightly more than half of the employees keep their jobs following the exit from the procedure. The transfer of employees via sales or restructuring averages 60 percent and 50 percent of employment at the time of application under the Marzano and the Prodi-bis procedures, respectively. In about 20 percent of the cases, more than 90 percent of employees are transferred.



A simple calculation suggests that the combined cost of the special regimes for creditors and the state during 2000–15 could have reached at least €19 billion. The dire financial situation of the companies when entering the regime, the length of time for resolution, and the prioritization given to job preservation suggest that creditors, and potentially the government, face large restructuring or liquidation costs. Given the lack of published data on credit recovery rates and sparse information regarding state aid support, or public funds used to support employment, for companies under extraordinary administration, a straightforward estimation of these costs is not possible. However, a proxy can be calculated from the

balance sheet data available prior to insolvency. The assumption is that during their reorganization, companies are recapitalized so they are ready to be sold on a sustainable financial footing. In this case, the total cost of restructuring would amount to close to €19 billion, equal to the sum of: (i) the cumulative net income losses (or negative profits) incurred during the reorganization phase (€12 billion), and (ii) the net wealth needed to recapitalize company groups to a viable net worth-to-assets ratio (about €7 billion).[52] As a comparison, the cost of immediate liquidation would be only €3 billion, corresponding to the total negative net worth that creditors and original shareholders would lose.

Put another way, the inefficiency of the special regime can be seen through the high cost of preserving employment. The additional cost to creditors, original shareholders, and the state for preserving employment, compared to liquidating the firms, translates to an average cost per transferred employee of €420,000, equivalent to about 14 times GDP per capita.

The cost of the procedure is likely to be larger than the one calculated using this proxy approach and is not easily amenable to a cost comparison with the general regime. The cost per transferred employee does not include attendant costs to the procedure such as the contribution from the wage supplementation mechanism, CIGS (see Box 3).[53] Unfortunately, data regarding the use of CIGS for the specific cases under extraordinary administration are not available. Relatedly, it would not be straightforward to compare the cost of the procedure to the one from the general regime for two reasons: 1) the general regime is much more complex, offering many different options to bankrupt companies than the special regime. As such, it would not be correct to compare extraordinary administration to liquidation (*fallimento*) under the general regime since the special procedure is designed to preserve the enterprise; 2) Since extraordinary administration does not preserve the managerial team, management might have an incentive to avoid insolvency and hence prolong the period of poor financial performance. Alternatively, companies that would use the general regime could keep good managers who might continue managing the company in distress under restructuring procedures.

V. ASSESSMENT OF THE REGIME

The existence of a special regime for the insolvency of large enterprises is rare in the EU. Except for Italy and Croatia, there are no other countries in Europe where the size of enterprises requires a special insolvency process that is quite different from the general insolvency law.[54]

[52] It is assumed that companies require at least a 20 percent net worth to assets ratio to be financially viable, a commonly used threshold (see, e.g., IMF, 2016a). Note that the recapitalization needs resulting from this metric do not account for the potential reductions in the size of the balance sheet following the reorganization of companies, a feature which is unobservable in the database.

[53] For instance, Mediobanca (2015) estimates that CIGS paid €660 million and the special fund for air transport (with a similar function) paid €1.2 billion.

[54] The only exception, together with Italy, is Croatia, where a law enacted in 2017 allows for the extraordinary administration of systemic enterprises (Law for the Extraordinary Administration for Companies with Systemic Importance for the Republic of Croatia, law n. 32/2017.) This special law, adopted for the insolvency of *Agrokor*—the largest company in Croatia- has been inspired by the Italian precedent.

An argument can be made that the special regime achieves its objectives. Employment is largely preserved, part of the groups under the procedures are sold off relatively quickly, while other parts of the groups are liquidated gradually. It could be argued that the latter preserves values by avoiding fire sales—although, as noted, data on recovery rates are not publicly available—and keeps firm-specific tangible and intangible capital. But countering these arguments are the above-mentioned facts that the special rules of extraordinary administration lead to costly and lengthy procedures, undermine the protection of creditor rights, and open opportunities for potential interference in the insolvency of large enterprises.

The shortcomings of the regime can be seen in the following aspects:

- *Companies that are admitted into the procedure are deeply insolvent and illiquid.* As shown in the previous section, the requirements for access to the procedure, in particular for the Prodi-bis law, do not guard against enterprises being in deep crisis at the onset of the procedure, making it costlier to restructure the company. As the law requires that the debts of the enterprise represent at least two thirds of the value of the assets or revenues, many businesses are in fact deeply insolvent in the balance-sheet sense, and this could reduce their possibilities for recovery.[55,56] As shown in the previous section, at least 20 percent of the companies have negative net worth, already two years before being admitted into the procedure. The assessment of the "specific prospects of economic recovery" does not seem to establish a demanding threshold for access to the procedure. The effect of the procedure, therefore, is to allow the continuation of the enterprise, even in cases where that continuation may not be justified by an analysis of the viability of the business.

- *Creditors' rights are sidelined.* As the business continues, these enterprises will accumulate new liabilities, derived from the continuation of existing contracts with workers and suppliers, and new financing, frequently provided by the state. As the new liabilities take priority over the pre-existing claims, the mere continuation of the enterprise can result in large losses to pre-existing creditors, with no possibility of stopping the losses by forcing a liquidation of the business. This could lead to other perverse effects such as lower future investment, including in large enterprises. Moreover, the data show that most of extraordinary administrations end in a sale of the business or in a protracted liquidation of the assets.

- *The cost of the procedure is large.* The practice of extraordinary administration suggests that the most important function performed is that of guaranteeing, for a certain period, the maintenance of jobs in cases of failure of large enterprises, which typically receive intense public attention. The maintenance of jobs can be achieved by

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[55] There is an alternative commencement criterion: that the debts of the enterprise represent two thirds of its sales—this alternative criterion is extremely controversial and debated. Under the Marzano procedure, the only requirement refers to the absolute amount of debt (at least 300 million euros), and for that reason, there is no discussion about the application of the threshold.

[56] If enterprises want to address their problems earlier, they can use the generally applicable procedures under the insolvency law (namely, *concordato preventivo*). However, there is little incentive for enterprises to pursue this route: in most cases, the debtors may consider that it is better to wait until extraordinary administration is applicable and they can receive a beneficial treatment, including public financial support and special treatment of labor contracts.

placing the losses on the pre-existing creditors, until the enterprise is restructured or, more often, sold to a third party. As shown in the previous section, the gross average cost per transferred employee appears to be very large. In the long run, the procedure cannot guarantee the maintenance of jobs, once the two years commitment period of the buyer lapses. The direct support of the state for maintaining jobs results in an additional collective cost (see Box 3) which adds to the general cost of the procedure while hampering a swift reallocation of workers to more productive uses.

- *Cases of special administration can be connected to advantageous state aid.* Extraordinary administration is often connected with state aid; the current laws have not been challenged before the ECJ, and they are very different in nature to the original Prodi law, which provided automatic advantages to the enterprises subject to the procedure. However, cases of extraordinary administration are frequently connected with special state aid provided to support business continuity. In these cases, state aid is communicated to the EC and is authorized if it complies with EC guidelines (see Box 2). Despite this, there are instances of illegal state aid being provided to enterprises in extraordinary administration.[57]

- *The MED decisions are primarily based on the industrial and social policy of the government*; the protection of creditor rights plays only a marginal role. Although the MED made efforts to increase the transparency of its decisions and internal processes, it is the design of the procedure itself that makes it subject to criticisms of political influence which could go beyond market considerations.

- *The strategic relevance of some groups and companies that apply to extraordinary administration is doubtful.* The thresholds of extraordinary administration imply that this procedure applies to medium-sized businesses in any economic sector, without any strategic relevance. Prima facie, it is difficult to justify the existence of a "public interest" in insolvency cases that involve medium-sized enterprises devoted to activities such as tourism or private security.

- *The regime likely harms investment and credit growth.* The regime sends a negative signal regarding the ease of doing business and investing in large enterprises, by subordinating private rights to broader social considerations, as creditor rights are disregarded to avoid the negative consequences of enterprise failure. This is macro-relevant not least because effective insolvency and restructuring regimes can facilitate credit growth, investment, and job creation while, as a general matter, larger firms may be more likely to be at the productivity frontier.

The regime itself deviates from international standards for insolvency. There are numerous differences between extraordinary administration and the recommendations from international insolvency standards, namely, the UNCITRAL *Legislative Guide on Insolvency Law* and the World Bank *Principles for Effective Insolvency and Creditor Rights Systems*.

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[57] A recent example refers to the steel company ILVA: see EC Decision of 21 December 2017, C (2017) 8391 final: it concludes that a state guarantee on a €400 million loan and a €300 million public loan, which served to finance ILVA's liquidity needs for its commercial activity, were granted on terms below market conditions and therefore represented illegal state aid.

Some of the deviations from the standard are *structural*, and deeply affect the design and operation of the insolvency process:

- *The objective of the insolvency process.* The fundamental assumption in extraordinary administration is that large enterprises deserve to be preserved. Although this can be a possible goal of insolvency, it should not be achieved at the expense of basic notions of viability and ignoring creditor rights.[58]

- *The role of the public administration*. International insolvency standards are premised on the idea that the process is overseen by a court and conducted by insolvency representatives of high professional standards.[59] The decisive intervention allowed by the MED is not in line with international standards, and illustrates a different approach to insolvency where the administration can take decisions based on non-economic grounds, e.g. industrial and social policy considerations.

- *The deficit in creditor participation rights*. As opposed to the standard, in extraordinary administration, creditors are not participants in the process, but mere bystanders of the attempts to preserve the business.[60] Creditors do not have a say in the commencement of the special insolvency process; do not have any influence in the selection of the extraordinary commissioner or the experts; cannot select any representatives to the surveillance committee, and their participation in the committee is limited; most importantly, creditors do not have a vote over the program to restructure or sell the company. Only in the cases where the extraordinary commissioner proposes a composition will the creditors have an opportunity to vote on issues that affect the satisfaction of their claims.[61]

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[58] The UNCITRAL Legislative Guide discusses the possibility that the insolvency law includes the objective of preserving enterprises, but this should not be achieved at the expense of ignoring creditor rights or basic notions of viability: "*adopting a reorganization-friendly approach should not result in establishing a safe haven for moribund enterprises: enterprises that are beyond rescue should be liquidated as quickly and efficiently as possible*" (UNCITRAL (2004), 15–16).

[59] See UNCITRAL (2004), 33–35 (on the role of courts and insolvency representatives in the insolvency system). The World Bank Principles state that "*Insolvency proceedings should be overseen and impartially disposed of by an independent court and assigned, where practical, to judges with specialized insolvency expertise. Nonjudicial institutions playing judicial roles in insolvency proceedings should be subject to the same principles and standards applied to the judiciary*" (World Bank (2016), Principle D.1.2). The World Bank Principles refer to countries where an administrative agency is in charge of applying insolvency law (e.g., Colombia): in those cases, the level of independence and accountability of staff charged with the application of insolvency law is the same as that of the judiciary.

[60] The role of creditors is crucial in the international insolvency standard: see UNCITRAL (2004), at 190: "*For a number of different reasons, many insolvency laws facilitate direct creditor involvement in the proceedings. As the party with the primary economic stake in the outcome of the proceedings, creditors may lose confidence in proceedings where key decisions are made without consulting them by individuals who may be perceived by creditors as having limited experience or expertise in the debtor's type of business or a lack of independence, depending upon the manner in which the representative is appointed*". See also World Bank (2016): "*Creditor interests should be safeguarded by appropriate means that enable creditors to effectively monitor and participate in insolvency proceedings to ensure fairness and integrity*" (Principle C.7.1).

[61] Moreover, the requirement of "specific prospects of economic recovery" is absent in the case of the largest enterprises (Marzano law).

The thresholds for the application of extraordinary administration do not correspond to the distinction in European standards for medium and large enterprises. Whereas the Marzano law covers large enterprises, the general regime for extraordinary administration is broad enough as to cover medium enterprises too: an enterprise employing 200 workers is a medium enterprise according to European standards. It is also hard to justify that a differentiated legal treatment should apply to a company depending on the fact that it has 199 workers or 201 workers. Moreover, the criterion of debt is based on a ratio between the amount of debt and the value of the assets or sales, which bears no relation with the size of the enterprise. In addition, these are not generally accepted metrics for the assessment of enterprise distress such as the most commonly used measures of interest-coverage-ratio or debt-over-EBIT.

VI. Lessons and Recommendations

The special insolvency procedure for large enterprises performed an important function during the industrial crisis affecting Italy in the 1970s. Given the inadequacy of the old insolvency regime, and especially its inability to preserve the going concern value of enterprises, extraordinary administration provided the only venue for the reorganization of businesses. In this respect, extraordinary administration acted as a *precursor* to the changes of the Italian insolvency framework, which eventually have resulted in much greater flexibility for the resolution of business distress.[62] Some of the technical innovations of extraordinary administration, such as the coordinated resolution of enterprise groups, still need to be incorporated in the general insolvency framework. In this regard, extraordinary administration has spearheaded some of the most important insolvency reforms in Italy.

Over time, extraordinary administration of large enterprises has shown many limitations and shortcomings. As discussed in the previous section, the special insolvency regime for large enterprises appears to be costly and have a poorly defined scope by covering medium-sized enterprises and all economic sectors, regardless of the strategic importance of the enterprises in question. The procedure assigns all the power to the public administration, and creditors are forced to be passive, with limited access to courts' protection. The procedure serves today as a shock-absorber, since it practically guarantees the continuity of the enterprise and the maintenance of jobs, at least temporarily, and thereby defusing the social tension in highly visible cases. However, the continuation of enterprises lacks a strict analysis of viability. By contrast, as the general insolvency regime continues to evolve, including not least after the October 2017 enabling reform, it offers a more balanced approach to the resolution of enterprise distress, including the possibility of continuing the business activity and restructuring business operations.[63]

Despite the initiatives of the MED to increase transparency of the process, there are still areas for future improvements. The MED has implemented a transparency plan, aimed at addressing governance considerations, based on clear and improved rules for the appointment

[62] In particular, the successive reforms of the composition procedure (*concordato preventivo*) have provided ample options for the reorganization of enterprises and the preservation of going concern value (see Garrido, J., 2016).

[63] The enabling legislation of October 2017 needs to be followed through with legislative decrees no later than end-2018 for the reform to be effective.

and remuneration of extraordinary commissioners.[64] The reform of remuneration was also important since a frequent criticism against extraordinary administration has been the high fees that extraordinary commissioners collect.[65] Nonetheless, market participants have expressed concerns that, in high-profile cases, it would appear that some fundamental decisions are not based on economic analysis, but rather on political considerations and the alignment with the objectives of the government. A key element that could meaningfully improve transparency is information about credit recovery in extraordinary administration cases. This would evidence the extent to which private creditors suffer the consequences of a policy of which aims at continuing the activity of a bankrupt enterprise. Such data would also allow for a more complete assessment of the efficiency of the procedure.[66]

There have been attempts at reforming the extraordinary administration regime but they do not overhaul the system. Different attempts have sought to unify the two procedures by eliminating the differences between the Marzano and the Prodi-bis proceedings.[67] One of the recent proposals sought to expand the scope of the extraordinary administration regime by lowering the thresholds for admission and sought also to eliminate the judicial phase of the proceedings. [68] The Rordorf commission, setup in 2015 to rationalize and simplify the insolvency framework, suggested to raise the quantitative thresholds for the special regime, in order to avoid its application to medium-sized businesses[69], and approximate the special procedures to the general insolvency regime, but still maintaining a differentiated treatment for very large enterprises[70], listed companies and providers of essential public services. However, the Rordorf proposal preserves many of the structural characteristics and inefficiencies of the current regime. Other proposals have sought to make the application of the special regime conditional on a determination of the strategic nature of the enterprise. However, this suggestion has been met with skepticism given the potential for political discretion and abuse. Currently, there is no legislative text that addresses the fundamental problems raised by this special regime.

Consideration should be given to folding the extraordinary administration regime into the general insolvency regime. This implies repealing the special regime or at least aligning it as much as possible to the general insolvency regime. In particular, since 2016, the

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[64] See http://www.sviluppoeconomico.gov.it/images/stories/documenti/amministrazioni_straordinarie.pdf.

[65] The reform of the remuneration system places more importance in the variable element, based on the results of the extraordinary commissioner's actions (e.g., sale of the business and sale of other assets).

[66] See IMF (2016b) for the type of data necessary to assess the efficiency of insolvency systems.

[67] The first proposal to unify the regime of the extraordinary administration was made in 2008 (see draft delegated legislation, 2 October 2008).

[68] The legislative proposal (AC 865, so called "Abrignani proposal") only required that the enterprises have 200 workers, and 100 million euros in debt.

[69] The Rordorf-inspired proposal proposed to cover enterprises with at least 400 workers (or enterprise groups with at least 800 workers), together with a requirement of size expressed in turnover during the last three exercises. The final proposal in Parliament (AC 3671-ter) reduced the required number of workers to 250.

[70] In the proposal, very large enterprises are defined as those with at least 1,000 workers and a turnover to be specified as a multiple to the one required for the other enterprises.

improvements to *concordato preventivo* (reorganization) provide a modern framework for the reorganization of enterprises, equally suitable to the needs of large enterprises.[71]

- Most importantly, the insolvency of large enterprises should be subject to the control of the enterprise courts and creditors should have the power to decide the economic outcome of the process: liquidation, sale as a going concern, or reorganization of the enterprise.

- Other rules also need to be aligned with the general insolvency framework: the insolvency administrator should have the ability to renegotiate all contracts, including labor contracts, to achieve the restructuring of the enterprise. Secured creditors should not be subject to an indefinite stay of creditor actions and should be allowed to request the lifting of the stay when their interests are not adequately protected.

- It would be possible to maintain some special rules to protect public interest: for instance, the MED would be entitled to receive information and reports from the insolvency representative and could also have the role of selecting highly qualified insolvency professionals who would become part of a restricted list of potential insolvency administrators for large cases, to be appointed by courts following the generally applicable rules[72].

The flexibility of the general insolvency regime could allow the resolution of complex insolvency cases within a shorter time frame than the one envisaged in the extraordinary administration regime which would result in savings for private and public creditors together with better economic outcomes.

Measures to improve social safety nets and labor market flexibility would address more directly the concerns over potential job losses. For instance, improving active labor market policies, strengthening the social safety net, and aligning wages with productivity at the firm level would help alleviate the long spell of unemployment following a downturn while supporting demand and reallocation of labor toward more productive sectors and activities.

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[71] This regime would improve even more should the changes suggested by the Rordorf commission be adopted, in particular as they relate to the coordination of procedures for enterprise groups.

[72] The insolvency standard is flexible on the matter of the selection and appointment of insolvency representatives: "*The insolvency law should establish a mechanism for selection and appointment of an insolvency representative. Different approaches may be taken, including appointment by the court; by an independent appointing authority; on the basis of a recommendation by creditors or the creditor committee; by the debtor; or by operation of insolvency law, where the insolvency representative is a government or administrative agency or official*" (UNCITRAL, 2004, recommendation 118). In all cases, however, the insolvency representative should be independent and free from conflicts of interest.

Box 1. EU State Aid Rules and the Italian Special Insolvency Regime

The provision regulating state aid in the EU is codified under article 107(1) of the EU Treaty, "*any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favoring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market*". During insolvency, state aid can be particularly pernicious as it creates moral hazard and can distort competition.

The conditions to be satisfied for classifying a specific action as state aid are:

(a) the beneficiary of the aid is an entity that engages in an economic activity;
(b) the measure is financed by State resources and is imputable to the State;
(c) the measure confers an economic advantage;
(d) this economic advantage is selective;
(e) the measure distorts or threatens to distort competition and may affect trade between Member States.

The original Prodi law was subject to the scrutiny of the EC[1] and the ECJ. The analysis of the ECJ in the cases of Ecotrade[2] and Piaggio[3] concluded that the original design of the Prodi law was incompatible with the European rules on state aid. In particular, the analysis of the court in the Piaggio case concluded that: 1) the undertaking has been permitted to continue trading in circumstances in which it would not have been permitted to do so under the rules governing ordinary insolvency law, or 2) has enjoyed one or more advantages, such as a State guarantee, a reduced rate of tax, exemption from the obligation to pay fines and other pecuniary penalties or a *de facto* waiver of public debts wholly or in part, which could not have been claimed by another insolvent undertaking under the rules governing the ordinary insolvency law. The Commission's decision of May 16, 2000 also analyzed the distortions to competition created by the original Prodi law. As a result of the ECJ decision, the Prodi law was amended by removing the automatic admission into the procedure and the use of financial privileges.

However, the current model of extraordinary administration in the Prodi-bis and Marzano laws continues to provide opportunities for the provision of state aid. In fact, there are frequent decisions of the EC and judgments of the ECJ that refer to specific cases of extraordinary administration. Because of the connection between extraordinary administration and industrial policy, enterprises subject to the proceedings often receive special financial assistance through (bridge) loans or guarantees. If these financial transactions are conducted at more favorable conditions than prevailing in the market, they may constitute state aid and require the authorization of the EC.

The EC has a set of guidelines for the approval of state aid measures in favor of distressed companies.[4] The Communication from the Commission outlines the requirements for legal state aid: enterprises are eligible for state aid only when they have exhausted all market options and where the aid is necessary to achieve a well-defined objective of common interest. The state aid should help the enterprise return to viability, include burden-sharing, and contain distortions to competition. Note that there are less stringent conditions for liquidity assistance, especially for SMEs, and state aid to the steel and coal sector is excluded from the scope of the EC guidelines.

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[1] The Commission issued several decisions on aid schemes linked to extraordinary administration: see, e.g. Decision 96/434/EC, 20 March 1996; Decision 96/515/ECSC of 27 March 1996; Decision 97/754/ECSC of 30 April 1997.

[2] Ecotrade vs AFS (Case C-200/97, [1998] ECR 1-7907).

[3] Industrie Aeronautiche e Meccaniche Rinaldo Piaggio SpA and International Factors Italia SpA (Ifitalia), Dornier Luftfahrt GmbH, Ministero della Difesa (Case C-295/97, 17 June 1999).

[4] See Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty, OJ C 249, 31.7.2014.

Box 2. The Marzano Law Through the Parmalat and Alitalia Cases

The failure of Parmalat was at the origin of the Marzano law. Founded in 1961, the Parmalat Group became in 2003 the world's seventh largest food company. But in this same year, it was revealed that its subsidiaries' losses were disguised via deceptive accounting practices, leading to one of the most notorious financial scandals in Europe. Given the large undisclosed economic losses, the authorities took control of the group to rescue it and minimize the potential negative consequences on employment. However, instead of relying on the Prodi-bis law, the government decided to issue a decree-law to avoid the judicial observation phase given the uncertainty over the true state of Parmalat's financial standing. The government did not consider it appropriate to sell the Parmalat group, providing the Marzano law absolute preference to restructuring of the enterprise. In this way, Minister appointed immediately an extraordinary commissioner who started working on a restructuring plan. The restructuring program involved the creation of a foundation, acting as the sole shareholder of a new company, "new Parmalat", which included all assets and liabilities of the 16 companies admitted to the proceedings. The program was based on a composition with creditors who were compensated in full, either in cash or through shares in "new Parmalat". The company was ultimately acquired by the Lactalis group in 2011. The case is regarded as a success, as the liquidation of the company was avoided, although it is an atypical insolvency case given that the failure was due to fraud committed by directors.

The Alitalia failure introduced the option to sell a company undergoing a Marzano proceeding. Alitalia is the principal airline in Italy with a 49.9 percent participation of the state. The airline experienced substantial losses following stiff competition and rising fuel costs in 2007. When the state decided to improve the financial standing of the airline, the Marzano law was found inadequate, as it only foresaw a restructuring of the business when Alitalia required a quick sale to an investor group. The authorities introduced special amendments to the Marzano law which would apply to enterprises providing "essential public services" by enabling a sale at market price, maintaining public services, and providing a special regime for transfer of licenses and the agreement of the competition authorities. The extraordinary commissioner sold the profitable parts of the Alitalia business for 1.05 billion euros to CAI (Compagnia Aerea Italiana), a company created by several investors, which proceeded to merge with another company, Air One, in what became known as the "new Alitalia". The sale was criticized on several grounds, including for the cost that the taxpayers had to face, estimated at €4.1 billion (see Mediobanca, 2015). Despite these efforts, Alitalia resumed making losses and was put under extraordinary administration again in May 2017. It then received a bridge loan from the government for €600 million, increased by €300 million in October 2017.

Box 3. Wage Supplementation Mechanisms (Cassa Integrazione Guadagni)

Casa Integrazione Guadagni (CIG) is a wage supplementation fund which provides cash payments to workers following reduced working hours or redundancies. CIG is administered by the National Institute for Social Protection (INPS), under the management of the Ministry of Labor. Entitled workers receive 80 percent of their average gross earnings of the previous 3 months, reduced by 20 percent after the first year, with time limits and caps on the amounts paid linked to the type of fund used.

CIG comprises two funds: 1) an ordinary redundancy fund (CIGO) which applies to temporary events of macroeconomic nature, not attributable to employers or workers, providing wage supplements for a maximum period of 12 months in 2 years, with a limit of 3 consecutive months; and 2) an extraordinary redundancy fund (CIGS), relevant for extraordinary administration proceedings, which applies to longer periods of shutdown of production—initiated by the employer—following industrial reorganization, sectoral shocks, or insolvency proceedings with continuation of the business activity. CIGS applies to companies with more than 15 employees (50 in case of commercial businesses), and to employees with more than 90 days of prior employment, with a benefit limit of 3 years over a period of 5 years in case of bankruptcy. To be activated, CIGS requires the Ministry of Labor's authorization on a case-by-case basis following negotiations between firms and trade unions. CIGS was reformed in 2015 as part of the Jobs Act where, among other things, an overall maximum limit of CIGO and CIGS support was set at 24 months over a period of 5 years.[1]

CIGS is primarily employer funded. Contributions are directly linked to salaries and amount to 0.9 percent, of which 0.6 percent is remitted by the employer and 0.3 by the employee. In addition, an extra contribution from the employee applies when payment begins. The contribution increases with the duration of use of CIGS: 1) 9 percent, up to 52 weeks over a 5-year period; 2) 12 percent up to 104 weeks; and 3) 15 percent beyond the 104 weeks. When CIGS's funds are insufficient to compensate employees, the state steps in to supplement it with additional funds.

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[1] The Jobs Act cancelled the use of CIGS for firms that have ended or about to end production, allowing it to be used only in cases of reorganization or financial and economic difficulties. The 2016 inter-ministerial Decree No. 950575 delayed the activation of this provision until 2018, conditional on the existence of good prospects for a rapid sale of the company. On September 13, 2018, the Council of Ministers decided to extend further this provision until 2020 under the so-called "Emergency Decree".

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Summary Timeline and Outcomes of the Marzano Procedure

Name of the Group	Number of companies in the group	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Number of companies out of the procedure	Number of bankruptcies	Number of restructured companies	Number of Companies still in Administration as of 2016	Has a company in the group been sold	Number of employees at the start of the procedure	Number of transferred employees
PARMALAT S.p.A.	70																51		17	2	Yes	3,826	3,543
FINMEK ACCESS S.p.A.	16																			16	Yes	3,080	681
VOLARE GROUP S.p.A.	4																			4	Yes	1,185	707
C.I.T.	31																			31	Yes	535	363
CONSORZIO GAIA S.p.A.	9																			9	Yes	1,067	650
GRUPPO ALITALIA	5																			5	Yes	18,000	10,500
GRUPPO MERLONI	4																			4	Yes	3,084	1,446
GRUPPO ITTIERRE	15																			15	Yes	1,414	887
TRIBUTI ITALIA	6																			6	Yes	605	372
FIREMA	2																			2	Yes	832	407
TIRRENIA	2																			2	Yes	2,148	2,148
LIVINGSTON spa	1																			1	Yes	521	328
VALTUR	10																			10	Yes	590	85
GHIZZONI SPA	1																			1	No	776	200
LUCCHINI SPA	4																			4	Yes	3,003	2,600
PICFIC (IDI- San Carlo)	5																			2	Yes	1,370	1,334
IMPRESA S.p.A	2																			5	Yes	626	233
MANCINI	7																			7	Yes	695	330
CONGREGAZIONE ANCEKKE DELLA DIVINA PROVVIDENZA	1																			1	Yes	1,440	1,440
ILVA	10																			10	No	14,000	10,000
MERCATONE UNO	9																			6	No	3,300	
GRUPPO TOSONI	9																			9	No	590	
MAZAL AIPA	2																			2	Yes	456	97
ALITALIA SAI	2																			2	No	11,418	
TECNIS S.p.A	4																			4	No	557	
TOTAL	231																51		17	160		75,118	38,254

Source: Ministry of Economic Development. Green squares denote the business operation phase (from the opening of the parent's company insolvency procedire to the termination of the business activity of the last company). Red squares denote the liquidation phase.

Summary Timeline and Outcomes of the Prodi-bis Procedure

Name of the Group	Number of companies in the group	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Number of companies out of the procedure	Number of bankruptcies	Number of restructured companies	Number of Companies still in Administration as of 2016	Has a company in the group been sold	Number of employees at the start of the procedure	Number of transferred employees
BONGIOANNI	21																			5	2		14	Yes	720	370
FIORONI	8																						8	Yes	265	201
CALZIFICIO CARABELLI	1		Converted into bankruptcy																		1		0	Yes	278	68
TIBERGHIEN MAN. TESSILE	1																						1	Yes	272	120
CONFALONIERI F.LLI DI MARIO	4																					3	1	Yes	721	528
SCALA S.p.A.	1																						1	Yes	432	177
K&M INDUSTRIE METALM	1																						1	Yes	265	233
FLEXIDER	1																						1	Yes	378	245
ILVA PALI DALMINE	3																						3	Yes	227	114
GRANDE DISTRIBUZIONE AVANZATA	1																						1	Yes	609	150
SOCIETA' ITTICA EUROPEA	1																						1	Yes	241	201
OCEAN	1																						1	Yes	1141	900
ITEA	2																						2	Yes	600	177
COSTA FERROVIARIA	3																						3	Yes	237	130
MILANO STAMPA	2																						2	Yes	253	173
A T B spa	1																						1	Yes	265	218
FEDERICI STIRLING	4																						4	Yes	239	24
ELDO	7																						7	Yes	313	146
MANZONI GROUP S.P.A.	2																						2	Yes	553	331
IST. VIGILANZA PARTENOPEA	1																						1	Yes	400	170
CE.DIS	3																				2		1	Yes	865	225
MERKER	6																			2			4	Yes	393	166
COOPCOSTRUTTORI	5																						5	Yes	2050	385
CIRIO	14																			1			13	Yes	1055	928
TECNOSISTEMI	8																						8	Yes	1723	201
GIACOMELLI	8																						8	Yes	1690	196
CE.SA.ME.	1																						1	Yes	348	140
MINERVA AIRLINES S.p.A.	1						Converted into bankruptcy														1		0	No	210	0
ALGAT S.p.A.	1																						1	Yes	570	386
FERRANIA S.p.A.	1																						1	Yes	890	632
ARQUATI Gmgh	4																			1		3	0	Yes	300	300
GA.MA S.p.A.	1																						1	Yes	1047	1047
COMPUTER MANUFACTORING	6																					5	1	Yes	227	31
CARTIFICIO ERMOLLI	3																						3	Yes	420	320
OLCESE S.p.A.	2																						2	Yes	607	185
LARES COZZI	2																						2	Yes	221	142
FORMENTI SELECO	2																						2	Yes	536	75
TREND S.p.A.	1																						1	Yes	205	205
TECDIS S.p.A	2							Converted into bankruptcy													2		0	No	275	0
F.D.G. S.p.A	2																						2	Yes	274	260
SELFIN S.p.A	10																						10	Yes	1017	716
LAMIER S.p.A.	3																						3	Yes	354	238
IAR SILTAL S.p.A.	2																						2	Yes	1472	911
SANDRETTO INDUSTRIE S.r.l.	1																						1	Yes	379	250
LANIFICIO LUIGI BOTTO S.p.A.	3																						3	Yes	465	302
TECNO.A	5																						5	Yes	249	69
BBS RIVA	1																						1	Yes	354	206
RAUMER	6																						6	Yes	214	60

Name of the Group	Number of companies in the group	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Number of companies out of the procedure	Number of bankruptcies	Number of restructured companies	Number of Companies still in Administration as of 2016	Has a company in the group been sold	Number of employees at the start of the procedure	Number of transferred employees
ISTITUTO VIGILANZA DELL'URBE	1																						1	Yes	850	850
SOCIETA' EUROPOL GUARDIE	1																						1	Yes	258	160
GRUPPO FILATURA DI GRIGNASCO	3																						3	Yes	393	60
ROMAGNA RUOTE	1																						1	Yes	208	85
GRUPPO CARROZZERIA BERTONE	2																						2	Yes	1100	1100
GRUPPO TOORA	2																						2	Yes	307	105
GRUPPO GBS GROUP	4																						4	Yes	257	150
GRUPPO ALPI EAGLES	1										Converted into bankruptcy										1		0	No	226	0
GRUPPO MAHA	1																						1	Yes	376	14
TEXFER già LEGLER	4											Converted into bankruptcy									4		0	No	1022	0
ASTIGIANA AMMORTIZZATORI	1										Converted into bankruptcy										1		0	No	241	0
AGES S.P.A.	2																						2	Yes	639	230
LINEAPIU' S.p.A.	2																						2	Yes	287	170
SOGESTER ITALIANA s.r.l.	2											Converted into bankruptcy									2		0	No	241	0
GRUPPO SNIA/CAFFARO	6																						3	Yes	373	179
AVICOLA MARCHIGIANA	1																						1	Yes	752	527
ATR	10														Converted into bankruptcy					10		0	Yes	661	188
CABLELETTRA S.p.A.	1																						1	Yes	312	123
IAL CISL PIEMONTE	2																						2	Yes	244	145
GRUPPO MAFLOW	3																						3	Yes	2239	1942
VYNILS	1														Converted into bankruptcy					1		0	Yes	425	37
ACMS	1														Converted into bankruptcy					1		0	No	506	0
CEIAS	4													Converted into bankruptcy						4		0	No	1239	0
ILMAS	3																						3	Yes	285	125
ZEN	5																						5	Yes	207	150
AMIA S.p.A.	2														Converted into bankruptcy					2		2	No	1940	0
MARIELLA BURANI	2														Converted into bankruptcy					2		0	No	180	0
CONSORZIO AZIENDA SERVIZI AMBIENTE	2																						2	No	350	127
SATURNO	3												Converted into bankruptcy							3		0	No	478	
EDILIBRO-BOCCATO	1																						1	Yes	205	10
AGILE	1																						1	Yes	1,498	184
EUTELIA	1																						1	Yes	406	266
LIRI INDUSTRIALE	1																						1	Yes	296	120
OMICRONS	1																						1	Yes	368	7
PIETRO MAZZONI AMBIENTE	1													Converted into bankruptcy						1		0	No	414	0
FADALTI	1																						1	Yes	287	125
MERAKLON	2																						2	Yes	228	90

Name of the Group	Number of companies in the group																			Number of companies out of the procedure	Number of bankruptcies	Number of restructured companies	Number of Companies still in Administration as of 2016	Has a company in the group been sold	Number of employees at the start of the procedure	Number of transferred employees
		2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017							
DEFENDINI	4																						4	Yes	244	49
SACAIM	2																						2	Yes	376	120
CEFOP	1																						1	Yes	1,017	650
GDM	1																						1	Yes	620	177
Pansac	2																						2	Yes	741	269
ACQUE POTABILI SICILIANE	1														Converted into bankruptcy						1		0	No	204	0
Form	1																						1	Yes	738	652
Migliore	4														Converted into bankruptcy						4		0	Yes	273	90
RDB	3																Converted into bankruptcy				3		3	Yes	676	45
Stefan srl	2																						2	Yes	288	35
Acc Compressors	2																						2	Yes	624	480
Franco Tosi Meccanica	1																						1	Yes	397	180
Gallazzi	1																						1	Yes	417	210
CSTP	1																						1	No	568	568
Opera21	1																						1	Yes	448	165
North East Services spa	5																						4	Yes	877	228
Bernardi Group	2																						2	Yes	322	80
Mabo prefabbricati	6																						5	Yes	395	45
Officine Ferroviarie Veronesi	1																						1	No	201	20
Blue Panorama	2																						2	Yes	400	400
Abbigliamento Grosseto	1																	Converted into bankruptcy			1		1	No	222	222
Geo Ambiente	1																	Converted into bankruptcy			1		1	No	250	0
Auselda Group	1																						1	Yes	290	152
Villa Tiberia	1																						1	No	234	234
Infocontact	2																						1	Yes	1,800	1490
Isotta Fraschini	8																						8	No	649	24
IMT	6																						1	No	586	152
La Ronda	1																						1	No	294	294
De Roma	6																						6	No	629	
SS71	1																						1	No	270	
TB Holding	1																						1	No	251	
Città Roma Metronotte	1																						1	No	629	
Sipro Sicurezza Professionale	1																						1	No	620	
Linkra Srl in Liquidazione	2																						2	No	308	
Artoni Trasporti S.p.A	1																						1	No	434	
TOTAL	329																			9	50	11	255		64409	27552

Source: Ministry of Economic Development. Green squares denote the business operation phase (from the opening of the parent's company insolvency procedire to the termination of the business activity of the last company).
Red squares denote the liquidation phase.