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LEGAL INFORMATIVE NEWSLETTER

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We are pleased to provide you with the new issue of our legal information newsletter.

Topical legal questions are discussed and those related to issues that you might encounter.

We hope that you will find it of interest. We would welcome any comment you might have.

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**OVERVIEW OF THE MAIN CLASSES OF DOMESTIC SHARE CAPITAL AND DEBT SECURITIES IN CORPORATIONS, THEIR ISSUANCE, REDUCTION AND ACQUISITION**

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**Introduction** - Since 2004, Italy has enacted new rules for company formation, start up, organization and administration. This reform trend introduced simplifications and greater flexibility for corporate decision-making.

The key element of the overall reform is self-regulation, which allows companies vast powers to establish specific rules in their By-Laws and Articles of incorporation, without too many strict, pre-defined mandatory requirements.

Other examples of flexibility can be found in the many financial tools available as well as in the different corporate governance forms.

Changes to the structure of limited companies which simplify and speed up the procedures for establishing a business were introduced, as well as new financial instruments for companies to create special categories of shares and new rules providing greater flexibility and choice in corporate governance.

Here in this article, we provide some general information about the domestic regulations on share/quota capital and debt securities of corporation and limited liability companies.

**Stock shares in Corporations** - Corporations are generally authorized according to their By-Laws to issue different classes of stock, which may differ in their right to dividends, their voting rights and their right to share.

Issuance of no par value shares is now allowed in Italy. Shares may be linked to a fraction of the stated capital, as well as it is possible for Limited liability companies. The only requirement is to make express reference about it in the By-Laws.

Nominal shares are transferable upon authenticated signature. Bearer shares are transferred with delivery of the certificate. Power to exercise corporate rights is transferred upon signature. If the share transfer is conditioned to the acceptance by either the other shareholders or the Board of Directors, By-Laws shall provide that in case such acceptance is denied:

[A] The company and/or its shareholders undertake to purchase the share; or

[B] The seller has a right to withdraw at expense of the company and/or its shareholders.

In order to be enforceable stock transfer restrictions must be mentioned on the stock certificate.

Issuance of redeemable shares is now permitted. Redeemable shares may be of relevant interest in case participation to the stock capital is connected to determined relationship from outside the company.

In case of assignment of shares, the transferor is jointly and severally liable with the transferee for a period of three years from the date of the transfer for payments still due on the shares.

**Principal classes of shares** - The following are the principal classes of shares:

[A] Common Stock – Full voting rights, save for those shares issued for specific corporate business activities

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[B] Stock having different rights – Upon specific mention in the By-Laws it is possible to create categories of stock having different rights even with reference to a predetermined and eventual level of losses

[C] Stock and other instruments to the benefit of employees – The extraordinary general meeting has the power to determine assignments, rules, rights, eventual expiration terms and faculty of repurchase

[D] Non-voting Stock – They have no voting rights. Such shares may be only issued by companies whose shares are traded on the Stock exchange for an amount of stock capital not greater than 51%.

[E] Stock of participation to a determined business – Financial instrument of participation, whose rights must be specifically predetermined.

A corporation may authorize – not more than 51% of stock capital – specific stock without voting rights, with restricted voting rights, with limited or subordinated voting rights.

Stock to the benefit of employees or issued pursuant to services or work contribution by shareholders or third parties may carry the right to vote on specific arguments of particular interest for the rights of the stock itself and a member of the controlling board may represent them.

The mandatory deposit with consequent prohibition of withdrawal of the shares for a corporate meeting has been eliminated.

**Shares representing assets dedicated to specific businesses** - Corporations may dedicate and link the result of a portion of the stock, not more than 10% of the stock capital, to the results of a determined area of business (with the exclusion of the business regarding activities with a reserved statutory regulation).

To that extent, a corporation may:

[A] Set up one or more assets specifically dedicated to the realization of a specific business (a single business or an entire business activity to be carried out along with the main business activity of the company).

[B] Establish that financial resources necessary for carrying on the activity have to come from the specific business itself

The purpose of this regulation is allowing to split management and result of different

activities and businesses each one valuable independently.

Possible purposes are:

[A] Disposition of assets – Setting up of a separate corporate entity internal to the company, without need of coping with rules and regulations of the Civil Code applicable to de-merge of companies, therefore without bearing related costs (i.e. investment of corporate equity in financial speculations aimed at risk diversification). By previous mention in the Bylaws of the criteria for calculation of outcome and income for the specific business, the issuance of stock directly linked to results of the specific business is permitted.

[B] New contributions and need of new resources for developing a new project – A separate accounting for the specific business activity is mandatory (Contributors may decide on the basis of the substance and the content of the single project or operation)

A specific resolution of the Shareholders Meeting is necessary in order to bind some assets to a specific business. The meeting shall determine:

[1] The object of the business

[2] Assets involved

[3] Financial and economical business plan (in order to determine congruity, criteria of management, expected result, guaranties etc.)

[4] Contributions specifically undertaken and financial instruments issued for the operation

[5] Appointment of an auditing company in case the corporation issues equity securities publicly traded and offered to non professional investors

[6] Rules of accounting of the specific business.

The resolution must be filed with the Companies Registry. Actual creditors may file an opposition within two months from the filing.

**Debt Securities** - Corporations are allowed to issue debt securities offered to the market for subscription. The decision to issue debt securities as a financial instrument, may be led by the:

[A] Preference of raising financial resources without granting new subjects the right to vote and without altering corporate control

[B] Necessity of financing projects or operations, which just need a temporary financing

[C] Circumstance that the purchase of equity stock is not a sounding investment during a particular period of time

Issuance of equity security instead may sound convenient for raising permanent resources, acquiring new resources without paying additional financial costs, or financing the stock capital without being subject to statutory limitations provided for the issuance of debt securities.

Unless otherwise provided by either the certificate of incorporation or the bylaws, the Board of Directors may adopt the resolution for issuance of debt securities. The extraordinary general meeting may vote for issuance of convertible bonds. To be enforceable, the resolution of issuance must be entered in the minutes of the meeting and must be filed in accordance with the regulation established for By-Laws amendments.

The threshold for debt issuance has now been raised to an amount equal to the double of the stock capital, of the legal reserve and of the available reserves as they result on the last approved balance sheet. It would seem possible to make reference to the subscribed stock capital and not to the stock capital paid in, since the law says nothing in respect.

The following situations are not subject to the above limitations:

[A] Bonds issued in excess that are subscribed by professional investors subject to prudential control in accordance with specific regulations and that are traded among non-professional purchasers (situation where bond subscribers are liable for the solvency of the company).

[B] Bonds backed by first mortgage over real estate owned by the company up to 2/3 of their value

[C] Authorization by governmental authority.

Rules and regulations concerning convertible bonds has not changed (extraordinary General Meeting + stated capital increase for an amount equal to the shares to issue in conversion). Stated capital must be entirely paid in.

**Reduction of Share Capital** – It may be effected, depending on the specific circumstances, as follows:

[A] Reduction of capital in excess – A reduction can be effected either by releasing shareholders from the obligation of making payments still due, or by reimbursing capital to the shareholders, within the following limits:

[1] Maintenance of the minimum share capital required for Corporations of € 120,000

[2] Maintenance of an aggregate amount not exceeding twice the stock capital, the legal reserve and the available reserves appearing from the last balance sheet approved in case the company has issued and outstanding debt securities.

This latter limits does not apply in case of issue of debt securities made by companies listed on regulated markets or guaranteed by a mortgage of first degree on real estate owned by the company, up to two thirds of the value of the real estate.

[B] Reduction of capital pursuant to losses – When the capital of the company has diminished by more than one third as a result of losses, the directors or the management committee, or failing them to do so, the Board of Auditors or the Supervisory Board, shall call the Meeting without delay to take appropriate action. A report on the financial condition together with the remarks by the Board of Auditors or the Management Supervisory Committee. The report and remarks shall be filed at the registered office of the company at least eight days prior to the date of the Meeting. At the Meeting, the directors must report on the eventual relevant facts occurred after drafting their report.

If the loss is not reduced to less than one third within the subsequent fiscal year, the Meeting or the Supervisory Board that approves the annual accounts, shall reduce the capital in proportion to the losses. Failing this, directors, auditors or the Supervisory Board shall petition the Tribunal to provide for a reduction of capital to that extent.

In the event that the shares issued by the company are without par value, the By-Laws, an amendment to the By-Laws or a resolution adopted with the majority requested for the extraordinary resolutions may provide that the reduction of capital be resolved by the Board of Directors.

[C] Reduction of capital below legal minimum threshold – If, due to the loss of over one-third of the capital, capital falls below the legal minimum of € 120,000, the directors or the Management Board, and failing them, the Supervisory Board shall without delay call the Meeting to decide on either the reduction of the capital and the concurrent increase thereof to an amount not less than the said minimum or the conversion on the company into another corporate structure.

**Purchase of own shares** - A company cannot purchase its own shares except to the extent of the profits available for distribution and of available reserves, as evidenced in the last balance sheet approved. Only shares that have been fully paid up can be purchased.

A purchase of own shares must be authorized by the Shareholders Meeting. The Meeting must set out procedure for the purchase, indicating maximum amount of shares to be purchased, the period of time not exceeding eighteen months, for which the authorization is granted, the minimum and maximum price.

Under no circumstances, can the par value of the shares purchased exceed one-tenth of the stock capital, taking into account to this extent the shares owned by eventual subsidiaries as well.

Shares purchased in violation of the above requirements must be sold within one year from their purchase. Failing this, action must be taken without delay for their cancellation and a corresponding reduction of the stock capital. If the Meeting fails to take such action, the directors and the auditors must file a motion to that purpose with the Court.

These mandatory requirements apply as well in case of purchases made through a fiduciary company or an intermediary.

There are some exceptions. The above limitations do not apply when the purchase of its own shares occurs:

[A] By implementation of a resolution by the Shareholders Meeting to reduce the capital, to be effected by way of redemption and cancellation of shares

[B] On a gratuitous basis, as long as the shares are fully paid up

[C] As a result of inheritance or a merger or demerger

[D] In connection with the enforcement of a debt collection, as long as the shares are fully paid up.

If the nominal value of the shares so purchased exceeds the limit of one-tenth of the capital, shares in excess must be sold within three year from the purchase.

Directors may not dispose of the company's own shares acquired without prior authorization by the Shareholders Meeting.

As long as the shares are owned by the company, the rights to profits and options are attributed in proportion with the other shares. The Shareholders Meeting may authorize the exercise of the option rights in part or in full. The voting rights are suspended, but the shares owned by the company are nevertheless computed in the stock capital for calculating the quorums and majorities for the resolutions by the Meeting.

Save for the eventual option rights above described, the company cannot subscribe to its own shares. As well, the company cannot:

[1] Grant loans or give guarantees for the purchase of or subscription to its own shares

[2] Accept its own shares as security, even through a fiduciary company or an intermediary. Such latter restriction does not apply to transactions effected to facilitate the purchase of shares by employees of the company or of its controlling or controlled companies. However, in these cases the sums invested and the guarantees granted have to be kept within the limits of the distributable profits and the available reserves evidenced in the last balance sheet.

**Acquisition of shares or quotas by controlled companies** - A controlled company cannot acquire shares or quotas of the controlling company except to the extent of the distributable profits and available reserves evidenced in the last balance sheet. Just shares that have been fully paid up can be purchased and the purchase must be authorized by the Shareholders Meeting.

Under no circumstance, the nominal value of the shares or quota purchased may exceed one-tenth of the capital of the controlling company, taking into account the shares and quotas owned by the

same controlling company and by the companies controlled by it.

A reserve equal to the amount of shares or quotas of the controlled company must be instituted and maintained up to the transfer of the shares or quotas.

A company controlled by another company cannot exercise voting rights in the controlling company.

Same provisions apply in case of purchases made through a fiduciary company or an intermediary.

The shares or quotas purchased in violation of the above described provisions must be sold within one year from their purchase.

Without doing so, the controlling company has to annul them promptly and proceed with the corresponding capital reduction with reimbursement. Failing to do so by its Shareholders Meeting, the directors and auditors must file a motion to that extent with the Court.

The above limitations do not apply when the purchase of the shares or quotas occurs:

[A] By implementation of a resolution by the Shareholders Meeting to reduce the capital, to be effected by way of redemption and cancellation of shares

[B] On a gratuitous basis, as long as the shares are fully paid up

[C] As a result of inheritance or a merger or de-merger

[D] In connection with the enforcement of a debt collection, as long as the shares are fully paid up.

If the nominal value of the shares or quotas so purchased exceeds the limit of one-tenth of the capital, shares in excess must be sold within three year from the purchase.

If the value in excess of the shares or quotas so purchased is originated by supervised circumstances, the controlling company has to annul them and proceed with the corresponding capital reduction with reimbursement within three years from their purchase. Failing to do so by its Shareholders Meeting, the directors and auditors must file a motion to that extent with the Court.

The controlled company cannot underwrite shares or quotas of the controlling company. The shares or quotas underwritten in violation of this provision of law, are deemed underwritten and must be released.

Whoever subscribes in her/his own name but on behalf of the controlled company shares or quotas of the controlling company is deemed to have acted on his own behalf. Unless they prove to have acted without negligence, directors of the controlled company are jointly liable for the release of the shares or quotas.

### **Prohibition of mutual subscription of shares -**

Companies are prevented from forming or increasing their own capital by means of mutual subscription of shares, even through a fiduciary or an intermediary.

### **Stock quotas in Limited liability Companies -**

Contributions by members of limited liability companies cannot be represented by shares, nor they can be publicly traded. If the Articles of incorporation do not provide differently, participation of the members is determined in proportion with the contribution. The Articles of incorporation may provide for granting to single members of special rights relating to the management of the company or the distribution of profit.

Transfer of quotas can be effected by acts inter vivos and by succession at death, unless otherwise provided in the Articles of incorporation. If the Articles of incorporation provide for non-transferability of the quotas or conditions such transfer to the agreement of the corporate bodies, without specifying the conditions and limits, the quota-holder or her/his heir may withdraw from the company. The articles of incorporation may provide for a term no longer than two years from the incorporation of the company before a quota-holder may exercise such right of withdrawal.

In case of assignment of a quota, the transferor is jointly and severally liable with the transferee for a period of three years from the date of the transfer for payments still due on the quota.

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