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The new "Growth Decree": another set of new opportunities for Project Bonds in Italy

On 15 June 2012, the Council of Ministers approved a set of urgent measures to implement part of the so-called "Agenda for sustainable Growth" (the "**Decree**"). The Decree addresses the need to foster competitiveness of Italian enterprise, to increase demand and to stimulate business growth. Among the new initiatives of the Decrees are the following: (i) to increase opportunities for Italian non-listed companies to access the capital markets (for example by introducing the so-called "mini bonds") and (ii) to increase investments in infrastructure generally and project bonds.

This client briefing focuses on project bonds, while our separate client briefing discusses the other measures to expand access to capital markets.

For the sake of clarity, Italian Project Bonds are a separate (but not incompatible) instrument from the so-called European Project Bonds currently being studied and introduced in the context of the Project Bond Initiative. European Project Bonds are meant to address a similar (although not identical) European need to create forms of financing for public infrastructure projects that will attract private capital, so as to meet the financing requirements for the European infrastructure investments to be made in the context of the Europe 2020 Strategy (currently estimated to require approximately Euro 1,500-2,000 billion) and are actually security and credit enhancement mechanisms provided by the European Investment Bank (within a risk sharing system between European Investmenet Bank and the EU Commission) in relation to notes issued by project companies that implement infrastructure projects in the energy, telecommunication and transport sectors, in the context of the Connecting Europe Facility. Please note that the final version of the Decree has not been published yet and therefore such Decree remains subject to amendments also by virtue of relevant implementing law.

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Similarly to the objective of the measures already included in Decree Law No. 201 of 6 December 2011 (the "**Salva Italia Decree**") and Decree Law No. 1 of 24 January 2012 (the "**Liberalizzazioni Decree**", and along with the "Salva Italia Decree", the "**Monti Decrees**"), the main objective of the measures of the Decree is that of accelerating construction of infrastructure, already behind schedule in Italy, to attract private capital to finance infrastructure projects and to simplify the investment process. The Decree, on the one hand, varies the fiscal regime applicable to notes and other debt securities issued by project companies (the "**Project Bonds**") pursuant to Art. 157 of Legislative Decree No. 163 of 12 April 2006 (the so-called "**Building Code**") and their underlying guarantees, and on the other hand allows the issue of Project Bonds also to refinance pre-existing debt already incurred by project companies that are in the process of implementing infrastructure projects.

Project Bonds generally

Through the Monti Decrees, the Monti government had already significantly amended the Building Code, reforming Art. 157 to promote private investments in the field of infrastructure. More precisely, the Monti Decrees introduced the following:

(i) expansion of the category of issuers

In its prior wording, Art. 157 of the Building Code allowed the issue of Project Bonds exclusively by the companies set out in Art. 156 of the Building Code (which is to say joint stock or limited responsibility companies that had been awarded a concession to create or to manage an infrastructure project or public service) and companies that had entered into public-private partnership contracts under Art. 3, para. 15-ter of the Building Code.

The Monti Decrees now allow also the following companies to issue Project Bonds: (i) those authorised to construct infrastructures for the transport of gas, (ii) those authorised to store and deposit of gas and (iii) those authorised to construct infrastructure projects in the context of the plan to develop the national electric grid.

(ii) removal of the limits under the Civil Code to the issue of Project Bonds

The Monti Decrees further (i) removed the obligation that Project Bonds be secured by mortgages, as was required under the previous legislation and (ii) allowed, in the context of an issue of Project Bonds, the non-application of the limits set out in Article 2412 of the Civil Code applicable to bonds generally. Similarly, the Monti Decrees allow the non-application of several other provisions of the Civil Code affecting the issue of notes by joint stock companies (e.g., on the meeting of the noteholders, on the common representative of the noteholders etc.).

(iii) investment in Project Bonds by insurance firms

The Monti Decrees provided that firms authorised to offer private insurance services can own, as part of their technical reserves, assets such as Project Bonds issued by companies authorised to construct and to manage road, railroad, port, airport, medical, and telecommunication infrastructures as well as infrastructures for the production and transport of energy and energy sources, within certain limits and subject to the terms and conditions to be set out in ISVAP regulations. For this purpose, on 17 May 2012 ISVAP started a public consultation procedure, which ended on 16 June 2012.

(iv) guarantees for Project Bonds

By express provision, until such time when the infrastructure begins to be managed by the concession holder, Project Bonds can be guaranteed by the financial system, by foundations and by private funds, on terms and conditions to be defined by a decree of the Minister of the Economy and Finance in agreement with the Minister of Infrastructure and Transportation, which decree has not yet been issued as of the date hereof (the "**Guarantees**").

Notwithstanding the breadth of the amendments under the Monti Decrees, the government had not yet addressed a crucial issue for the success of Project Bonds: i.e., the applicable tax regime. With the Decree, the government has expressly governed this tax aspect, providing a new and novel regime.

New tax regime applicable to Project Bonds and to the Guarantees

The Decree provides for the following:

- the withholding tax on the interest received will be same as that currently applicable to government bonds; therefore, interest paid to investors resident in Italy will be subject to withholding tax (*imposta sostitutiva*) of 12.5% while interest paid to investors resident in countries with which Italy has an adequate exchange of information will be exempt from withholding tax;[1]
- remuneration paid to the investor will be deductible by the issuer without the restrictions that limit deductions of interest arising from notes issued by non-listed companies (also to be amended by the Decree); therefore, the interest paid by the issuer of the Project Bonds will be deductible similarly to interest paid on bank financing (i.e., up to 30% of EBITDA, as shown in the most recently approved financial statements);
- security of any type, from any type of guarantor (and therefore the Guarantees), given at any time in relation to the notes will be subject to a fixed stamp, mortgage and cadastral duty of Euro 168, rather than the ordinary indirect ad valorem taxes on security; this favourable regime also applies to transactions for subrogation, subordination, splits and cancellations affecting the infrastructure financed with the Project Bonds.

Refinancing

The Provisions also create an interesting new alternative, by allowing the issue of Project Bonds also to refinance existing debt before maturity, thus allowing placement of Project Bonds on the market before the project is completed and begins operations.

Conclusions

The current legislative framework applicable to Italian Project Bonds still gives rise to several issues and controversial interpretations, which must be addressed in the short term: for example, to mention a few regarding the Guarantees, the issue of the compatibility of the proposed "Solvency II" directive, of the creation of instruments for ring fencing of assets, the amendment and waivers upon a default of the issuer of the Project Bonds, and of credit monitoring. We believe that the amendments set out in the Decree are a positive response to the needs of the market, making Project Bonds attractive to both Italian and foreign investors; as such these amendments are significant progress towards the successful outcome of those initiatives that were promoted, started and that are now underway as a result of the government's vigorous efforts and of the Monti Decrees.

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[1] Project Bonds can be subscribed for only by qualified investors, as defined in Art. 34-ter, paragraph 1(b) of CONSOB Regulation 11971/98, as amended.