Italy

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1. Evaluation of the company/determination of the purchase price

The parties to a contract for the acquisition of an Italian private company or going concern are free to negotiate and determine the price to be paid by the purchaser.

With regard to evaluation methodologies, in addition to the discounted cash-flow methodology, a fairly common valuation methodology is to use comparable transaction multiples. With comparable transaction multiples, the parties select some of the key transactions that have taken place in the sector in which the target operates within a specified period. They then apply the resulting multiples to the valuation of the target company. The various methodologies can be applied on their own or jointly for the purpose of determining the purchase price.

In general terms, the following additional elements can be taken into account in the determination of the purchase price:

- The acquisition of control of a company may determine an increase in the purchase price (the so-called 'control premium');
- The acquisition of a minority stakeholding may trigger a discount; and
- The results of the due diligence exercise may have an impact on the determination of the purchase price.

2. Structuring the acquisition

Decisions regarding the structure of the acquisition are based upon a number of elements, including those outlined below.

2.1 Asset or share sale

An acquisition in Italy can be carried out either by purchasing the shares of the target company or by purchasing the relevant going concern (or branch of the going concern). The same rules apply to the sale of a going concern or a branch of a going concern. This chapter does not deal with the sale of single assets; nor does it consider the acquisition of a shareholding in an Italian company carried out through the subscription of its corporate capital.

The choice between an asset deal and a share deal will depend on a number of factors, including tax evaluations (see Section 2.2 below).

In particular, the following main elements are taken into account by the purchaser and the vendor in deciding whether the acquisition will be a share deal or an asset deal.

(a) Sale of shares

By purchasing shares of an Italian company, the purchaser indirectly acquires all the company's assets and liabilities since these continue to belong to the company even where control over the company changes, except for those assets and liabilities (within permitted limits) which the parties decide to spin off from the target or to extinguish prior to completion of the sale. The risk of the existence of unknown or undisclosed liabilities is generally mitigated by inserting in the sale and purchase agreement representations and warranties concerning the target and its business, given by the vendor to the purchaser. Any violation of the representations and warranties is secured by the inclusion of indemnities in the sale and purchase agreement.

Contracts also continue after completion of the sale, save for those subject to change of control provisions.

The treatment of employment issues is also an evaluation issue (see Section 4 below).

With regards to tax, the target company retains all tax liabilities.

(b) Sale of a going concern

As regards the sale of a going concern, the assets, contracts (other than those with a 'personal' rationale) and liabilities of the going concern are transferred to the purchaser by execution of the notarial deed of transfer, unless the parties state otherwise in the deed. In particular, the counterparties to a transferred contract may withdraw for just cause from the contract within three months of receipt of the notice of transfer. With regard to the transferred liabilities, the vendor will remain jointly liable with the purchaser for debts incurred before the transfer took place, unless the creditors consented to the vendor's release. On the contrary, the purchaser is jointly liable with the vendor for debts remaining with the vendor resulting from the mandatory accounting books and pertaining to the going concern being sold.

The treatment of employment issues is also an evaluation element (see Section 4 below).

With regard to tax, the purchaser is jointly liable with the vendor for:

- any tax and/or penalties relating to tax underpayments and infringements occurring in the year in which the transfer occurs, even if not yet challenged at the time of the transfer; and
- all outstanding disputes arising during this period, even if relating to previous years' infringements of tax law. The law provides a procedure aimed at mitigating the liability of the purchaser.

2.2 Tax

In the case of both a transfer of shares and a transfer of a going concern, capital gains tax is charged on the vendor. In particular, capital gains are subject to ordinary taxation consisting of both IRES (corporate national tax of 33%) and, in certain cases, IRAP (regional tax of 4.25%, which may be increased by up to 1% on a regional basis).

The transfer of shares is subject to stamp duty equal to 0.14% of the purchase price. In addition, contracts concerning the transfer of shares filed with the relevant registration office are subject to a flat registration tax, presently set at €168 irrespective of the price of the shares.

The transfer of a going concern is subject to a registration tax of 3% on the value of the net assets. In certain cases, other rates apply. In particular, where real estate is involved in the going concern to be sold, the registration tax rate is increased and certain other taxes might also apply.

2.3 Financing

If the purchaser is unable to self-finance the acquisition, it can be financed by way of loans or other forms of debenture provided by banks or other financial institutions, or by the issue of bonds by the purchaser (or other companies within its group).

Under Italian law, it is illegal for the target company to finance the acquisition of its own shares by a third party. In particular, the target company cannot grant loans or guarantees over its assets for the purpose of financing the acquisition or subscription of its own shares. The target cannot accept its own shares as security, even through a fiduciary company or an intermediary. Any breach of this rule is regarded as financial assistance and, as a consequence, the loan or the security is null and void. These restrictions also apply to the provision of financial assistance by a subsidiary of the target company in connection with the acquisition of shares in the target.

There are no exceptions to the prohibition on financial assistance, other than in relation to financial assistance given to employees of the target company (or its subsidiaries) in the finance of stock option plans.

2.4 Structure of consideration

Lawyers have identified and implemented a wide range of formulae in order to structure the purchase price. Our assumption here is that the purchase price is paid in cash.

In general terms, the purchase price can be either fixed or variable. The purchase price is variable when its determination is based on parameters such as the working capital, net worth, net profits or turnover of the target company or going concern. The variable purchase price is determined by the parties as at a certain date (the reference date) and is subject to adjustment to account for the variation of the parameters in the period between the reference date and the completion date.

The adjustment is generally made after completion of the acquisition. In particular, it can be in favour of either the vendor or the purchaser.

In addition, the parties can agree that part of the purchase price be paid by the purchaser after completion of the acquisition (ie, a deferred purchase price). Where the purchase price is deferred in this way, the purchaser will normally be required to guarantee the payment of the deferred part of the purchase price. The most common means of guarantee include irrevocable letters of credit, first demand guarantees and escrow deposits.

3. Pre-contract

After (or simultaneously with) the preliminary steps described above, but prior to the execution of the sale and purchase agreement, the parties will normally exchange a number of documents, each of which deals with a specific aspect of the transaction. The parties to the acquisition will not necessarily enter into every one of the contracts described below (eg, the heads of agreement may contain an exclusivity clause rather than the parties entering into an exclusivity contract).

3.1 Exclusivity agreements

By entering into the exclusivity agreement, the bound party undertakes to negotiate exclusively with the other for a specified period of time and in connection with a specified transaction. In the majority of cases exclusivity is granted by the vendor in favour of the purchaser. In fact, without exclusivity it would not be worth a potential purchaser investing time and resources in the proposed transaction. The length of the exclusivity period depends on the complexity of the transaction.

Italian law does not provide for a specific regulation concerning the exclusivity agreement as such. Rather, it treats the issue within the regulation of agency and supply agreements.

The most important issue for the party granting exclusivity is the ability to terminate the agreement if expectations are not met. For the party receiving exclusivity, a key issue is making sure that the scope of the exclusivity is sufficiently broad and there are no unexpected ways that the 'bound' party or third parties can circumvent the exclusivity and compete on the market. Again, in order to protect each party, the written agreement on exclusivity should deal clearly with the following issues:

- scope of exclusivity;
- duration;
- requirements of the exclusive arrangement;
- what is intended in the agreement by the term 'exclusivity'; and
- objective standards for termination of the exclusivity, specifying the obligations of both parties upon termination.

3.2 Non-binding 'heads of agreement'

In the context of or prior to engaging in a transaction, the parties may decide to enter into non-binding heads of agreement – for example, in order to record the status of the negotiations between the parties or to determine the framework for future negotiations.

In line with general Italian law principles, the existence of non-binding heads of agreement strengthens the general obligation of the parties to negotiate in good faith. Any party which violates the obligation to negotiate in good faith (eg, in case of unjustifiable termination of the negotiations) must pay damages to the other party.

However, careful attention must be paid to the wording of the heads of agreement (and the parties' conduct) in order to avoid their being interpreted by the competent court as a binding agreement. Even express wording stating that the document is not intended to be legally binding may not fully cover such risk. Indeed, according to case law, if all the terms of the agreement are set out in sufficient detail, the signature on the heads of agreement could lead an Italian court to determine that the document is binding as the substantial terms of the deal have been agreed by the parties.

In addition, even if the heads of agreement are not binding, particular terms of the agreement, such as exclusivity and confidentiality, can be made binding. Penalties may be agreed for breach of such binding clauses.

It is also possible to agree that heads of terms of agreement be governed by a law other than Italian law, even if the parties are all Italian.

3.3 Confidentiality agreements

Any acquisition involves the exchange of a certain amount of information and data, much of which will be sensitive for the disclosing party. Consequently, in order to protect its interests, the disclosing party will request the recipient to undertake not to reveal the confidential information to any third parties and to use such information only for purposes stipulated in the agreement.

Any breach of the non-disclosure obligations will enable the injured party to claim damages from the breaching party.

Any confidentiality agreement should be framed to do at least the following:

- Define in detail what form of information is to be considered confidential or proprietary and, as a consequence non-disclosable;
- Identify excluded information (ie, information which is not confidential and which, as a consequence, is not subject to the confidentiality agreement). Common exclusions are:
  - information which the recipient can show it had prior to receipt of the information from the discloser;
  - information which becomes known to the recipient from a third party that had a lawful right to disclose the information;
  - information which is or becomes available in the public domain other than via the recipient; and
  - information the disclosure of which is required by law.
- Limit each party's use of confidential information.
- Describe the standards according to which the parties shall handle confidential information. Generally, each party must treat confidential information provided by the other party in the same way as it treats its own. However, information processing is acceptable only if the recipient has its own standards for handling confidential information (eg, limiting access to information or other methods of preserving secrecy). Therefore, before signing a confidentiality agreement, it is prudent to investigate the recipient's practices to maintain secrecy of its own information.
- Identify third parties to which disclosure can be made, subject to their meeting certain specified requirements.
- Make it clear that the confidentiality agreement must not be interpreted as granting an implied licence to the recipient with regard to any disclosed information.
- Set out the duration of the confidentiality obligation (varying, normally, from 18 to 24 months).

Finally, the disclosing party should ensure that its disclosures do not infringe any contractual obligation or any privacy law (ie, Legislative Decree 196/2003).

3.4 Due diligence

In the commercial practice of acquisition transactions, the term 'due diligence' refers to the investigatory activity carried out by the potential purchaser (and/or advisers) on the target company and the vendor. The main purpose of this activity is to identify the economic risks connected with the acquisition. The term 'due diligence' can also indicate the report containing the results of this investigation.

Due diligence normally includes a legal, accounting, financial and business review of the target and its business. It is common practice for the vendor to set up a data room where the due diligence activity is conducted.

Depending on the structure and purposes of the transaction, due diligence may be carried out at different stages of an acquisition process – in particular:

- before commencing negotiations, in order to verify the existence of the preliminary assumptions and offer useful elements for the negotiation of the agreement;
- between the execution of the agreement and completion, in order to determine the price or, in case of material discrepancies, to allow for termination of the agreement; and
- after completion, in order to execute checks with respect to the representations and warranties.

With regard to the information to be supplied to the purchaser, international practice has resulted in the creation of a checklist – a document produced by the purchaser listing the information required of the vendor. One issue raised under Italian law, which is still under discussion, is the limit of the vendor's duty to disclose information to the purchaser concerning itself and the target. In particular, under Italian law, the vendor must compensate any damage suffered by the purchaser if it fails to inform the purchaser of any event or circumstance which may cause the contract to be invalid. This duty of information is further widened by the legal duty of the parties to negotiate in good faith, which can include keeping the other party informed and cooperating with the other party, with a view to entering into a final binding agreement.

An additional issue with regard to listed or public companies concerns the potential liability of the directors of the target in disclosing information to the purchaser.

Finally, pursuant to Italian law, the different advisers carrying out the due diligence on behalf of the purchaser, in carrying out such activity, must observe particular standards of professional diligence. In particular, under Italian law, the liability of the adviser with respect to the client is limited to fraud or gross negligence.

4. Employment law issues

Employment issues in acquisition transactions vary depending on the nature of the deal (ie, whether it is an asset deal or a share deal).

4.1 Share deals

Here the employees continue to be employed by the target company after completion of the acquisition. A dismissal directly attributable to the change of control is unlawful and the dismissed employee may claim damages and, if the employer has more than 15 employees, reinstatement. However, when material changes occur in the ownership of an Italian company by means of a transfer of shares, any executives, if certain major collective labour agreements apply, may be entitled to resign and receive special compensation. There is no procedure under Italian law for the provision of information or consultation with employee representatives and trade unions during the sale of an Italian company. However, such an obligation might be set out in collective labour agreements.

4.2 Asset deals

In the case of an asset deal, there is an automatic transfer to the purchaser of the employment contracts of the going concern being sold, and continuity of employment and the conservation of all employees' rights and benefits. The vendor and the purchaser are jointly liable for all the employees' rights at the date of the transfer. The vendor may be released from such obligations only with the consent of the employees and by following a special procedure. The employees are protected from being made redundant as a result of the going concern transfer. In particular, if the vendor employs more than 15 employees, both the vendor and the purchaser must inform the employee representatives and the trade unions of the transfer and consult with them. The procedure must be started 25 days prior to any binding transfer agreement being reached. Any employees may resign with just cause within three months of the transfer, if such transfer involves a substantial change in their working conditions. In this event, the employee will be entitled to receive compensation in lieu of notice. Even after this three-month period, executives may resign and receive compensation if major collective labour agreements apply and if the specific time limit is respected. A special additional liability regime applies to the vendor of a going concern where the transfer of the going concern is followed by the execution of a supply agreement between the vendor (as customer) and the purchaser (as contractor), which is to be performed by using the transferred part of the going concern.

5. Competition law

Acquisitions may involve merger control by either the European Commission or the member state(s), and additionally, from outside the European Union.

This chapter addresses only issues concerning Italian competition law.

The Italian Competition Law (287/1990) and Presidential Decree 217 of April 30 1998 (which provides for a number of procedural rules, particularly in relation to the protection of the rights of the parties) are enforced by the *Autorità Garante della Concorrenza e del Mercato* (AGCM), an independent institution of the Italian government.

In particular, any relevant transaction (eg, merger, acquisition of control, full-function joint venture) will be subject to review by the AGCM if it satisfies