

# New rules for financial leasing in Italy

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## New rules establish a legal framework for financial leasing agreements in Italy

### Introduction

Before the new rules, financial leasing agreements lacked a dedicated legal regime in Italy. Instead, Italian courts applied - at times inconsistently - principles developed for other types of commercial transactions (e.g., a sale with retention of title). This resulted in uncertainty among the parties as to the applicable rules.

The new rules include:

- a definition of “financial leasing agreements” to clearly define the scope of the new rules;
- a concept of “material breach” as a trigger to terminate a financial leasing agreement;
- a precise definition of the consequences of termination for breach of contract; and
- a market valuation obligation for the lessor when a repossessed asset is sold or reallocated.

### A. Definition of “financial leasing”

Confirming the views of legal scholars and courts, the new rules define a financial leasing agreement as an agreement where:

1. a bank (or a licensed financial intermediary) undertakes to purchase, or procure the construction

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of, an asset selected by the prospective lessee and in accordance with the lessee's instructions, and makes the asset available to the lessee for a specified time in exchange for the payment of rent (which is calculated taking into account the purchase or construction price and the duration of the agreement);

2. the lessee assumes all risks relating to the asset, including deterioration risk;
3. upon expiry of the agreement, the lessee shall have (a) the right to purchase the leased asset at a pre-agreed price or (b) should the right not be exercised, the obligation to return the asset to the lessor.

## B. "Material breach" by the lessee

To protect the lessee's interests, the new rules identify events of "material breach" that allow the lessor to terminate the lease agreement. A material breach occurs if the lessee fails to pay at least:

1. six monthly installments or two (including non-consecutive) quarterly installments (or an equivalent amount) for real estate leasing agreements; or
2. four (including non-consecutive) monthly installments (or an equivalent amount) for any other leasing agreement.

## C. Termination and consequences

In case of termination of the agreement for a "material breach" (see paragraph B above), the lessor:

1. shall have the right to repossess the asset; but
2. shall pay an amount equal to the proceeds of the sale (or other form of disposal of the asset) at market value (see paragraph D below), net of an amount equal to the aggregate of (i) any due and unpaid installments through the termination date of the leasing agreement, (ii) the principal component of any installment due to expire after the termination date and (iii) the agreed final purchase option price (as well as any costs incurred by the lessor for repossession, valuation and management of the asset for the time necessary to complete a sale).

If the proceeds of the sale (or other form of disposal) of the asset are lower than the amount due from the lessee under paragraph 2 above, the lessor shall have the right to claim the payment of any negative difference from the lessee.

## D. The concept of "market value"

When marketing the repossessed asset for disposal, the lessor shall take into account its "market value", which shall be calculated:

1. on the basis of market evaluations available to the public and prepared by experts; or
2. in the absence of public market evaluations, on the basis of an estimate made by an expert appointed by the parties within twenty days of termination of the agreement, or, should the parties fail to reach an agreement within that period, an independent expert selected by the lessor from a list of at least three experienced candidates previously disclosed to the lessee, who will be entitled to choose for one of the candidates within ten days of receipt of the list.

## E. The provisions of Article 72-*quater* of the Italian Bankruptcy Law and the special form of residential leasing

The new rules do not affect the application of certain other provisions already applicable to financial leasing agreements.

In particular, in case of bankruptcy of the lessee, the obligation to perform the agreement is suspended (unless the bankruptcy court authorizes a temporary continuation of the business) until the bankruptcy receiver decides either:

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(a) to maintain the agreement in force (following authorization by the creditors' committee); or

(b) to terminate the agreement, in which case the leased asset shall be returned to the lessor and the lessor shall pay to the bankruptcy estate the positive difference between the proceeds of the sale (or other form of remarketing) at market value and the remaining principal amount to be paid under the financial leasing agreement.

The lessor shall remain entitled to file for admission to the bankruptcy estate for an amount equal to any residual claim towards the lessee.

Certain provisions<sup>1</sup> shall also continue to apply to financial leasing agreements of residential real estate assets to be used as a primary dwelling. This special regime was introduced in 2016, and so far has had limited use in practice.

The new regime, which is primarily relevant to commercial banks, leasing companies and their clients, should resolve past uncertainties and, together with recent changes to the Italian securitization law, benefit global and domestic investors in portfolios of non-performing leasing receivables.

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<sup>1</sup> Article 1, paragraphs 76, 77, 78, 79, 80 and 81 of Law No. 208 of 28 December 2015.