

# Companies limited by shares

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# Bonds

To raise funding, companies limited by shares may issue bonds.

Bonds are debt securities that represent equal-value fractions of a unit operation in the form of a loan.

Like shares, bonds have:

- equal nominal value
- grant equal rights (not administrative rights)

Unlike shares:

- bonds grant the status of creditor of the company
- funds raised by the company from bondholders are not provided as contributions, but go to form the so-called loan capital, and they are placed in the company's assets as loans
- so, the bondholders have the right to receive a fixed remuneration (interests), which normally doesn't depend on the financial results of the company; also, at the deadline set for the loan, they have the right to receive repayment of the capital loaned.

Except for these few common rules, there are many kinds of bonds:

- index-linked bonds (structured bonds)
- convertible bonds
- warrant bonds
- subordinated bonds
- participating bonds

## Bond issuance limits

→ *ratio*

→ art. 2412, par. 1, c.c.: bonds may be issued for an amount that in the aggregate does not exceed twice the share capital (subscribed capital, not just paid-up capital), plus the legal reserve and the available reserves resulting from the latest approved financial statements; the statutory auditors shall certify compliance with this limit

→ guarantees that the company has eventually given for bonds issued by other companies are also calculated in this sum (art. 2412, par. 4, c.c.)

→ in addition, those financial instruments that contain an obligation to repay the capital, including conditional repayment, should be calculated

The ratio between bonds issued and capital plus reserves must remain unchanged during the life of the bond, so:

→ the company may not pass a resolution to voluntarily reduce the share capital (i.e. material reduction) if the limit would no longer be met

→ compulsory reduction for losses (ex art. 2446 and 2447 c.c.) is allowed, but in this case (or also when reserves are reduced) profits cannot be distributed until the ratio between bonds and capital plus reserves is restored

There are some situations where the limit (ratio between bonds and capital plus reserves) can be exceeded (so bonds can be issued for an amount exceeding the legal limit):

1. subscription by institutional investor that are subject to prudential supervision
2. bonds are guaranteed by a first priority mortgage (ipoteca)
3. for reasons that involving the national economy
4. bonds are to be listed on regulated markets or another multilateral trading venue
5. convertible and warrant bonds

a mortgage is a right *in rem* that ensures that the creditor has priority satisfaction on a property (bene immobile)

## Issuance procedure

- competence: the issuance of bonds is approved by the directors (unless otherwise provided by the bylaw or the law)
- the minute must be drawn up by a notary, so it is subject to a legality check
- the minute must be recorded in the Business register
- the resolution shall only take effect and may only be implemented after its recording
- bonds content (art. 2414, c.c.)
- bond register (art. 2421, c.c.)

## Convertible bonds

Convertible bonds are bonds that give the right to subscribe shares of the same company, based on a predetermined exchange ratio (conversion rate), using the amounts paid when the bonds are purchased as contributions.

The one who exercises the conversion right ceases to be a bondholder and becomes a shareholder.

The issuance of convertible bonds implies the need to also pass a resolution for a share capital increase (against contributions, i.e. material increase) that will be subscribed when the bondholders exercise their right to subscribe the new shares (right of conversion).

→ persons eligible to subscribe to the convertible bonds (shareholders and holders of convertible bonds already issued, art. 2441, par. 1, c.c.)

→ conditions for issuance 2420-*bis*:

- share capital must have been fully paid up
- convertible bonds cannot be issued for an amount lower than their nominal value (and that of the shares offered for conversion: it will apply art. 2346 c.c.)

→ Competence (art. 2420-*bis* c.c.): extraordinary shareholders' meeting

→ delegation of competence to directors in the instrument of incorporation: 2420-*ter* c.c.

(the delegation must determine a specified amount and a maximum period, which may not exceed five years)

→ Content of the issuance resolution: conversion rate, period and procedure

→ Rules that prevent the right of conversion from being affected:

- 1) in the event of a paid capital increase and of new issues of convertible bonds, pre-emptive rights also accrue to existing convertible bond holders
- 2) in the case of a free capital increase and a reduction for losses, the conversion rate is automatically adjusted to the amount of the increase or reduction
- 3) the company may not pass a resolution to materially reduce the share capital, to merge, to divide, or to change the criteria for the distribution of profits until the deadline set for conversion has expired (unless the bondholders are granted the option of early conversion)

## Organization of bondholders (art. 2415-2418 c.c.)

- bondholders' meeting
- bondholders' common representative

## Bondholders' meeting:

- *ratio legis*
- competences
- rule of the extraordinary shareholder's meeting
- call
- changes to the bond terms and conditions: higher majority
- recording in Business register

## Bondholders' common representative

- appointment and removal
- termination of office
- competences

# Participating equity instruments

- Companies limited by shares can issue participating equity instrument to acquire assets other than from contributions.
- Those assets contributed are not subject to the same rules as for contributions (they will not be attributed to the share capital).
- Introduced with the 2003 reform.

## Discipline

- Very flexible in terms of rights which may be granted to them (rules provided by the Italian Civil Code are very generic)
- Rights of patrimonial nature
- Administrative right (not the right to vote in the general meeting)

→ With the bylaws the company has full autonomy to provide rules on how and under what conditions those instruments can be issued, the rights attributable and the rules for their circulation.