RECENT CHALLENGES OF LBOS IN ITALY AND INSTITUTIONAL INSIGHTS: THE DEVIL LIES IN THE DETAILS

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Abstract

This study highlights recent institutional challenges faced by Private equity (PE) investors in Italy. These challenges increased the debate on the admissibility of LBOs, especially with reference to the actual nature of the debt underlying LBOs and the deductibility of the related interest payments. Despite the enactment of the 2004 corporate governance reform, which legalized LBOs under specific conditions, and the introduction of the European AIFM Directive (2011/61/EU), the doubts on the admissibility of LBOs have not been fully resolved. Up until recently, the Italian Tax Authority continued to challenge LBOs by interpreting them as tools fraudulently adopted by PE investors to elude the law and evade taxes. As a result, PE investors had to face a number of fiscal challenges and sanctions, which added more uncertainty to the legal admissibility of LBOs in Italy. Recently, new fiscal guidelines and jurisprudence finally changed this perspective, confirming the legitimacy of LBOs.

Keywords: Buyouts, Private Equity, Regulation, AIFMD, Tax Treatment

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1. INTRODUCTION

When considering the possibility of implementing a merger and acquisition (M&A) and a leveraged buyout (LBO), for private equity (PE) investors it is essential to carefully understand the details of each country's legal and fiscal environment. This need is especially relevant within the European Union, where countries, such as Italy, have implemented a number of legal reforms that can significantly affect the PE industry (Cao, Cumming, Goh, & Wang, 2019; Gibson & Witney, 2018; Amess, 2018; Fox, 2017; Femino, 2014; Cumming & Zambelli, 2010; 2013; 2017).

The purpose of this study is to shed some light on the recent institutional challenges faced by PE investors in Italy, especially with reference to the fiscal treatment of LBO transactions. An LBO is a financial technique employed to accomplish the acquisition of a company (*target*) by another company (*newco*), with the prevailing adoption of debt capital relative to the asset value of the target company (Stanfield, 2020; Bacon, Hoque, & Wright, 2019; Wright, Amess, Bacon, & Siegel, 2018a, 2018b; Hammer, Hinrichs, & Schwetzler, 2018; Capizzi, 2017; Renneboog & Vansteenkiste, 2017; Reddy et al., 2016; Cao, Cumming, Qian, & Wang, 2014; Axelson, Jenkinson, Strömberg, & Weisbach, 2013).[1]

One of the most critical aspects related to LBOs is that the debt financing is acquired by the *newco* under the expectation that it will be repaid by the target company, through the future cash flows generated by the renewed target firm or through the sale of its non-strategic assets. Furthermore, the typical structure of an LBO deal involves the merger between the *newco* and the target, after which the target's assets serve as a guarantee for the debt originally acquired by the *newco* to accomplish the buyout (Amess, 2018; Zambelli, 2008; 2010; Femino, 2014; Bacon et al., 2019; Reddy et al., 2016).

Over the last decade, LBOs have been severely criticized, especially after the 2008 crisis. In the aftermath of the global financial crisis, media,

[1]For more details on the financial structure of LBOs see Engel and Stiebale (2018); Scholes (2018). See also Harris, Siegel, and Wright (2005); Wright and Robbie (1991, 1999); Capizzi, Giovannini, and Pesic (2009). Another type of buyout is represented by the Reversed Leveraged Buyout (RLBO), which involves two sequential steps: 1) a public company is first delisted and turned into a private firm through an LBO; 2) once the underlying restructuring process is completed and the LBO debt is repaid, the company is listed again, becoming a public firm again. For more details on this type of transaction, see Datta, Gruskin, and Iskandar-Datta (2013).

regulators, and policymakers around the world increased their criticism against leveraged buyouts for their potential detrimental effects on target companies and their stakeholders. These types of the transaction have been widely accused of involving a lack of full disclosure and a dangerous increase of the debt-equity ratio of target companies, which in turn could increase their default rate (Zambelli, 2008; 2010; Giannino, 2006). Private equity investors who finance LBOs have even been accused of being "locusts" or "asset strippers", under the view that the debt underlying an LBO deprives the target company of crucial cash flows and strategic assets (The Economist, 2016; Cumming & Zambelli, 2010; 2013; Bacon et al., 2019; Amess, 2018).[2] While it is widely recognized that PE funds did not cause the global financial crisis (Allen & Carletti, 2010; Ferran, 2011), PE investors have increasingly been accused of providing insufficient disclosure by enjoying a lack of regulation. At the EU level, new regulatory proposals and reforms of private equity funds were introduced after the financial crisis (see the Directive 2011/61/EU on Alternative Investment Fund Managers Directive, also known as the AIFMD Regulation), in order to increase the disclosure requirements for buyout deals and guarantee more legal protection to target firms and their stakeholders (Cumming & Wood, 2018; Annunziata, 2019; Gibson & Witney, 2018; Claessens & Kodres, 2014; Thomsen, 2009; Ferran, 2011).[3]

In Italy, the debate against LBOs started even earlier. During the 90s, legal scholars and judges severely challenged the legitimacy of LBOs and accused these types of transactions of producing an illegal weakening of the target companies by eluding Italian law, especially with reference to the provisions regulating the acquisition by a company of its own shares (Articles 2357 and 2358 of the Italian Civil Code).[4] As a consequence, LBOs experienced a period of uncertain legality (also called "the dark period" by Cumming and Zambelli, 2010, 2013), which became even darker in 2000, when the Italian Supreme Court intervened and proclaimed LBOs illegal in Italy (Supreme Court Decision 5503/2000). According to this Supreme Court's Decision, LBOs were no longer admissible in Italy because they were interpreted as a fraudulent way to elude Italian law, especially with reference to the financial assistance ban set by Article 2358 of the Civil Code (Zambelli, 2008). The Supreme Court's Decision added new uncertainty and doubts about the legitimacy of LBOs and was strongly criticized by PE investors (Zambelli, 2010). In 2003, after a long period of uncertainty with regards to the legality of LBOs, the Italian Government introduced new corporate governance (CG) reform (Legislative Decree 17/01/2003, No. 6) in order to clarify the legal status of LBOs and render these types of transaction legal in Italy.[5] This new CG reform became effective on January 1, 2004.

Despite the enactment of the 2004 reform (which created a safer harbor for LBOs in Italy) and the introduction of the European AIFM Directive, the doubts on the admissibility of LBOs in Italy were not over. Paradoxically, PE investors had to face further fiscal challenges, which added more uncertainty to the legal admissibility of LBOs in Italy, especially with reference to the fiscal treatments of interest payments underlying LBO deals, as will be discussed more deeply in this study.

The remainder of this study is structured as follows. The next section highlights the 2004 reform introduced in Italy, which clarified the legal status of LBOs from a governance perspective. Sections 3-4 focus on the subsequent fiscal challenges faced by PE investors and Section 5 provides concluding remarks.

2. THE 'MADE IN ITALY' REGULATION OF LBOS

With the corporate governance reform introduced by the Legislative Decree 6/2003, Italy became the first country in Europe to regulate leveraged buyouts, well before the global financial crisis and the subsequent European AIFMD regulation (Alternative Investment Fund Managers Directive, 2011/61/EU).

The Italian corporate governance reform became effective as of January 2004 (hereafter known as the "2004 reform") and positively affected the PE industry and the governance of target firms (Cumming & Zambelli, 2010), as well as the performance of PE funds (Cumming & Zambelli, 2013), and the accuracy of their due diligence (Cumming & Zambelli, 2017).[6]

Among other things, the 2004 reform added a new provision to the Italian Civil Code (Article 2501-bis) in order to outline a number of specific conditions and disclosure requirements to be satisfied for the legality of LBO deals (contingent legalization). This new reform created a safer harbor for LBOs in Italy and reversed the burden of proof: if all the conditions set by the law are fulfilled, LBOs are presumed legal, unless proven otherwise (Zambelli, 2010). This regulation was introduced with the purpose of preventing opportunistic behavior by investors against the interests of the target companies and their stakeholders (Silvestri, 2005; Giannino, 2006).

As anticipated in the Introduction of this study, the 2004 reform has brought to an end a strong debate on the legitimacy of LBOs, which started in Italy in the 90s and intensified in 2000, when the Italian Supreme Court declared LBOs illegal and prohibited their implementation in Italy (Supreme Court Decision 5503/2000; Zambelli, 2008). By looking at the market evolution of the PE industry in Italy, it is puzzling to observe that, over the period

[2]For a general overview of LBOs and the risks involved, see Bacon et al. (2019); Fox (2017); Malenko and Malenko (2015); Axelson et al. (2013); Davis, Haltiwanger, Handley, Jarmin, Lerner, and Miranda (2014); Femino (2014); Jensen (2010); Kaplan (1988; 1989; 1991); Kaplan and Stromberg (2009); Krieger (1994); Smith (1990); Wight and Robbie (1991; 1999); Diamond (1985); Gitman (1997); Ferrario (1991).

[3]The 2011/61/EU AIFMD Regulation was enacted in Europe as a consequence of the 2008 financial crisis in order to increase transparency and disclosure requirements imposed on alternative investments funds (AIFs), such as hedge funds and PE funds. After a transition relief period, the AIFMD Regulation became fully effective in Europe as of 2014. The Directive is applicable to hedge funds and PE fund managers who invest in the European Union or manage funds in Europe. For an overview of PE regulation in Europe see Payne (2011). The original purpose of this regulation was to create a harmonized regulatory and supervisory framework for private equity funds and other alternative investments funds. The AIFMD Regulation is scheduled to be reviewed in 2020 (for more details on this regulation see Ferran, 2011; Claessens & Kodres, 2014). For a recent overview on studies analyzing PE regulation see Cumming and Wood (2018); Cao et al. (2019).

[4]For more details on this matter see Zambelli (2008, 2010).

[5]This Decree followed the Bill of Law 366, issued by the Italian Parliament in 2001.

[6]For a recent overview of the economic impact of the Italian corporate governance reform, see Cumming and Zambelli (2018). See also Cao et al. (2019); Block, Fisch, Vismara, and Andres (2019).

of the illegality and uncertain legitimacy of LBOs (the "dark period"), LBOs were still carried out despite their prohibition (Cumming & Zambelli, 2010). Furthermore, LBOs were implemented in a less efficient way: 1) with a pyramidal structure, involving more than one *newco*, one of which was typically established abroad (Zambelli, 2008; 2010); and 2) with a lower managerial involvement of PE funds, to the detriment of the target firms' interests and performance (Cumming & Zambelli, 2010; 2013). Paradoxically, the results of such a prohibitive ruling produced negative effects on target companies, exactly the opposite of what was expected.

Over the period of legality, instead, LBO transactions were structured with a stronger involvement of PE funds in the management of the target companies (especially in terms of invested capital, ownership, and board control), and these types of transactions showed higher performance, both for target firms and PE funds (Cumming & Zambelli, 2010; 2013). Cumming and Zambelli (2017) also showed that the new LBO reform had a positive impact on the entire due diligence process implemented by PE funds. The 2004 reform also diminished the incentive of adopting complex pyramidal structures to accomplish LBOs.

In conclusion, the prohibition of LBOs was not an efficient tool to better protect the interests of the target companies and their stakeholders. The 2004 reform, which legalized LBOs under certain conditions, represented a more effective instrument to prevent opportunistic behavior and protect target companies. This reform represented an important turning point for the Italian buyout market and produced a positive impact for the buyout industry, not only in terms of frequency of LBO deals but also in terms of deal structure and governance of the target firms involved (Cumming & Zambelli, 2018).

3. THE SUBSEQUENT TAX DEBATE AND DRACONIAN FISCAL INTERPRETATIONS OF LBOS

Despite the 2004 reform, which legalized LBOs in Italy, an intensive fiscal debate followed. The Italian Tax Authority continued to challenge these types of deals by interpreting them as tools fraudulently adopted by *newco* firms and private equity investors solely to elude the fiscal law and evade taxes (Italian Tax Authority, 2009; Clifford Chance, 2010; 2016; Morri & Guarino, 2016; Cumming & Zambelli, 2018). This criticism was especially raised against cross-border LBOs, especially if characterized by pyramidal (or multi-layered) deal structures with multiple *newco* companies: one *newco* established abroad (*newco* 1) and the other one (*newco* 2) established in Italy with the purpose of acquiring the Italian target (Zambelli, 2010). A crucial decision of the Supreme Court (Fiscal Section, November 25, 2011, No. 24930) and various Tax Authority interpretations (Circular 19E/2009) have reopened the debate on the admissibility of LBOs in Italy. At the core of the dispute has been the interpretation of the actual nature of the debt underlying the LBO transaction, and the deductibility of related interest expenses. Another highly contested issue has been the interpretation of the effects and nature of the merger between the *newco* and the target, which represents a typical step to complete an LBO deal, at least in Italy (Zambelli, 2008; 2010).

With reference to the first issue highlighted above (deductibility of interest payments), Italian tax law distinguishes two cases, according to the legal structure of the firm: a) individual enterprises (for which Article 63 TUIR applies); b) corporations (for which Articles 96 and 109 TUIR apply).

For individual entrepreneurs, Italian law specifies that interest expenses are deductible only if they are strictly connected to the revenues generated by the business activity of the firm ("pertinence rule", set by Article 63 of the TUIR). A strict connection, or direct pertinence, between costs and business activity, must always exist in order to ensure cost deductibility from the taxable income.

For corporations, Italian tax law outlines two different and general provisions (Articles 96 and 109 TUIR), which may be subject to divergent interpretations.

- Article 96 refers to interest costs and specifies that these types of expenses are deductible only up to 30% of EBITDA. This provision does not mention the need for the corporation to fulfill any pertinence rule.
- Article 109 TUIR further specifies that costs "other than interest expenses" are deductible only if they are strictly related to the business activity ("pertinence rule"). Therefore, it appears that the burden of proving the pertinence principle applies only to costs "other than interest expenses" (Grimaldi, 2014).

By combining the provisions of Articles 96 and 109, a legal uncertainty emerges and the following questions arise:

- Why does Article 96 not mention the need for corporations to fulfill the pertinence rule in order to guarantee the deductibility of interest payments? Is it because the pertinence rule is irrelevant for ensuring the deductibility of interest payments? Or, instead, is it a mere legal oversight?
- Why does Article 109 literally exclude interest expenses from the pertinence rule?

From a fiscal perspective, two opposing interpretations of the above articles have emerged.

One interpretation is literal and emphasizes that for interest expenses only Article 96 matters. Therefore, to guarantee interest deductibility it is not necessary to prove a strict connection, or pertinence, between the interest payments and the business activity.

However, another less literal interpretation may be possible. As argued by a few scholars (Scotto di Santolo, 2010) and judges (Supreme Court, Fiscal Section, No. 24930, November 25, 2011), the pertinence rule is a general fiscal principle and, as such, it does not need to be explicitly mentioned by law. Therefore, the need for proving the pertinence rule should always be assumed. By following this line of thought, the pertinence rule must always be fulfilled, both for entrepreneurs and corporations. This interpretation was adopted by the Italian Tax Authority ("Agenzia delle Entrate") until February 2016 (Italian Tax Authority, 2009). According to this interpretation, the deductibility of interest payments related to LBO transactions was determined, first, by considering the pertinence principle and, second, by applying the 30% of EBITDA, in line with the interest cap set by Article 96 TUIR (Morri & Guarino, 2016).

The aforementioned legislative gap and legal uncertainty in the tax law reopened the debate on

LBOs and their admissibility in Italy. In some cases, the Italian Tax Authority challenged LBOs by contesting the lack of pertinence between the debt acquired by the *newco* and the business activity of the target firm. As such, the Tax Authority contested the deductibility of the underlying interest expenses.

This fiscal interpretation of LBOs was strongly criticized by private equity funds. From a financial point of view, it is difficult to justify this interpretation of the fiscal treatment of LBOs. Even accepting the legal need to prove a connection between interest expenses and the business activity of a firm, it sounds bizarre to argue that there is a lack of pertinence between the loan underlying LBOs and the business activity of the target company, especially after the merger between the *newco* and the target has occurred.

The legal uncertainty surrounding the tax treatment of LBOs most likely diminished the incentive to invest in Italy (Invest Europe, 2017; Ernst & Young, 2016a). As emphasized by Clifford Chance (2010), policymakers should carefully consider a delicate trade-off: countries that apply the most stringent and draconian rules on debt treatment and interest deductibility are most likely to attract fewer investments from abroad and face a high probability of forcing domestic firms to emigrate toward other countries (such as Ireland) that guarantee a more favorable tax treatment of inward investments.

3.1. Further fiscal challenge and contradicting interpretations of LBOs

In other cases, the Italian Tax Authority did not challenge the deductibility of the interest expenses for a lack of pertinence, but contested the effects of the merger between the *newco* and the target, considering this type of merger as a way to generate tax-evading results. Despite the fact that the 2004 reform legalized LBOs that are accomplished with a merger between a *newco* and a target, the Tax Authority continued to view the merger with great skepticism, as a tool adopted by investors with the sole purpose of eluding the fiscal law and evading taxes (Ernst & Young, 2016a; 2016b). In fact, according to the traditional interpretation of the Tax Authority, the sole purpose of the merger is to transfer or push down, the debt originally acquired by the *newco* onto the target's liabilities ("debt push down") and, as a result, the merger helps the newly combined entity to reduce the taxable income and evade taxes (Cumming & Zambelli, 2018).

In the case of cross-border LBO acquisitions, with multi-layered structures characterized by two *newco* companies (*newco* 1, established abroad, and *newco* 2, established in Italy), the Tax Authority strongly challenged LBOs. In these cases, once the merger between the Italian *newco* and the target was completed, the Tax Authority would apply the "transfer price rule" (outlined by Article 110 TUIR) by allocating a higher taxable revenue to the newly merged Italian company, on the basis of the amount of debt pushed down to the target (Grimaldi, 2014). In this way, the Italian Tax Authority applied a tax on a debt and interpreted the loan underlying an LBO transaction as a sort of revenue received by the *newco* in exchange for the service of financial assistance granted by the target company for the acquisition of its own shares, to the exclusive benefit of the *newco* (Grimaldi, 2014; Cumming & Zambelli, 2018).[7]

4. THE RECENT CHANGE OF PERSPECTIVE

The fiscal interpretations of LBOs highlighted in the previous sections were inconsistent with the OCSE Guidelines and have been highly criticized by PE investors, who had to face higher taxes and fiscal sanctions, even if they applied all the rules and legal conditions introduced by the 2004 reform (Article 2501-bis of the Civil Code). A strong debate on the admissibility of LBOs reemerged in the Italian PE industry.

The subsequent public pressure raised by the PE community reopened the discussion on LBOs and probably forced the Italian Tax Authority to reconsider its interpretation of the tax treatment reserved for these types of deals (Saltarelli, Bosco, & Schiavello, 2016).

This change of perspective was motivated by the public pressure and criticism raised by the PE community, which strongly highlighted the inconsistencies between the fiscal interpretation of LBOs provided by the Italian Tax Authority, and the legal interpretation of LBO provided by the 2004 corporate governance law reform, as discussed in the previous sections. In order to reduce these inconsistencies, in March 2016, the Italian Tax Authority published new guidelines on LBOs and provided new clarifications about the essence of merger LBOs (Circular 6/E, March 30, 2016[8]). In these guidelines, the Tax Authority confirmed the legitimacy of LBOs, as well as the deductibility of the related interest expenses. According to this new fiscal treatment of LBOs, the deductibility of the related interest is guaranteed as long as LBOs are carried out by following all the requirements set by the 2004 reform.[9] Furthermore, the Tax Authority accepted that the Italian *newco* may deduct interest expenses only within the limits provided by Article 96 TUIR. The Tax Authority has clarified that interest payments underlying LBOs should now always be considered pertinent and are deductible within the limit of 30% of EBITDA, in line with Article 96 TUIR (Morri & Guarino, 2016; Clifford Chance, 2016). This new fiscal clarification put an end to the past debate on the pertinence issue.[10]

Contrary to what occurred in the past, the most recent case law has reinforced this new change of perspective, by confirming the non-elusive nature of LBOs (see the Supreme Court Decision 868, issued on 16/01/2019; Supreme Court Decision 19430/2018). Eventually, the Tax Authority has now the burden of proving the existence of an elusive and fraudulent purpose underlying an LBO deal.[11]

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[7] See also Clifford Chance (2010); Committeri (2014); Spataro (2012).

[8] The Circular issued by the Italian Tax Authority (2016) is available at: https://dato-images.imgix.net/45/1461337783-Circolaren.6_Edel30marzo2016.pdf?ixlib=rb-1.1.0. For further details, see Clifford Chance (2016); Morri and Guarino (2016); Deloitte (2016); Ernst & Young (2016b); Assonime (2016); D'Agostino (2016).

[9] See Morri and Guarino (2016); Ernst & Young (2016b); Saltarelli et al. (2016); Clifford Chance (2016); Deloitte (2016).

[10] For multinational groups, the OECD "arm's length" principle should also be applied (see Clifford Chance, 2016, for more details).

[11] Previous jurisprudence, instead, provided an opposite interpretation of the deductibility of the interest payments underlying LBOs by requiring the application of the pertinence rule (see Supreme Court 7292/2006; Supreme Court 24930/2011; Supreme Court 4115/2014). For more details on the recent

Despite the above recent clarifications provided by the Italian Tax Authority, the fiscal debate on LBOs is not completely over, and a number of further doubts and questions arise, especially with reference to the tax treatment reserved for foreign shareholder loans. Paradoxically, these types of loans have been interpreted as equity contribution by the Italian Tax Authority. Such an interpretation implies disallowance of the related interest costs and denial of the tax deduction (Clifford Chance, 2010; 2016).[12] From a financial point of view, this is another draconian interpretation that does not seem justified by convincing and objective reasons or rational criteria. Furthermore, it is inconsistent with International Accounting Standard No. 32, which sets objective criteria to distinguish equity and debt instruments (Morri & Guarino, 2016).[13]

Another closely unresolved issue is associated with the different tax treatment reserved for domestic shareholder loans, which are not interpreted as equity contributions. What is the reason justifying this arbitrary disparity of treatment between domestic and foreign shareholder loans? No objective arguments were provided by the Italian Tax Authority. For foreign shareholder loans, the Tax Authority seems to apply the "substance over form" principle (originally set by OECD Transfer Pricing Guidelines), according to which the tax authority has the power of not recognizing some particular loans as debt instruments ("non-recognition power"). For fiscal purposes, the tax Authority may interpret a loan as equity when the underlying investment has, de facto, an equity nature or an equity function ("lack of substance" principle). As emphasized by Morri and Guarino (2016), this interpretation is not in line with the new updated OECD Guidelines, which strictly limit the "non-recognition power" granted to Tax Authorities. According to the new Guidelines, this power is now narrowed to cases involving transactions with no "commercial rationality" ("lack of commercial rationality" principle). Even accepting the applicability of the "substance over form" principle, the disparity of treatment reserved for foreign shareholder loans remains unjustifiable, and there should be no space for subjective discrimination based on the foreign or domestic nature of an investment. Both types of loans should be treated equally by the Tax Authority (Morri & Guarino, 2016).[14] We shall wait for more jurisprudence on this matter.

5. CONCLUSION

This study highlights the critical issues raised against LBOs in Italy, from governance and fiscal perspective, as well as the subsequent legal and fiscal interpretations provided within the Italian institutional environment.

After a long debate surrounding the admissibility of LBOs in Italy, both from a civil and fiscal point of view, the recent Tax Circular 6/E/2016 issued by the Italian Tax Authority and the most recent case law (e.g., Supreme Court Decision 868/2019; Supreme Court Decision 19430/2018) represent an important change of perspective for the tax treatment of LBOs, in line with the 2004 reform that legalized these types of transactions. The Tax Authority has clarified that interest payments underlying LBO transactions should now always be considered pertinent and are deductible within the limit of 30% of EBITDA, in line with Article 96 TUIR.

Despite this important change of perspective, a number of doubts and fiscal problems still remain unresolved. The details of the LBO structure will continue to be carefully evaluated by the Tax Authority and the deductibility of shareholder loans may remain challenged. We shall wait for more jurisprudence on this matter.

By highlighting the most recent financial, legal, and fiscal challenges faced by LBOs in Italy, this study aims at contributing to advancing the law and finance literature on the crucial role played by the institutional environment on PE investor behavior.

The main limitation underlying this study, and any study on LBOs in Italy, is represented by the lack of detailed and publicly available data on the structure of LBO deals and the governance of the target firms involved in LBO acquisitions.

This lack of detailed data on LBOs strongly limits the empirical investigations regarding the impact of new regulations on investor behavior. The empirical analyses by Cumming and Zambelli (2010; 2013; 2017) represent the first step in this direction, by demonstrating the significant impact the legalization of LBOs (which occurred in Italy in 2004) had on the governance of target firms, the performance of PE investors, and their due diligence process. However, future research is needed in order to fill this gap. Further empirical research could focus, for example, on the impact of the new fiscal guidelines, recently issued by the Italian Tax Authority, in order to provide policymakers around the world with new insights on how to better motivate LBOs while protecting the interests of the acquired target companies.

jurisprudence and its change of perspective about the deductibility of the interest payments underlying LBOs, see Brunello and Ronca (2019).

[12] See Italian Tax Authority (2016), paragraph 3.3.

[13] According to IAS 32, equity instruments have the purpose of absorbing losses (buffer role) and identify contracts that provide the holders with a residual claim on the assets of a company, which in turn has no contractual obligation to pay a reward to equity holders. Equity holders may receive payment only after all the debt holders are fully satisfied.

[14] See paragraph 1.65 OECD Transfer Pricing Guidelines. For more details, see also Clifford Chance (2016); Morri and Guarino (2016).

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