JUDGMENT NO. 170 YEAR 2013

In this case the Court heard a referral from a bankruptcy judge questioning legislation which enabled certain amounts due to the state in respect of tax to be granted priority ranking in bankruptcy proceedings, notwithstanding their otherwise unsecured status, and stipulated that such arrangements were to apply with retroactive effect to bankruptcy proceedings that had already been initiated when the legislation came into force. The Court held, referring also to the ECHR, that whilst retroactive legislation in the area of private law was permitted as a matter of constitutional law, it must be justified by "compelling reasons of general interest", which did not obtain in the case before it.

[omitted]

THE CONSTITUTIONAL COURT

[omitted]

gives the following

JUDGMENT

in proceedings concerning the constitutionality of Article 23(37), last sentence, and (40) of Decree-Law no. 98 of 6 July 2011 (Urgent provisions on financial stabilisation), converted with amendments into Law no. 111 of 15 July 2011, initiated by the designated judge at the Bankruptcy Division of the *Tribunale di Firenze* in the proceedings relating to the bankruptcy of Macchine Utensili s.r.l. by the referral order of 17 July 2012, registered as no. 288 in the Register of Referral Orders 2012 and published in the Official Journal of the Republic no. 1, first special series 2013.

Considering the intervention by the President of the Council of Ministers;

having heard the Judge Rapporteur Marta Cartabia in chambers on 8 May 2013.

[omitted]

Conclusions on points of law

1.– The designated judge at the Bankruptcy Division of the *Tribunale di Firenze* has raised a question concerning the constitutionality of Article 2752(1) of the Civil Code "in conjunction with Article 23(37) and (40)" of Decree-Law no. 98 of 6 July 2011 (Urgent provisions on financial stabilisation), converted with amendments into Law no. No. 111 of 15 July 2011, due to a violation of Article 3(1) and (2) and Article 117(1) of

the Constitution and Article 6 of the European Convention for the Protection of Human Rights and Fundamental Freedoms, signed in Rome on 4 November 1950 and ratified and implemented by Law no. 848 of 4 August 1955 (Ratification and implementation of the European Convention for the Protection of Human Rights and Fundamental Freedoms, signed in Rome on 4 November 1950, and the Additional Protocol to the Convention, signed in Paris on 20 March 1952), hereafter referred to as the ECHR.

The referring judge considers that the contested provisions not only change the rules on privileged ranking in relation to bankruptcy procedures, but also provide for their retroactive application; it is asserted that this would enable State claims in respect of penalties relating to direct taxes, which have already been included as unsecured claims in an enforceable statement of liabilities confirmed as definitive, to be reallocated a privileged ranking in breach of the principles of reasonableness and equality pursuant to Article 3 of the Constitution, in addition to Article 6 ECHR as applied by the European Court.

In particular, Article 23(37) of Decree-Law no. 98 of 2011, converted with amendments into Law no. 111 of 2011, provides that: "In Article 2752(1) of the Civil Code, the phrase: 'for income tax for natural persons, for taxes on earnings for legal persons, for the regional business tax and for local income tax other than those referred to in the first paragraph of Article 2771 that have been officially registered and become enforceable during the year in which the concessionary for the collection service commences with or intervenes in enforcement procedures and during the previous year' shall be replaced by the phrase: 'for taxes and penalties due according to the legislation on income tax for natural persons, taxes on earnings for legal persons, corporation tax, the regional business tax and local income tax'. The provision shall also apply to claims arising prior to the entry into force of this Decree".

Article 23(40) of Decree-Law no. 98 of 2011, converted with amendments into Law no. 111 of 2011, went on to provide that: "The holders of privileged claims that have intervened in the enforcement procedure or were registered as creditors in the bankruptcy procedure prior to the entry into force of this Decree may dispute any claims that, as a result of the new provisions set forth in the previous paragraphs, have been ranked higher than their own claims, and may invoke the remedy provided for under Article 512 of the Code of Civil Procedure upon distribution of the proceeds or file an

appeal in accordance with Article 98(3) of Royal Decree no. 267 of 16 March 1942 within the time limit specified in Article 99 of the Decree".

2.– As a preliminary matter, it is necessary to identify correctly the *thema decidendum* in the light of the overall wording of the referral order (see *inter alia* judgments no. 25 of 2012, no. 128 of 2010 and no. 350 of 2007).

Despite the reference to "in conjunction with Article 2752(1)" of the Civil Code, the judge questions the constitutionality only of the retroactive effect of the contested provisions. On the other hand, the extension of privileged ranking to the amounts payable to the state in respect of tax penalties arising as a result of the amended legislation introduced by Article 23(37) of Decree-Law no. 98 of 2011 is not in itself contested.

These proceedings thus concern exclusively Article 23(37), last sentence, and (40) of Decree-Law no. 97 of 2011, as subsequently converted into law, insofar as it provided for the retroactive application of the new provision contained in Article 2752(1) of the Civil Code, which extends privileged ranking to State claims in respect of IRES (corporate income tax) and tax penalties relating to specific direct taxes.

As a matter of fact, the legislation at issue in these proceedings is comprised of several provisions: first and foremost, Article 23(37) amended Article 2752(1) of the Civil Code by expanding the range of State claims that are eligible for privileged ranking in bankruptcy procedures. This provision – as noted above – is not contested in itself by the referring judge, who directs his challenges against the rules establishing the time from which the legislative amendment is to take effect laid down in the last sentence of Article 23(37), which provides that: "The provision shall also apply to claims arising prior to the entry into force of this Decree". Moreover, again as regards the temporary effects of the legislative amendment, the judge also challenged Article 23(40) of the legislation, which provides that creditors with a privileged ranking that have already been included in a statement of liabilities in bankruptcy may challenge claims that have been ranked above their own as a result of the new provisions contained in Article 23(37).

It is clear from a combined reading of the two provisions mentioned above – Article 23(37), last sentence, and (40) – that the extension of the privileged ranking provided for under the first sentence of paragraph 37 has retroactive effect, such as to influence

any enforceable statement of liabilities already confirmed as definitive, thereby encroaching on a final decision "within the bankruptcy procedure".

3.– The President of the Council of Ministers intervened in the proceedings and requested that the question be ruled inadmissible on the grounds that it [the court] failed to search for an interpretation compatible with constitutional law and on the grounds that it was insufficiently motivated.

The objections are groundless.

3.1.– It must be observed first and foremost in this regard that the provisions of the final part of Article 23(37) – according to which the privilege is extended "also to claims arising prior to the entry into force of this Decree" – cannot have any meaning other than to enable the reclassification to a higher ranking of a claim included as an unsecured claim in an enforceable statement of liabilities that has already become definitive.

Indeed, according to the general principles applicable to bankruptcy procedures, the introduction of a new privileged ranking by the legislator must at all times be applied immediately by the designated judge since the procedural rules on the ranking of claims are identified with reference to the time when the claim is invoked. Therefore, a provision such as that contained in paragraph 37 cannot have any meaning other than to extend retroactively the applicability of the new rule beyond the situations permitted under general principles, and hence to those in which the enforceable statement of liabilities is already definitive.

Moreover, similar provisions stipulating that a new privileged ranking should apply to claims that had previously arisen have in the past on all occasions been unequivocally and clearly interpreted as extending the possibility to grant privileged ranking also to claims definitively recorded as unsecured claims, provided that the proceeds of the estate have not already been distributed. This occurred in particular in relation to the provisions of Article 15 of Law no. 426 of 29 July 1975 (Amendments to the Civil Code and to Law no. 153 of 30 April 1963 on privileged ranking), which introduced a new system governing privileged ranking: the clear and unequivocal position stated by the civil division of the Court of Cassation regarding this matter (see judgment no. 235 of 1980) was that the meaning of the provision was to set aside the principle of "final decisions within the bankruptcy procedure", a view acknowledged also by this Court in

judgment no. 325 of 1983, which held that it constituted "living law" [i.e. the uniform and settled interpretation of the law followed in practice]. That interpretation has not subsequently been reversed.

3.2.– The retroactive scope of the provision under examination is also established by Article 23(40) according to which, as mentioned above, privileged creditors already registered as creditors in the bankruptcy procedure may challenge claims that have been ranked above their own as a result of the new provisions. Indeed, not only does that provision have the effect of establishing a new time limit for opposing a statement of liabilities that has been declared enforceable, but it also confirms that the new and broader privileged ranking granted to State claims has retroactive effect and covers situations in which the statement of liabilities has already become definitive.

Indeed, Article 23(40) would be superfluous in situations in which the statement of liabilities has not yet become definitive before the State's claim is granted privileged ranking, as any privileged creditor already included would be able to object to the reclassification of the State's claim in accordance with the general provision laid down by Article 98 of Royal Decree no. 267 of 16 March 1942 (Provisions on bankruptcy, compositions with creditors, controlled administration and mandatory administrative liquidation) within the time limit laid down by Article 99 of the Royal Decree (thirty days after notification of enforceable status or notification of inclusion, if later). Conversely, a statement of liabilities will become definitive and any opposition will be inadmissible following expiry of that time limit given that, according to settled case law, any amendment to the ranking of a claim (whether unsecured or privileged) already included is "precluded outwith the remedies provided for under Articles 98 *et seq* of the Law on Bankruptcy" as laid down in the Royal Decree (see judgment of the Civil Division of the Court of Cassation no. 17888 of 2004), and it is therefore "not possible to raise any other question relating to the existence, quality and quantity of the claims and privileged rankings", as such questions "must be raised by way of an opposition to the statement of liabilities pursuant to Article 98 of the Law on Bankruptcy." (see the judgments of the civil division of the Court of Cassation no. 13289 of 2012 and no. 12732 of 2011). It must therefore be concluded that the provision laid down in paragraph 40 applies precisely to situations in which the statement of liabilities, as originally drawn up, classified State's claims for corporate income tax and tax penalties

as unsecured claims, and subsequently became definitive in that form on the grounds that the period during which oppositions could be brought pursuant to Articles 98 and 99 of the Law on Bankruptcy (Royal Decree no. 267 of 1942) has already expired.

In such a scenario, the privileged creditor would no longer have any grounds to challenge the statement of liabilities during the period provided for under Article 99 of the Law on Bankruptcy given that the State's claim for penalties and corporate income tax was originally registered as an unsecured claim: therefore, the interest in bringing a challenge only arises at the time when the definitive statement of liabilities is altered, and this in turn is made possible (by the legislative amendment contested here) when stipulating that claims for tax penalties and corporate income tax originally registered as unsecured claims are to be reclassified under a privileged ranking. In such cases, Article 23(40) has the effect of protecting the interests of creditors with a privileged ranking other than the state, the aim of which is precisely to enable such creditors to object to the alteration of the enforceable statement of liabilities after it has become definitive in order to protect their own interests which, under the general rules, would not have any other remedy.

In other words, as a result of Article 23(40), the holders of claims with privileged ranking included in a statement of liabilities in bankruptcy that became definitive prior to the entry into force of the Decree-Law may file an challenge (as provided for under Article 98(3) of the Law on Bankruptcy) against any claims that are now ranked above them as a result of the new provisions, within the time limit set forth under Article 99 of the Law on Bankruptcy, time limit which commences on the date of the "delayed" recognition of the new State claim relating to tax penalties, as permitted under the contested provisions.

Therefore, while Article 23(40) does not contain an explicit transitory provision, it presupposes that the extension of privileged ranking to State claims applies retroactively, thereby setting aside the procedural bar resulting from final decisions "within the bankruptcy procedure" arising when the statement of liabilities becomes definitive.

3.3.– In the light of the above considerations, the objections raised by the State Counsel that the question is inadmissible on the grounds both that the retroactivity of

the provisions at issue in these proceedings was insufficiently motivated and due to the failure to search for an interpretation compatible with constitutional law are groundless.

In fact, it does not appear that any possible interpretation may be inferred from the wording of the contested paragraphs 37 and 40 of Article 23 of Decree-Law no. 98 of 2011 other than that illustrated in the previous section, that would enable State's claims for corporate income tax and tax penalties to be allocated a priority ranking, thus setting aside the procedural bar applicable due to the adoption of a final decision within that bankruptcy procedure.

It must therefore be concluded that the referring judge correctly argued that the question of constitutionality raised is significant with regard to the retroactive application of the new Article 2752(1) of the Civil Code and that the judge also complied with the obligation to consider the possibility of an interpretation consistent with the Constitution and the ECHR: indeed, this canon of interpretation is always and in any case subject to the limit of the unequivocal wording of the contested provision, where it is impossible to attribute to it a meaning other than that suspected to be unconstitutional (see *inter alia* Judgment no. 26 of 2010), which is the case in these proceedings.

4.– On the merits, the question is well founded.

4.1.– As is clear from the position stated in the previous sections, the contested provision enables the new rules on privileged ranking for the State's claims to be applied also to bankruptcy procedures in which the enforceable statement of liabilities has already become definitive, setting aside the so-called final decision "within the bankruptcy procedure". Consequently, it not only has retroactive effect, but also alters relations between creditors, which have already been established by a court order that has become definitive following the operation of the procedural bar on challenges, thereby favouring the financial claims of the state, to the detriment of the competing claims of private parties.

As the contested provisions have these effects, it is necessary to examine the question of constitutionality brought before this Court in the light of the constitutional and supranational case law on retroactive legislation, respectively with reference to Article 3 of the Constitution and Article 6 ECHR, as referred to by Article 117(1) of the Constitution, which constitute the terms of reference for these proceedings.

4.2.– The grounds for unconstitutionality raised by the referring judge must be examined jointly, such that Article 6 ECHR, as applied by the case law of the Strasbourg Court, is read in conjunction with other provisions of constitutional law, including in particular Article 3 of the Constitution, in accordance with the position followed under constitutional case law on the efficacy of the provisions of the ECHR since Judgments no. 348 and no. 349 of 2007. Indeed, this Court has asserted that "insofar as it supplements Article 117(1) of the Constitution, as an interposed source of law the ECHR provision must be balanced, in accordance with the ordinary operations that this Court is required to apply in all proceedings falling within its remit" in order to ensure the necessary "integration of protection" (see judgment no. 264 of 2012), which it falls to this Court to ensure in performing of its unique role. Therefore, even when the provisions of the ECHR are relevant pursuant to/as per Article 117(1) of the Constitution, the assessment of constitutionality "must be made on a systemic level, and not with reference to individual provisions considered in isolation" since "a fragmentary interpretation of the legislative provisions […] risks leading, in many cases, to paradoxical results, which would end up contradicting their very own goals of protection" (see Judgment no. 1 of 2013). In other words, this Court carries out a "systemic and non-fragmented" assessment of the rights affected by the relevant provision examined, striking the necessary balance in such a manner as to ensure the "fullest expansion of guarantees" for all relevant/significant constitutional and supranational rights and principles, considered as a whole, which are at all times engaged in relations of reciprocal integration (see Judgments no. 85 of 2013 and no. 264 of 2012).

4.3.– As regards the case under examination, it must be pointed out in relation to the principles referred to above first and foremost that "whilst the prohibition on retroactive legislation (Article 11 of the provisions on the law in general) represents a fundamental value of legal culture, it does not qualify for privileged protection under Article 25 of the Constitution", which is reserved to the criminal law. This means that "the legislator may – acting in accordance with that provision – enact retroactive legislation, including legislation specifying an authentic interpretation, provided that the retroactivity is adequately justified by the requirement to protect constitutionally relevant principles,

rights and interests, which also amount to compelling reasons of general interest" pursuant to the ECHR (see *inter alia* Judgment no. 78 of 2012).

However, the retroactivity must not contrast with other values and interests protected under constitutional law (see *inter alia* Judgments no. 93 and no. 41 of 2011), and this Court has therefore identified a range of general limits on the retroactive effect of legislation with the aim of safeguarding constitutional principles and other values of legal culture, which include "the observance of the general principle of reasonableness, which is reflected in the prohibition on creating unjustified differences in treatment; the protection of the legitimate expectations of individuals as a principle inherent within the rule of law; the consistency and certainty of the legal order; and respect for the functions reserved under constitutional law to the judiciary" (see *inter alia* Judgments no. 78 of 2012 and no. 209 of 2010).

In particular, the Court has already taken the opportunity to specify, in situations comparable to that under examination, that the retroactive provision cannot breach the legitimate expectations of private individuals, especially if these result from the consolidation of substantive interests, even where the retroactive provision is dictated by the need to contain public expenditure or to confront any exceptional contingent liabilities (see *inter alia* judgments no. 24 of 2009, no. 374 of 2002 and no. 419 of 2000).

4.4.– The principles applicable to retroactive legislation which have been developed within the case law of the European Court of Human Rights in relation to Article 6 ECHR are entirely similar, which/and apply also in relation to bankruptcy proceedings, as has been confirmed by specific rulings of the European Court concerning Italy (see the judgments of 11 December 2003 in *Bassani v. Italy* and of 15 November 1996 in *Ceteroni v. Italy*).

Indeed, the Strasbourg Court has repeatedly asserted with specific regard to the retroactive legislation of the Italian legal system that, as a matter of principle, the legislature is not prohibited from enacting new private law legislation with retroactive effect on rights available under the law previously in force. However, the principle of the pre-eminence of law and the concept of a fair trial enshrined in Article 6 ECHR preclude any interference by the legislature with the administration of justice with the aim of influencing the outcome of a judicial dispute, except in cases involving

compelling reasons of general interest (see the judgments of 11 December 2012 in *De Rosa v. Italy*, of 14 February 2012 in *Arras v. Italy*, of 7 June 2011 in *Agrati v. Italy*, of 31 May 2011 in *Maggio v. Italy*, of 10 June 2008 in *Bortesi v. Italy* and of the Grand Chamber of 29 March 2006 in *Scordino v. Italy*). The Strasbourg Court has also noted that the grounds invoked in order to justify retroactive legislation must be construed narrowly (see the judgment of 14 February 2012 in Arras v. Italy) and that a merely financial interest of the State does not enable retroactive legislation to be justified (see the judgments of 25 November 2010 in *Lilly France v. France*, of 21 June 2007 in *Scanner de l'Ouest Lyonnais v. France*, of 16 January 2007 in *Chiesi S.A. v. France*, of 9 January 2007 in *Arnolin v. France* and of 11 April 2006 in *Cabourdin v. France*).

Conversely, the stage of the proceedings and the extent to which rulings have become definitive, the unforeseeability of the legislative intervention and the fact that the state is a party *stricto sensu* to the dispute are all factors considered by the European Court when assessing whether retroactive legislation results in a breach of Article 6 ECHR: see the judgments of 27 May 2004 in *Ogis Institut Stanislas v. France* of 26 October 1997 in *Papageorgiou v. Greece* and of 23 October 1997 in *National & Provincial Building Society v. United Kingdom*. Whilst the judgments referred to above do not relate directly to Italy, they contain general assertions which the European Court considers to apply beyond the specific case and which this Court regards as binding also under Italian law.

4.5.– In the present case, as mentioned above, the proceedings concern legislation which, in expanding the class of State claims eligible for privileged status in relation to bankruptcy procedures, retroactively regulates private law relations between fellow creditors with the same debtor, and alters the enforceable statement of liabilities which has already become definitive, thereby encroaching on a final decision "within the bankruptcy procedure".

Since this is the effect of the contested provision, in view of the principles of constitutional case law set out above, as developed both by this Court and by the European Court, the provision must be ruled unconstitutional, since adequate significance must be ascribed to the following circumstances: the consolidation through the final decision "within the bankruptcy procedure" of the legitimate expectations of creditors, which are affected by the retroactive legislation; the unforeseeability of the

legislative amendment; the alteration in favour of the state – which is a party to the bankruptcy procedure – of the relationship between fellow creditors brought about by the provision under discussion; and the lack of sufficient grounds to justify the retroactive effect of the law.

In relation to this last aspect, it is important to stress that, in contrast with other retroactive provisions recently scrutinised by the Constitutional Court (see Judgment no. 264 of 2012), the contested provisions do not seek to pursue interests of constitutional standing, which could justify their retroactivity. The only interest is the financial interest of the state as a party to the bankruptcy procedure. However, such an interest is in itself incapable of legitimising legislation such as that under examination, which provides for less favourable treatment for the fellow creditors of the state, whose legitimate expectations in a share of the claim which they have lawfully accrued are unfairly breached.

4.6.– Therefore, the contested legislation proves to be unconstitutional on the grounds that it violates both the principles of equality and reasonableness under Article 3 of the Constitution and also Article 117(1) of the Constitution in relation to Article 6 ECHR, in view of the detriment caused by it to the protection of legitimate expectations and legal certainty, given the absence of any compelling reasons of general interest relevant under constitutional law.

ON THESE GROUNDS

THE CONSTITUTIONAL COURT

declares that Article 23(37), last sentence, and (40) of Decree-Law no. 98 of 6 July 2011 (Urgent provisions on financial stabilisation), converted with amendments into Law no. 111 of 15 July 2011, is unconstitutional as set out in the conclusions on points of law.

Decided in Rome at the seat of the Constitutional Court, *Palazzo della Consulta*, on 1 July 2013.