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New Tools to Encourage Shareholder Participation in the Life of Italian Listed Companies

Record date, electronic vote, tools to map and identify the shareholders, a new regime of proxy voting and increased dividends for long-term investors are among the principal changes introduced by Legislative Decree No. 27 of January 27, 2010, implementing E.U. Directive 2007/36/EC of July 11, 2007, on the exercise of certain rights of shareholders in listed companies. While the Legislative Decree entered into force on March 20, 2010, the new rules relating to the shareholders meeting will apply only starting from October 2010.

Legislative Decree No. 27 of January 27, 2010 (the “Decree”) brings significant changes into the landscape of Italian listed companies and their shareholders.

The Decree, adopted pursuant to Article 31 of Law 88 of July 7, 2009 (the “Law 88”) and implementing E.U. Directive 2007/36/EC of July 11, 2007, shapes new voice rights for the shareholders of listed companies with the intent to encourage their participation in the corporate life and, notably, the exercise of their voting rights.

The Decree, which amends the Italian Civil Code and Legislative Decree No. 58 of February 24, 1988 (the “Italian Securities Act”), introduces a variety of changes. This client publication briefly addresses some of the new rules that may trigger the interest of banks, investment funds and other institutional investors, as well as listed companies themselves. Most of the provisions discussed hereinafter do not apply to cooperatives.

The Record Date

The shareholders of Italian companies listed on any Italian or E.U. regulated market¹ will be allowed to attend shareholders meetings by means of a notice of ownership issued by their financial intermediary to the issuer, on the basis of the intermediary’s records at closing of business on the seventh trading day prior to the date of the meeting (Article 2370(5) of the Civil Code and Article 83-*sexies*(1)(2) of the Italian Securities Act)².

This is the so called *record date*, and pursuant to this new regime shareholders may attend a meeting and exercise voting rights in respect of those shares even if they transfer their shares after the record date. Conversely, the purchaser of the shares after the record date will not be entitled to attend the meeting (Article 83-*sexies*(2) of the Italian Securities Act). The Decree however provides that a person that purchases shares

¹ This provision also applies to the shares listed on any Italian or E.U. multilateral trading facility.

² Article 2370(5) of the Civil Code indeed refers to Article 83-*sexies* of the Italian Securities Act as regards companies where shares are held through a center depository system.

after the record date will have standing to challenge the resolution or exercise withdrawal rights, where applicable (Article 127-*bis*(1)(2) of the Italian Securities Act).

Listed companies must receive the relevant notices of ownership on or before the third trading day prior to the date of the meeting (Article 83-*sexies*(4) of the Italian Securities Act). This term, however, is not final: shareholders will be entitled to attend the meeting and cast their vote to the extent that the issuer receives the relevant notice prior to the opening of the meeting.

The introduction of the record date might trigger investment strategies arbitraging on the decoupling of the voting rights and the economic effects of the vote. Both the shareholders who transfer their shares after the record date (who will not bear the economic effects of their vote) and the purchasers thereof (who will be able, under certain circumstances, to insulate themselves from the consequences of a vote they did not take part in) might devise profit strategies on stock trading around the meeting.

Mapping the Shareholders of Listed Companies

A rule bearing the potential to significantly impact the transparency of the shareholdings of listed companies³ is new Article 83-*duodecies* of the Italian Securities Act, which affords issuers a tool to map their shareholders, if their bylaws so provide.

Upon a request submitted by a listed company (which may be bound to act also on the written request of a number of shareholders owning half of the percentage of the issuer's share capital necessary to file slates for the election of the board of directors), financial intermediaries must communicate certain identification information on the issuer's shareholders within ten trading days of the request (Article 83-*duodecies*(1)(2) of the Italian Securities Act)⁴. The company (but not, based on the black letter of the law, the requesting shareholders) needs to motivate its request to the intermediaries (Article 83-*duodecies*(4) of the Italian Securities Act). If the request is submitted upon

shareholders' request, the concerned issuer is required to disclose the identity of, and the interests held by, the requesting shareholders (Article 83-*duodecies*(4) of the Italian Securities Act).

The new provision also introduces certain disclosure requirements. Listed companies must disclose the submission of the request to the market (outlining the reasons thereof, if the request is being submitted by the company itself), have to make the information obtained from the intermediaries available to the shareholders and are further required to update their stock ledger accordingly (Article 83-*duodecies*(4) of the Italian Securities Act). This provision seems to resemble the rules on the disclosure of significant shareholdings in listed companies, requiring that the information obtained from the intermediaries be shared with all other shareholders and the market.

The shareholders requesting to map their fellow holders of interests in a listed company will share with the company the costs associated therewith, in accordance with the criteria that the Commissione Nazionale per le Società e la Borsa, the Italian securities regulator ("CONSOB"), will determine (83-*duodecies*(3) of the Italian Securities Act)⁵.

Privacy protection concerns might, however, limit the application of this new shareholder mapping tool. Any requested financial intermediaries will be bound only to communicate the data and information regarding shareholders who did not expressly forbid them to do so (Article 83-*duodecies*(1) of the Italian Securities Act).

Proxies and Proxy Solicitation

The previously applicable rules entailed strict quantitative and qualitative requirements applicable to proxies, including the prohibition on proxies granted to the directors of the issuer or any of its subsidiaries.

Not only the Decree repeals these restrictions (Article 2372(8) of the Civil Code), but it now allows listed companies to adopt a new tool to encourage shareholders' attendance in meetings: the «designated representative» of the company.

³ This provision also applies to Italian companies with shares listed on any Italian or E.U. multilateral trading facility being held by a central depository system (Article 83-*duodecies*(2) of the Italian Securities Act).

⁴ This term may be amended by CONSOB through a regulation to be adopted jointly with the Bank of Italy (Article 83-*duodecies*(2) of the Italian Securities Act).

⁵ Prior to the adoption of the relevant CONSOB regulation, the costs will be borne by the motioning shareholders (Article 7(3) of the Decree).

The «Designated Representative»

Unless otherwise stipulated in the bylaws, listed companies must appoint a single representative per each meeting to which the shareholders, no later than the end of the second trading day prior to the meeting, may grant proxies to vote their shares (Article 135-*undecies*(1) of the Italian Securities Act). Proxies granted without specific voting instructions relating to the agenda of the meeting will be ineffective (Article 135-*undecies*(1) of the Italian Securities Act). Moreover, proxies must be granted on a CONSOB-approved form. Further rules apply to certain conflicts of interest of the «designated representative» (Article 135-*undecies*(4) of the Italian Securities Act).

Individual Proxies

Notwithstanding the corporate «designated representative», shareholders will still have the power to appoint their own representatives at each meeting, whose conflicts of interest are also regulated in the statute (Article 135-*novies et seq.* of the Italian Securities Act).

Proxy Solicitation

In an attempt to simplify a set of rules that so far raised scarce interest from the market, the Decree also amended the regime of proxy solicitations.

First, the Decree introduced a *de minimis* exemption: rules on proxy solicitation will not apply if the solicitations is addressed to no more than 200 shareholders, provided that the solicitation does not come with indications that may influence the voting process (Article 136(1)(b) of the Italian Securities Act).

Second, the person promoting a proxy solicitation will no longer be required to hold 1% of the company's stock capital.

Third, the person soliciting proxies will no longer need to appoint a financial intermediary, although the solicitation will continue to require a prospectus (Article 138(1) of the Italian Securities Act). The repeal of the financial intermediary requirement and the elimination of the minimum holding requirement respond to the directive of «simplifying the regulation of proxy voting», indicated by the Parliament (Article 31(1)(n) of the Law 88).

Shareholders Meetings: Notice, Financial Report, Disclosure, Participation and Vote

The Decree significantly amends the regulation of the shareholders meetings.

Call of the Shareholders Meetings upon a Shareholders Request

The Decree reduces to 5% the interest that any shareholders who intend to have a meeting called must own (Article 2367(1) of the Civil Code).

The requesting shareholders must now prepare a report on the items on the agenda that they seek to be voted on. The directors, who may add their observations and remarks, are required to make this report available to all shareholders along with the notice of meeting (Article 125-*ter*(3) of the Italian Securities Act).

Notice of Meeting

The Decree also amends the timeline and deadlines applicable to the call of the shareholders meeting. Notably, a notice of meeting must be published on the company's website, in accordance with CONSOB requirements:

- within the 30th day prior to the date of the meeting (Article 125-*bis*(1) of the Italian Securities Act)⁶; or
- in the event of a meeting called to appoint the administrative or auditing bodies, within the 40th day prior to the meeting, to allow an easier submission of slates of candidates by the shareholders (Article 125-*bis*(2) of the Italian Securities Act); or
- in the event of a meeting called after the reduction of the share capital due to losses or below the minimum statutory requirement, within the 21st day prior to the meeting (Article 125-*bis*(3) of the Italian Securities Act)⁷; or

⁶ This provision also applies to private companies with a broad shareholders base, or *emittenti azioni diffuse tra il pubblico in misura rilevante* (Article 116(2-*ter*) of the Italian Securities Act).

⁷ This provision also applies to private companies with a broad shareholders base, or *emittenti azioni diffuse tra il pubblico in misura rilevante* (Article 116(2-*ter*) of the Italian Securities Act).

- in the event of meetings called to authorize defensive measures pending a take-over bid, within the 15th day prior to the meeting (Article 104(2) of the Italian Securities Act).

Supplementing the Agenda

Shareholders may now request that the agenda of the meeting be supplemented with additional items within ten days of the publication of the call notice of the meeting (Article 126-*bis*(1) of the Italian Securities Act)⁸, as opposed to the previously applicable five-day period.

The call notice must clearly indicate the deadline to exercise this right (Article 125-*bis*(4)(b)(1) of the Italian Securities Act).

«Single Call» Shareholders Meetings

Listed companies will now be allowed to hold «single call» meetings if their bylaws so provide.

The bylaws can exclude calls after the first, provided that the following quorum apply to any «single call» meeting (Article 2369(1) of the Civil Code):

- in the event of an ordinary shareholders meeting, the quorum currently applicable to second calls applies;
- in the event of an extraordinary shareholders meeting, the quorum currently applicable to any meeting after the second applies.

Right to Ask Questions before the Shareholders Meeting

The shareholders will now have the right to ask questions regarding items on the agenda even before the meeting (Article 127-*ter* of the Italian Securities Act).

The company, which is required to answer no later than the meeting, may discharge this duty through a Q&A providing the requested information, to be made available on its website (Article 127-*ter*(2) of the Italian Securities Act).

Financial Reporting Disclosure

Listed companies whose bylaws allow that a shareholders meeting may be called to approve the financial statements within 180 days from the end of the fiscal year (as opposed to the normal 120-day period) will only be required to make available (and no longer to approve) their draft financial statements within 120 days from the end of the fiscal year (Article 154-*ter*(1) of the Italian Securities Act).

Furthermore, the shareholders meeting called to approve the financial statements may only be held upon the lapse of a 21-day period starting on the date on which the financial statements are made available to the shareholders (Article 154-*ter*(1-*bis*) of the Italian Securities Act).

Electronic Vote

To the extent that the bylaws so provide, Italian companies may now allow their shareholders to cast their vote not only via mail (as currently permitted by the Civil Code), but also electronically (Article 2370(4) of the Civil Code).

The details of the electronic voting process will be set forth in a CONSOB regulation (Article 127 of the Italian Securities Act)⁹.

Special Increased Dividends

A new provision not expressly included among the guidelines set forth by the Parliament (as noted in the Government Report on the Decree) will allow the bylaws of listed companies to establish a dual regime for dividends payable to their common shareholders (Article 127-*quater* of the Italian Securities Act, which expressly deviates from the pro-rata standard set out in Article 2350(1) of the Civil Code).

Under this new rule, the bylaws may entitle companies to distribute increased dividends by up to 10% to any persons holding common shares for at least one year (Article 127-*quater*(1) of the Italian Securities Act). The bylaws, however, may subject the payment of the increased dividends to additional requirements.

⁸ This provision also applies to private companies with a broad shareholders base, or *emittenti azioni diffuse tra il pubblico in misura rilevante* (Article 116(2-*ter*) of the Italian Securities Act).

⁹ This provision also applies to private companies with a broad shareholders base, or *emittenti azioni diffuse tra il pubblico in misura rilevante* (Article 116(2-*ter*) of the Italian Securities Act).

Any shares subject to a shareholders' agreement, or owned by shareholders exercising a significant or dominant influence over the issuer, do not qualify for increased dividends (Article 127-*quater*(2) of the Italian Securities Act). Similarly, increased dividends cannot be paid out on any shareholding or part thereof exceeding 0.5% of the issuer's share capital (Article 127-*quater*(2) of the Italian Securities Act).

The Government Report on the Decree construes this provision, in line with the opinion of the Justice and Finance Committees of the Camera dei Deputati, the lower House of the Italian Parliament, as an instrument «to foster long-term investments by minority shareholders, a prerequisite for their higher involvement in the exercise of corporate rights».

It seems difficult to predict, prior to the application of the new rule, what effects increased dividends might have on the contestability or the liquidity of the concerned shares.

Entry into Force

The amendments brought by the Decree and briefly discussed in this client publication will apply to the

shareholders meetings whose call notice will be published after October 31, 2010 (Article 7(1) of the Decree).

The provision allowing issuers to map their shareholders will not be subject to such delayed entry into force, although for it to be fully operational companies will need to amend their by-laws.

Preliminary Considerations

The Decree provides the shareholders of Italian listed companies with a set of instruments that, properly operated, may intensify their involvement and influence on the life of listed companies.

The introduction of the record date, the new regime for the proxy voting and proxy solicitation, the possibility to map the shareholders and the new participation tools, if properly combined, may prove to raise the voice rights of shareholders of Italian listed companies.

Only time will tell whether and how minority shareholders (and among them, notably, institutional investors) will be willing to operate any of these new tools, and to what extent they will be keen to use them to increase their returns.

This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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