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Italian National Reports to Washington 2010: Lener on Hedge Funds

Raffaele Lener, Hedge Funds, Private Equity Funds and Sovereign Funds.

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Raffaele Lener, University of Rome Tor Vergata, Italian report

HEDGE FUNDS, PRIVATE EQUITY FUNDS AND SOVEREIGN FUNDS

1. Legal issues relating to hedge funds (HF) and private equity funds (PEF).

1. The existence of a legal regime, whether in regulation or outside regulation could be mentioned briefly. Analysis of the different regulations relating to hedge funds can i.e. be found in the recent IOSCO consultation paper.

   In Italy there is a legal regime regarding the HF and the PEF.

   These funds are regulated by:

   (i) the Consolidated Law on Finance – Italian Legislative Decree of 24 February 1998, no. 58 ("***TUF***");

   (ii) the Italian Decree of the Ministry of Finance of 24 May 1999, no. 228 ("**D.M.**");

   (iii) the joint regulation on the organisation and procedure of intermediaries providing for the investment or portfolio management services, issued by the Bank of Italy and CONSOB (*Commissione Nazionale per le Società e la Borsa*) on 29 October 2007 (the "***Joint Regulation***");

   (iv) the Supervisory regulations on asset management companies/collective investment undertakings, including the Regulation of the Bank of Italy of 14 April 2005 on undertakings for collective investment in transferable securities (the "***Bank of Italy Regulation***");

   (v) the Government anti-crisis measures contained in Italian Decree no. 185 of 29 November 2008, converted into Italian Law no. 2 of 28 January 2009 (the "***Decree 185***") and implementing Bank of Italy regulations of 16 December 2008 (the "***December 2008 Bank of Italy Regulations***") with the aim of limiting any increase in requests for the early redemptions of units due to the current situation in the financial markets.

   The question will arise as to the definition of HF or PEF: I would propose that we do not attempt to draw up a definition, as this has proved impossible by several international regulatory bodies. Especially for HF, the formula is so elusive and adapts so rapidly to market circumstances that any definition would run behind the facts. One can refer to attempts made by i.a. the IOSCO paper mentioned in the attached list.

   In the more recent terminology, HF are referred to as "private pools of capital" and I'm not sure that is a right designation.

2. If there is regulation specifically applicable to HF and PE funds, please mention the nature and general features of the regulation, e.g. whether this is public or private regulation, and in the latter case, if it is followed up in practice, and enforced by some external body.

The regulation specifically applicable to HF and PEF, indicated above, is a public regulation, followed up by the asset management companies ("**SGR**"), which manage the fund, and enforced by the relevant Italian authorities: Bank of Italy and CONSOB.

Most of the HF are registered in some tax heaven: why is this feature considered important for the application of the regulation in your jurisdiction?

I do not believe that the registration of the HF in tax heaven may have a direct impact on the application of the regulation in Italy.

3. How many of these funds are registered?

If the question concerns "HF registered in tax heaven" I am not aware of this kind of information.

4. As to the general purport, it would be useful to indicate whether the regulation addresses the manager, or also the fund, as both systems are practised. The main subjects that are covered in the regulation should also be mentioned, e.g. whether there is registration of the manager, what are the criteria applicable to it, are there restrictions with other activities e.g. asset management for other funds that HF.

The management of the funds at hand is reserved to SGR authorised by and registered with the Bank of Italy. Italian regulation addresses the SGR as well as funds and provides for detailed rules in respect of both of them.

With reference to the main subjects dealt with in relation to SGR, Italian provisions concern, inter alia:

- the authorisation by the Bank of Italy to act as a SGR; (the relevant requirements are, for example, a minimum share capital, the integrity, professional and independence requirements for the members of its bodies; a programme of activities and a report on the organisational structure that the SGR is required to file when asking for the authorisation, etc.)

- the registration of the SGR - following the authorisation by the Bank of Italy;

- the constraints for having shareholdings in other companies;

- a list of permitted activities for the SGR;

- specific provisions in case of mergers and de-mergers between SGR;

- accounting provisions;

- provisions concerning the deposit and sub-deposit of the financial instruments and money pertaining to clients;

- the shareholders of SGR;

- the organisation of SGR (e.g. administrative and accounting organisation);

- the information/communications to be sent to the authority;

- the power of inspection of the Bank of Italy;

- accounting prospectuses;

With reference to the main subjects dealt with in relation to the funds, Italian provisions concern, inter alia:

- the general criteria and minimum content that the regulation of fund is required to comply with;

- procedures for the approval of the regulation of fund;

- the investments, proscriptions and prudential provisions connected to the risk;

- the criteria for the assessment of the assets and calculation of the fund unit value;

- specific provisions in case of mergers and de-mergers between funds;

- details on the certificates representing the participations to funds;

- details on the depositary bank.

5. In the future it is likely that the regulation will be more developed about the creation of HF and PEF: own funds, gearing ratio's, conduct of business rules, information and /or disclosure rules, accounting provisions, rules on manager's remuneration.

With reference to any further provisions which may be developed in the future, it should be noted that, following the financial crisis, the European Commission, has focused its attention on the activity of both hedge and private equity funds, drafting, together with the Council, on 30 April 2009, a Proposal for a new directive on alternative investment fund managers (hereinafter the "***Proposal for directive***"), with the precise aim of preventing, for the future, any repercussions for all financial market participants and for the stability of the underlying markets, through specific rules concerning, inter alia, the issues mentioned in the question above.

6. The public - distribution of shares in these funds deserves some mention, as in many states, these funds cannot be offered to the public. In fact they may be offered indirectly, through Funds of Hedge Funds (FoHF), through insurance

products, or in other forms. The disclosure and other investor protection rules could be different depending on the legal structure chosen. Here a few mentions would be useful. What is the status of this debate about "alternative products," or "substitute products"? Some in the EU consider extending the MiFid[1] rules to all investment products: what is your reaction to this?

In Italy, HF cannot be offered to the public and the most common type of fund is the fund of hedge funds ("**FoHF**"), also called the 'fund of second level', which invests its assets in units of different hedge funds called 'funds of first level', mainly operating in the US and off-shore markets. With reference to foreign HF, it is worth noting that Italian law provides for a specific authorization procedure in connection with their offer in Italy. In particular, any offer must be previously authorized by the Bank of Italy, after consulting Consob, provided that the fund's operational schemes are consistent with those provided for Italian funds

Regarding the status of the debate about the "alternative products" or "substitutive products" please consider that, according to a Report issued by the Bank of Italy, Consob and the Ministry of Finance on July 2008, over the last ten years, alternative products, such as HF, "have proved to be a useful instrument for diversifying investment portfolios". However, the Report has declared that, after ten years from its introduction in Italy, the HF regulation should be modified in order to allow further development of this type of investment and to promote the competition of the Italian funds in the international context. In particular, the new regulation should aim at: (i) reducing heavily the minimum subscription amount of the investment in HF which currently cannot be less than €500,000; (ii) diversifying the regulation between FoHF and HF, in order to allow the offer to a broader public.

However, following the recent financial crisis the proposal put forward by the Report above does not appear to be so easy, as the Deputy General Manager of the Bank of Italy has recently declared that "the international market of HF is undergoing profound restructuring, the outcome of which is not currently predictable. In such situation, it appears to be more opportune to clarify the tendency in the international context before proceeding with the modification of the internal rules".

With reference to the extension of the MiFid rules to all investment products, I believe that it could represent a positive measure in order to strengthen the protection of all the investors.

7. Have there been cases of mis-selling of HFs or FoHFs? Were these decided in court? Have investors been indemnified?

We are not aware of cases of misselling of HFs or FoHFs in Italy.

8. Except in case of public distribution, it would be useful to have some idea about the nature of the holders of shares in these HF or PEF: traditionally, it was said that these were wealthy individuals, but it appears that apart from

[1] Esp. rules on know your customer, suitability, and so on.

FoHF, institutional investors (pension funds, insurance companies, investment funds) are increasingly acquiring shares in these funds: is the protection regime sufficient, and should regulation contribute to improve the position of these not always so sophisticated investors.

In order to answer to this question, it is necessary to distinguish the HF from the PEF.

With reference to HF, please consider that, in Italy, HF cannot be offered to the public and the minimum subscription amount must not be less than €500,000. This implies that the holders of shares in Italian HF are institutional investors. This also implies that the protection regime provided is sufficient for this kind of investors.

With reference to PEF, the increase of institutional investors is also confirmed, although, according to the data published by Italian Private Equity and Venture Capital Association (hereinafter "***AIFI***") on its website, it emerges that, with respect to the year 2008, the typical international subscribers of PEF (as FoHF are) have been reducing their participation in PEF, instead of industrial groups and individual investors. Pursuant to a survey carried out by AIFI at the end of the year 2007, 85 funds out of 98 were reserved to institutional investors.

The level of protection may be improved although, for example, with particular reference to Italian pension funds, it should be noted that they have been less affected by the financial crisis, compared to other foreign pension funds, and this is confirmed by the lack of any massive behaviours (such as an escape by subscribers from funds) with respect to Italy.

According to the report for the year 2008, the opinion of pension funds' authority ("***COVIP***") in respect of the management and strategies of investments made by funds is quite positive, notwithstanding the awareness of the need for improvements.

Restrictions on investments are governed by an Italian Legislative Decree of 1996, according to which such funds are required to comply, inter alia, with the principle of the diversification of investments in order to ensure their sound and prudent management. In fact, a pension fund may hold units of closed-ended funds not exceeding the limit of 20 % of its assets and 25 % of the value of the closed-ended fund.

It is possible, however, that such restrictions would be amended in such a way that may be lead to the aforementioned connection to specific quantitative parameters being surpassed, in accordance with a more general European concept of the prudent diversification of investments.

With reference to insurance companies, instead, they are allowed to invest in both PEF and HF. However, pursuant to Regulation n. 2530 of 3 July 2007, issued by the Italian Insurance Authority ("***ISVAP***"), the total investments in unlisted, reserved and HF may not exceed 5% of the technical reserves of the

company, while the exposure of any insurance company towards a single fund may not exceed 1% of the same technical reserves.

9. Where do you stand in this debate about extending the protections to a wider public that these so-called sophisticated investors? This is not typical for HF but has caused most concern if HF were involved.

It is crucial in a financial market to extend protection to a wider public.

10. Do investors in HF and PEF have sufficient information, whether on entry or on a continuous basis? Should this be left entirely to the freedom of contract or should the law provide for a generic measure. As HF are increasingly placed with a large public but even without a public issue how should the information system not be adopted? Continuous information on the evolution of the portfolio is even more important, as investors often are left in the dark until it is too late.

According to the Italian regulations, SGR are required to operate diligently, correctly and transparently in the interests of the unit-holders and the integrity of the market and the unit-holders are to be informed on the management of the fund. Having said that, it is necessary to differentiate the HF from the PEF.

Regarding the information reserved to the investors of HF, please consider that, since HF cannot be offered to the public, there is no duty to publish a prospectus. This implies that Italian law only provides generic measures concerning the information to the investors. However, there is a duty to deliver the up-to-date fund rules to each subscribing investor. It is noteworthy that the fund rules of an Italian HF must, inter alia, mention: (i) the risks deriving from investments (if any) in foreign HFs (e.g.: if such HFs are managed from off-shore centers) and (ii) the maximum amount of loans and leverage. Moreover, the accounting documents shall be made available to the investors and to the public according to the modalities specified in the HF rules.

With reference to the information reserved to the investors of PEF, a balance-sheet, and a six-month report on the management of the fund should be kept at the public's disposal on the SGR premises, within 30 days from the relevant draft, while the most recent versions of such documents should be made available to the public on the depositary bank's premises and also at the branches indicated in the regulation of the fund. The investors have the right to obtain a copy of these documents, free of charge and with home delivery.

Moreover, notwithstanding the provisions of law, the management of funds usually seek the trust of investors in a long-term perspective in order, for example, to ensure any further participation by them in any fund raisings they would promote in the future. Broadly speaking, for such purpose, PEF usually maintain relations with its investors by means of institutional meetings (e.g. general meetings of investors, held at least once a year) and periodical reports. In this sense it is possible to say that information to investors is left to the freedom of contract.

Notwithstanding the foregoing, according inter alia to the considerations in the Proposal for the directive of the European Commission and the Council, and in light of the consequences of the financial crisis, it would appear that investors do not receive sufficient information on a continuous basis.

11. If in your jurisdiction the managers have to be licensed, what are the conditions for obtaining the license: a few items might be:

    a. Fit and proper character of the managers

    b. Rules on conflict of interest

    c. Rules on risk management: these have been considered too weak

    d. Internal rules on valuation: contractual rules or IFRS?

    e. Internal rules on compliance

    f. Internal rules on asset segregation, on due diligence of investee

    g. Is there an internal and /or an external audit

    And are these conditions verified by an external body initially upon registration and from time to time?

    In our jurisdiction the SGR, manager of the funds, has to be licensed. The SGR must file the relevant application with the Bank of Italy which, after consulting CONSOB, issues the license where the following conditions are satisfied:

    a) the legal form adopted is that of a joint stock company (società per azioni);

    b) the registered office and the head office of the company are in Italy;

    c) the paid-up capital is not less than that established on a general basis by the Bank of Italy;

    d) the persons performing administrative, management and supervisory functions fulfil the professional, independence and integrity requirements;

    e) the owners of shareholdings fulfil the integrity requirements;

    f) the structure of the group of which the company is part is not prejudicial to the effective supervision of the company and at least the information required by the applicable law is provided;

    g) a programme of initial operations and a description of the organizational structure have been submitted together with the instrument of incorporation and the bylaws;

h) the name of the company contains the words “società di gestione del risparmio”.

The authorization is denied where verification of the conditions indicated above shows that sound and prudent management is not ensured.

These conditions are verified by the Bank of Italy upon registration and from time to time through the activity of supervision.

Some of these issues are particularly important for PEF: valuation, conflicts of interest are well known problems. How does your legal system deal with these?

The Italian legal system provides for specific rules in connection with conflicts of interest. Mainly, SGR are (i) subject to restrictions with other activities; (ii) subject to restrictions in the selection of the investments and (iii) required to appoint a depositary bank, with supervisory duties in their respect.

Moreover, SGR are required to manage the conflicts of interest through the implementation of a proper policy for the purposes of avoiding (i) any further encumbrances or exclusions of UCITS from any due gains, and (ii) in any event, any prejudices deriving from such conflicts to both the managed UCITS and participants. If the organisational measures adopted (the aforementioned policy) are not sufficient to exclude such conflicts of interest, proper resolutions should be taken by the SGR, for the purpose of ensuring that participants as well as UCITS would receive an equivalent treatment.

12. The recent crisis has indicated that HF may be exposed to substantial systemic risk, and hence that central banks, as systemic and prudential supervisors want to obtain data about their portfolios and their behaviour in the markets of at least the largest of these funds:

h. Do HF and PEF usually inform these authorities about their portfolio, even if only some time ex post?

According to the Supervisory and Statistical Reports, both PEF and HF are required to inform the Bank of Italy about the composition of their portfolio, on a six-monthly basis.

The SGR submit to the Bank of Italy, with reference to each fund or sub-fund managed only:

- within 60 days of the end of the semester, copy of the half-yearly report;

- within 90 days of the end of the year, copy of the balance sheets of the fund, together with the reports of the directors and the audit.

i. Have these authorities access through their prime brokers? And can the information be aggregated?

Please consider that the Italian rules require that the SGR may have a prime broker for each fund. The agreement between the SGR and the prime broker has to be delivered to the Bank of Italy. However, the appointment of a prime broker does not impact ton the functions and responsibilities of the custodian bank which is responsible for verifying compliance with the law and is liable vis-à-vis the fund manager and each unit-holder for any failure to fulfil its duties. Furthermore, the custodian bank has to monitor constantly the amount of the fund's assets and verify the collateral released in favour of the prime broker by the HF.

j. Is apart from leverage, the built up of important positions in certain assets that could trigger significant price movement upon a certain liquidity need, a point of concern?

If the question is to be intended as generically referring to acquisitions by PEF of positions into other companies, it should be noted that the current regulation already provides for duties of communications for SGR acquiring a significant position into companies.

In particular, SGR are freely allowed to have shareholdings in companies exercising in the banking, financial and insurance sectors, as well as in companies with an instrumental nature, but not in companies operating in non-financial sectors, and are required to file with the Bank of Italy, at least 60 days before the transaction, a request for the relevant authorisation, as well as a subsequent communication after the acquisition.

This issue is considered a point of concern even at a European level.

In fact, in their Proposal the European Commission and the Council suggested the provision of specific and detailed rules in this regard, introducing also duties of communication by the SGR to the other shareholders.

k. Should these funds disclose their portfolios publicly?

The disclosure of their portfolio would be a very opportune step in order to provide the investors and the authorities with the data necessary to evaluate their behaviour in the market. However, they are not currently required to publicly disclose their portfolio.

The only documents that SGR are required to put at the public's disposal are a balance-sheet and a six-monthly report on the management of the fund.

13. What is the position on the remuneration of the HF managers: is there a public debate in your country and are there proposals to improve on this point?

There is no public debate on the remuneration of the HF managers in Italy.

14. PEF, and to a lesser extent, HF have been accused to destroy the companies they invest in: the so-called "locust" phenomenon. Is this a public debate in your country and have the authorities dealt with it? What answers have been given, or what remedies could apply? (this could also be dealt with in part 2)

There is no specific public debate in Italy on the "locust" phenomenon which actually concerns the European debate.

15. Market abuse by HF is often mentioned: are there cases that have been reported in your country? Were these specific to HF activity, e.g. related to the volume of their business in a given market? Is there a policy dealing with rumours?

Market abuse by HF is discussed also in Italy even if I am not aware of cases of market abuse in my country.

16. Clauses about the withdrawal from HF or PEF: how are these structured? How did they work in the downward markets? Have investors complained about unjust treatment on exit? What techniques have been used to postpone the exercise of exit rights?

As far as the structure of the withdrawal is concerned, the redemption of fund units shall be effected on or before the expiry date set out for the relevant fund, according to the indications of the relevant regulation of fund.

Broadly speaking, the regulations of funds usually provide that the right of withdrawal may be exercised (i) in relation to off-site contracts, within 7 days from the day of the investor's subscription and, (ii) if the fund has to be reduced due to the total subscriptions being less than the envisaged amount, within usually 10 or 15 days after the relevant communication of the SGR to the investors, and by means of return registered mail.

There is no news on complaints about unjust treatment upon exit. Anyway, it should be noted that, irrespective of the withdrawal, other ways of exiting funds are available for investors.

In particular: (i) on the one hand we have been assisting, both at a national and international level, the significant development of specialized operators (being, almost always, funds as well) acquiring fund units, for a negotiated price, from investors interested in early disinvestments, and acting in a secondary market; (ii) on the other hand, a way of exit is even more ensured in respect of listed funds negotiated in a regulated market, which have therefore a daily determined unit price.

Finally, it is worth mentioning that investors may also turn to specific structured products, created for the purpose of providing them with liquidity. In light of the foregoing, it would appear that the early exercise of exit rights has been raised more concerns that its late exercise, with regard to which, I have no knowledge of any techniques used.

Part II: the social role of the Hedge funds, Private Equity Funds

2.1 What has been the role of PEF in your country: there are widely divergent opinions, the PEF stating themselves that they mainly offer management services, with an equity investment to maximise their returns.

On the other hand, HF and PEF have been accused of destroying firms through excessive leverage and appropriation of financial substance. What is the prevailing opinion on this subject in your jurisdiction?

They also have been accused of destroying employment[2]: what is the prevailing opinion in your country.

Have measures been taken to curb these negative consequences, e.g. regulating closures of plants, or massive lay-offs? What is their effectiveness? Have these aspects been litigated in court?

Although there is an opinion in Italy which deems this phenomenon negative for the market, we are not aware of specific cases of employment or firms destroyed through the excessive leverage and appropriation of financial substance by HF in our jurisdiction. The Italian Government has not adopted any measure in order to curb these negative consequences.

Is there any government's measure that has been taken, or is envisaged on these topics? Is there voluntary restraint by the PEF themselves? What kind of measures have they taken: Reducing leverage, duration of investment, etc.

With respect to the issues above, both positive and negative considerations can be reported. In light of some recent surveys on the development of Private Equity in Italy, carried out by AIFI association, it emerges that, in our country, a culture supporting funds' activities and participation in Italian enterprises is now spreading. In fact, according to the data at our disposal (published on AIFI website), investments made during the year 2008 by PEF in Italian enterprises increased by 30 % compared to the previous year (although it should be noted that, as a consequence of the financial crisis, the resources raised by PEF in 2008 for investments to be made in 2009 substantially reduced, compared to those raised in 2007 for investments related to the year 2008).

Broadly speaking, it demonstrates that the Italian sector of enterprises (traditionally represented by the so-called "PMI" which are small/middle-sized enterprises, on a family basis) has now an increasingly positive opinion on the intervention of PEF in the enterprises.

In particular, according to a survey carried out by AIFI and published in a paper on the Bank of Italy website, Italian enterprises turning to PEF, are quite satisfied with the contributions received by these funds (these contributions concern above all financial aspects, the definition of strategies, and

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[2] From European Venture capital Association:
Investments by European private equity and venture capital firms amounted to €73.8bn in 2007, and approximately 5,200 European companies received private equity investments. About 85% of these companies have fewer than 500 employees. Studies show that between 2000 and 2004 European private equity and venture capital financed companies created 1 million new jobs, which translates to a compound annual growth rate of 5.4% per year (eight times the EU25 total employment rate of 0.7%). Between 1997 and 2004, the average employment growth in buyout-financed companies was 2.4%, compared to 30.5% for venture-backed companies.

management of human resources, rather then technical improvements related to the products).

With reference to the issue of employment, instead, pursuant to the AIFI survey mentioned above, the occupational level has been enhanced, following the intervention of PEF. It should be noted, however, that the highest data refers to young enterprises with strong potential for growth.

Additionally, it is worth noting that there is lively debate on the performance of the enterprises participated by PEF and the relevant positive or negative influences in our country and all over the world.

Notwithstanding the positive observation above, with particular reference to the locust phenomenon, it is arguable that such an issue is also a point of concern in our country.

In the last few years, in fact, investments made by funds, aimed at maximising returns without any scruples by the strong recourse to the leverage by-out, have been increasing, especially involving large Italian enterprises. The financial crisis has been demonstrating the failure of the leverage and has led to the impossibility for certain enterprises controlled by PEF to pay their debts. Enterprises feel therefore that they have been set aside by funds.

It should be noted, however, that these investments have been carried out above all by foreign funds. Moreover, since the typical Italian enterprise is small- to medium-sized, it is arguable that the phenomenon under discussion is not a central point of concern in the Italian debate.

This phenomenon developed all over the world, and is now under the attention of the European Commission, which has drafted the aforementioned Proposal for a directive which is very much aimed at preventing, for the future, any reoccurrence of the negative consequences for the economy subsequent to the crisis.

2.3 HF and to a more exceptionally PEF have been known for their activist stand as shareholders, although they are by no means the only ones. Usually they put the board under pressure so that it would adapt its policies to their views.

How should board react to these attempts? What are the limits for boards to enter into contact with these activist shareholders?

From a regulatory perspective there are no rules in Italy regarding the way of reaction or the limits to the board in respect of the attempts made by the activist shareholders.

I may confirm that, even with respect to Italy, when the activities of PEF are aimed at expanding the enterprise, “the entrepreneur” is usually reluctant to have any interference by the fund, which is often considered useless because it does not have a in-depth knowledge and experience of the activities carried out by the enterprise.

In fact, pursuant to the available data (from AIFI) the entrepreneur is usually afraid to lose the majority of its firm, and therefore refuses any requests of PEF in this direction. On the other hand, PEF do not usually ask for the majority. Nevertheless, PEF are activist shareholders.

From the material and surveys available, it emerges that PEF and the manager of the enterprise usually set off their interests by entering into a shareholder's agreement before starting any cooperation in the management of the invested company. Sometimes, instead, they prefer to directly modify the company's by-laws (see answer to question 2.4 below).

As a consequence, any tools at disposal of each party is agreed previously.

2.4 What are the techniques used to pursue their position even owning only a minor block of shares?

Proxy voting

Voting agreements

Alliances with institutional investors

Short sales as an activist instrument

Media alerts

All the techniques listed above could be used by the activist shareholders in the case in which they hold just a minor block of shares.

Normally, PEF own a minor block of shares and the most common technique used to pursue their position is entering into a shareholder's agreement, or amending, either directly or through such a shareholder's agreement, the by-laws of the invested company.

With reference to the aforementioned shareholder's agreement, although its content depends on the transaction, it should be noted that there are some provisions which are typical.

These are usually aimed, inter alia, at (i) ensuring the maintenance of the same management (representing a very important element for PEF in the evaluation of the convenience of the investment), (ii) providing for the case of selling of the majority to third parties, (iii) providing for a pre-emption right in favour of PEF in case of selling of the minority; (iv) granting PEF a proper representation on the boards of the enterprise; (v) providing for amendments to the company by-laws in connection to the percentage required to the general meeting in relation to certain significant resolutions, (vi) providing for acceptance clauses in favour of PEF with respect to the appointment of the main people managing the enterprise, (vii) providing for a non-competition clause for the entrepreneur; (viii) granting PEF the right of withdrawal in case of losses exceeding an agreed threshold, (ix) providing, in general, for easy ways out for investors.

It should be noted, however, that the execution of a shareholders' agreement could be subject to restrictions under Italian law, such as the maximum duration of five years.

Although it is definitely not easy to have knowledge of the specific information required in the question, it is reasonable to believe that the techniques listed therein (which are provided by the Italian Civil Code) are available and also practised by Italian investors like funds and often regulated through the execution of a shareholder's agreement.

Regardless the foregoing and the specific means used from time to time (a direct amendment of the company's by-laws or the execution of a shareholder's agreement), it is worth pointing out that PEF investing in enterprises seek, first of all, to be granted with a right of information, wider than that of any shareholder, and aimed at monitoring the management of invested companies and the compliance with the plan agreed. Often, a representation of the fund on the boards of the relevant invested enterprise turns out to be the most efficient means of achieving such objective.

2.5 Can any of the following be used as techniques to exercise pressure by HF or PEF

- Right to call the general meeting

- Motion to dismiss the board of directors

- Motion to split-up the company, or to merge it with another

- Motion to close down certain parts of the business, or to sell it off to third parties (major disposals).

Do these decisions belong to the competence of the general meeting or can the board of directors take them.

Is the present threshold to call a general meeting widely accepted or are they criticised.

Even in this case the techniques listed above could be used as techniques to exercise pressure by HF depending on the amount of the participation held by the HF in the company. Generally the adoption of these decisions is remitted to the general meeting.

With reference to PEF, as mentioned in the answer to the previous question, funds and the other shareholders usually enter into a shareholder's agreement granting the investors specific powers. Pursuant to the Italian Civil Code the decisions mentioned in the question are mainly referred to the general meeting, while the call of the general meeting is generally required to a resolution of the Board of Directors, even following a specific request from shareholders representing at least 10% of the share capital or the minor percentage provided by the relevant company by-laws.

Moreover, as mentioned above, the company by-laws may be amended through such shareholder's agreement, and the percentages required for the resolution by the general meeting upon certain significant decisions of the company (such as the ones concerning extraordinary transactions of split-up, merger or close down of businesses may be) may be modified, so allowing investors owning a minor block to exercise a relevant influence.

One of the most important instruments used by PEF to exercise pressure is the veto power, usually granted in relation to certain specific and significant issues for the enterprise. Also the veto power could be provided through shareholder's agreements. It is used, above all, in the transactions at an early stage, where the risk connected to the investment is higher for PEF and the fund needs to exercise a significant influence in the relevant enterprise's decisions.

2.6 Are HF known for gaining support to their ideas?

- By using the media: are measures against equity manipulation effectively put in action? Should public announcements about forthcoming action not be subject to the same rules as for board announcements see: reg FD)

-Should there not be more transparency about the identity of the owners of voting rights in general? And about the shareholders in activist funds (concert action)

- Companies generally do not know the names of their shareholders due to the indirect ownership structures; what measures should be taken to ensure that boards have the names of their shareholders, and engage in a debate with them. What is being done about it?

- Important shareholders hide their ownership by the use of derivatives or complex financial constructions; by entering into equity swaps, contracts for difference and similar transactions

- By creating secret alliances with other shareholders, or by hiding their own voting position: what are the techniques usually followed? .

P.M. is there a debate in your jurisdiction about "empty voting" and how do you think this can be solved.

The use of media by HF widely represents a way to support their ideas. In Italy, for instance, recently a national newspaper reported the reprimand moved by Algebris, a HF which holds a participation equal to 0.3 % of Assicurazioni Generali ("***AG***"), one of the greatest Insurance Italian companies, to the board of AG highlighting the negative corporate governance and management inducement rendered by the board but the chance for Algebris to increase the amount of its participation in the insurance company.

As for the transparency about the identity of the owners of voting rights, usually the Funds do not know individually the shareholders. In this regard we are not aware of particular measures to be taken by the board.

Both the secret alliances with other shareholders and the hiding of the voting position represent techniques that should be followed.

We are not aware of any debate in our jurisdiction about "empty voting".

2.7 What defences can boards use to resist pressure from activist shareholders?

Is there a board neutrality rule, or only in Takeover bids?

Some advise to engage with the activists: defensive action is a last resort: Can boards communicate with activist shareholders, or should they abstain on the basis of equal treatment?

No information is available on the matter indicated above.

2.8 Some actions by minority shareholders are close to greenmail: does this happen in your country, what is the attitude of the courts and what can be done about it? What is the liability of directors in giving in to greenmail? Disclosure?

Italian case law does not provide for any judgement with reference to the "greenmail practice" or to practice carried out by the minority shareholders reflecting a nature close to the "greenmail practice" yet. In this respect please consider that the HF phenomenon, and of course the problems arising from it, is still developing in Italy and that the minimum subscription amount must not be less than €500,000 for each shareholder who decides to enter into an Italian HF.

From a general point of view, the liability of directors in giving in to greenmail should be inserted in the general liability of the directors toward the company.

2.9 Does your legal system recognise an obligation of the shareholders to act in the interest of the company, or to can he act in his own selfish interest?

There are no legal provisions expressly providing for an obligation for SGR to act in the interest of the company. In fact, SGR are only required (i) to adopt measures to protect the rights of the unit-holders and have sufficient resources and suitable procedures for the efficient provision of services and (ii) exercise, in the interests of the unit-holders, the voting rights attached to the financial instruments.

Does a shareholder have to act taking into account the respect for the interest of other fellow shareholders (fiduciary duty of the control shareholder)?

According to the current regulation it seems that, apart from the general rules of correctness required from SGR and its members in the exercise of the relevant activities, SGR are not expressly required to take any particular cautionary measures in respect of other fellow shareholders.

Part 3 the sovereign wealth funds

The notion of SWF is somewhat ambiguous: the aspect discussed here refers to the fact that foreign entities are owned by a foreign state and/or act on the orders of a foreign state. Some of these may be specific funds, funded out of excess foreign exchange reserves; other may be longstanding companies with a "public mission".

The potential detrimental policy influence has been at the centre of the debate, although the sheer size of their portfolio's and the lack of transparency may also be mentioned as points of concern. In case of difficulty, position may be imposed outside the boundaries of company law, but by e.g. the rules protecting direct foreign investment.

The Subject has now found a new equilibrium due to the financial crisis. The Santiago rules have also contributed to calming the debate.

Does your country regulate the activity of SWF and in which way?

No specific provisions have been issued in Italy with specific reference to WSFs so far.

Nevertheless, a first attempt to endorse the Santiago rules has been registered in 2008: in fact, according to Italian Law n. 133 of 6 August 2008 an Interministerial Strategic Committee has been established with functions of advising the government and devising policies on foreign investments and SWFs, mainly in order "to promote useful investments and prevent dangerous ones" (the committee's name is "Comitato Strategico per lo Sviluppo e la Tutela all'Estero degli Interessi Nazionali in Economia", literally "Strategic Committee for Development and Protection Abroad of Economic National Interests").

The Ministry of Foreign Affairs will issue specific provisions relating to participation in the committee and other operative matters. The Committee's purpose is to collect information from SWFs willing to invest (or already investing) in Italy in order to evaluate the transparency and reliability of their investment policy. The Committee will therefore report to the government (and companies) such evaluations, which are not binding.

There is still no web site on which it is possible to collect information about the activity currently carried out by the Committee, and no specific reference is made to such Committee in official legislative acts. Moreover, the decree which was supposed to provide rules on its activity has not been issued yet.

It is worth noting that Italian Law n. 133 of 6 August 2008 envisages also the possibility to constitute in Italy investment funds with both private and public assets investing in innovative economic activities and, for such purpose, delegates the Ministry of Economic Affairs to grant the public company Cassa depositi e prestiti S.p.A. with the power to create a fund allowed to invest in certain predetermined funds.

Are there figures available about the inflow of capital coming from SWF?

No official figures about the inflow of capital coming from SWF have been published by either the competent authorities or the Strategic Committee for Development and Protection Abroad of Economic National Interests.

Some unofficial information about the of SWFs currently holding shares in Italian listed companies at the end of 2008 may be available consulting national and international newspapers[3] and can be summarised as follows:

(i) Libyan investment authority holds a $500 million joint fund with Mediobanca, 4.9% of Unicredit, 1% of Eni, 45% of Tamoil Italia and 14,79% of Retelit. It recently closed a joint venture agreement with Sirti and is investigating the possibility to purchase shareholdings in Impregilo and Terna.

(ii) Mubadala, a fund of United Arab Emirates, holds 5% of Ferrari and 35% of Piaggio Aero Industries.

(iii) Kuwait Investment Authority holds 100% of Gulf and Mobil Oil distribution network and 50% of an oil refinery in Milazzo.

(iv) Singapore's fund Temasek holds 100% of Sinport, trough which indirectly controls 100% of Voltri Terminal Europa (VTE) in Genoa's Harbour, 100% of Venezia Container Terminal (VeCon), 55% of Voltri Terminal 2 and 10% of Rome Container Terminal.

(v) Singapore's fund GIC purchased the commercial centre Roma Est and paid Euro 850 million for shareholdings in Sintonia, a company that holds shares in Gemina, Telco, Atlantia and Aeroporti di Roma.

Can you briefly describe some cases in which access to SWF have been refused, indicating the grounds on which this refusal was based.

No information is available on this matter so far.

Have you in your legal order introduced procedures – possibly generally applicable – that are applied to SWF and ensure openness of their activity.

In Italy no specific provisions have been issued with exclusive reference to WSFs, but as SWFs can be classified as non-harmonized collective investment undertakings (and, in the majority of cases, they are incorporated under the laws of a non-EU country) they shall comply with all requirements and disclosure obligations, in relation to the specific investment activity they are willing to carry out, set forth in relation to (foreign, as the case may be) non-harmonized collective investment undertakings, for example:

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[3] The sources to which reference is made are: www.mariosechi.net/2009/05/05/italia-a-caccia-del-tesoro-dei-fondi-sovrani ; http://blog.panorama.it/economia/2008/10/26/fondi-sovrani-ecco-la-lista-dei-buoni/ ; http://209.85.229.132/search?q=cache:2DfvvNs_W_UJ:www.forexpros.com/news/financial-news/factbox-libyan-investments-in-italy-62226+libyan+investment+authority+telecom&cd=3&hl=it&ct=clnk.

- In relation to public offerings, article 42 TUF provides that non-harmonized investment funds willing to sell in the Italian market their units shall be authorized by the Bank of Italy, after consulting Consob, provided the operating arrangements are compatible with those prescribed for Italian undertakings. As a consequence their activity will be subject to the competent authorities' supervision.

- The new Italian Regulation (implementing Italian Legislative Decree No. 58 of 24 February 1998) on issuers (the "***Regulation on Issuers***"), recently amended by resolution no. 16893 of 14 May 2009, set out some integrated provisions on foreign non-harmonized collective investment undertakings, which are willing to operate in Italy provided that they comply with several disclosure and transparency obligations. These provisions relate to disclosure with respect to offering prospectuses and their publication.

- With reference to direct investments carried out by SWFs, the Bank of Italy's "Supervisory regulations on asset management companies and collective investment undertakings" of 14 April 2005 sets out, in relation to risks' concentration, certain limitations to the entity of the investments carried out in listed companies, bank's deposits and investment funds. (For example, a non-harmonized investment fund, as a general rule, shall not invest more than 5% of its assets in securities issued by each listed company; it being intended that there are some exemptions to the rule depending on the type of securities and on the target company).

- In relation to purchase offerings, the Articles 35 and followings of the Regulation on Issuers set forth the applicable procedures to carry out a public tender to purchase shares of listed companies, including a mandatory bid in the event the offeror already holds more than 30% of such company.

Have SWF published their policy objectives, whether in general or upon a specific investment. Do they publish their voting polices, and the way these are implemented

No official release on this point has been disclosed or is available on the websites of the relevant Italian Authorities. In some cases, SWFs disclose on their websites certain brief information about shareholding in target companies and the economic fields of interest for the purpose of their investments (see, for example, the website www.mubadala.ae).

Do SWF usually delegate a member to the board? Are there special rules applicable to that member e.g. with respect to secrecy?

No information is available on this respect on the basis of the information collected in the relevant web sites.

Should investee companies include a passage in their annual reports about the presence of a SWF and its action within the investee company? Or on the way the SWF has voted

Regulation on Issuers sets forth the applicable rules for the various financial reports to be drafted by the board of directors in connection with the financial statements of the company. Such provisions do not make any references to the duty to disclose information about SWFs holding shares in such company and their role during the past fiscal year.

It is worth noting that the disclosure of voting polices and exercise of voting rights is not mandatory under Italian law. The only disclosure requirements in this respect relate to the duty of the company to inform shareholders on how they can exercise their voting rights and to the duty to insert in the shareholders' minutes passages about the participation to the meeting in force of a proxy and the presence at the meeting of shareholders holding more than 2% of the company's share capital (articles 84 and 85 of the Regulation on Issuers).

Have there been mechanisms introduced reviewing, or surveilling the activity deployed by SWF in investee companies?

No specific provision has been set forth so far under Italian law in this respect.

The role of SWFs in investee companies shall be subject to the ordinary supervision activity carried out by the relevant national authority - CONSOB - according to the regulations and provisions applicable to any collective investment undertakings.

Since 2008 the only specific monitoring activity is that to carried out by the Interministerial Strategic Committee which was established in 2008, which is aimed at supervising the activity of SWFs in order to provide the Italian government and companies with reports and non binding advice on the investment strategies and the role of SWFs in the Italian market.

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