РАЗДЕЛ 1
НАУЧНЫЕ ИССЛЕДОВАНИЯ И КОНЦЕПЦИИ

SECTION 1
ACADEMIC INVESTIGATIONS & CONCEPTS

CORPORATE GOVERNANCE IN ITALY AFTER THE 1998 REFORM: WHAT ROLE FOR INSTITUTIONAL INVESTORS?

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Abstract

This paper tries to answer two questions: first, whether the changes in the law resulting from the 1998 reform are able to positively affect the attitude to activism of institutional investors in Italy; and second, whether, legal rules aside, it is reasonable to expect significant institutional investor activism in Italy. We provide both an empirical analysis of the factors affecting institutional investor activism in Italy and a legal analysis of the most relevant changes in the Italian mutual funds and corporate laws, following the 1998 reform. The empirical analysis shows that institutional shareholdings and investment strategies are compatible with the hypothesis that institutional investors can play a significant role in the corporate governance of Italian listed companies. However, a curb to their playing such an active role may derive from the predominance of mutual fund management companies belonging to banking groups (giving rise to conflicts of interest) and from the prevailing ownership structure of listed companies, which are still dominated by controlling shareholders holding stakes higher than, or close to, the majority of the capital (implying a weaker bargaining power of institutions vis-à-vis controllers). The analysis of the legal changes prompted by the 1998 financial markets and corporate law reform indicates that the legal environment is now definitely more favorable to institutional investor activism than before. However, the Italian legal environment proves still to be little favorable to institutional investor activism, when compared to that of the U.S. or the U.K.

Keywords: corporate control, institutional investors, legal rules, Italian companies

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Introduction

In February 1998 the Italian Government passed an Act reforming the law on financial services, stock exchanges and listed companies[1]. In a nutshell, with regard to listed companies, the reform was intended to strengthen minority shareholders' rights: new rights were granted to minority shareholders; the exercise of existing minority rights was made easier; proxy fights, which previously were *de facto* banned, were allowed; the powers and liabilities of the board of auditors ("collegio sindacale", a sort of audit committee separated from the board of directors) were extended.

The idea behind the new rules on corporate governance was that active institutional investors would make use, if necessary, of these powers in their monitoring of listed companies. A reduction of the agency costs stemming from the separation between ownership and control in listed companies would follow, with beneficial effects for shareholders' wealth and for the Italian economy as a whole.[2]

We do not question here whether the view that institutional investor activism is beneficial for shareholders' wealth is correct.[3] We simply take it as given that the 1998 reform was intended to provide a more favorable legal environment for institutional investor activism and try to answer two questions: first, whether the changes in the law resulting from the 1998 reform encourage institutional investor activism in Italy; and second, whether, legal rules aside, it is reasonable to expect significant institutional investor activism in Italy. Clearly enough, the second question has to be answered before the first, because if the answer were no, the other question would be moot, at least for the time being.

This paper is organized as follows. Part I provides an overview of the various economic and legal prerequisites for institutional investor activism. Drawing on Anglo-American experience, we observe that the basic conditions are: the size of the single institution's holdings in portfolio companies, the adoption of investment techniques other than pure indexing, the absence (or limited importance) of conflicts of interest at the institutions' level or, alternatively, a tough market discipline at the same level, contestable control structures for listed companies, and legal rules favorable to activism.[4]

Part II tries to answer the question whether it is reasonable to expect significant institutional investor activism in Italy: it provides an empirical analysis of Italian mutual funds' and foreign institutional investors' holdings, of their investment strategies, their ownership, and of Italian listed companies' ownership structures. Part III finally addresses the first question outlined above, by focusing on the innovations introduced by the T.U. More specifically, we consider the minority rights introduced or broadened by the T.U., in order to see whether they enhance institutions' bargaining power vis-à-vis directors and blockholders. We answer with a qualified yes both of the questions we try to address. We find in fact that the largest Italian and foreign institutions do hold significant shares in Italian listed companies, and that they do not adopt passive investment strategies; however, on the one hand the fact that most Italian mutual funds are controlled by banks and, on the other hand, the high concentration in the ownership structure of Italian listed companies may act as countervailing factors. The changes in the legal rules prompted by the T.U. do encourage activism in Italy, by strengthening to a certain degree institutional investors' bargaining power vis-à-vis managers and controllers. We show, however, that, on the whole, the legal environment in Italy is still quite unfavorable for shareholder activism, especially as regards rules on shareholders' meetings. Part IV is a conclusion.

I. Economic and Legal Conditions for Institutional Investor Activism

Following Black, 1998, we define institutional investor activism as the monitoring of the performance and governance of portfolio companies by institutions (i.e., mutual fund management companies, pension funds, insurance companies, individual portfolio management companies, and so on), coupled, if necessary, with "*proactive* efforts to change firm behavior or governance rules".[5] Institutional investors' initiatives usually comprise a first, secret stage,

[1] Legislative Decree no. 58/1998, "Testo unico delle disposizioni in materia di intermediazione finanziaria" (Consolidated Act on Financial Intermediation), hereinafter T.U.

[2] See Preite, 1993; Preite and Magnani, 1994; Costi, 1994; Associazione Disiano Preite, 1997; Jaeger and Marchetti, 1997; Vella, 1998.

[3] As is well known, the empirical evidence on the effects of institutional investor activism on shareholders' wealth is, at best, mixed. For a survey of the empirical literature, see Black, 1998. In Italy, a negative forecast on the effects of institutional investor activism has been made by Gambino, 1998, and by Angelici, 1999 (respectively suggesting that institutions' interests are different than those of generic shareholders, and that institutions will collude with incumbent controllers).

[4] We do not include the effect of activism on corporate performance as a factor affecting the willingness of institutions to become active, because, in the absence of convincing evidence on this point (see *supra*, note 3), what counts is instead whether institutions' managers *perceive* that activism positively affects performance.

[5] Black, 1998 (distinguishing activism from "institutional investor ownership of shares, coupled with the institutions' *reactive* willingness to vote, usually in accordance with self-interest, on an issue presented by someone else"; emphasis in the original).

called "jawboning", which consists of behind the scenes negotiations between one or more institutions and managers or controllers of a company: the former try to convince the latter to adopt some changes or not to pursue courses of action they do not like. In order to succeed in their negotiating effort, institutions may threaten:
(1) to sell their shares on the market, thus causing a decrease in their market price (no matter how liquid the market is, the fact that a large institution divests from a company is a very bad signal, so that the market price will drop in any case);[6]
(2) to refuse to buy new issues of shares (again, this would send a bad signal to the market);[7]
(3) to publicize the failure of the negotiations and their dissatisfaction with managers[8] (this also can have a negative impact on share prices);
(4) to use shareholders' rights in order to obtain directly (e.g., via a binding shareholder resolution) the changes they propose;
(5) to exercise shareholders' rights in a way that would not lead to the achievement of the proposed changes, but which would instead create trouble for directors and/or controllers (for instance, institutions may threaten to sue directors for liability if a company enters into a transaction which they oppose).

If negotiations with management fail, then institutions will usually put the threats they have made into practice, thus bringing the initiative to the attention of the public. Before assessing whether institutional investor activism can be expected to play a significant role in Italian corporate governance what impact the 1998 reform of company law had, we provide a description of the economic and legal factors which most influence institutional investor activism. Reference will be made to experience in the U.S. and the U.K., where the phenomenon has received the most attention.

A. Institutional investors' shareholdings. – A necessary condition for an institution to become active with regard to a specific company is the holding of a significant share in it,[9] whether in absolute terms (e.g., a fraction of the capital of more than 5 percent, as is the case for many British institutional investors with regard to British companies[10]) or relative to other classes of owners (as is the case in many American public corporations[11]). The reasons why significant shareholdings in individual companies are a condition for activism are fairly intuitive: the larger the shareholding, the less important is the problem of collective action facing institutions as shareholders in a public corporation,[12] and the more managers and controllers will be willing to listen to the active institution, i.e., the greater the institutions' bargaining power.[13] According to a commonly held view, there would be an inverse correlation between institutions' willingness to become active and the liquidity of their holdings; in other words, institutions would tend to raise their voice when the exit option is not available due to the size of their holdings. However, this view does not consider that large shareholdings by institutions may be the result of either of two investment techniques: indexing or stock picking. In the former case, the institutions will not care about exit and liquidity, since they will never consider the idea of divesting from any single company in the index.[14] In the latter case, one would think that, *ex ante*, the more liquid the market of any single stock, the larger the holding an institution will be willing to buy.[15] In fact, stock pickers' willingness to build a block will depend crucially on whether they will be able to sell it, once the market price has risen, without dumping the stock.

Of course, large shareholdings by an institution are a necessary but not sufficient condition for it to become active,[16] because of other counterbalancing factors, such as those we will focus on below.

B. Investment strategies. – Activism on the part of an institution is often said to be crucially dependent upon whether it invests its portfolio by indexing or by stock picking. As a matter of fact, in the former case, competition among institutions will regard the cost of managing the portfolio; since "monitoring and intervention increase management costs for the individual fund managers, while potentially improving the performance of non-intervening index-match funds",[17] each fund management company is like the prisoner of the dilemma: being unable to co-ordinate with other fund managers, it will stay passive, although all of the indexed fund managers would supposedly gain if they were active. The

[6] See Short and Keasey, 1997. See also Holland, 1998 (referring that British institutions use selective stock sales to the market in order to encourage board action).
[7] See especially Black and Coffee, 1994.
[8] See, *e.g.*, Holland, 1998.
[9] See Davies, 1997a; Del Guercio and Hawkins, 1999.
[10] See Goergen and Renneboog, 1998. See also Black and Coffee, 1994, reporting that Prudential, which was dubbed by the press "the unofficial 'High Sheriff of the City'", held "a 5% or greater stake in 'probably 200 companies'". Davies, 1997a, reports that in 1991-1992 Prudential held stakes higher than 3% in 57 out the FT-SE 100 companies.
[11] See Barnard, 1991 (reporting that, at the end of 1989, institutional investors held the biggest blocks in companies such as Mellon Bank, Exxon, IBM, General Electric, Chrysler, Amoco, Dow Chemical, Xerox, and Lockheed); Clyde, 1997.
[12] See Black, 1990.
[13] See Del Guercio and Hawkins, 1999.
[14] See Black, 1992.
[15] See Maug, 1998. And see also Coffee, 1991 (arguing that liquidity constrained institutions will refrain from building sufficiently big blocks).
[16] See Coffee, 1994; Clyde, 1997.
[17] Short and Keasey, 1997.

only way for indexers to become active is then to co-ordinate their efforts.[18]

One may argue that many (but not all of the)[19] active institutions in the U.S. have heavily indexed portfolios. However, these institutions are public pension funds: product market discipline does not concern such institutions' management as much as private ones'.[20] In the light of this, it is fair to say that, unless institutions are public or unless they succeed in overcoming collective action problems by co-ordinating their monitoring efforts, stock picking, or, more generally, the adoption of investment techniques other than indexing,[21] is a condition for activism. With specific regard to stock picking, one can observe that institutions which use this investment technique choose stocks after acquiring information about the issuer. Of course, the knowledge of a company's characteristics and problems is a necessary condition for intervention. On the other hand, such institutions may take high bets in a single company and hence have strong incentives to take an active stance if managers fail to deliver. Moreover, when institutions own a higher share of a single company than their competitors (i.e., if they are "overweighed" in that stock), the problem of collective action will be less of an obstacle to their activism.[22]

C. Ownership of institutional investors and conflicts of interest. –A factor which may prevent institutions holding large stakes in one or more companies from becoming active has to do with the ownership of institutions themselves.

First, if institutions or their parent companies are themselves listed companies, as often happens, "reciprocity" conflicts of interest may arise: institutions may prefer not to interfere with the way their portfolio companies are managed so as to avoid interference by other institutions in their own companies.[23] As is well known, a similar kind of conflict of interest prevents corporate pension funds (which are managed under the supervision of the board of directors of sponsoring companies) from taking an active stance with regard to the companies in which they invest.[24]

Second, if institutions provide not only investment management services but also investment banking, commercial banking, or insurance services, "scope" conflicts of interest may arise: institutions may prefer passivity, in order to avoid losing (the prospects of) other business relationships with the companies they invest other people's money in.[25] And even institutions specializing in investment management may prefer not to take a critical stance vis-à-vis the way investee companies are managed, because among their best (prospective) clients are externally managed corporate pension funds.[26]

Product market discipline (i.e., competition among institutions for final investors' money) may help to curb the problem of conflicts of interest and their negative effect on activism.[27] This may be so, however, only if (at least) the following conditions hold: (a) final investors perceive monitoring as a good thing, i.e., something that increases their return on investment; (b) in the case that money managers are selected by other final investors' agents (such as pension funds with externally managed assets), these agents face no conflicts of interest themselves (alternatively, their opportunism must as well be sufficiently constrained by market discipline at their level); (c) the costs of switching from one money manager to another are sufficiently low.

Finally on this point, it is to observe that, as a matter of fact, British institutions, and especially

[18] See Part I.E.

[19] For instance, TIAA-CREF devotes 20% of its portfolio "to take large bets" and the State of Wisconsin Investment Board fund does not index at all (Del Guercio and Hawkins, 1999).

[20] It is interesting to recall the "fiduciary energy" hypothesis proposed by O'Barr and Conley, 1992, in order to explain heavily indexed public pension funds' activism: they argue that if an institution indexes, "there is not that much to do" for pension fiduciaries; however, they "must expend a certain amount of fiduciary energy". Governance activity may be seen by them as the only thing to do. Eventually, a private player would simply get rid of the managers who do not have "that much to do".

[21] For instance, the institutions may "create reduced-portfolio index funds, that hold, say, 100 stocks instead of the entire S&P 500" (Black, 1992). In such a case, an investor also has overweighed positions (see *infra*, text accompanying note 22) and may justify the costs of intervention – provided, of course, that monitoring significantly improves performance – because its portfolio's performance would be different from that of current indexes replicated by indexers. Compared to stock picking, this investment techinque has the advantage that institutions adopting it do not face any "trade-off between liquidity and influence, nor do they care … about short-term performance" (see again Black, 1992). The only trouble with this is that collective action problems are still possible, albeit to a lesser degree, if the potentially active index-picking institution fears that other money managers will replicate the sub-index and free ride on its monitoring effort.

[22] See Black and Coffee, 1994.

[23] See Short and Keasey, 1997; Mallin, 1998. These conflicts of interest are exacerbated when, as happens in continental Europe, the institution or the company controlling it are part of agreements aimed at exercising joint control on several listed companies. See Cortesi and Musile Tanzi, 1998.

[24] See, *e.g.*, Black and Coffee, 1994.

[25] See, among others, Black, 1990; Coffee, 1991; Short and Keasey, 1997; Van Nuys, 1993, and Payne, Millar, and Glezen, 1996, provide empirical evidence on the relevance of scope conflicts of interest (the former, finding that banks and insurance companies tend to vote pro-management, no matter whether the relevant company is their client; the latter, finding that such intermediaries tend to vote pro-management only when they have commercial relationships with the company).

[26] See, *e.g.*, Black and Coffee, 1994.

[27] See, *e.g.*, Bianco and Signorini, 1994.

insurance companies, such as Prudential (which also has an investment banking branch), have traditionally been much more active than their American counterparts,[28] even though the conflicts of interest they face are the same.[29]

D. Ownership structure of listed companies. – Two features of the ownership structure of listed companies affect the probability of their being the target of active institutional investors: first, the share of capital, if any, held by the controller or by the controlling coalition and, second, the total share of capital held by institutional investors.

The consequences of a decrease in the market price of a company's share following the decision of one or more institutions to exercise the exit option are potentially much worse for the controlling shareholders if a company's control is contestable by way of a hostile takeover, since the decrease in the market price will make an acquisition more probable. The threat of exit is thus more effective when control is unstable, so that institutions' initiatives will be more probably successful when companies with this kind of control structure are targeted. Much in the same way, the threat of making a shareholder proposal or of starting a just-say-no campaign is stronger for companies with controlling shareholders holding a smaller fraction of capital, since the probability is higher that such initiatives will be successful.[30]

This aspect is usually ignored by American and British scholars, since ownership structures with strong controlling shareholders are uncommon for U.S. and U.K. listed companies, at least compared to continental Europe.

In the choice of targets, active institutions are usually careful to select companies in which institutional ownership is high.[31] Even though, for the U.S., according to Professor Black, there is no empirical evidence of any correlation between institutional ownership and an initiative's probability of success,[32] this attention to institutional ownership by active investors in the selection of targets is easily understood: institutions' holdings are on average larger than individuals'; hence, institutions will exercise their rights (especially their voting rights) in accordance with their self-interest (presumably, in favor of the active institution's initiative) more frequently than individuals. In fact, the probability that the vote of an institution will be pivotal is on average higher than the probability that an individual's vote will be.[33] The threat of taking the matter to the shareholders' meeting is therefore more effective when institutional ownership is high.

E. Co-ordination among institutional investors. – As already mentioned, institutions face collective action problems when deciding whether to become active.[34] It is clear that activism will be more frequent if institutions are able to co-operate with each other, by taking each a leading role in the monitoring of one or more companies or by acting jointly.

Not only does joint action allow institutions to share the costs of activism, but it also makes initiatives more prone to success and, hence, *ex ante*, more attractive. In fact, the threat of selling stock, of refusing to underwrite new issues or of using shareholders' rights will be more credible and effective if it comes from more than one institution.[35] In the U.K., as reported by Black and Coffee, 1994, "an institution needs to line up 10-15 percent of the company's stock before requesting a formal meeting [with the independent directors] – or before the board will pay serious attention". As a matter of fact, it is not so uncommon that coalitions of institutions form in order to promote changes in underperforming companies.[36] Usually, coalitions are led by an overweighed institution holding the largest share in the target company; rarely, however, do these coalitions assemble more than five members: above this threshold, "forming and maintaining a cohesive group [becomes] much more difficult."[37]

In the U.S., active investors have usually acted as lone wolves, or through organizations such as the Council of Institutional Investors, which had a role in the dismissal of the CEOs of companies such as GM, Westinghouse and IBM.[38]

F. Legal rules. – Legal rules affect activism both negatively and positively. Negatively, by means of laws and regulations which: (1) impose limitations on institutions' holdings; (2) discourage the assumption of control or close-to-control positions, *e.g.* in order to separate financial institutions from commerce; (3) directly or indirectly put obstacles to co-ordination among institutions. Positively, by means of laws and regulations which provide institutions

[28] As is well known, in the U.S., activism is quite rare and basically limited to public or quasi-public pension funds, such as CalPERS and TIAA-CREF. See, *e.g.*, Black, 1998.
[29] See Davies, 1993; Black and Coffee, 1994.
[30] Cf. Monferrà, 1998.
[31] See Smith, 1996; Carleton, Nelson and Weisbach, 1998.
[32] Black, 1998. But compare Zanglein, 1998, reporting data by the Investor Responsibility Research Corporation showing that "all of the corporate governance shareholder resolutions that passed in the 1998 proxy season were passed at corporations with institutional holdings of fifty-three percent or more."
[33] See Black, 1992.
[34] See especially Utset, 1995.
[35] See Black and Coffee, 1994.
[36] See Black and Coffee, 1994.
[37] See Black and Coffee, 1994; Holland, 1998. It is worth to note that this difficulty arises in spite of the unique "geographic and cultural cohesion of the City, where contact among institutional investors is constant" (Black and Coffee, 1994. See also Short and Keasey, 1997 [highlighting the possibility that the "well-developed networks (including the so-called 'old boys' network') and codes of practice and behaviour which have arisen from the City's long history of trading" may help overcoming collective action problems].
[38] See Thompson and Davis, 1997.

with bargaining tools vis-à-vis the target companies' managers and controllers. In the U.S., legal rules imposing quantitative limitations on institutions' holdings are very restrictive, albeit to a different degree for the single categories of institutions.[39] Moreover, many laws and regulations impose duties and prohibitions on controlling and large shareholders, the most discouraging for institutions being rules requiring extensive and "litigation-intensive" disclosure to any holder of more than 5 percent of the shares willing to influence control of the corporation and those providing short-swing profit liability.[40] On the contrary, "Britain today has few significant obstacles to owning equity or to holding large stakes,"[41] even though the risks of becoming an insider for insider dealing law purposes or a controlling shareholder for control-person liability laws may be a disincentive for institutions willing to become active.[42]

Usually, U.K. and U.S. laws and regulations define control broadly, so as to cover also joint control; moreover, rules imposing duties and prohibitions on those holding a stake higher than a certain percentage of capital normally aggregate the holdings of persons acting in concert. This implies that all these rules may apply also in the case of more institutions acting together. This may discourage joint action, which, as we saw before, may be the only way for institutions' activism to be effective.

Regulation may help to alleviate the risk of conflicts of interest hindering institutions' willingness to become active. It is well known that the U.S. Department of Labor, both under Republican and Democratic administrations, has urged pension funds' officials to vote proxies and, more generally, actively monitor the management of investee companies, deriving such obligations from the fiduciary duties applying to fund officials.[43] In the U.S. there are also rules which require the board of investment fund companies to include a minimum percentage of independent directors.[44] It is doubtful whether such measures are likely to induce institutions, directly or indirectly, to take proactive initiatives. However, they may at least make it easier for proactive institutions to gain the support (for instance, in favor of their proposals) of other, more conflict-of-interest prone, institutions. As we mentioned above, institutions' bargaining power vis-à-vis managers increases if there are shareholders' rights which they can *credibly and effectively* threaten to use when managers refuse to comply with institutions' requests. The exercise of shareholders' rights may enable institutions either to obtain what they want directly (e.g., via a binding shareholder resolution) or to create trouble for directors and/or controllers. In the former case, the effectiveness of the threat will depend on the probability of success of the initiative. In the latter case, the higher the prospective damage to managers and controllers from the actual exercise of the rights by the institution, the more effective the threat. And in both cases, the less costly the exercise of the right, the more credible the threat. Of course, institutions can increase the credibility of their threats of using costly rights by making use of them even in cases when it would not be cost-justified.[45]

In the U.S., the shareholders' right most commonly exercised by institutional investors after the failure of talks with management is the right to present a shareholder proposal. The threat of using such right is highly credible, because it is recognized in wide enough terms by S.E.C. regulations and because the costs for the institution exercising it are very low: in fact, the target corporation bears most of these costs and there is no need for prior coordination with other institutions.[46] However, the fact that most shareholder proposals are rarely binding for the board of directors reduces the effectiveness of the threat.[47] It is also interesting to note that shareholder proposals may not be used to nominate candidates for the board of directors.[48] Proxy contests are very rarely used by institutions, both in the U.S. and in the U.K., because of the high direct and indirect costs they involve.[49] But in a few instances, British institutions did use proxies to oust managers, this meaning that in the U.K. the very effective threat of their use by institutions has become credible.[50]

Accounts of institutional investor activism in the U.S. and the U.K. usually say nothing about whether active institutions resort to litigation when the outcome of jawboning or other initiatives is negative.[51] It would thus seem that the threat of bringing suit, even in the U.S., is not common among active institutions[52]. Probably, this is because

[39] See Roe, 1991.
[40] See Roe, 1991.
[41] Black and Coffee, 1994.
[42] Black and Coffee, 1994.
[43] See, *e.g.*, Brancato, 1997.
[44] See Levitt, 1999 (expressing the S.E.C. view that funds should be mandated to have a majority independent directors in their board instead of 40 percent as is now the rule). But see also, Kim, 1998 (arguing that also independent directors face severe conflicts of interest and that, hence, excessive faith has been placed in the independent directors by U.S. laws and regulations).

[45] According to Black and Coffee, 1994, this has been the case in the U.K., where institutions have occasionally resorted to collecting proxies even if they perceived it was not cost-effective for them to do so in the specific case.
[46] See, *e.g.*, Loss and Seligman, 1995.
[47] See, *e.g.*, Black, 1998.
[48] Id.
[49] See Black and Coffee, 1994.
[50] Id.; Davies, 1997a.
[51] In the U.K., beside the fact that it is very difficult for shareholders to sue directors, due to limitations deriving from common and statutory law, "[institutions] are usually unwilling to litigate": Davies, 1997b.
[52] See also Johnson, 1997, reporting that "[t]o date, only a small number of institutional investors have chosen to file

of the costs litigation entails, especially the costs implied by engaging in direct confrontation with boards of directors: in fact, directors of other companies may consequently stop their relationships with the litigating institution, fearing for instance that any soft information they provide it with may be "used against them." Indirectly, institutions' bargaining power is affected by the laws allocating powers between the board of directors and the shareholders' meeting: the more power is allocated to the latter, the more institutions can threaten to make shareholder proposals or engage in "just-say-no" campaigns against proposals by the board of directors. Finally, the rules governing shareholders' meetings may also prove to be very important. First, a crucial element in order for the threat of making a shareholder proposal to be effective is whether the law allows (or, as the case may be, imposes) confidential voting. In fact, as we saw, institutions' voting behavior will normally be influenced by scope conflicts of interest. Confidential voting allows institutions to vote without having to fear loss of business relationships with the target company.[53] Second, legal rules lowering (or, at least, which do not raise) the cost of voting are also important, since they make it more probable that minority shareholders will exercise their votes.

G. Summary. – We have provided here a description of the main economic factors affecting institutional investor activism. We have seen that the holding of a significant stake in the investee company is a precondition to activism. Market liquidity *positively* affects activism, since the more liquid the market, the more the institution will be disposed to build a big block. Second, institutions have to adopt non-indexing investment strategies, because otherwise coordination among all of the institutions – which would be difficult – would be necessary to avoid free riding problems. Third, the institution must not face significant "reciprocity" or scope conflict of interests. Fourth, the more contestable the control of listed companies, the stronger will be the bargaining position of the institutions vis-a-vis the managers or the controlling shareholders. Much in the same way, the institutions will have more bargaining power if they succeed in coordinating their initiatives.

Finally, we have seen that legal rules can have both a negative and a positive impact on institutions' willingness to become active, since they can either attach negative consequences to the fact that an institution gets involved or may get involved in the control of a listed company, or grant powers and rights to shareholders, that institutions may use or threaten to use against managers or controlling shareholders.

class complaints or to intervene in existing securities class litigation".

[53] See Rock, 1991, and Black, 1998.

II. Institutional Investor Activism in Italy: An Empirical Analysis of Economic Conditions

We have shown in Part I that the development of institutional investor activism depends on a number of conditions of both an economic and a legal nature. The purpose of this Part is to provide indications on whether the economic conditions for institutional investor activism in Italy exist. To this end, rather than reporting single episodes of activism,[54] we try to evaluate the "potential" activism of institutional investors in Italy, *i.e.*, on the one hand, how probable it is that institutions will consistently take an active stance in the corporate governance of Italian companies, and whether, on the other hand, institutional investors would be *able to* exert effective pressure on the management of portfolio companies, should they decide to become active. Our analysis concentrates upon Italian open-end mutual funds (in the following, mutual fund management companies) and foreign investment management companies[55] for a variety of reasons.

First of all, there is already some anecdotal evidence about activism by these categories of institutions during the past few years.[56]

Second, the potential activism of the other Italian institutional investors seems, at present, limited by regulatory and structural factors. Corporate pension funds have traditionally invested very little in equity[57] and, as also happens in the U.S. and the U.K., due to reciprocity problems, have a totally passive record, whereas multi-employer pension

[54] Cortesi and Musile Tanzi, 1998, and Rubino and Verna, 1996, have provided a case history analysis on institutional activism in Italy. Cortesi and Musile Tanzi report 27 cases of institutional investor activism in Italy between 1993 and 1997. Among these 27, 11 were cases in which institutions sought to obtain the disclosure of material information by listed companies. As noted by Rubino and Verna, initiatives aimed at obtaining more information serve the institutions' interest to take buy and sell decisions on an informed basis rather than their interest in playing an active role in listed companies' governance.
The problem with such kind of studies is that they are unable to provide data on behind-the-scenes activism, which, as teaches the British and American experience, is much more frequent than publicized activism (see Davis, 1997; Short and Keasey, 1997; Holland, 1998). Moreover, at least in theory, the relative paucity of cases of institutional investor activism as testified by the studies cited above could mean either that institutions are passive or that corporate actors (blockholders, managers etc.), knowing that institutions would act if something went wrong with their companies, avoid taking courses of actions which institutions would dislike.

[55] We will refer to these two categories of institutions as "institutional investors".

[56] See *supra*, note 54.

[57] As reported by Enria, Focarelli, and Landi, 1998, in 1995 pension funds invested 3 percent of their assets in equity.

funds (for which a new legislation was enacted in 1993 and 1995) are not yet fully operational in Italy, due to regulatory hurdles.[58] As far as insurance companies are concerned, it was impossible for us to get comprehensive data about their holdings in Italian listed companies. The only available data regard major shareholdings according to the laws on ownership transparency (*i.e.*, information on holdings greater than 2 percent of the voting capital of listed companies), and the impressionistic evidence is that these holdings are managed in a passive or collusive way.[59] Individual portfolio managers, operating mainly within banking groups, have no discretionary power with regard to the voting rights attached to the shares held on behalf of their clients, so they cannot exercise any direct role in corporate governance. Banks' direct holdings in non-financial companies are negligible.[60] Third, Italian mutual fund management companies are the most important asset managers in the Italian financial market: at the end of 1998 they managed assets worth approximately 400 billion Euros, compared to the 280 billion Euros managed by individual portfolio managers, the 105 billion Euros managed by insurance companies and the 60 billion Euros managed by pension funds.[61] Furthermore, the mutual funds invest in shares much more than the other Italian institutional investors: at the end of 1998, the investments in Italian stock carried out by the mutual funds represented 10 percent of the assets they managed, while this percentage was about 7 percent for insurance companies, 5 percent for individual portfolio managers and 3 percent for pension funds.[62] Our analysis has been conducted using a database which includes:

- ❖ holdings greater than 2 percent of voting capital in Italian listed companies at the end of 1998, as published by Consob in accordance with the listed companies' ownership disclosure requirements; this data set is our only source of information for shareholdings held by foreign asset managers; we lack, in other words, data on such managers' holdings lower than 2 percent;
- ❖ all the stakes held by Italian mutual fund management companies at the same date, as gathered by the Bank of Italy.

We are talking about 3,480 stakes,[63] 3,409 of which being held by 59 Italian mutual fund management companies and 71 (all of which, as we said, greater than 2 percent) by 35 foreign asset management companies. The companies for which at least one stake held by an institutional investor is present are 184 out of a total of 218 listed companies.

A. Institutional investors' shareholdings. – The first variable we mentioned in Part I concerns the shareholdings held by each single institutional investor. As we saw, activism might be expected only by institutions holding individually a sufficiently high stake in the company.

At the end of 1998, 43 percent of the 3,409 stakes held by Italian mutual fund management companies in listed companies were lower than 0.1 percent of the capital; 39 percent were between 0.1 and 0.5 percent of the capital, and 11 percent were between 0.5 and 1 percent. Only 7 percent of the stakes (221 holdings) were greater than 1 percent. Since the T.U. grants minority rights to shareholders representing more than 1 percent of the capital (see Part III), we call these 221 holdings the relevant shareholdings for institutional investor activism. Among these, 160 are between 1 and 2 percent of the capital, and the remaining 61 are between 2 and 5 percent. No stake is above 5 percent, in accordance with the limits imposed by the rules prohibiting higher holdings by each management company (Table.1). The relevant shareholdings are held by 24 Italian management companies.

At the end of 1998, foreign institutional investors held 71 relevant shareholdings. More than two thirds of these (49 stakes) were between 2 and 5 percent of the voting capital, about one fourth (17 stakes) were between 5 and 10 percent, while 5 stakes were greater than 10 percent (Table 1). The foreign asset management companies' holdings were in the portfolio of 35 institutions.

[58] See Enriques, 1999.

[59] Excluding the blocks (held mainly in other insurance companies or in banks) granting insurance companies the sole control of a listed company, at the end of 1998, insurance companies hold a total of 45 blockholdings; in 29 cases, insurance companies take part to shareholders agreements granting them joint control of the investee company. Fourteen of these 29 holdings are in banks while 15 are in non-financial companies. The remaining 16 blockholdings by an insurance company are, in most of the cases, held in companies affiliated to groups including also other firms in which the same insurance company is part of the controlling coalition. Their role as institutional investors can thus be conditioned by strategic bonds with such groups.

[60] See Bianco and Chiri, 1997.

[61] Source: Assogestioni's website (www.assogestioni.it).

[62] See Banca d'Italia, 1999.

[63] We take into account only full-voting shares. We do not consider preference shares, which give voting rights only in the extraordinary shareholders' meetings (see *infra*, Part III.E). This could be partially misleading when we analyze the availability for institutions of minority shareholder powers (see Part III), some of which are granted to shareholders representing a proportion of the voting capital. However, preference shares represent a small fraction of the equity issued by Italian listed companies: only 9 out of 218 listed companies have issued preference shares, representing an average of approximately 10 percent of the voting capital of the issuing companies.

Table 1. Institutional investors' shareholdings in Italian listed companies
(number of holdings by class of voting capital held – 31 December 1998)

% of voting capital	number of holdings		
	foreign management companies (1)	Italian management companies	total
<0.1%	n.a.	1468	1468
0.1%-0.5%	n.a.	1343	1343
0.5%-1%	n.a.	377	377
1%-2%	n.a.	160	160
2%-5%	49	61	110
5%-10%	17	-	17
>10%	5	-	5
Total	71	3409	3480

(1) Only for holdings higher than 2 percent.

Therefore, 292 are the relevant shareholdings held both by Italian mutual fund management companies and by foreign asset management companies. These holdings regard 119 listed companies out of a total of 218; 17 of them are among the 30 companies whose shares compose the largest companies Italian Stock Exchange Index (mib30). Over 40 percent of relevant shareholdings are concentrated in the hands of 5 mutual fund management companies, holding more than 20 relevant shareholdings each. Assuming that the probability that an institution becomes active is positively correlated with the number of relevant shareholdings held,[64] these 5 mutual fund management companies – leaving aside for the moment the possibility that other counterbalancing factors may be in place – can be considered good candidates for activism.

B. Investment strategies. – The second variable to be examined regards the investment strategies followed by management companies. Our data do not provide significant information about whether institutional investors tend to adopt indexing or other investment strategies.[65]

However, our database allows us to analyze the concentration of the Italian mutual fund management companies' portfolios invested in Italian listed shares (both in absolute and relative terms).[66] This analysis may provide an indirect indication of mutual fund management companies' investment strategies.

Our analysis is aimed, in particular, at singling out the investors with equity portfolios so concentrated as to make it worth focusing their attention on a restricted number of companies in order to undertake proactive initiatives.

We find an average of 58 shareholdings per fund management company. Therefore, the average portfolio includes about 25 percent of the total number of listed companies, with a narrow variance of data: only 3 portfolios include less than 10 percent of total listed companies, and, on the other side, only 5 portfolios include more than 40 percent (Table 2). Portfolio diversification is thus relatively low, even when taking into account that some of the 218 listed companies' stock is very illiquid. As we mentioned in Part II.A, institutions tend to privilege liquid securities even when they adopt stock picking policies. Such a tendency is of course strengthened in the case of open-end funds, because of the short-term structure of their liabilities.

If we consider the market value of the mutual fund management companies' holdings, we find that the largest stake (c1) is on average equal to 11.1 percent of the total value of each mutual fund management company portfolio, the largest three stakes (c3) equal 29.5 percent, the largest 5 (c5) equal 43.1 percent and the largest 10 (c10) equal 63.1 percent (Table 3). These data also reflect the high concentration of the Italian stock market: the values of the concentration indexes for a stock market portfolio (c1 = 10 percent, c3 = 28 percent, c5 = 42 percent, and c10 = 56 percent) are just a little lower than the average mutual fund portfolio.

[64] The intuition behind this assumption being that there should exist economies of scale in the monitoring activity. Cf. Blair, 1995.

[65] The indexing strategy is not expressly declared by any Italian fund management company. Some recent studies have compared the yield of mutual funds with the yield of benchmarks such as the most common stock exchange indexes. These studies provide different answers to the question whether it is common for Italian fund management companies to adopt *de facto* passive strategies. Beltratti and Miraglia, 1999, find a difference of returns which would support the hypothesis of active policies; Hamaui and Ratti, 1999, conclude that most of the funds follow passive strategies. Cesari and Panetta, 1998, find that Italian equity funds' performance (evaluated on the basis of gross returns) has been consistently better than the market's.

[66] The analysis of portfolios concentration can be conducted only on the Italian mutual fund management companies, since the available data for the foreign asset management companies, which includes only shareholdings higher than 2 percent, does not allow calculating their portfolio concentration.

Table 2. Distribution of Italian mutual fund management companies by number of shareholdings in Italian listed companies, 31 December 1998

number of holdings (in % of total number of listed companies)	number of fund management companies
<10%	3
10%-20%	15
20%-30%	17
30%-40%	19
40-50%	3
>50%	2
Total	59

Table 3. Concentration of Italian mutual fund management companies' portfolios (Average % of portfolio value - 31 December 1998)

	mean	minimum	maximum	standard deviation
C1 (1)	11,1%	6,5%	17,7%	0,02
C3 (2)	29,5%	18,2%	47,3%	0,05
C5 (3)	43,1%	27,9%	64,8%	0,06
C10 (4)	63,1%	43,8%	90,7%	0,08

(1) Value of the largest holding as a percentage of total portfolio value. (2) Value of the sum of the largest three holdings as a percentage of total portfolio value. (3) Value of the sum of the largest five holdings as a percentage of total portfolio value. (4) Value of the sum of the largest ten holdings as a percentage of total portfolio value.

Even though portfolio concentration is homogeneous enough among the various fund management companies, we identified the 21 mutual fund management companies, out of 59, showing an above average portfolio concentration with regard to the three largest stakes (c3). The low number of stakes held on average by the majority of mutual fund management companies compared to the total number of listed equity securities and the sufficiently high concentration of their portfolios should encourage active policies with regard to portfolio companies. Furthermore, the high average "overweighting"[67] of the single mutual fund management companies' holdings, compared both to the composition of the aggregate Italian equity portfolio of all the mutual fund managers and to the aggregate market portfolio, suggests that their portfolios are also sufficiently differentiated among each other. These differences should reduce free-riding problems. In the light of these data, we can now integrate the data provided in Parts II.A and II.B. In Part II.A we identified 24 Italian mutual fund management companies holding at least one relevant shareholdings (more than 1 percent of the investee capital), and found 5 good candidates for activism, i.e. the institutions holding more than 20 relevant shareholdings. Now, we see that, out of the remaining 19, 6 mutual fund management companies, holding together 21 relevant shareholdings, present a high portfolio concentration (considering the first three stakes, c3). If we consider both the "specialization" of investments in relevant shareholdings (as identified in Part II.A) and the concentration of portfolios (as identified in Part II.B) as requirements for activism, we end up with 11 potentially active mutual fund management companies, owning together 146 relevant shareholdings in 85 listed companies (representing approximately one third of the total stock exchange capitalization).

C. Ownership of institutional investors and conflicts of interest. – The third relevant variable to be considered here regards the institutional investors' ownership structure, in the light of the risk of conflicts of interest, which may be related to it. The Italian mutual fund management companies belong, in the majority of cases, to diversified financial groups, i.e., groups carrying out more than one activity of financial intermediation: 47 mutual fund management companies out of 59, representing about 99 percent of the total assets managed, are part of bank groups or insurance groups, with a clear prevalence of the former. The "independent" management companies, i.e., those not belonging to bank or insurance groups are 12, but they have a very low market share (1 percent in terms of managed assets) and operate in small market niches (Table 4).

[67] The weight of each holding within the portfolio of a single mutual fund management company is on average 6 times the weight of each investee company's equity within the overall Italian equity portfolio of all the mutual fund management companies. The weight of each of the relevant shareholdings within the portfolio of a single mutual fund management company is on average 17 times the weight of each investee company's equity within the overall Italian equity portfolio of all the mutual fund management companies. We obtain lower values, but nonetheless significant (respectively equal to 3 and 13), by comparing the weight of each holding within the portfolio of the single mutual fund management company with the weight of each investee company with reference to the total capitalization of the stock exchange.

Table 4. Ownership of Italian mutual fund management companies, 31 December 1998

Owner	number of fund management companies	funds managed (as a % of total)	shareholdings in the Italian listed companies		
			number of holdings	holdings value (as a % of total)	number of relevant holdings (1)
Insurance group	8	5,0%	417	7,4%	12
Banking group	39	93,9%	2499	90,4%	205
Independent	12	1,1%	493	2.2%	4
Total	59	100%	3409	100%	221

(1) See note to Table 2.

The predominance of diversified financial groups in the Italian mutual funds market is also confirmed with specific regard to the assets invested in Italian equity: most of the shareholdings are held by mutual fund management companies belonging to such groups (about 85 percent of the holdings, representing 98 percent of mutual funds' overall portfolio). Within financial groups, there is a predominance of banking groups (Table 4).

Of the 221 relevant shareholdings only 4 belong to "independent" mutual fund management companies, 205 belong to mutual fund management companies affiliated to banking groups and 12 are held by mutual fund management companies affiliated to insurance groups (Table 4).

Sub B, we identified 11 mutual fund management companies with the highest potential for activism: only one of these is independent, and holds only one relevant stake. The other 10 mutual fund management companies all belong to banking groups. Furthermore, 8 of the mutual fund management companies which have a banking origin are controlled by banks listed on the stock exchange.

As we noted in Part I, product market discipline may help to curb the problem of conflicts of interest and their negative effect on activism. The fact that most mutual funds are controlled by banks is negative from this point of view, because banks' clients buy not only investment services from their banks (which are in fact the distribution channels for their mutual funds), but also other financial services, and specifically, banking services. The result of this is that the costs borne by clients to switch to another investment manager are higher, because one usually switches the whole cluster of services one buys from the bank. Hence, dissatisfaction with investment management services results may not automatically drive clients to switch to another intermediary, if they are satisfied on the whole with the bank's services or have a strong tie with the bank (for instance, because it has granted them loans). The allegedly high level of management fees charged by Italian mutual fund companies compared to those charged by American ones confirms the low degree of competition among mutual funds in Italy.[68]

D. Ownership structure of listed companies. – The ownership structure of Italian listed companies, notwithstanding the profound changes which have recently occurred following the privatization process, is characterized by a high level of concentration and limited contestability of control. The privatization of large companies, which has mainly occurred through public offerings, has in fact considerably reduced the average ownership concentration: floating capital has risen from 38.9 percent in 1986 to 56.5 percent in 1998, but there remain many companies controlled by one shareholder or by a coalition of shareholders with very high ownership shares (Table 5): public companies, defined as companies in which no controlling shareholder or coalition can be identified, at the end of 1998 were 35 out of a total of 218 listed companies. For 128 of the other 183 companies the control share is held by a single shareholder and is greater than 50 percent of the capital (absolute majority); for 31 companies the control share is held by a single shareholder and varies between 30 and 50 percent, with an average of 40 percent (de facto control); finally, for 24 companies the control share is held by a coalition of stockholders and is on average equal to 50 percent.

[68] See Oddo, 1999a, who so concludes on the basis of data provided by Mediobanca. And see also Oddo, 1999b (reporting the opinion of a director of an Italian investment company according to whom all Italian mutual funds investing in equity are heavily indexed, but charge fees which would be justified only if they did stock picking, and concluding that there is no competition among Italian investment management companies).

Table 5. Models of control of Italian listed companies, 31 December 1998

model of control (1)	number of companies	market value (in % of total)	average controlling share
absolute majority	128	32.3%	63.1%
"de facto" control	31	21.7%	40.7%
coalition control	24	7.4%	49.6%
public companies	35	38.7%	-
total	218	100%	57.6%

(1) See text for definitions.

Considering the control model of listed companies (Table 6), we find that institutional investors (considering both the Italian fund management companies and the foreign asset management companies) invest more in public companies (with an average of 25 holdings per company and 10,4 percent of capital held) and in *de facto* control companies (21 holdings per company and 8,1 percent of capital held) than in "absolute majority" companies and coalition-controlled companies (for both of which we observe an average of 13 holdings per company and respectively 5,7 and 6,8 percent of capital held).

Table 6. Institutional investors' shareholdings by model of control of portfolio companies, 31 December 1998

model of control (1)	average aggregate share of voting capital held (2)	average number of holdings per company	
		held by foreign management companies	held by Italian management companies
absolute majority	6,8%	0,3	12,5
"de facto" control	8,1%	0,3	20,7
coalition control	5,7%	0,2	13,3
public companies	10,4%	0,5	24,1
total	7,5%	0,3	15,6

(1) See text for definitions
(2) By all institutional investors.

There seems to be a positive correlation between institutional investors' equity investment decisions and the degree of contestability of control of the investee companies: institutional investors tend in fact to invest more in companies where control is more fragile, even if this relation is not so strong as we expected (considering that for the controlled companies the floating capital is on average lower than 50 percent).

However, it must be considered that public companies also tend to be larger and, therefore, the greater tendency of institutions to take on such shares could also depend on the size factor. In order to verify the incidence of these two factors (size and control model), we calculated the correlation coefficient between each of these two variables and the total share held by institutional investors in the single companies. The correlation with the control model (measured by control share) is of the expected sign (negative) and significant (–0.30), while the correlation with company size (measured by market capitalization) is approximately null (0.06), even if we consider only the market capitalization of the floating capital (0.08). Therefore, we can assume that the size factor does not affect significantly the concentration of mutual funds investments in companies with less stable control.

E. Co-ordination among institutional investors. – An important element affecting institutional investor activism is represented by the costs of co-ordination among institutional investors, which must normally be faced in order to take proactive initiatives. Such costs obviously equal zero when a single fund holds enough shares, while they grow as the number of funds having to co-ordinate their actions increases and the stake held by each of them decreases.

In this paragraph, we find the aggregate share held on average by the institutional investors (considering both the Italian mutual fund management companies and foreign asset management companies) with the largest holdings in each company, in order to find out whether this aggregate share is higher than the thresholds defined by the T.U. for the exercise of minority shareholders' rights.

The average largest stake held by institutional investors is 2.5% of the voting capital. This percentage increases to 5.3% if we consider the five largest stakes and to 7.2% considering the twenty largest stakes (Table 7).

Table 7. Shareholdings of groups of institutional investors by model of control (1) of listed company held (average share as a % of voting capital - 31 December 1998)

	absolute majority	de facto control	coalition control	public companies	total
largest investor	2,3%	2,1%	2,1%	3,5%	2,5%
3 largest investors	4,2%	4,0%	3,5%	6,1%	4,4%
5 largest investors	5,1%	5,0%	4,2%	7,2%	5,3%
10 largest investors	6,0%	6,4%	5,0%	8,7%	6,4%
20 largest investors	6,6%	7,6%	5,5%	9,8%	7,2%

(1) See Part II. D for definitions

The concentration on the largest institutional investors shareholdings seems to be affected by the control model of the investee listed companies: the concentration for public companies is notably higher than the average one (Table 7).

Albeit lower than the comparable data on U.S. companies[69], the data on institutional investors' shareholdings in Italian listed companies do not appear to be discomforting, especially if one considers that our data strongly underestimate the presence of foreign investors.[70] Furthermore, we are talking about mean values, which reflect a very diverse reality: if we consider, for example, the data on the share held by the largest institution, while the average value is 2.5 percent, the median is 1.5 percent and the highest and lowest figures are respectively 19.74 percent and 0.04 percent. We have also verified in how many cases institutions' holdings exceeded specific capital thresholds. We singled out the thresholds (1 percent, 5 percent and 10 percent) on the basis of the legal rules granting shareholder rights, which the institutions can use in order to engage in proactive initiatives (see Part III).

The overall participation of the institutional investors considered as a whole is greater than 1 percent for 162 companies, greater than 5 percent for 106 companies and greater than 10 percent for 52 companies (Table 8). In order to evaluate the real possibility of such companies becoming the targets of active institutions, taking also into account the coordination problems between institutional investors, we considered the share held by the largest investor and the share held by the 3, 5 and 10 largest investors (Table 8). For over half of the listed companies (118 out of 218) the share held by the largest investor exceeds the threshold of 1 percent. In 20 companies, at least one holding greater than 5 percent can be observed, while a holding greater than 10 percent is present in only 5 companies.

If we consider the five largest investors, whose coordinating costs can be considered manageable in the light of the Anglo-Saxon countries experience, we observe figures notably higher for the 5 percent threshold (72 companies), and for the threshold of 10 percent (24), while they remain substantially the same for the 1 percent threshold. The percentage of companies for which the relevant thresholds are crossed by institutions increases as the stability of control decreases: considering the aggregate holdings of the 5 largest institutional investors, the percentage of companies for which the relevant thresholds are crossed is higher for public companies (86 percent for the 1 percent threshold, 46 percent for the 5 percent threshold, and 17 percent for the 10 percent threshold) than for the controlled companies (72 percent, 31 percent, and 10 percent, respectively).

Finally, it has to be mentioned here that Italian mutual fund management companies are all members of Assogestioni, an association of asset management companies that has taken some initiatives in the corporate governance field.[71] This association is often where active institutions have coordinated their efforts before starting their initiatives.[72]

F. Conclusions. – In this Part we gave some quantitative elements concerning the potential role of institutional investors in the corporate governance of Italian listed companies. We concentrated our analysis on Italian mutual fund management companies and, only for some aspects, on foreign asset management companies. The main findings can be summarized as follows. There is a considerable number of shareholdings exceeding 1 percent of the voting capital: 292 shareholdings concerning 119 listed companies out of a total of 218. Furthermore, we identified a high concentration of shareholdings, in particular for Italian mutual fund management companies: 5 fund management companies, each holding more than 20 relevant shareholdings, have more than 40 percent of the total relevant shareholdings.

[69] According to Coffee, 1994, in 1991 the five largest institutional investors held 10.6% of the voting capital of the top 25 U.S. listed companies and the twenty largest institutional investors held 22.2%.

[70] Il Sole 24 Ore, 1998, reports data provided by Telecom Italia, according to which on 31 March 1998 institutional investors other than those taking part to the "noyeau dur" of such company held 54 percent of its outstanding voting shares, compared to the 10 percent resulting from our data.

[71] See Assogestioni, 1999.

[72] See Cortesi and Musile Tanzi, 1998.

Table 8. Italian listed companies where institutional investors' holdings are higher than the activism thresholds (31 December 1998)

	activism thresholds					
	1% (1)		5% (2)		10% (3)	
	number of companies	as a % of total	number of companies	as a % of total	number of companies	as a % of total
largest investor	118	53%	20	9%	5	2%
3 largest investors	159	72%	56	25%	17	8%
5 largest investors	161	72%	72	32%	24	11%
10 largest investors	162	73%	95	43%	35	16%
all investors	162	73%	106	48%	52	23%

(1) Percentage required soliciting proxies.
(2) Percentage required to bring a derivative action against directors and to file an art. 2409 complaint.
(3) Percentage required calling a shareholders' meeting.

The analysis of the portfolio concentration of Italian mutual fund management companies suggests the prevalence of non-indexing approaches. This can reduce the negative impact on activism of the free-riding problem. By focusing on the "specialization" of investments in relevant shareholdings and on the concentration of portfolios, we identified 11 mutual fund management companies with a high potential for activism: they hold 146 shareholdings in 85 listed companies (about 40 percent of the total).

Most Italian mutual fund management companies belong to banking and insurance groups: 39 mutual fund management companies are controlled by banking groups and 8 by insurance groups; only 12 are independent, and they have a very limited share of the market. Ten bank-controlled management companies hold 145 of the 146 shareholdings with a high potential for activism, emphasizing the risk that conflicts of interest prevent such management companies from taking an active stance.

The control structure of the listed companies is another factor that can negatively affect institutional investor activism: 183 out of 213 listed companies are controlled by a single shareholder or by a coalition of shareholders and the control stake is in general very high. For these companies, the managers are virtually entrenched, and will normally be little bothered by institutions' initiatives. The fact that institutional investors invest more in companies with a weaker control structure offsets this problem to some extent. To conclude, institutional investors seem to be in a position to play a role in the corporate governance of Italian listed companies: they hold many relevant shareholdings and their portfolios are sufficiently concentrated; coordination problems do not seem to be serious: the largest five institutional investors' shareholdings exceed the relevant thresholds of 1, 5 and 10 percent respectively in 72, 33 and 11 percent of listed companies. To be sure, conflicts of interest, due to the dominance of the mutual fund market by banking groups, together with the concentrated ownership structure of listed companies, can be an obstacle to activism. The importance of the former factor may, however, diminish in the future if one considers that conflicts of interest are relevant only for Italian fund management companies, or at least much more for them than for foreign management companies, whose presence is growing in the Italian market.[73]

III. Has the T.U. Provided a More Favorable Legal Environment for Institutional Investor Activism in Italy?

Having concluded in Part II that the possibility that mutual fund management companies and foreign institutions play an active role in the monitoring of Italian listed companies is not to be excluded in the light of the empirical analysis we provided, we can turn to the question whether the T.U. provided a more favorable legal environment for institutional investor activism.[74]

A. Limits to holdings. – Before the T.U., the law regulating open-end mutual funds provided that any mutual fund management company may not hold together more than 5 percent of any listed company's outstanding voting shares or, in any case, a number of shares permitting the management company to exercise significant influence over the management of the issuing company.[75] Moreover, the law previously imposed minimum diversification rules, according to which no more than 5 percent of a mutual fund's portfolio could be invested in securities issued by the same issuer.[76] The T.U. has modified this legal regime by delegating the power to define holding limits to the Treasury and to the Bank of Italy. The Government has introduced a distinction, for-

[73] The number of relevant shareholdings held by foreign institutional investors in the Italian listed companies has increased from 46 at the end of 1996 to 71 at the end of 1998, and their weight on the stock-exchange capitalization has almost doubled in the same period (from 0.38 percent to 0.70 percent).
[74] Consistently with the premises of Part II, we will continue to restrict our analysis to mutual funds.
[75] See Directive n. 85/611/CEE.
[76] The limit was 10 percent, provided the total holdings representing each more than 5 percent of the portfolio do not exceed 40 percent of the mutual fund's portfolio.

merly unknown to Italian law, between harmonized and non-harmonized open-end mutual funds.[77] In September 1999, the Bank of Italy has provided that:

❖ non-harmonized and harmonized open-end mutual funds managed by the same investment management company may not hold together more than 10 percent of any listed company's outstanding voting shares or, in any case, a number of shares permitting the investment management company to control the issuing company;

❖ no more than 5 percent of a mutual fund's portfolio can be invested in securities issued by the same issuer. With regard to listed securities, the limit rises to 10 and 15 percent respectively for harmonized and non harmonized mutual funds, provided, in both cases, the total holdings representing each more than 5 percent of the portfolio do not exceed 40 percent of the mutual fund's portfolio.

B. Rules discouraging the building of control blocks and legal obstacles to co-ordination. – As we have just seen, mutual funds may not hold blocks allowing them to exercise a control over portfolio companies.[78] If several institutions co-ordinating their action were to put together a stake which allowed any of them to exercise control, the directors of the mutual fund exercising it would risk a fine and removal from office by the supervisory authorities. A set of rules which may put an obstacle to institutions' co-ordinating efforts is the one concerning shareholders' agreements.[79] Article 122 of the T.U. provides that shareholders' agreements regarding the exercise of voting rights or the acquisition of the company's stock, those limiting the freedom to sell shares, and those aiming at the exercise of (joint or individual) control over the listed company must be immediately disclosed to the public. If they are not, any shareholders' resolution passed with the determining vote of such shareholders is voidable and shareholders (or, if shareholders are themselves companies, their directors) are liable to a fine. Suppose there is a group of institutions willing to co-ordinate their monitoring activities and finding it convenient, for instance, to commit to a certain voting behavior: these institutions may either avoid formal commitments or have to disclose their full content to the public. In the former case, it will be more difficult for institutions to commit each other to co-operative behavior (because there will be no binding agreement among them), and they will in any case face the risk that a court will hold that a shareholders' agreement exists among them. In the latter case, they will face the compliance costs of such disclosure rules and have no choice between keeping their initiative secret and making it public: they will have to disclose their plans, even if their best course would often be to act behind the scenes.[80]

C. Rules on conflicts of interest. – Before the T.U., there were neither rules mandating or urging activism on the part of mutual funds nor rules concerning the corporate governance of mutual fund companies designed in order to ensure that their management would act independently and in the interests of the unit-holders. The T.U. and its connected regulations have not introduced rules of either kind. The only provision that can be recalled here is the one according to which "voting rights attaching to the financial instruments belonging to the funds under management" have to be exercised "in the interests of the unit-holders". This rule does not mean that it is mandatory for mutual fund management companies to exercise the voting rights, but only that all decisions regarding voting rights (i.e., whether and how to vote) have to be taken in the interests of the unit-holders.[81]

D. Mandatory disclosure. – A critical issue for the governance of Italian listed companies is information. Traditionally, due to cultural and tax reasons and to the lack of satisfactory mandatory disclosure rules, Italian companies have disclosed too little information to the market. In the nineties, partly owing institutional investor pressure on companies,[82] the situation has greatly improved, but the standards still can hardly be said to be up to those prevailing in American and British markets.[83] The T.U. and the Consob regulation implementing it have, however, significantly improved the legal framework for company disclosure: first, the law now imposes full disclosure of information regarding not only the listed company, but also the companies it controls and those controlling the listed company; second, agreements among shareholders of the listed company or among shareholders of a company controlling a listed company have to be fully disclosed, thereby making it easier for investors to identify the true controllers of listed companies; third, the Con-

[77] See "Regolamento recante norme per la determinazione dei criteri generali cui devono essere uniformati i fondi comuni di investimento", adopted by the Ministry of the Treasury with the Decree 24 May 1999, n. 228, articles 8 and 9. Before 1998, open-end investment funds in Italy were regulated in conformity with the UCITS Directive and non-harmonized open-end investment funds were not allowed under the Italian law.

[78] Until September 1999, the Bank of Italy forbade mutual funds to be part of shareholder agreements granting the control of the company. See Lener, 1999.

[79] See Cariello, 1999.

[80] As we hinted above (see *supra*, note 54), most of the institutions' initiatives in the U.S. and in the U.K. do not become known to the public, because institutions usually prefer so.

[81] See Costi, 1998.

[82] See *supra*, note 54.

[83] As an example, one may consider the disclosure rules on related party transactions: while they are very stringent both in the U.S. and in the U.K., in Italy listed companies are still required to provide very little information about them. For a comparative analysis of these rules in the legal systems just mentioned, see Enriques, 1998a.

sob regulations now impose quarterly reports and full disclosure of directors' compensation.

Improved regulation and enforcement on mandatory disclosure has clearly a positive impact on institutions' willingness to become active. In fact, the lower the disclosure standards of listed companies, the more heavily institutions depend on managers to leak (soft) information, and hence the less free they are to confront managers.[84] Threats to challenge managers' choices with a public campaign, thus probably breaking the relationship with the managers, are more credible when the informational disadvantage of investors with no access to soft, or in any case privileged information, is smaller, *i.e.*, when mandatory disclosure rules are more effective.

E. The new rules on shareholders' meetings. – In Italy, as in many other European countries, shareholders' meetings have traditionally had wider powers than in the U.S. According to the Italian Civil Code, ordinary shareholders' meetings are called to "approve" the annual accounts (thereby giving shareholders the chance of expressing their satisfaction with the management of the company and with the information provided in the accounts), to appoint directors and members of the board of auditors (every three years), to determine (in part) their compensation, to authorize liability suits against directors and members of the board of auditors (this power being partly derogated by the T.U., as we shall see in Part III.F), and to authorize buybacks. Extraordinary shareholders' meetings are called to change the company's bylaws (this meaning that new issues of shares, mergers and spin-offs have to be authorized by the extraordinary meeting) and to authorize issues of debt securities called "obbligazioni". The T.U. has increased the role of shareholders' meetings in the key area of takeovers, by prescribing that defensive tactics may be adopted during a takeover bid only after the shareholders' meeting has authorized them with the favorable vote of at least 30 percent of the outstanding shares (Art. 104). This innovation provides institutional investors with a significant arbitration power during control contests.[85] The bargaining power of institutions vis-à-vis managers of underperforming companies which may become a takeover target is thus increased.

The new rules on majorities required for the validity of shareholders' resolutions may also strengthen active institutions' bargaining power. The T.U. provides that extraordinary shareholders' meetings held at first, second, or third call shall adopt resolutions with the favorable vote of at least two thirds of the capital represented at the meeting. Prior to the T.U., such resolutions were adopted by a majority of the shareholders represented at the meeting, provided they represented at least one fifth of the outstanding shares.[86] The new rules increase the probability of a shareholder's vote being pivotal in extraordinary meetings. Institutions' threat to veto managers' proposals on strategic issues will thus be more credible and effective and institutions' bargaining power greater.[87]

We have verified how often institutions hold a "blocking minority" in the MIB30 companies (i.e., the 30 most liquid – and hence normally the largest – listed companies). Assuming that only the controlling shareholders (single or coalitions)[88] and the institutional investors vote in the shareholders' meetings,[89] we found that all of the institutions as a group (Italian fund management companies and foreign management companies with stakes higher than 2 percent) hold a blocking minority in only 5 companies. Assuming that only the controlling shareholders and the 10 largest institutions vote, the institutions have a blocking minority in only 3 companies.[90]

According to the Civil Code, shareholders representing at least one fifth of the outstanding shares may ask directors to call the meeting without delay. If directors fail to do so, shareholders may ask for a court order calling the meeting and directors may be held criminally liable for their omission.[91] For listed companies, the T.U. makes it (slightly) easier for minority shareholders to call shareholders' meetings, providing that shareholders representing at least one tenth of the outstanding shares (or the lower percentage prescribed by the company bylaws)[92] may ask directors to call the meeting within 30 days. How-

[84] Cf. Monferrà, 1998.

[85] As hinted above, this is exactly what happened during the Olivetti/Telecom contest, the outcome of which was decided after the decision by many institutions' not to take part to the shareholders' meeting called to authorize Telecom's defensive tactics.

[86] Art. 2369-*bis* cod. civ., repealed by the T.U.

[87] In the Summer of 1999, investment funds opposed the merger between Riva Finanziaria (a listed company) and Intek (the company controlling Riva Finanziaria with 29.95 percent of the shares) on the account that the exchange ratio would be unfair to Riva's shareholders; institutions tried to form a coalition of shareholders big enough to veto the merger proposal at the shareholders' meeting, in order to obtain a fairer evaluation of their shares. See Martino, 1999.

[88] In the case of public companies, for which it was impossible to identify a controlling shareholder, we considered the shareholdings held by the informal coalition which appointed the board of directors at the latest shareholders' meeting.

[89] More precisely, we assumed the percentage of capital represented at the meeting to be the sum of the control block and of the share held by institutional investors and saw how often institutions put together more than one third of this sum.

[90] Assuming further that only the controlling shareholders and the 5 largest institutions vote, the institutions put together the blocking minority in only 3 companies. No single institution holds a blocking minority stake.

[91] Artt. 2367 and 2630 Cod. Civ.

[92] If the request is presented by shareholders representing one fifth of the shares, the Civil Code applies.

ever, within the same time limit, the directors, in view of the items to be discussed, may, in the company's interest,[93] decide not to do so. In such case, the shareholders requesting the meeting may petition the court to order the meeting to be called (Art. 125). The right to call the shareholders' meeting as recognized by the T.U. does not significantly favor institutions willing to take an active role. Not only is the percentage of capital required so high as to make it impossible for single mutual funds to exercise the right (so that co-ordination among them will always be necessary and very often insufficient),[94] but the "right" itself is very weak, since it is not self-enforcing (as the analogous right is, for instance, in the U.K.):[95] if directors refuse to call the meeting, institutions must turn to the courts, with all the costs this entails. A major shortcoming in the corporate law reform (as analyzed from the point of view of its ability to favor institutional investor activism) is that it grants no right to present shareholder proposals. To be precise, in the absence of any specific rule, the only way for shareholders to submit an issue to the shareholders' vote is by calling for a shareholders' meeting under Art. 125. In other words, shareholder proposals may be presented only by shareholders representing at least 10 percent of the shares, and directors may, in the company's interest, refuse to submit the proposal to the shareholders' vote. In the light of the role played by institutional investors' proposals in the U.S., their very restricted availability for shareholders of Italian companies deprives potentially active institutions of an effective bargaining tool.[96] An important innovation of the T.U. is the new regime for proxy solicitations. Before the T.U., proxy solicitations were not prohibited, but the proxy rules introduced in 1974 were so strict (especially in that they provided that no one may represent more than 200 shareholders in a meeting) that proxy solicitations were unknown to the Italian corporate governance system[97]. The T.U. does not repeal the 1974 rules, but declares that they do not apply to proxy solicitations promoted pursuant to the rules established by the T.U. and Consob. These rules also are, however, quite restrictive. In fact, not everyone is allowed to solicit proxies for a company's shareholders' meeting: the T.U. provides that only shareholders representing at least 1 percent of the outstanding shares, and having held such stake at least for six months prior to the shareholders' meeting, may do so.[98] Moreover, shareholders soliciting proxies are obliged to avail themselves of an intermediary (either a bank, or an investment services company, or a mutual fund management company, or a proxy services company),[99] charged with making contact with the shareholders and guaranteeing that the information provided by the solicitor in the proxy documents is complete. Consob authorizes proxy solicitations after checking that the proxy documents contain all the information required. The 1 percent threshold is sufficiently low to make the power of soliciting proxies an option available to institutions. A stake higher than 1 percent is held by a single institution in 118 of the 218 listed companies and in 17 of the MIB30 companies. The five largest institutions hold a stake higher than this in 161 listed companies. In March 2000, Consob made use of the power granted by art. 139 of the T.U.,[100] reducing the 1 percent threshold to 0.5 percent for one fifth of the listed companies, those with the highest market value of the floating capital. If this threshold had been in force in December 1998, a single institution would have been able to solicit proxies for the shareholders' meetings of 137 companies, and for the shareholders' meetings of all of the MIB30 companies. According to prevailing case law, confidential voting is not allowed under Italian law.[101] The T.U. does not bring any change in this respect, which, as we saw before, may be crucial for the success of institutions' initiatives.[102] Moreover, the T.U. did very little to lower the cost of voting by institutions. First, voting by mail, which was previously prohibited but for privatized companies (for which it was mandated), has been made possible, but it is up to the company bylaws to decide whether to introduce it. No listed company, as far as we know, has done so. Second, the T.U. left in place the rule according to which shareholders may not delegate their voting rights,

[93] The meaning of this expression is debated. According to some, directors may take into account interests other than those of shareholders and refuse to call the meeting if they deem that such other interests should prevail (Gambino, 1998). According to others, directors may refuse to call the meeting only in the case of a frivolous request (Santoro, 1999).

[94] See Table 10: the five largest institutions hold a 10 percent stake only in 11 percent of the companies.

[95] See Section 368, Paragraphs (4) and (6) of the Companies Act 1985.

[96] See also, critically, Perna, 1999.

[97] See, *e.g.*, Jaeger and Marchetti, 1997.

[98] Art. 139, which provides that Consob may fix thresholds lower than 1 percent for companies with a high capitalization and widely dispersed ownership. As we shall see below, Consob made use of this power in March 2000.

[99] It is widely debated whether the law requires that shareholders soliciting proxies avail themselves of an intermediary also when such shareholders are themselves banks, investment services companies, mutual fund management companies or proxy services companies. See Tonelli, 1999, also for further references on this issue.

[100] See *supra*, note 101.

[101] See, *e.g.*, Campobasso, 1999.

[102] The relevance of the prohibition of confidential voting is highlighted by the Olivetti/Telecom case. During the Olivetti's bid many Italian investment fund management companies declared that they would not take part to the shareholders' meeting called in order to authorize Telecom's defensive tactics, because they would not like it to be known that they had voted in one way or another, although most of them had clear ideas on how they would have voted. See Riolfi, 1999.

once and for all, to someone like a proxy services company: they may delegate a proxy to vote only prior to each shareholder meeting (Art. 2372 Italian Civ. Cod.). Third, the T.U. did not repeal a rule stating that the right to vote may be exercised only by shareholders who deposit their shares at the company's site or at a bank at least five days before the shareholders' meeting: this means that shareholders may not vote their shares, unless they forgo the opportunity to trade them for one week.

F. Minority shareholders' rights. – An area in which the 1998 reform has brought significant changes is that of minority shareholders' rights, and it has done so by granting them to shareholders representing a proportion of the outstanding shares, ranging from 2 percent (for the right to file a complaint to the board of auditors about "censurable facts"[103]) to 10 percent (for the right to call a shareholders' meeting.)[104] The only important power which the law has granted minorities independently of their holdings is that of electing some of the members of the board of auditors. This power, however, needs to be implemented, with wide margins of flexibility, by the bylaws. And, as a matter of fact, most bylaws have provided that lists of candidates for the election of auditors may be presented only by shareholders representing a minimum proportion of the capital, ranging between 2 and 10 percent.[105] This means that, *de facto*, all such rights have been made available to: (1) to shareholders taking part, formally or informally, in controlling coalitions, (2) to raiders having built a toehold, and (3) to institutional investors. The T.U. grants minority shareholders with at least 5 percent of the capital (or the lower figure determined by the bylaws[106]) the right to bring derivative actions against directors (Art. 129) and the right to file a complaint to the court for serious irregularities by directors or members of the board of auditors (Art. 128, in connection with Art. 2409 of the Civil Code).[107] In the former case, shareholders are required to have held shares in the company for six months before filing the suit.[108] As we have shown in Part I, in the experience of British and American activism, derivative suits are very rare indeed. The prohibition on contingency fees under Italian law makes it more costly for shareholders of Italian companies to sue directors (or file an Art. 2409 complaint) than for a plaintiff shareholder in the U.S.[109] Besides, the gravity of a judicial initiative and the negative effects it would have on the relationships between fund management companies and directors make the threat of a liability suit or of an Art.2409 complaint hardly credible. Moreover, in the light of the data on institutions' shareholdings we provided in Part II, these rights can be exercised in relatively few listed companies. There are only 20 companies in which one single institution holds more than 5 percent of the shares, while the five largest institutions hold together such a share in 72 companies and in one third of the MIB30 companies.

The T.U. provides for the board of auditors to be composed of three or more members. If it is composed of three members, one of them has to be appointed by minority shareholders; if it is composed of more than three members, two of them have to be appointed by minority shareholders. Not surprisingly, most companies' bylaws have chosen a three-member board.[110] During the first year of application, Italian mutual funds have jointly presented lists for the election of auditors in many listed companies.[111] They have also presented lists of candidates for the board of directors of privatized companies for

[103] We will not deal here with such right, given the easily predictable ineffectiveness of the threat of making use of it by institutions, *i.e.*, given its irrelevance for activism: see Enriques, 1998b.

[104] See Part III.D.

[105] See Sabbatini, 1999. For example, one of the first companies to implement the T.U. rule, Fiat, which has a sort of leading role among listed companies with regard to company law issues, set a 3 percent threshold for the presentation of lists of candidates. Most other companies have followed suit.

[106] No listed company, as far as we know, has decreased the statutory percentage.

[107] Art. 2409 Cod. Civ. provides that shareholders representing at least 10 percent of the shares (5 percent for listed companies, as we said) may ask the court to order an investigation of the company by an inspector. If the inspector finds that the alleged irregularities exist, the court adopts the provisions it thinks fit and calls the shareholders' meeting for the consequent resolutions; in the most serious cases, the court may appoint a "judicial administrator", who substitutes directors and the board of auditors and who may also sue directors for liability. The appointment of a judicial administrator is very bad for directors, less because they lose their job (since they may well be re-elected by the shareholders' meeting after the judicial administration is over, if they, as often happens, still deserve the trust of majority shareholders) than because this judicial administrator is held by the law as a public official, this meaning that she has the duty to report any criminal offence she might get the knowledge of (consider that violations of tax laws and accounting laws are rather frequent in Italy, especially but not exclusively in close corporations).

[108] It is not clear whether the law requires that the 5 percent share be held for six months or that any share, however small, be held in the same period. For the latter solution, see Rossi, 1999. Nor is it clear whether the plaintiffs have to hold the share until the suit is over: for a negative answer see again Rossi, 1999.

[109] According to the T.U. (art. 129(3)), "[i]n the event of a favorable judgement, the company shall reimburse the plaintiffs the costs of the action which the judge did not charge to the defendants and which it is not possible to recover following the exhaustion of the latter's property". A similar rule applies in the case of art. 2409 complaints (see Ferrara and Corsi, 1999).

[110] See Sabbatini, 1999.

[111] For example, a group of mutual funds has presented lists for the election of the board of auditors in Unicredito, INA, Telecom Italia, and IMI-San Paolo.

which the 1994 law on privatization provides that minority shareholders have a right to be represented.[112] This shows that in Italy there are no such problems for institutions as those created by the U.S. and U.K. rules placing burdens on controlling persons etc. It is too early to judge whether auditors elected by minority shareholders, and more specifically, by institutions, will act independently of managers and what their relationships will be with the institutions electing them; more explicitly, whether boards of auditors will be more effective monitors than they have traditionally been in Italy,[113] or whether such members will just be a source of inside (soft) information for institutions.

In any case, auditors have wide powers of information: they have the right (and the duty) to take part in the meetings of the board of directors' and the executive committee, to ask directors for information about single transactions, and to make investigations at any time. However, they have no autonomous powers of reaction in the event of abuses or irregularities: they may only report their findings to the board of auditors, which will decide what to do about them. Such being the powers of individual auditors, one cannot expect that they can effectively play the role of whistle blowers, unless also the other auditors are really independent from management.

G. Summary and conclusions. – Undoubtedly, the 1998 company law reform, by granting minority shareholders more extensive powers, has strengthened institutions' bargaining powers vis-à-vis managers and controllers. Among the various minority rights we have described above, the most promising from this point of view seems to be the one allowing any shareholder holding at least 1 percent of the shares to solicit proxies. It is true that proxy solicitations are very costly.

However, given that other legal tools may be even more expensive to use (as is the case for the right to sue directors or the right to file an Art. 2409 complaint) or difficult to exercise (as is the case for the power of vetoing resolutions at extraordinary meetings and the right to call shareholders' meetings and to make shareholder proposals), proxy fights may be the best way for active institutions to confront managers unwilling to come to terms with them. To be sure, for the threat of soliciting proxies to be credible and effective, institutions should start doing it, at least sporadically. The Government's choice of granting the relevant minority powers only to shareholders assembling a specified proportion of the capital makes it often necessary for institutions to co-ordinate their action. This implies that the exercise of such rights will be more difficult, and that, *ex ante*, the threat of using them will be less effective. This is particularly true for the right to call shareholders' meetings, which is the right that needs to be used in Italy in order to make a shareholder proposal. This right may be exercised only by shareholders representing at least one tenth of the shares, a proportion which the largest institutions hold in relatively few listed companies. It is true that the T.U. enables the bylaws to fix a lower threshold for the right to call shareholders' meetings. But, it would be only as a result of institutional investors' proposals that companies might "opt-down" below the ten percent threshold.

IV. Conclusions

We have provided both an empirical analysis of the factors affecting institutional investor activism in Italy and a legal analysis of the most relevant changes in the Italian mutual funds and corporate laws, following the 1998 reform. The empirical analysis shows that institutional shareholdings and investment strategies are compatible with the hypothesis that institutional investors can play a significant role in the corporate governance of Italian listed companies. However, a curb to their playing such an active role may derive from the predominance of mutual fund management companies belonging to banking groups (giving rise to conflicts of interest) and from the prevailing ownership structure of listed companies, which are still dominated by controlling shareholders holding stakes higher than, or close to, the majority of the capital (implying a weaker bargaining power of institutions vis-à-vis controllers). The analysis of the legal changes prompted by the 1998 financial markets and corporate law reform indicates that the legal environment is now more favorable to institutional investor activism than before. However, notwithstanding that the declared purpose of the Government in the making of the reform was to enhance institutions' role in the corporate governance of Italian listed companies, the T.U. does not significantly change rules on shareholders' meetings, which make it difficult and costly for institutions to make shareholder proposals and to exercise their vote.

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[112] In the past, there have been cases of lists of candidates presented by mutual funds controlled by the same entity controlling the listed company. See Schiano, Ristuccia, and Segni, 1995.

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