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Shareholdings of alternative investment funds in listed companies and in banks

A legal perspective

S. Alvaro, F. Annunziata; with preface by M. Stella Richter jr

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Shareholdings of alternative investment funds in listed companies and in banks

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S. Alvaro, F. Annunziata***

Abstract

The harmonization of the European regulations on collective investment schemes (CIS) – with UCITS regulation first and, most recently, with the AIFM Directive - has expanded the areas of operation of asset managers. In particular, Alternative Investment Funds are emerging as increasingly relevant shareholders in listed companies and banks. In light of such market development, the paper explores the interaction of CIS regulation with corporate governance regulation and prudential supervision rules. First, the paper shows that the application of takeover rules to CIS as shareholders raises significant complexities. These complexities derive from the fact that the Italian law on listed issuers (takeovers, disclosure of significant shareholdings, groups and conflict of interest, slate voting, etc.) implicitly assumes that shareholders are mainly individuals or joint-stock companies rather than funds managed by a third party. Second, the paper discusses the issues posed by the acquisition of qualifying shareholdings in the capital of banks by CIS in the perspective of the compliance with micro-stability rules. The paper argues that the typical objectives of CIS regulations, in terms of transparency, fairness of conducts and the duty to serve at best CIS investors, may trade off with the need to ensure compliance with prudential rules for the invested company. More specifically, though the investment policies of CIS are obviously targeted to the search of the specific risk-return profile declared in the fund prospectus, the need to take into account further interests, such as stability and sound and prudent management of the invested banks, may not necessarily be in the best interest of CIS investors.

The papers are presented in their original Italian version, along with a shorter English version, that is intended to target foreign audiences, so that they may better contribute to the international debate.

JEL Classifications : K2, G1.

Keywords: Alternative Investment Funds - Collective investment schemes – Listed companies.

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Contents

Preface

*Mario Stella Richter jr**

1. According to some rather accurate investigations[1], in 2004 assets under management[2] amounted overall to USD 37.3 trillion. In the following years, this amount has constantly grown: USD 59.4 trillion in 2007, USD 63.9 trillion in 2012, USD 71.9 trillion in 2013, USD 78.0 trillion in 2014[3], USD 78.7 trillion in 2015 and USD 84.9 trillion in 2016. This in spite of the great crisis of 2007-2009[4].

Such a significant growth reflects an equally substantial increase of wealth on the investors' side, i.e. of (current or perspective) clients of the assets and wealth management industry. In 2004, the total value of investable assets amounted to USD 120.9 trillion, in 2007 it had increased to USD 159.7 trillion, in 2012 to USD 175.1 trillion, in 2015 to USD 202.3 trillion and in 2016 to USD 214.6 trillion.

A third phenomenon, directly inferable from the first two, seems significant for the purposes of our discussion: the share of wealth managed by the management industry has grown more than proportionally as compared to the increase of investable assets. In 2004, it accounted for 30.9% of the total wealth; in 2016 the assets under management represented 39.6% of investable assets.

It appears that this threefold trend – increase of wealth, increase of assets under management, increase of the share of assets under management on investable wealth – is not likely to change over the medium term.

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1 Data processed by PwC AWM Research Centre, on the basis of those taken from the following sources: Lipper, ICI, Preqin, Hedge Fund Research, EFAMA, City UK, Insurance Europe, Financial Stability Board, Credit Suisse, Towers Watson, OECD and World Bank. See PwC, *Asset Management 2020: Taking Stock*, in *Asset & Wealth Management Insights*, May 2017, at p. 5; Id., *Asset & Wealth Management Revolution: Embracing Exponential Change*, n.p., 2017, at p. 6-7.

2 This expression covers the assets managed by all types of asset and wealth managers in the world.

3 Thus, more than doubled, within ten years.

4 This growth on the global level coincided with a growth on the regional level, even if in Europe this growth was less substantial than in other geographic areas. In Europe, assets under management have increased as follows: USD 12.9 trillion in 2004; USD 21.0 trillion in 2007; USD 19.7 trillion in 2012; USD 21.9 trillion in 2016.

Some studies estimate that in 2020 investable assets will be equal to USD 284.4 trillion[5] and assets under management to USD 112.0 trillion; therefore, the penetration rate of the latter on the former should be equal to 39.4%[6]. Two-fifths of all investable assets will be managed by assets and wealth managers.

Similar estimates are made also with reference to a longer period: in 2025, investable assets could amount to USD 345 trillion and assets under management to USD 145.4 trillion, with a resulting penetration rate of 42.1%[7].

2. These numbers represent the starting point to understand the reason for the continuous and radical changes affecting the discipline of asset and wealth management, not only in Italy. These numbers justify the growth of collective investment schemes, their diversification and their increasing uses.

Moreover, the growth of the resources managed and of the size of this industry has led to employ ever new technological and IT innovations in the field of asset management, with economic and business prospects that are still to be fully comprehended. Technology is thus deeply re-designing not only the entire asset management field and the way the various phases of this industry's supply chain are organized, but also the typical risk scenarios of this type of business, where the importance of cyber risks is emerging. This determines the undoubted relevance of what is generally called, using a popular and suggestive expression, "Fintech". Artificial intelligence, robotics, big data and blockchain are changing and will increasingly reshape the ways asset management activities are carried out, not only as concerns services and activities offered to savers, but also as concerns the relations between asset managers and the companies where the latter invest.

3. In turn, all the aforementioned transformations are now raising a great number of legal issues that formerly did not exist or appeared of lesser importance, when the first attempts of a specific legislation on asset management were experimented in Italy and in Europe. It seems ages since then, but actually, it was just a few decades ago.

5 This estimate is essentially based on the growth of Gross Domestic Product.

6 See PwC, *Asset Management 2020: At Brave New World, 2014; Id., Asset Management 2020: Taking Stock, supra* note 1.

7 PwC, Asset & Wealth Management Revolution: Embracing Exponential Change, supra note 1, p. 6-7.

The current issues represent an extremely wide problematic area, which, I would say, has not even been exhaustively identified yet. This area includes – certainly not in a negligible position – the subject matters of this issue of Consob's *Quaderni Giuridici*.

At a closer look, the economic phenomena of the growth and transformation of financial wealth are those that underlie the abundance of regulatory interventions concerning the asset management industry at the international, transnational and national levels.

As rightly recalled at the beginning of the paper, one of the main streams of recent legislation results from the attempt to regulate, in a macroprudential perspective, the so-called Shadow Banking System, i.e. those intermediaries (such as, for example, loan-originating funds, hedge funds, private equity funds, venture capital funds, real estate funds, commodity funds, money market funds, infrastructure funds, etc.), which operate collecting savings and lending to businesses, similarly to the credit institutions system but without being part of it.

Obviously, an urgent need to regulate this phenomenon is felt internationally, considering its economic relevance and that in many geographical areas (Europe first) it has outdone the traditional banking system in size.

More generally, at least in the European Union, we have witnessed the construction of a second pillar of the discipline of collective investment management, aimed at regulating, by looking at the subject and not at the product, the by-now huge and varied world of asset and wealth managers, which comprises all that is not included in the category of *Undertakings for the Collective Investment of Transferable Securities* (UCITS): hedge funds, private equity funds and venture capital funds, loan funds, real estate funds, etc. This second pillar, dedicated to the so-called *Alternative Investment Funds* (AIFs), is largely composed of "subjects" that also or mainly invest in controlling holdings of companies and that, in any case, are free from the rigid criterion of investment diversification.

This new stream of regulatory intervention revolves around Directive 2011/61/EU, the well-known *Alternative Investment Fund Managers Directive (AIFMD)*, which uses a non-specific approach to regulate the organisation and conducts of all those subjects that are negatively identified as not managing products falling within the scope of the UCITS directives.

Yet, the guiding principles and criteria of the AIFMD do not exhaust the complex series of interventions that pertain to the sphere of alternative management, and not even the sources of European law. A series of regulatory provisions focuses on particular and specialised alternative investment funds. For example, I am thinking of European rules and regulations on European Venture Capital Funds (EuVECA), European Social Entrepreneurship Funds (EuSEF) and European Long-Term Funds (ELTIF). I am also thinking of the very recent Regulation (EU) 2017/1131 on Money Market Funds (MMF).

4. In this context, the pages that make up this issue of *Quaderni Giuridici* have more points in common with each other than it might seem at first sight.

The subject matter in the second chapter is, in fact, a direct consequence of the development and growth of the asset management industry toward multiple directions. Specifically, he begins from the growing presence of private equity funds in the share capital of banks, either as holders of qualified holdings or even of controlling holdings.

Also the first chapter is aimed at investigating a series of issues that have become relevant as a result of the economic growth of the asset and wealth management industry. This part of the paper has a composite subject matter and a two-fold soul. On the one hand it reflects on the peculiar problems that arise when an asset manager manages a majority or controlling holding in a company on behalf of a managed (alternative) investment fund. On the other hand, it adopts a more analytical approach, in order to investigate the peculiarities of a take-over bid on the shares of mutual funds, a transaction that – it goes without saying – is aimed at obtaining the majority if not even the totality of such financial instruments (hence the parallel between the control of the company and the "control" of the fund).

5. Reading this issue of *Quaderni Giuridici* suggests – or at least suggested in my case – new perspectives for observing the world of mutual investment funds and for further investigating the new legal problems raised by it.

The radical and deep transformation of the figures, size, relevance and structure of the asset management industry requires to rethink the relations between the different souls of the financial market. The traditional vision of asset management, seen as a secondary activity as compared to banking and insurance (its "big sisters"), is largely outdated by the current financial reality. Asset management has now come out of the shadow that banks and insurance companies had cast on it. Asset management activities have gained centre stage in the financial scene and represent now the moment of expansion and the most profitable portion of financial activities in general.

However, I believe that the time has come to try and adapt the way we consider company law and corporate governance issues, at least as regards widely-held companies. The albeit natural tendency to think as if the typical shareholder of widely-held companies is a natural person or a collective subject (legal person) which brings its "own interest" (whatever this might mean in the case of a company) must be overcome, and it should always be borne in mind that, at least in an interpretation based on the typological method, investors, shareholders (and often majority and controlling shareholders) are nowadays mainly funds, i.e., autonomous assets managed (generally) in an independent way by professional and institutional asset managers, in the interest of third parties and according to logics and policies that are structurally different from those of the specific investment.

In other words, the *fund as a shareholder* not only raises problems regarding the regulation of the conduct of its manager, but also requires that the discipline of issuers, their corporate governance and financial market law be interpreted in a way that better suits the relevance of the phenomenon.

1 Holdings of an AIF reserved for professional investors in a listed company and in other mutual funds

1.1 From the shadow banking system to the European Alternative Investment Fund Managers Directive (AIFMD)

Before the economic and financial crisis of 2007-2008, both regulation and supervision had essentially been aimed at the protection of the consumer, the depositor and the investor, through rules that aimed to guarantee the stability of the individual intermediary (in addition to the transparency and correctness of its conduct) from a "micro-prudential" perspective. With the financial crisis, however, the attention of policy makers and regulators turned to another perspective: that of systemic risks and the potential negative effects on economic growth and on public accounts, i.e. a "macro-prudential" perspective [1].

This new perspective has also resulted in the onset of conviction - first, within the scope of the G20[2] and, then, within all major countries with advanced economies - about the need, among other things, to extend the perimeter of financial regulation and supervision to the so-called shadow banking system[3].

According to the Financial Stability Board's definition (hereinafter "FSB"), shadow banking consists of "credit intermediation involving entities and activities (fully or partially) outside the regular banking system"[4] (such as managed savings, monetary funds, hedge funds, private equity funds, real estate funds, commodity funds, monetary funds, infrastructural funds, financial companies in general, etc.), i.e., a type of intermediation that operates in parallel to the credit system in the collection of savings and in the provision of credit to companies. As it is not subject to the strict capital requirements and supervision envisaged for banks, by reason of its close

1 For a review of the doctrine see: S. Alvaro, G. Siciliano, *Crisi sistemiche e regolamentazione finanziaria. Dai bulbi di tulipano ai mutui sub-prime*, Consob, Quaderni Giuridici (Legal Papers), n. 10, July 2016.

2 It is essentially in November 2010 that the leaders of the G20 meeting in Seoul - after completing the new rules on the bank capitalisation (Basel III) – have started focussing on shadow banking. They requested the Financial Stability Board (hereinafter "FSB") to develop, in collaboration with other international standard setting bodies, recommendations aimed at enhancing the supervision and regulation of the shadow banking system (cf. the *Seoul Summit Document*, November 2010, para. 41). In its response of October 27, 2011, regarding the enhancing of supervision and regulation of the shadow banking system, the FSB highlighted how the failure of entities in a shadow banking system could result in systemic risk, both directly and through their interconnection with the normal banking system, and that their lesser regulation with respect to the financial sector could push a substantial part of the banking activities toward the shadow banking system. The same risks were also discussed by the European Parliament in its *Resolution of 20 November 2012 on Shadow Banking* (2012/2115(INI). See E. Gualandri and M. Noera correctly point out in *Rischi sistemici e regolamentazione macroprudenziale*, in *Lo stato della finanza - Scritti in onore di Marco Onado*, (edited by Bisoni, Gualandri, Landi, Lusignani), Bologna, 2014, p. 15.

3 In its *Report on Risks and Vulnerabilities in the EU Financial System* of September 7, 2016, the *Joint Committee of the European Supervisory Authority (ESA)* stated that in Europe the assets managed by shadow banking have reached 28 thousand billion euros, a figure higher than that of the entire EU banking system (cf. https://esas-joint-committee.europa.eu/Publications/Reports/JC%202016%2047%20RSC%20-%20Joint%20Risk%20Report%20-%20Autumn%202016%20-%20Public.pdf). The same report also indicates that at the end of 2015, investment funds and alternative funds held assets of monetary funds and financial vehicle corporations for over 7,400 billion euros.

4 Financial Stability Board, *Shadow Banking: Strengthening Oversight and Regulation - Recommendations of the Financial Stability Board*, October 27, 2011, according to which in 2010 the value of shadow banking was equal to 60 thousand billion US dollars.

links with the regulated financial sector, as already mentioned, the shadow banking system brings about significant systemic risks[5] as well as possible regulatory arbitrage consisting in the movement of assets from the regulated sector to the shadow banking system.

The action of the European Union on shadow banking essentially consisted of responding to the indications given in the context of the aforementioned G20. Specifically regarding the asset and wealth management industry, the European legislator has intervened for the first time with Directive 2011/61/EU[6] of June 8, 2011, on *Alternative Investment Fund Managers* (so-called AIFM Directive) for subjecting all Alternative Investment Fund Managers (so-called AIFMs) to a uniform regulatory framework, with AIFMs meaning all collective investment undertakings other than those covered by Directive 2009/65/EC (UCITS IV).

For the first time, this directive has created a regulatory framework harmonised at the European level for supervision of alternative fund managers with managed assets greater than a predetermined threshold; the supervision is founded on the principles of home country control and "passportisation" of national authorisations in the case of cross-border operations.

1.2 The rules that govern the purchase of a major holding in a listed company by an Undertaking for Collective Investment in Transferable Securities (UCITS) and by an Alternative Investment Fund (AIF)

The AIFM Directive has taken account of that which has always been one of the main characteristics of AIF and distinguishes them from traditional Undertakings for Collective Investment in Transferable Securities (so-called UCITS funds[7]), i.e., the subscribers of the fund units being professional investors with particular expertise in financial transactions (institutional investors and high net worth individuals)[8] and not – at least in principle - retail investors[9].

Precisely for this reason the AIFM Directive did not consider it necessary to include the guarantees and safeguards provided for by the UCITS Directive in favour

5 On this point cf. G. Gasparri, *I nuovi assetti istituzionali della vigilanza europea sul mercato finanziario e sul sistema bancario*, Consob, Quaderni Giuridici (Legal Papers), n. 12, september 2017.

6 Directive 2011/61/EU of the European Parliament and of the Council of June 8, 2011, on Alternative Investment Fund Managers, amending Directives 2003/41/EC and 2009/65/EC and Council Regulations (EC) no. 1060/2009 and (EU) no. 1095/2010, in the Official Journal of the European Union of July 1, 2011.

7 Acronym for *Undertakings for Collective Investment in Transferable Securities*, which identifies mutual funds covered by Directive 2009/65/EC.

8 According to Art. 4, para. 1, letter ag) of the AIFM Directive professional investor means "investor which is considered to be a professional client or may, on request, be treated as a professional client within the meaning of Annex II to Directive 2004/39/EC".

9 This paragraph and those following until paragraph 1.6 retrace in part that which has already been written in S. Alvaro, Risparmio gestito e personalità giuridica nei mercati finanziari: alcune peculiari interazioni tra fondi comuni e società quotate nella prassi applicativa, in Rivista Bancaria, 2017, no. 6, pp. 81 et seq.

of retail investors in the regulatory framework for AIFs reserved for institutional investors, guarantees and protections that however exist for non-reserved AIFs.

Particularly significant to this study is that while a strict regulatory framework on the acquisition of a major holding or control in a listed company is provided for UCITS, this framework is not present for reserved alternative funds.

To understand the reasons for this different regulatory framework it seems appropriate to briefly recall the main economic and legal characteristics of the financial transaction that is put in place with the establishment of an UCITS.

From the economic point of view UCITS funds are the tool intended to facilitate (also) the access of a large number of investors to share ownership. Compared to investment in shares, whose value fluctuations directly affect the shareholder, investment in mutual fund units reduces exposure to these fluctuation, precisely because of the diversification of risk and investment resulting from the regulatory decision to impose the allocation of investment to multiple issuers. This determines greater 'attenuation' in the effect of the fluctuation of one or more securities covered by the investment on the fund investors. Obviously the investor could create a diversified portfolio of shares by himself to spread the risk across several companies, but in this case the transaction costs would be very high.

From a strictly legal point of view, the economic transaction of the UCITS funds is composed of two distinct moments: a market operation for the collection of "public" savings and subsequent intermediary activities. These characteristics make it so that two distinct regulatory frameworks apply to this type of transaction, mainly aimed at protecting retail investors: (a) the regulations on transparency of financial instrument issuers and transactions (regulations able to eliminate the position disparities in the access to information between those who collect the assets and the investors) and (b) that relating to the rules of conduct of the financial intermediary aimed at guaranteeing the liquidity of the system of intermediaries as a whole as a necessary condition for guaranteeing the indispensable intermediation function of savings.

In particular, the latter regulatory framework, by ruling out the possibility of the fund assuming excessively speculative positions (since this would be contrary to the objectives pursued by the legislator in terms of splitting of investment and therefore risks) has made it so that mutual funds have necessarily become minority shareholders of the investee companies.

The general problems related to a mutual investment fund having holdings in a listed company were carefully analysed by the Italian doctrine in the Eighties of the last century, on the occasion of the introduction of the regulatory framework on investment funds in Italy.

The said analysis highlighted a number of reasons justifying the introduction of a framework that restricted the possibility for a mutual investment fund to have holdings in a listed company[10].

Nowadays, in Italy the rule that prohibits mutual UCITS funds from acquiring or exercising control (or significant influence) over the investee companies in order to limit risk concentration was introduced by Art. 4 of the Law no. 77 of March 23, 1983, establishing mutual investment funds, and was then further specified by the Bank of Italy as an overall limit to the holding of fund units or shares (and participation in voting syndicates) with respect to the assets held by the fund and the capital represented by securities with voting rights of the company in which the fund invests.

The Bank of Italy extended the limitations set for the shareholdings that can be held and voting rights that can be exercised by UCITS to also apply (with an increase of the maximum limits) to open-end and closed-end AIFs not reserved for professional investors, i.e., AIFs that also collect assets from retail investors [11].

Conversely, these limitations do not apply to AIFs reserved for professional investors, as these funds are not 'physiologically' intended for retail investors and therefore, the European legislator did not considered it necessary to set a regulations aimed at reducing the risk of the investment and imposing conducts rules on operators.

In relation to major holdings or control held by an asset manager in listed or unlisted companies on behalf of EU or non-EU AIFs, the AIFM Directive has also introduced the obligation for the manager to disclose information on the intentions for the future activities of the company and the sources of financing for the acquisition[12].

The difference in the regulations on the holdings that can be held, respectively, by a UCITS fund and an AIF reserved for institutional investors can determine (and has already partly determined) important effects on the Italian corporate control market.

It can be observed that the UCITS funds are 'institutionally' minority shareholders of listed companies as they hold shares in a relatively low percentage that is usually less than the thresholds laid down by the Italian Civil Code for the exercise of certain shareholder rights and in particular of the so-called minority rights; this, in turn, has led to the emergence of the need for funds to cooperate between themselves in order to be able to exercise these rights.

10 Precisely restated by R. Costi, *Profili organizzativi dei fondi*, in *I fondi comuni di investimento* (edited by P.G. Jaeger and P. Casella), *Quaderno di giur. comm.* no. 57, Milan, 1984, p. 102. In the same sense also, among others, F. Vella, sub art. 40, in *Commentario al Testo Unico della finanza* directed by G.F. Campobasso, Turin, 2002, p. 357.

11 Bank of Italy's Regulation, *Regulation on collective asset management*, Title V, Chap. III, Sect. III, para. 1 and Sect. V paras. 2, 3.1 and 6.

12 The intention of the AIFMD Directive is to forbid private equity funds from acting as locust funds, i.e., undertaking opportunistic and not very transparent behaviour.

The problem has become particularly evident with reference to the exercise of the right to submit lists of candidates for the appointment of corporate bodies: among the many, the most famous cases are those occurred at the shareholders' meetings of Telecom in April 2014, Unicredit in 2015 and UBI of 2016. The list submitted by the funds for the appointment of members to the board of directors (to the supervisory board in the case of UBI) obtained the relative majority of votes, overruling the list submitted by the respective majority shareholders, but did not obtain the majority of directors precisely because it was composed of a number of candidates less than half of the number of directors to be appointed.

It should also be observed that AIFs may lawfully acquire controlling shares in the capital of unlisted companies as well as in listed companies.

So much so that in 2016 a real estate AIF - following a mandatory full takeover bid - became the controlling shareholder of a company listed on the MTA market (Mercato Telematico Azionario) of the Italian Stock Exchange, acquiring a shareholding of over 84% of the capital[13].

1.3 The general problems related to the holding of an Alternative Investment Fund in a listed company

The mentioned acquisition of control of an Italian listed company by an Alternative Investment Fund set a new theme - that is to consider if and to what extent the rules essentially designed by the legislator for subjects with legal personality (or capacity ad litem) can be applied (e.g., with analogous or extensive interpretation) to subjects with no legal personality such as mutual funds (theme on which we will come later)[14] – and also reproposes, although in different terms, a consideration previously developed by Italian doctrine in the mid-1980s, downstream of the law establishing investment funds in Italy and already mentioned in the previous paragraph. This is the consideration on the risk that an investment fund could become a holding company (failing the management principle of investment diversification), find itself in a situation of a conflict of interest (decisions should be aimed at ful-

13 This is the mandatory full takeover bid promoted by Sorgente SGR S.p.a. on behalf of the Tintoretto Fund - Akroterion Sub-fund on ordinary shares issued by Nova Re S.p.a. pursuant to Articles 102 and 106, para. 1, of the Consolidated Law on Finance; the subscription period ran from February 8 to 26, 2016. The obligation to launch this takeover bid had arisen as a result of the purchase by the aforementioned AIF of all shares of the listed company Nova RE S.p.a. (which was in the circumstance envisaged by Art. 2446, para. 1, of the Civil Code, having suffered a decrease of its assets such as to reduce it over a third below the net share capital) owned by its majority shareholder Aedes s.p.a. and equal to 80.29% of the share capital. Within the meaning of Articles 102 and 106, para. 1, of the Consolidated Law on Finance, the fund was therefore obligated to carry out a takeover bid on the shares still in circulation and equal to 19.71% of the share capital of Nova RE, at a price equal to that paid by the bidder fund to Aedes for the sale of their own shares. For the AIF the acquisition of control over the company Nova RE carried out the strategic objective of "*offering investors, through a primary operator, an opportunity of access to real estate investment capable of producing a significant annual return as well as an appreciable revaluation in the medium and long term*" (as appears in the prospectus of Sorgente SGR S.p.a. which also indicated the intention to request access for the listed company to the special scheme for a listed real estate investment trust- so-called REIT, pursuant to Art. 1, paragraphs 119 et seq. of Italian Law no. 296 of December 27, 2006, as subsequently amended).

14 On the general theme of the recognition of legal subjectivity to a common fund in jurisprudence see: Corte di Cassazione, sent. n. 16605, of 15.7.2010 and Court of Milan, sent. n. 7232 of 10.06.2016.

filling the interests of the investee company rather than those of the fund investors), and have more difficulty in liquidating its investment[15].

Obviously for an alternative fund reserved for institutional investors, most of the risks mentioned will be managed at a private and contractual level between the fund manager and its investors.

In fact, the legislator has not deemed it necessary to introduce rules to ensure the diversification of the investments, to limit financial leverage and to safeguard their immediate liquidability, as well as to prevent the acquisition of significant holdings; such rules would essentially be aimed at protecting the retail investor and not the professional investor.

The same issue of the conflict of interest - which is less binding for reserved AIFs compared to UCITS funds, as professional investors have more instruments of control over the work of managers - was in some way resolved by the AIFM Directive by an approach that uses the internal and procedural settings of asset management companies as the means to prevent situations of conflict of interest rather than transparency rules for investors. Such solution was already adopted by the Directive 2009/65/EC for UCITS mutual funds.

The substantial alignment between the regulations of UCITS and AIF managers in relation to conflicts of interest has led the Italian legislator to locate a single *corpus* of rules applicable to the whole asset management sector[16].

Today any asset management company carrying out intermediation in Italy, whether managing a UCITS or managing an AIF (reserved or non-reserved), is bound to the same rules of conduct on conflicts of interest.

Still with regard to conflicts of interest, it can be observed that as regards the procedures followed by asset management companies to exercise the right to attend and vote in the assemblies of the companies invested in by the managed funds, the same rules of conduct highlighted by the doctrine for UCITS funds must apply to AIFs: the exercise of shareholders' rights should not be considered free and discretionary, but rather the object of a power in the technical sense, of a function that is carried out in favour of the subscribers of fund's shares or units[17].

15 Although, the stability spoken of in the Eighties was actually perceived to be primarily a micro-prudential viewpoint and did not take into account, as we must today, systemic effects that the stability of a financial intermediary may have on the system.

16 On this: G. Frati, *Conflitto di interessi. Profili evolutivi, in Profili evolutivi della disciplina sulla gestione collettiva del risparmio* (edited by R. D'Apice), Bologna, 2016, p. 493 et seq.

17 As known to asset management companies, the law confers a right (attendance and voting) that must be exercised in the interest of others, i.e., of the investors in the fund. It is for this reason that the doctrine has underlined how, in general, in asset management companies corporate interest is manifested in a different way with respect to all other public limited liability companies (M. Stella Richter, *L'esercizio del voto con gli strumenti finanziari gestiti*, in *I contratti del mercato finanziario*, edited by E. Gabrielli and R. Lener, Turin, Utet, 2010, II ed., p. 791 et seq.). In fact, in asset management companies there is an additional conflict of interest, i.e., that between the shareholders of the asset management company and investors in the funds managed by this company. From this point of view, the interests of asset management companies are enriched by the interests of subscribers of the fund, i.e., investors whose capital is managed by the asset management company. This means that in the management of asset management companies, directors should consider both the interests of the company's shareholders and those (and in certain

However, the general problem connected with the fact that the controlling (or in any case major) holding held by an AIF in a listed or unlisted company generates the risk that the manager (or the fund itself) is transformed into a holding company appears unresolved.

This issue is only mentioned here in general terms to illustrate its more problematic aspects.

Firstly, this involves considering whether the legislation in force alone is sufficient to guide the investment strategy of the operator of a reserved AIF towards the return expectations of the fund investors, and to minimise agency costs stemming from the risk that the asset management company avails itself of the prerogatives of the majority shareholder to pursue its own interests, or those of its group companies, of possibly consolidating business relations with the issuing company[18].

The single regulatory framework on this matter is in fact that dictated by Art. 30 of the AIFM Directive, which provides for specific guarantees against asset stripping in the case of control of an unlisted company or an issuer[19].

Second, this involves reflecting on the interactions that may exist more generally between an independent asset - typically a mutual investment fund - and a subject with legal personality - which is typically the public limited liability company.

The question that arises in this regard is, should the listed company whose absolute majority shareholder is an AIF be considered as controlled by the fund itself or by the asset management company that manages the fund?

From here a series of further questions arises.

cases exclusively) of investors in the assets managed; and this does not only apply to decisions regarding investment or disinvestment in financial instruments, but also to the exercise of the rights conferred (cf. Art. 40, para. 2, Consolidated Law on Finance). The content of the right to attend and vote must thus only be determined by taking into consideration the interests of the investors in the funds; the exercise of shareholders' rights will not be at free prerogative, but will become the subject of a power in the technical sense, a function (in this sense always Stella Richter, *op.loc. cit.*).

18 The following have investigated the general issue of asset management companies exercising the right to vote: M. Maugeri, *Proxy advisors, esercizio del diritto del voto e doveri "fiduciari" del gestore*, in *Orizzonti dir. comm.*, 2016 I, p. 2; M. Stella Richter, *Intervento e voto con strumenti finanziari di pertinenza di fondi comuni d'investimento*, in *L'attuazione della MiFID in Italia* (edited by R. D'Apice), Bologna, 2010, p. 444; *id.*; *L'organizzazione e il governo societario del gestore*, in *Profili evolutivi della disciplina sulla gestione collettiva del risparmio* (edited by R. D'Apice), Bologna, 2016, p. 61 et seq.; F. Bordiga, *Partecipazione degli investitori istituzionali alla s.p.a. e doveri fiduciari*, in *Riv. soc.*, 2013, p. 202 and ff.

19 Art. 30 of the AIFM Directive provides that: "Member States shall require that when an AIF, individually or jointly, acquires control of a non-listed company or an issuer pursuant to Article 26(1), in conjunction with paragraph 5 of that Article, the AIFM managing such an AIF shall for a period of 24 months following the acquisition of control of the company by the AIF:

(a) not be allowed to facilitate, support or instruct any distribution, capital reduction, share redemption and/or acquisition of own shares by the company as described in paragraph 2;

(b) in so far as the AIFM is authorised to vote on behalf of the AIF at the meetings of the governing bodies of the company, not vote in favour of a distribution, capital reduction, share redemption and/or acquisition of own shares by the company as described in paragraph 2; and

(c) in any event use its best efforts to prevent distributions, capital reductions, share redemptions and/or the acquisition of own shares by the company as described in paragraph 2".

How should the independence requirements of the members of the management and control bodies of the investee company be assessed? With respect to the bodies of the asset management companies?

How to apply the regulatory framework of cross-holdings?

Should the regulatory framework on the purchase of own shares and shares of the parent company be considered to be applicable to shares of the controlling AIF?

Might funds managed by the same asset management company (and companies controlled by the these funds) be in some way assimilated to sister companies within a group of companies?

How would the institution of the increased dividend and increased voting right operate if the investment in a company were to be moved from one fund to another managed by the same asset management company?

With the acquisition of an absolute majority shareholding could it be argued that the asset management company would be able to use a separate asset (the mutual fund managed) and a corporate structure in the form of a public limited liability company (the listed company) to manage a company, albeit indirectly?

How can we apply the regulatory framework on the code of remuneration envisaged by the AIFM Directive in the event that the EU AIF delegates management of their portfolio to a US manager? Should the rules on remuneration also apply to the US manager?

1.4 Voluntary takeover bids on units of closed-end real estate investment mutual funds

Another theme that the new regulatory framework and, especially, the operations of AIFs must bring to the attention of scholars with renewed vigour, is that of (voluntary) takeover bids on units of mutual funds.

As known, the units of a mutual investment fund - whether listed on a regulated market, significantly widespread among the public or not listed - can lawfully be the subject of a voluntary takeover bid just like any other financial product[20].

In the last ten years eighteen voluntary takeover bids[21] and one exchange tender offer[22] have been promoted on units of mutual investment funds in Italy (mainly deals on closed-end real estate funds).

20 On the general theme cf. for all: M. Stella Richter, *Fattispecie e disciplina delle offerte pubbliche di acquisto*, in *Le offerte pubbliche di acquisto* (edited by M. Stella Richter), Turin, 2011, p. 3 et seq.; M. Tesei, *Commento all'art. 102, in Il testo unico della finanza*, edited by M. Fratini and G. Gasparri, Turin, 2012, vol. II, 1212 et seq.

21 These are the following bids: 1) bid promoted in 2007 by Capitalia Merchant s.p.a. on the units of the closed-end mutual investment fund Sofipa Equity Fund managed by Capitalia Sofipa Sgr s.p.a.; 2) and 3) bids promoted in 2007 by Gamma Re bv on units of the closed-end mutual real estate funds Tecla and Berenice managed by Pirelli & C. Re

This kind of takeover bid and exchange tender offer on closed-end funds did not cause particular problems for the interpretation or application of the legislation in force.

First, takeover bids on units of a mutual fund are always classified as *voluntary* and not mandatory offers, under the Italian legal system. In fact, Art. 101-*bis*, para. 2, of the Consolidated Law on Finance envisages that the rules on mandatory bids contained in Section II, Chapter II of Title II of Part IV of the Consolidated Law on Finance should not necessarily be applied to those instruments which, like the units of a mutual fund, do not confer the right to vote, even limited to specific matters, in the ordinary or extraordinary assembly of a listed company.

Another characteristic of public takeover bids on shares of mutual funds is that the *subject required to disseminate the notice* referred to in Art. 103, para. 3, of the Consolidated Law on Finance (so-called "Issuer's Notice") is the asset management company that manages the fund.

This is an exclusive competence of the board of directors of the asset management company, even if the internal governance of the fund - as outlined by the fund's regulation - could envisage that the board of directors of the asset management company can avail themselves of the advisory opinion of one or more internal technical committees which may also include subjects external to the company. In this case, however, the opinion expressed by the technical committee must not be considered as binding and will not detract from the right and duty of the board of directors to issue the issuer's notice and assume the relative responsibilities.

SGR s.p.a.; 4) competing offer promoted in 2007 by Zwinger Opco 6 bv on units of the closed-end mutual real estate investment fund Berenice managed by Pirelli RE SGR s.p.a.; 5) competing offer promoted in 2007 by Galante Sarl on units of the closed-end mutual real estate investment fund Berenice managed by Pirelli RE SGR s.p.a.; 6) bid promoted in 2007 by Chrysalis s.p.a. on units of the closed-end mutual real estate fund Beta Immobiliare managed by Fondi Immobiliari Italiani SGR s.p.a..; 7) bid promoted in 2010 by the Donatello Fund - Iris Sub-fund, set up and managed by Sorgente SGR s.p.a. on units of the closed-end real estate fund Caravaggio; 8) bid jointly promoted in 2014 by Europe Plus SCA SIF - RES Opportunity and by Italy Investment s.a.r.l. on units of the real estate fund Unicredito Immobiliare Uno managed by Torre SGR s.p.a..; 9) bid promoted in 2014 by Oceano Immobiliare s.a.r.l. on units of the closed-end real estate fund Atlantic1 managed by IDeA Fimit SGR s.p.a.; 10) joint bid promoted in 2014 by SP 101 Finance Ireland Limited and Capstore Equities Capital management LP on units of the closed-end mutual real estate fund Fondo Europa Immobiliare n. 1managed by Vegagest SGR s.p.a.; 11) partial competing voluntary takeover bid promoted in 2016 by Mars Grafton Sarl on the entirety of the units of the closed-end Alternative Investment Fund Delta Immobiliare; 12) partial voluntary bid promoted in 2016 by Navona Value Opportunity S.à.r.l. and concerning a maximum of 1,263,194 units of Delta Immobiliare - 'Fondo di Investimento Alternativo (FIA) istituito in forma di Fondo Comune di Investimento Immobiliare di Tipo Chiuso', equal to 60 % of the entirety of units issued by the same Fund; 13) full voluntary takeover bid promoted in 2016 by Duomo Holdings, LLC concerning a maximum of 8,283,782 class "A" units and 66,746,587 class "B" units of the closed-end alternative real estate investment fund "Mediolanum Real Estate", managed by Mediolanum Gestione Fondi Società di Gestione del Risparmio S.p.A., equal to the entirety of the units issued by the Fund; 14) partial voluntary takeover bid promoted in 2016 by Gsf Eagle Opportuniy Sarl on units of the Alternative Investment Fund Delta Immobiliare; 15) full voluntary takeover bid promoted in 2016 by Blado Investments SCA on units of the real estate investment fund Polis; 16) full voluntary takeover bid promoted in 2016 by Blado Investments SCA on units of the real estate investment Immobiliare Dinamico; 17) full voluntary takeover bid promoted in 2016 by Blado Investments SCA on units of the real estate investment fund Mediolanum Real Estate; 18) full voluntary takeover bid promoted in 2016 by Blado Investments SCA on units of the real estate investment fund Alpha Immobiliare.

22 This is the bid promoted in 2010 by Yorkville Bhn s.p.a. pursuant to Art. 102 et seq. of the Italian Legislative Decree no. 58/1998, concerning the units of the closed-end mutual real estate investment fund Investietico managed by Aedes Bpm Real Estate Sgr s.p.a.

1.5 A particular case: the public takeover bid on a fund's units launched by another mutual fund managed by the same asset management company that manages the issuer

Another particular feature of takeover bids on units of mutual funds - a direct consequence of the mutual funds lacking legal personality - is that the takeover bid may legitimately be launched by another mutual investment fund (*bidding fund*). The latter fund can then be managed both by an asset management company other that the one that manages the fund whose shares are subject to the takeover bid (*bidding fund*), and by the same asset management company.

The circumstance materialised in September 2010, when a voluntary full takeover bid was launched on units of a closed-end real estate investment fund admitted to trading on the MIV market (the Market of Investment Vehicles, dedicated to Alternative Investment Funds - AIFs) by another mutual fund (a sub-fund of another fund) managed by the same asset management company that managed the fund subject to the takeover bid[23].

The particular criticality highlighted in the case of the said takeover bid is that, since the asset management company that managed the *bidding fund* and that managed the *issuing fund* were the same entity, the same management company was required, on the one hand, to determine the consideration to offer for the fund units on behalf of the bidder and, on the other, to express a general financial assessment of the financial on the offer itself and to communicate any useful data for its evaluation (this data that must be inserted inside the offer document) on behalf of the issuing fund[24].

In this case and according to that which was disclosed by the asset management company, the offer was justified in the fact that, approaching the maturity date of the issuer's fund[25] and in view of the poor performance of the reference real estate market, the low volumes handled and the significant real estate assets held, there was, on the one hand, the concrete risk of a disposal of assets that would be detrimental to the holders of units in the issuing fund and, on the other hand, the opportunity for the bidding fund to buy the shares at a reasonable price.

In order to preserve the value of the assets of the issuing fund invested in real estate, the asset management company had then chosen to put a transaction in place that would not allow the said real estate to be transferred of in the short term,

23 This is the full voluntary takeover bid promoted in September 2010 by the Donatello Fund - Iris sub-fund, set up and managed by Sorgente SGR S.p.a. on units of the Caravaggio Fund, a closed-end real estate fund. At the time of the launch of the takeover bid, the Donatello Fund already held 73% of unit in the Caravaggio Fund.

24 This case was particularly delicate as the bidder was a sub-fund of a closed-end mutual real estate investment fund reserved for qualified investors (as referred to in Art. 1, para. 1(h) of Italian Ministerial Decree 228/1999), whereas the units of the issuing fund, originally offered for subscription to the general investing public, were in the hands of 1,504 subscribers and, for these subjects the public bid, as known, represented a request for disinvestment.

25 Set at December 31, 2012.

starting a process of concentrating the issuing fund with a sub-fund of the bidding fund to be carried out in two distinct phases:

a) the takeover bid on units of the issuing fund by the bidding fund[26];

b) the subsequent merger between the two funds[27].

In fact, without launching the public takeover bid and obtaining control of the assembly of the issuing fund the bidding fund could not in any way influence the management programmes and resolve upon the merger between the funds.

Aware of the situation of conflict of interest in which the asset management company had found itself as the manager of both the bidding fund and the managed fund, the Board of Directors of the asset management company chose to adopt some 'precautions'.

Firstly, the initiative was submitted to the opinion of the board of statutory auditors of the asset management company and the independent director, also asking them to carefully verify compliance with the company's internal procedures on conflicts of interest.

Secondly, it was deemed appropriate to appoint:

(i) A financial advisor on behalf of the bidder for the purposes of issuing a price recommendation on the basis of which determine the consideration, and

(ii) Another financial advisor on behalf of the issuing fund , for the purposes of issuing an opinion on the adequacy of the consideration offered.

In the case of a voluntary takeover bid on the units of a mutual fund, an asset management company that manages both the issuing fund and the bidding fund could find itself in the situation described above. Such a situation clearly shows that which what seems to be the main criticality in terms of relations between asset management, independent assets and legal personality: most of the rules contained

26 Page 57 of the Bid Document of October 6, 2010, with which the Donatello Fund - Iris sub-fund (established and managed by Sorgente SGR) launched the voluntary full takeover bid on units of the Caravaggio Fund (also established and managed by Sorgente SGR) reads as follows, "Pursuant to Art. 36 of the Consolidated Law on Finance mutual investment funds, and therefore the Caravaggio Fund, are managed by an asset management company which is responsible for the administration of the assets of the fund managed. Therefore, the bidder may only influence the management programmes of the company that manages the Caravaggio Fund through the participation in the shareholders' assembly according to the methods and within the limits of the law and those provided for by the management regulation of the Caravaggio Fund and limited to matters of law and envisaged in the management regulation itself".

27 The asset management company - as manager of the fund resulting from the possible merger - intends to offer investors in the issuing fund not participating in the offer, a treatment similar to that which it would have received if, as a result of the merger, the issuer had not been extinguished, therefore granting them the option to liquidate, using the assets of the Fund, their own investment on December 31, 2012, at a value equal to the net asset value (NAV) at the same date, according to the methods, terms and conditions that will subsequently be identified within the framework of the merger process. It should be noted that the predicted NAV will be that of the fund resulting from the possible merger.

in the Consolidated Law on Finance (regarding control, group, conflicts of interest, governance, the right to vote in shareholders meetings and the right of list voting, etc.) has been dictated with exclusive reference to subjects with legal personality (or, at least, capacity ad litem) and not the independent assets collectively managed such as mutual investment funds.

Also consider any confidential information that could be accessed and the conflict of interests in which the asset management company that manages both the bidding and issuing fund finds itself.

In this regard it seems then that interpretation can play an important role in understanding whether and to what extent it is possible to apply (for example with interpretation by analogy or extension) the rules designed by the legislator essentially for those with legal personality (or capacity ad litem) to mutual investment funds. Consider, for example, the legal rules and principles established in the matter of control and groups, conflicts of interest, liability actions against directors for damage to the minority, confidential information, etc.

Secondly, in relation to this delicate matter it also seems possible to say that it is time to make a serious reflection about the opportunity of introducing general rules on the governance and internal organisation of mutual funds, to include in the fund's regulations and aimed at preventing situations of potential conflict of interest in a stable way.

In this respect it is worth noting how the best operating practice has already been aimed in this direction, attributing an increasing number of tasks and prerogatives to investors in the life of the fund (for example by setting up bodies such as the assembly of the fund, the assembly of the sub-fund, the sub-fund committee, etc.)[28].

28 In practice the *assembly of the fund* gathers all fund investors. It is convened by the board of directors of the management company, at its own initiative or when a request is made by as many investors as represent at least a certain percentage (e.g., 10%) of units in the fund. Generally, the assembly of the fund resolves, inter alia, on proposals for the amendment of the regulations that do not exclusively affect the specific characteristics of the individual sub-fund and the replacement of the management company. Each fund unit entitles the holder to a vote in the assembly of the fund. The assembly of the fund is regularly constituted with the presence of as many investors as represent the majority of the shares issued as a whole and resolve by a majority of the shares of the investors attending. The *assembly of the sub-fund* gathers the holders of the units of the relevant sub-fund. It is convened by the board of directors of the management company, at its own initiative or when a request is made by as many participants as represent a certain percentage of the shares of the relevant sub-fund. In general, this body shall resolves on the appointment of the chairman of the assembly of the sub-fund, and the members of the sub-fund committee, and the changes to the fund's regulation proposed by the asset management company or imposed by law, only involving the variation of the specific characteristics of the individual sub-fund. Each fund share of each sub-fund entitles the holder to one vote in the assembly of the relevant sub-fund. The assembly of the sub-fund is regularly constituted with the presence of as many investors as represent the majority of the shares issued in the individual sub-fund and resolve by a majority of the shares of the attending investors. The *sub-fund committee* is established by the asset management company on request of one or more investors that hold, even jointly, a certain percentage of the units of that sub-fund (e.g., 25%), otherwise at the initiative of the asset management company. The sub-fund committee has advisory functions in relation to the board of directors and, in general, expresses its precautionary and mandatory, but not binding, opinion on the following matters: (*i*) proposals for early liquidation of the sub-fund, (*ii*) proposals for amendment of the regulation on the sub-fund, (*iii*) advance repayment and (*iv*) transactions in conflict of interest. The *general assembly of all sub-funds* that gathers all the investors in the mutual fund.

Actually, a sort of framework rule aimed at regulating conflicts of interests in the context of collective asset management already exists in Italian law: this is the *Regulation on collective asset management* of the Bank of Italy (hereinafter also only "Bank of Italy's Regulation"). But this rule, besides only covering the (albeit important) theme of conflict of interest, leaves the concrete protection of the rights of the fund and its investors at the discretion of the management body.

The above leads to another and more general consideration: if this were the norm - i.e., to ensure that the fund further develops internal organisational structure rules to remedy situations of potential conflict of interest and that, in this way, could in some way weaken the direct relationship between fund investors and the management company in favour of the growth of the relationship with other investors - could it not be argued that, at least from a conceptual point of view, the differences between investment bodies with bylaws schemes (such as SICAVs and SICAFs) and those under a contractual scheme (such as mutual funds) dissipate more and more to some extent, as a result of contamination from one another[29]?

In addition to the trivial consideration that even the company - although with its own legal personality and its own organisation - is in any case still a contract and that, therefore, both forms of organisation of CIUs (whether under the contractual or bylaws scheme) are based on a contract, where mutual funds are also required to follow internal organisational rules to remedy situations of potential conflict of interest, both contracts (the contract of companies of the SICAV and the fund regulation for mutual funds) would be organise investment activity in a similar way through the creation of bodies and rules of conduct[30].

Leaving all reasoning on these questions to the third chapter of this study, devoted to the conclusions, it is however possible to confirm as of now that which was stated previously, namely that interpretation seems to play an important role in this matter, to understand whether and to what extent the rules essentially designed by the legislator for subjects with legal personality (or capacity ad litem) can be applied (e.g., with analogous or extensive interpretation) to subjects with no legal personality such as mutual funds.

29 In fact, it is traditionally said that investment funds are set up as a category of investments under a contractual scheme as the proportion of interest held in the entity is regulated by a contractual document, i.e., by the fund's regulation (approved by the Bank of Italy) and that SICAVs, instead, represent the model of entities under a bylaws scheme in which the proportion of interest held in the entity is governed by provisions contained in the bylaws (the bylaws of the SICAV). On this point cf. also F. Annunziata, *Gli organismi di investimento collettivo del risparmio (OICR): fattispecie e disciplina*, Milan, 2017, p. XIII of the introduction; *id.*, *Fondi comuni di investimento e forme di gestione collettiva del risparmio*, in *L'ordinamento finanziario italiano*, edited by F. Capriglione, Padova, 2010, p. 453 et seq.

30 For the nature of the contract of CIUs cf.: L. Seminara, *Natura dei fondi comuni di investimento e responsabilità della SGR*, in *Giur. comm.*, 2016, II, 1115 et seq.; G. Leggieri, *Commento sub art.* 39, in the Il testo unico della finanza, edited by M. Fratini and G. Gasparri, Turin, 2012, vol. I, p. 591 et seq.

2 Private equity funds and qualifying holdings in banks: a possible hybridisation?

2.1 The issue

Some recent studies analyse the proprietary structure of so-called "*significant*" banks in the Euro area and end by suggesting that an effort should be undertaken in order to stimulate a wider recourse to listing banks on recognized trading venues[31]. The virtuous effects that would ensue from such a process would be represented by easier access to new capital, and by expected positive impacts on the governance of the bank, including its capacity to better organize its strategic development. The bond between proprietary structures and bank governance does, in fact, represent one of the typical cornerstones of banking supervision. The question raised in that context is whether a relationship exists – and, if so, of what type – between ownership structures, governance and business models of the bank (and, consequently, its performance)[32].

The aforementioned investigations – so it seems – do not appear to directly take into consideration the very particular phenomenon which sees the growing presence in the capital of banks of private equity funds, as qualifying holders of significant stakes in the bank's capital or, even, of controlling interests[33]. This is a

31 See, e.g., N. Véron, *The governance and ownership of signicant euro-area banks*, Bruegel, Policy Contribution, n. 15, May, 2017. Several studies are centred on this subject: see, *ex multis*, E. Levy Yeyati – A.Micco – U. Panizza, *State-Owned Banks: Do They Promote or Depress Financial Development and Economic Growth?*, *background paper prepared for the Inter-American Development Bank conference on 'Public Banks in Latin America: Myths and Reality*', 2005, available at *www.iadb.org/res/publications/pubfiles/pubs-491.pdf*; P. Sapienza, *The Effect of Government Ownership on Bank Lending*, in *Journal of Financial Economics*, 72, 2004, no. 2 (May); A.C. Bertay – A. Demirgüç-Kunt – H. Huizinga, *Bank Ownership and Credit Over the Business Cycle: Is Lending by State Banks Less Procyclical?* (June 1, 2012), World Bank Policy Research Working Paper No. 6110 available at *https://ssrn.com/abstract=2096779*; Th. Barry – L. Lepetit – F. Strobel, *Bank Ownership Structure, Lending Corruption and the Regulatory Environment* (August 3, 2015), in *Journal of Comparative Economics*, available at *https://ssrn.com/abstract=2574816*; A. N. Berger – L. F. Klapper – P. Martinez – S. Maria – R. Zaidi, *Bank Ownership Type and Banking Relationships (March 1, 2006)*, *World Bank Policy Research Working Paper No. 3862* available at *https://ssrn.com/abstract=922988*; G. De Nicolo – E. Loukoianova, *Bank Ownership, Market Structure and Risk (September 2007*), *IMF Working Papers*, pages 1-44, 2007, available at *https://ssrn.com/abstract=1033208*.

32 This idea is taken from the already cited report presented by G. Lusignani at the Conference *La banca nel nuovo ordinamento europeo: luci ed ombre*, Courmayeur, 22-23 September 2017, which illustrated the preliminary results of a research work under way and soon to be published. I thank Giuseppe Lusignani for having kindly provided me with a first draft of his written paper.

33 Among the operations concluded in Italy is the acquisition, in 2015, of the Istitituto Centrale delle Banche Popolari (ICBPI) Group by three private equity funds, which acquired almost 90% of the target bank. In 2015, a US-based private equity fund acquired 54.212% of the capital of Banca Popolare Lecchese (sold by Nuova Banca Etruria spa). Similar transactions were carried out for payment institutions: in 2016, a private equity fund acquired 100% of Sisal Group spa (formerly fully owned by three private equity funds). Again in 2015, Fortress Group took over control of Do Bank (sold by Unicredit). In 2017, the extraordinary administration procedure of Gruppo Banca Mediterranea spa ended, *de facto*, with the acquisition of the Bank by a private equity fund. On the other hand, a number of other operations in which large private equity operators showed interest in acquiring the *entire* capital of banks in difficulty, or which involved the insurance sector, did not come to a successful conclusion (see http://www.repubblica.it/economia/affari-e finanza/2016/10/17/news/al_private_equity_piacciono_le_banche_un_affare_grazie_ai_prezzi_stracciati-150016031/). Further back in time, but not because of this less important, was the case which led, in 2011, Investindustrial fund to purchase an interest of around 10% in the capital of the Banca Popolare di Milano: in many ways a pioneering operation considering that, so it seems, this was one of the very first cases in which a private equity fund was allowed to acquire a significant share of the capital of a large Italian bank. The operation was also notable because of the introduction into the bank's articles of association of special provisions, intended to reflect the specific "weight" of the fund and to grant to it special rights for the

case which only approximately might fall in one of the categories that are usually used in order to analyse the ownership structure of banks. With respect to those schemes, the case of banks participated by private equity funds does present various profiles of speciality: for example, with respect to the case of a typical "qualified" minority shareholder, the peculiarity of the case is to be found where one remarks that investment funds are structurally characterized by ways of actions that provide for the pursuit of third party interests (investors/participants in the fund), according to a specific model that sees the structural separation between investors and the fund's managing entity. The fund which holds a material number shares of a bank might well be treated as a general "qualified" minority shareholder, but, nonetheless, it is a shareholder with elements of speciality, because of the hetero destination of the investment results to the exclusive benefit of the participants in collective investment undertaking ("CIU"). Further elements of speciality are represented – as we shall discuss – by the particular *time perspective* in which, typically, the investment of a fund is framed, if compared to a different entity. Above all, the specific procedures and the very nature of the activity performed by an investment fund – which is distinguished by the pursuit of an investment policy of a clearly *financial* nature – end up by tinting the situation with very particular contours. In fact, the holding of a qualifying interest needs to be combined with the typically *financial* perspective of the investment. All these issues tend to become more specific and complex when, eventually, the fund holds a controlling stake in the bank's capital.

The purpose of this paper is to focus on the very specific questions that prudential regulation and supervision raise in relation to the case of qualifying holdings of CIUs in the capital of banks. It also serves as an observation point for various intersections between regulation of capital and securities markets, on the one hand, and regulation of banks and banking activities, on the other: the analysis shows that the compartmentalisation of financial markets regulation in the EU, still structured in "silos" that tend to be independent of each other, is likely to create frictions that are not easy to solve but which, at the same time, may provide stimulus for more general reflections.

Financial crisis and regulatory frameworks

As is widely known, the financial crisis placed the topic of banking crises at the centre of the debate, from the twofold point of view of their prevention and management, thus triggering enormous transformations, reflected in wide-ranging reforms of the EU framework, including, naturally, the Single Rulebook, the Single Supervisory Mechanism and the Single Resolution Mechanism.

appointment of corporate bodies and in corporate governance matters generally. Among the considerable number of operations in other Countries of the European Union, worth mentioning is the acquisition of 75% of the capital of Novo Bank, in Portugal, by the US fund Lone Star: a transaction completed in October 2017. Another significant case in Italy is represented by the Atlante Fund, set up by Quaestio SGR in 2016 in order to try and "rescue" two locally important banks (Veneto Banca and Banca Popolare di Vicenza), which ultimately were subject to resolution in 2017.

The weaknesses that came to light during the crisis have, however, also triggered major reforms in virtually all neighbouring compartments of capital and financial markets legislation and, among the latter, also that of collective asset management, which culminated in the last revision of the UCITS Directive (the original core of which dates back to 1985) and in the new Directive on alternative investment fund managers (AIFMD)[34]. Due to the very effect of this development, the EU system today offers a sufficiently complete regulatory framework for investment funds and investment funds managers.

Concretely speaking, the purchase of a qualifying holding in the capital of a bank by an undertaking for collective investment can be inspired by different logics: those of a more strategic nature, those of an economic-financial nature, or a combination of the two. The phenomenon can be studied from a typical prudential supervision viewpoint prevalently focused on profiles of sound and prudent management of the target bank. The phenomenon, however, can also be investigated from the perspective of EU collective asset management rules, whereby the latter offers some particularly useful elements for categorizing the different cases and elaborating, if possible, a first taxonomy of a phenomenon which is still evolving.

In fact, on the basis of regulatory developments in the field of collective asset management and funds regulations, two basic patterns can be distinguished, at least by way of first approximation: a first pattern would lead to consider the investment of a fund in a bank the same way as any other kind of financial asset; a second pattern would instead see the CIU develop an investment strategy characterised by further elements, typical of so-called "private equity" operations. In the first perspective, in particular, the case under discussion can respond, as regards the CIU, to the logic of a purely financial investment, without bringing with it any implication in terms, for example, of management of the target bank, or the creation of a stable link with it. This is the case, for example, when the CIU does not intend in any way to intervene in the strategic or governance processes of the target bank[35].

34 Most of the ideas which sparked the reforms introduced over the last decade originate, as is known, from the Report of the Group chaired by Jacques de Larosière, published in February, 2009 (this document, of which we shall never tire of stressing the importance, is available at
http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf).

35 See M. Notari, *Diritti di voice degli azionisti e tutela delle minoranze*, in *Il Testo Unico della Finanza. Un bilancio dopo 15 anni*, edited by F. Annunziata, Milano, Egea, 2015, 247 and following pages. Recent studies have focused on the implications which the phenomenon assumes in a transversal logic, which brings into play antitrust considerations: see A. Ferrell – J. Morley, *New Special Study of the Securities Markets: Institutional Intermediaries*, Yale Law & Economics Research Paper No. 580, available at the address *SSRN: https://ssrn.com/abstract=3005542*, who observe that "*Some of this research suggests that the largest managers' stakes are so vast and so widespread that they might be tilting toward monopolization. In one paper, José Azar, Martin Schmalz, and Isabel Tecu (2016) show that as a handful of large investment managers came to control increasingly large stakes in every major airline, the intensity of price competition among the airlines decreased.39 Labeling this phenomenon "horizontal ownership," a number of legal scholars have argued that although the declines in competition likely do not reflect direct collusion by investment managers, overlapping ownership by investment managers should nevertheless be regulated as an antitrust problem (Elhauge, 2016; Posner, Morton & Weyl, 2017). The investment management industry, understandably, tends to believe there is nothing to worry about. And even many academics argue that there are yet reasons to remain skeptical of the academic evidence. Still, even if one feels inclined to accept the investment management industry's skepticism, it is important to take the issue of horizontal ownership seriously. Though no one can tell the future, the potential impact of concentrated ownership is vast. It is now possible to foresee a day when the clients of two or three large investment managers might hold thirty percent of the shares of a majority of America's large public companies.*

In a second perspective, and without prejudice to the above, the operation that leads a CIU to acquire a significant shareholding in the capital of a bank may however respond to a more articulated investment strategy, whereby the CIU aims to increase the value of its investment over time, according to a medium-long term investment logic, characterized by the exercise of its prerogatives as a *qualified* shareholder (appointment of corporate representatives; participation in the definition of strategic plans; medium-long outlook of the investment period, etc.)[36]: this is typically the logic which distinguishes private equity transaction, in what, in truth, is the very diversified universe of closed-type CIUs traceable to such category (which – it should be pointed out – remains purely descriptive at regulatory level)[37].

Of course, in practice, it may not be easy to clearly distinguish the various situations.

In both cases, the "qualified" presence of collective investment undertakings in a bank's capital raises complex problems, many of which belong, so to speak, to the mainstream of the issues connected with corporate governance, in its various forms, and, in this context, with those relating to the participation of institutional investors in the capital of companies[38]. However, transactions specifically related to the private equity sector raise specific issues in terms of prudential supervision, which arise from the very nature of investment funds, and from the interferences between banking regulations on the one hand, and rules on collective asset management on the other.

Though the intentions of investment managers may be entirely benign, the power that these growing stakes will bring is too significant to ignore". The phenomenon should also be examined from a "horizontal" competition viewpoint – i.e. the purchase by several entities of holdings in competitor companies – as is evident from E. ELHAUGE, *Horizontal Shareholding*, in *Harvard Law Review*, 2016, vol 129:1267 and following pages.

36 Again (see footnote 7 above) this is a point of possible contact, or assonance with antitrust rules: the criteria set out in the text are very close to the notion of "strategic influence", which is relevant for the purposes of recognising decisive influence in antitrust legislation. See, in this regard, *Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/20004 on the control of concentrations between undertakings*, in particular sub par. 66-72.

37 There is no legislative definition of private equity in either European or internal sources: CIUs which, descriptively, are classified within this category, at regulatory level, are usually closed CIUs, falling therefore within the scope of the AIFM Directive, but with potentially very diversified characteristics. The European framework only contains sector-specific rules for certain specific types of CIUs in the broad sense related to this category, such as the so-called "EuVeCa","EuSeF", or "ELTIFs" which have entered the EU regulatory landscape as a result of the AIFM Directive: in this regard see J. PAYNE, Private Equity and its Regulation in Europe. Oxford Legal Studies Research Paper No. 40/2011, available at SSRN: https://ssrn.com/abstract=188618186. In legal literature, the boundaries of the notion are therefore indirectly derived from economic-financial literature, where, on the other hand, private equity CIUs are treated as having more distinctive characteristics.

38 The growing focus on the issue of corporate governance of banks - which is inextricably linked to that of ownership structure and prudential supervision - is a well-known issue, but its full implications are still in the pipeline, also as a result of the still in process edification of the Banking Union. It is, however, clear that, after the financial crisis and the failure of traditional banking supervision models, the growing weight attached to bank governance reflects a new supervisory and regulatory approach, whereby the issue of capital and liquidity is at least to be assessed in a holistic approach compared to the former.

2.2 The collective management regulation perspective: CIUs and qualifying holdings from UCITS to AIFMD

The UCITS regime

With regard to the EU framework, the primary form which collective investment undertakings took on in the original UCITS Directive (1985) and in almost all European legislation is typically that of a mass investment scheme, aimed at an indistinct public, characterised by a high rate of liquidability: the so-to-speak canonical form of the "open-ended" collective investment undertaking, addressed to the general public (and therefore, as such, also subject to the rules on public offers and prospectus).

In this first perspective - dating back to the archetype schemes of the Anglo-American model of investment trusts - the CIU operates in a logic generally characterized by the non-acquisition of qualifying holdings and, from a regulatory point of view, by precise prohibitions which, in different ways, prevent the collective body from exercising a dominant, or even only a significant influence in the life of the target companies themselves. Quite apart from detailed changes which have occurred over the years, this approach continues to distinguish EU rules on UCITS[39], and is substantially confirmed by rules which also apply to alternative non-reserved funds falling within the scope of the AIFMD[40].

AIFMD and reserved CIUs

The approach followed by the AIFM Directive differs from that of the UCITS Directive with regard, above all, to alternative CIUs aimed at <u>professional investors</u>.

For these CIUs, in fact, limitations on shareholdings regulated by the UCITS Directive do not apply: they may therefore also acquire a significant holding or the control of a listed or unlisted company and, in principle, also of a bank, as the rules applicable to such CIUs do not place any sectorial limit on the type of eligible investments.[41]. Naturally, specific regulations continue to apply, starting with antitrust rules, rules on transparency of the ownership structure of listed companies, takeover bids, or rules pertaining to those sectors which require, in the case of acquisitions of equity holdings above certain thresholds, the obligation to obtain prior authorisations, or to carry out some kind of ex-ante notification, as is typically the case for financial institutions, or for companies operating in national strategic fields. Howev-

39 As example, it should be considered that the Bank of Italy's Regulation on Collective Asset Management, as last amended and supplemented on 17 January 2017, provides for UCITS: (i) limits on investments in financial instruments issued by the same entity, inasmuch as a fund may not invest more than 5% of its total assets in the financial instruments of a same issuer; (ii) limits on the fund's assets, as the fund may not invest more than 20% of its total assets in financial instruments, bank deposits or exposures obtained through derivatives of a same entity; (iii) voting right limits, in that an Asset Management Company cannot hold, through all the open-ended mutual funds or assets of the funds it manages, voting rights of the same company for an amount - in relation to the total voting rights - equal to or greater than 10% if the company is listed and 20% if the company is not listed.

40 For alternative funds, falling within the scope of the AIFMD, the limits are higher than those for UCITS: see Bank of Italy Regulation on Collective Asset Management, Title V, Chap. III, Sect. III, par. 1 and Sect. V, paragraphs 2, 3.1 and 6.

41 The concept of control of an offeree company adopted by the AIFM Directive is fulfilled by reference to art. 5 (3) of Directive 2004/25/EC on takeover bids.

er, these are rules that derive not from the way in which CIUs are regulated, but rather from the rules applicable to specific types of target companies.

Legislation, after the AIFM Directive, is not completely indifferent to transactions such as those under discussion, although - again - in a perspective that ignores a sectorial logic, and which therefore applies to investments by a CIU in both industrial and/or financial enterprises. For example, specific provisions are found, in the context of the AIFMD, with regard to the so-called prohibition of "asset stripping", that apply when the fund acquires a controlling interest in a target company.

Naturally, as appears intuitive, where the target company is a financial intermediary or a bank, the provisions on stripping have specific relevance in terms of prudential supervision rules: however, without prejudice to the previous statement – which is rather obvious - from the perspective of the regulation of collective management, the acquisition of a shareholding, including a controlling interest, in the capital of a bank by a CIU reserved to professional investors does not encounter any *a priori* limits.

Possible limitations could, if anything, derive from the contract: it is in fact up to the CIU's investment policy, as defined in the relevant incorporation documents, to regulate any limits or criteria in this regard, e.g., by establishing concentration limits, criteria concerning the type of target company, limits to the recourse to leverage, identification of specific geographical or business areas, etc. Such limits - reflected in the CIU's investment policy - will naturally influence investment strategies and, in this context, also the acquisition of significant holdings in a given enterprise (whether financial or not).

The investment policy of CIUs: a key element

The constitutive elements of the general notion of "collective investment undertaking" affects, indirectly and, at the same time decisively, the nature and characteristics of the transactions under discussion.

Without going into the details of a particularly complex subject, the element of the definition provided by art. 4 AIFMD which, in our opinion, has the greatest capacity to characterise the very general notion of a CIU - and, in many respects, also the one most difficult to identify - is that the collective investment undertaking operates, as a distinctive feature, on the basis of a "defined investment policy" which is binding upon the CIU in its relations with the CIU's participants.

In particular, on the basis of the ESMA Guidelines on AIFMD (par. 20) a "defined investment policy" consists, first and foremost, in the <u>criteria</u> to be followed by the investment manager for the investment activity of the CIU. According to the Guidelines, these criteria include *one or all the following*: (i) to invest in certain categories of assets, or conform to restrictions on asset allocation; (ii) to pursue certain strategies; (iii) to invest in particular geographical regions; (iv) to conform to restrictions on leverage; (v) to conform to minimum holding periods; or (vi) to conform to other restrictions designed to provide risk diversification.

It is clear that, according to the ESMA Guidelines, the investment policy fulfils, as a matter of priority, the function of delimiting the manager's activity.

Assuming the basic bipartition between the two macro-families of funds (retail vs/professional), even in the case of private equity or closed-end type CIUs, reserved to professional investors, investments in banks' capital will always and in any case be part of a financial strategy, characterized by a precise time frame, and by the inherent risk management of the relative portfolio. In such perspective, any rights which – as is typical, and according to what has been recalled – a *private equity* CIU reserves for itself at the time of the investment, and which can affect, for example, the target company's *governance*[42] or its strategies, do not respond to a logic of an industrial type, but remain within the perimeter of an investment which is always, and in any case, of a financial nature, inasmuch as respondent to the need to optimize the risk/return profile of the portfolio, as identified in the defined investment policy of the CIU[43].

As we shall see, this perspective, typical of the transactions under discussion, may be difficult to reconcile with the rules which, from the perspective of prudential regulation over financial institutions, may be relevant in the context of the acquisition of qualifying holdings in the capital of banks. Specific attention must therefore be paid to these latter provisions.

2.3 The problem seen from the banking regulation angle

Rules that govern the acquisition of qualifying holdings in the capital of banks are rather complex[44]. They are articulated in two basic sets: on the one hand, an ad-hoc authorisation scheme for so-called qualifying holdings (in other words, those that exceed 10% of the bank's capital or voting rights); on the other hand, the specific requirements for shareholders who acquire or hold qualifying holdings.

On the background of the need to ensure the sound and prudent management of the bank, the rules introduced over time - starting with the 2nd EU Banking Directive of 1989, up to Directive 2007/44/EU and the CRD IV "package" - required from "qualified" shareholders ever more stringent requisites, whereby a clear bond appears between *shareholding structure* and bank's corporate governance, mention of which was made right at the beginning of these notes. These rules apply both at the time of the initial authorisation granted by Supervisors to carry out banking activities, as well as in the event of the acquisition of qualifying holdings at a later stage. For the purposes of interest here, the latter naturally take on greater importance

42 Cf. V. Donativi, *Strumenti di* corporate governance *nel rapporto tra fondi di private equity e PMI*, in *Banca, borsa*, 2008, I, 207 and following.

43 Such statement can be entrusted to qualitative or quantitative parameters, as when, for example, the constitutive documents of the CIU identify specific return objectives (the so-called "IRR – *Internal Rate of Return*"), to which the remunerations of the managers, such as *performance commissions* or *carried interest* are related.

44 This is not the place for a complete recognition of the ample bibliography on the subject. For an updated reconstruction and further references, see, lastly, P. DE BIASI, *Note preliminari su chi possa essere l'ottimale proprietario di una banca (universale)*, in *Banca, Impresa, Società*, no. 3/2017, 417 and following.

because they descend from the already recalled Directive 2007/44. The case of a bank[45] which - already in the process of the initial authorisation – sees a CIU with qualifying holdings in its capital cannot be ruled out: however, this is a situation which, to the best of our knowledge, is currently lacking material empirical evidence even though - over time - it might become more significant on the basis of the development of newly-established banks operating in the Fintech sector (inasmuch as it is a sector with rapid growth perspective, potentially attractive for private equity transactions)[46]. On the other hand the criteria for assessing the "quality" of a shareholder in the two situations coincide and, therefore, the analysis is not affected by this initial point of reference.

The declination of the criteria laid down by the Directives – in particular that of 2007[47] – is currently largely entrusted to the Guidelines issued by the three European Authorities (EBA, ESMA, EIOPA), most recently updated in 2016[48]. Five are the elements for assessing the suitability of the entities that intend to acquire a qualifying holding in a bank, and more specifically:

a) *Reputation and professional competence;*
b) *Reputation and experience of those who will direct the business of the target undertaking – second assessment criterion;*
c) *Financial soundness of the proposed acquirer – third assessment criterion*;
d) Compliance with prudential requirements of the target undertaking – fourth assessment criterion;
e) The anti-money laundering and terrorist financing assessment complements the integrity assessment and should be carried out regardless of the value and other characteristics of the proposed acquisition.

45 The approach followed by the 2007 Directive - of a cross-sectoral nature and oriented towards maximum harmonisation criteria - has had a significant impact in many Member States and, in particular, in Italy, where it led to the overcoming of the traditional principle of separation between banks and industry which, for a long time, set specific limits to the participation of non-financial entities in the capital of banks. The literature on this subject is vast, and its recognition, by now of an essentially historical type, goes beyond the scope of the present notes. For useful references see G. ROTONDO, (Note 27) espec. pages 1-100.

46 For banks operating in the wide and varied "Fintech" world, the intervention of venture capital funds could also be envisaged, given the innovative nature of the sector. Recent studies have highlighted the positive effects that the presence of a venture capitalist in the capital of a company can have, not only thanks to the financial support it can provide, but also in terms of its managerial support and know-how: see on this topic R. BRONZINO - G. CARAMELLINO - S. MAGRI, *Capitalists at Work: What are the Effects on the Firms They Finance? Bank of Italy Discussion Topics, Working Paper No. 1131*, available at https://ssrn.com/abstract=304827.

47 In the previous system, the assessment of the investor's requirements was entrusted to the verification that conditions were met to ensure the sound and prudent management of the bank (art. 19, sub-section 5, in the previous formulation). The general wording of the legislative text was supplemented by further regulations, which showed that the Bank of Italy's assessment focused on transparency of ownership structure, reliability and financial situation, as well as fairness in the shareholder's business relations. The quality of the participant had to be assessed in relation to the governance structure and the economic and financial situation of the bank, as well as to the nature of the relationships that the shareholder would establish with the bank (as per Bank of Italy's, Supervisory Instructions, Sect. II, Sub-section 5.2.1, page 10 and following). Now the criteria are more directly identified by Article. 19 TUB. On the subject see C. BRESCIA MORRA, *Commento sub art. 19*, in *Commentario al TUB*, edited by F. CAPRIGLIONE, 2012, page 255.

48 Joint Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector, 20 December 2016, JC/GL/2016/01.

Among the above mentioned elements, two have particular relevance in the current analysis: the financial soundness of the proposed acquirer and the prudential requirements of the target undertaking.

The *"financial soundness"* criterion

According to what is set out in the inter-sectorial Guidelines, the *financial soundness* criterion must be, first of all, understood as the capacity of the potential partner to sustain the financial impact of the acquisition. Verification of the requirement, which is naturally up to the *target supervisor* (i.e., the banking supervisor, and *not* the supervisor of the CIU) should therefore determine whether the proposed acquirer "*is sufficiently sound from a financial point of view to ensure the sound and prudent management of the target undertaking for the foreseeable future (usually three years), having regard to the nature of the proposed acquirer and of the acquisition*" (par. 12.2).

In the case of entities subject to prudential requuriements, the Guidelines point out that the assessments must take into account such profiles and – if the supervision is exercised by another European Authority – "*the target supervisor should take into account the assessment of the proposed acquirer's financial situation by such other supervisor, together with the documents gathered and transmitted directly by the supervisor of the proposed acquirer to the target supervisor*" (par. 12.7).

Financial soundness inevitably touches on the core topic of the resources for the financing of the acquisition. Traditionally, the approach to this issue has been quite restrictive, especially in Italy: in practice, the potential buyer was supposed to always have sufficient own funds to finance and support the transaction, without any recourse to leverage or external sources of financing. The Guidelines, on the other hand, now appear to be much more accommodating: they do not consider leverage to be unacceptable, although the profile is worthy of specific attention.

One last matter concerns the impact which the presence of an institutional investor can have on the financial soundness of the target enterprise. For banks, this should be assessed in the light of the specific situation of each case[49].

Prudential requirements of the target company

Equally important, especially in the context of private equity transaction, is the criterion regarding the compatibility between the acquisition project and compli-

49 S. Bernstein – J. Lerner – F. Mezzanotti, Private Equity and Financial Fragility During the Crisis, NBER Working Paper No. w23626, available at the address https://ssrn.com/abstract=3011104. The Authors conclude in the sense that "We find that during the 2008 financial crisis, PE-backed companies increased investments relative to their peers, while also experiencing greater equity and debt inflows. The effects are stronger among financially constrained companies and those whose private equity investors had more resources at the onset of the crisis. PE-backed companies consequentially experienced higher asset growth and increased market share during the crisis". As stated in the text, such statements ought to be inserted in the context of the acquisition of qualifying holdings in bank capital.

ance with the complex requirements of prudential supervision applicable to the target financial entity.

The financial sustainability of the acquisition project should be considered in a perspective static *and* dynamic, taking into account therefore the possible evolution over time of the target company's situation (par. 13.8).

The financial sustainability of the acquisition over time is tied to the business plan of the target company, and consequently (par. 13.10) "*The business plan should clarify the plans of the proposed acquirer concerning the future activities and organisation of the target undertaking. This should include a description of its proposed group structure. The plan should also evaluate the financial consequences of the proposed acquisition and include a medium-term forecast*."

The above elements are, in the case of CIUs, closely related to their investment policy, as defined first in their instruments of incorporation (fund rules, articles of association, deed of trusts, etc.), and then applied in the relevant investment strategies. With this in mind, it is clear that the CIU's policy must be compatible both with the *initial* prudential requirements of the target bank - i.e. those existing at the time of the acquisition - and with those that may become apparent *over time*, after the acquisition. This raises specific concerns in the context of private equity transactions by CIUs, which may suffer from the rigidity of their pre-defined investment policy, and from the fact that investors do not assume any (further) payment or subscription commitment other than that connected with the subscription of the units or shares. Facing further funding requirements from the bank might, therefore, be an issue difficult to deal with for a private equity fund with a qualifying holding and, still more, when the fund holds the control, or even the entire capital, of the bank.

2.4 The qualifying points resulting from the crossing of the two systems of regulation

The comparison between the two systems of rules involved in private equity funds as qualifying shareholders of banks raises various points of friction, so that a particularly qualified reconstructive effort is necessary. In particular, there appears to be a potential contrast between the *financial* perspective which typically characterises investments carried out by a CIU - articulated over a period of time that tends to be precise and, in any case, limited - and the perspective that derives from banking regulation. The latter assumes, in fact, time horizons that tend to be not predefined, and focuses on the need to ensure the financial stability of the bank in the long term, and its compliance with the requirements deriving from prudential regulations[50].

50 V. Th. Barry – L. Lepetit – A. Tarazi, Bank Ownership Structure, Market Discipline and Risk: Evidence from a Sample of Privately Owned and Publicly Held European Banks (December 21, 2008), available at http://dx.doi.org/10.2139/ssrn.133115. Though not very recent, the study concludes by identifying a correlation between risk propension and risk of default of the bank, and a material presence of institutional investors in the capital: "the probability of default of banks is higher when non-financial companies or institutional investors hold a higher proportion of total equity. However, these results do not hold for listed banks in which non-financial compa-

A first conclusion which can be drawn from the cross-referenced reading of the rules on collective management and banking prudential requirements must, in our view, be that there is no *structural* incompatibility between the two regulatory sub-systems, such as to prevent or exclude the possibility of a CIU acquiring and holding a qualifying holding - including a controlling stake - in the capital of a bank. Besides the fact that such a prohibition should clearly result from the Law, and not simply be the result of interpretations, such statement is also contradicted by the contents of the Guidelines elaborated under the scope of Directive 2007/44/EU which in some points (which do not seem to be mere *obiter dicta*) makes explicit reference to such specific situation. Our conclusion is also supported by the considerable amounts of precedents already mentioned.

At the same time, and without prejudice to the above, there remains a clear need to strike a balance between the tendentially *dynamic* approach of the investment policy of a CIU, and the decidedly more *static* vision that derives from prudential regulations in the matter of qualifying holdings in banks. Of course, this element is central, especially when the CIU acquires a shareholding which allows it to exercise a dominant influence or the control over the target bank, but it should not be devalued where the shareholding is significant, albeit not such as to grant control over the bank to the CIU.

In the light of the considerations set out in the preceding paragraphs, a first balance should be struck between, on the one hand, the investment policy of the CIU and, on the other, the bank's strategic and business plan. On a *static* level, the point of balance is naturally represented by the moment when the CIU's assets are invested in the bank's capital: the point of balance requires, at that stage, compliance with the criterion of financial soundness, taking as an element of evaluation the CIU's assets, and any financial support deriving from leverage. On a *dynamic* level, the balance is represented by at least two elements: firstly, the conditions ensuring that the exit of the CIU from the bank's capital occurs during a stage of development and of the strategic plan of the latter, and in such a way, as to enable the bank not to suffer negative repercussions, or - at worst - to minimise them. Especially, projects regarding the acquisition of qualifying holdings in the capital of banks by CIUs should therefore be accompanied by a clear divestment strategy, notified in advance to the Supervisory Authority, to be specifically appreciated in the context of the evaluation of the acquisition project. The acquisition plan should also be updated over time to reflect significant changes in the situation of the target bank as well as in the CIU's conditions.

Besides the above, the point of balance being discussed must also be determined taking into account the compatibility between the CIU's situation and any *additional* funding commitments which the Supervisory Authority may require, or impose, in the context of the proposed acquisition, and even thereafter. Therefore, if additional funds are required, these should - first of all - be calibrated having regard

nies hold higher stakes suggesting that the market might be limiting the risk-taking incentives of such shareholders. We further show that market forces might be more effective in influencing risk in banks with a higher involvement of non-financial companies than in banks with a higher portion of stock held by institutional investors."

solely to the current or prospective - but in any case, *predefined* - perimeter of the CIU's assets, since the latter obviously cannot have any certainty of being able to draw on any resources other than those initially collected. Always from a dynamic perspective, the CIU should therefore include, in the definition of its investment strategy connected to the proposed acquisition of the participation, moments and phases which, alternatively, or cumulatively, contemplate, for example: (i) the divestiture of any assets in the portfolio, in accordance with a time cycle that potentially makes available resources to be used for future funding needs of the target bank; (ii) if practicable, possible issues of new units or CIU shares (eventually accompanied by preliminary commitments to this effect by CIU participants, where deemed compatible with applicable regulations[51]); (iii) residual use of leverage, for example where the first two pathways are not sufficient or practicable, in order to meet additional funding demands. This assessment should also take into account the duration of the CIU, which must, of course, be compatible with the overall proposed acquisition and future prospects.

It should also be considered that, in private equity transactions, the use of leverage is often a major component of the relative transactions; however, it is also a possible critical factor for the acquisition project and its subsequent fate, as it might raise specific negative risks for the target bank. The CIU will therefore necessarily need to adapt and structure the size, repayment and leverage support plan (including debt amortisation and interest payments) on the basis of the bank's performance and its ability to generate - *under normal conditions* - sufficient resources. The analysis of this element should also involve taking into consideration possible stress situations, as a result of which the bank might be unable to distribute dividends or reserves for extended periods of time.

2.5 Final remarks

The analysis carried out has moved along two main lines: on the one hand, that of rules that apply to collective asset management; on the other hand, prudential regulation and supervision over banks and financial institutions. The two perspectives are different, but not incompatible. The typically financial perspective from which the CIU operates must, in fact, be combined with the need to ensure compliance with the requirements stemming from the core rules on prudential requirements. On the other hand, the prudential supervision requirements must take into account the very specific nature of a (qualified) participant in the bank's capital which, in its turn, is subject to quite distinctive supervisory and regulatory regimes. The tension that arises between the two perspectives tends to increase along with

51 The issue is a sensitive one, and it touches on profiles that we need not discuss in depth here. In fact, within the typical perimeter of a CIU, specific obligations for participants to provide the CIU with additional resources are (at least generally) not included (and, in fact, they are not considered as potential elements of a CIU by the ESMA Guidelines under the AIFMD). However, distinct commitments whereby participants, with varying degrees of intensity, declare themselves willing or committed to provide the CIU with such resources, should in principle be considered eligible. These commitments stand however on a different plan from the structural documents that constitute a CIU: as regards these profiles, allow us to make reference to F. Annunziata (nt. 16), page 156 and following.

the complexity of each transaction, and the specific "weight" that the CIU may have in the bank's capital.

The current state of legislation, and the quite recent experiences of transactions involving the acquisition by private equity CIUs of qualifying holdings in the capital of banks, do not allow final conclusions to be drawn, although they provide an opportunity to represent at least some of the most relevant issues that arise in this area.

If one looks at rules on CIUs (especially, the AIFM Directive) the classical conception of a CIU needs to be re-considered in order to take into account the specific prudential requirements of the target company: the alteration affects essential elements of the "genetic" code of a CIU. The very notion of "investment policy" (a key element in the definition of CIUs) must be set in the broader context of prudential regulation of the financial target institutions: the investment policy, in fact, shall no longer be characterized, simply, by the search for a certain risk-return profile of the portfolio, or by the achievement of certain return objectives, because it is affected by the need to take into account further interests - different from those of the CIU, or of its investors - represented by the stability and the sound and prudent management of the target bank. This is a situation absolutely peculiar to the case in question and which is not present when a CIU invests in a kind of enterprise that is not (also) a financial entity subject to prudential supervision and, especially, a bank. As a consequence thereof, the perimeter of the interests that are pursued by a CIU is altered, and expanded, thus producing a "quasi-institutionalisation" of the role of the CIU when acting as a qualified shareholder of a bank.

Banking regulations are also affected by this hybridization: the presence of CIUs in the capital of a bank, with a qualified holding, requires a new approach to fundamental issues such as the role of a bank's key shareholder; its objectives; the impact on the bank of the use of leverage by the shareholder; the development of the strategic plans of the bank; risk management (without mentioning, once again, further issues which we have not deliberately addressed here and which relate to aspects of corporate governance in a broader sense).

The huge reforms which have characterised European capital market regulations after the financial crisis still move – and perhaps necessarily – according to sectorial logics, leaving unresolved many sensitive issues which inevitably arise in contexts which appear to operate in an increasingly integrated way, whereby distinctions between traditional sectors of financial regulations are thinning down, if not disappearing. It is, finally, up to the interpreter to try and bring the system back to a more unitary approach. The case of private equity funds as qualifying shareholders of banks may not be an isolated example.

3 Conclusions and policy implications

The issues addressed in the previous chapters offer fertile grounds for investigation and reflection. Collective asset management is in fact a multidimensional phenomenon, whose regulatory framework is struggling to remain confined in the "silos" of the relevant EU and national legislation. The structure and *modus operandi* of the funds raise issues involving many other sectors of the regulatory framework of the financial market (understood in the broadest sense); these issues are increasingly central, as more investment funds are operating in sectors and with logics far removed from those that, although many decades ago, had inspired the first legislative approaches to the matter. Of these issues, those - addressed in this study - that relate to the crossing or overlapping, so to speak, between (on one hand) collective management and the regulatory framework of listed issuers, and (on the other hand) between collective management and prudential supervision rules applicable to the company invested in are of particular importance. As has been shown, these are veritable true "crossroads" that relate to one or another of the regulatory frameworks at stake.

In terms of the relationship between collective management and the regulatory framework of listed issuers, points of tension emerge, mainly dependent on two factors: the first is the fact that the regulatory framework for issuers, in its most qualifying moments, is obviously designed having the model of public limited liability companies in mind. The difficulties that occur with regard to the listed CIUs arise, inter alia, due to the fact that CIUs can (and often do) assume a different form, i.e., that of the contractual CIUs, characterised by rules and structures far removed (at least at first sight) from corporate schemes. In truth, even in cases where the CIU assumes a corporate form (as may be the case for SICAFs or SICAVs), deviations from the rules of the jus commune that, in this case, connote the CIU companies, require significant adjustments.

At a more general level, it can be said that coordination difficulties arise from the basic approach of the regulatory framework for collective management , this approach regulates the CIU as an *intermediary* and therefore, neglects to (also) consider the CIU in the same way as a possible *issuer* (in the sense in which this term is used in the context of the regulatory framework of listed companies).

A particularly significant case relates to the takeover bid: the regulatory framework, in this case, is ill-suited to entities that are "mere" separate assets that lack - at least at first sight - a corporate organisation. The issue of the exercise of shareholders' rights relating to majority shareholdings held by an AIF and managed collectively in collective asset management, is not fully resolved.

The debated problem of recognition, or lack thereof, of funds' capacity ad litem, raises further difficulties in the contexts discussed. Most rules - often based on EU legislation - formulated by the Consolidated Law on Finance (regarding control, group, conflicts of interest, governance, the right to vote in shareholders meetings and list voting, etc.) have been established with exclusive reference to subjects with legal personality (or, at least, capacity ad litem), and are therefore difficult to apply to independent assets management collectively, such as contractual CIUs.

Some of the gaps reported could, perhaps, be overcome by using analogy: for example, filling the gaps in the regulatory framework for contractual CIUs with the rules dictated for bylaw-scheme CIUs and, as a last resort, those for public limited liability companies under jus commune. However, the hypothesis of intervening with rules that deal more directly with the issues discussed and that could clarify whether, and to what extent, the provisions of the Issuers' Regulation apply to CIUs (especially contractual CIUs), should not be completely ruled out: this could be interventions that do not necessarily need to have an impact on European standards or primary law, since they could often be placed on the regulatory level, or could even be guidelines or other instruments of soft law. An area that, in this respect, might lend itself to interventions of this kind seems, for example, to be governance 'inside' the CIU.

The examination of the issues that arise with regard to the purchase by CIUs of qualifying holdings in the capital of banks - extendible, with the appropriate adjustments, to all those subject to prudential supervision - was conducted by moving along two different guidelines: on the one hand, the perspective of the regulatory framework of collective management, and on the other hand, that of prudential supervision of banks. These two perspectives are different, but not incompatible. The typically financial perspective in which the CIUs operate should, in fact, be combined with the need to ensure respect for the rules of prudential supervision; at the same time, the application of the latter must take into consideration the very peculiar nature of such a (qualified) shareholder of the bank's capital and the interests it pursues. The tension that is generated between the two perspectives becomes even greater as - in light of the concrete circumstances of the case - the identification of an acceptable balance between the two perspectives becomes more complex. The current state of legislation and the very recent experience of transactions that have seen CIUs have holdings in the capital of banks, are factors that do not allow definitive conclusions to be made, although they offer the opportunity to represent at least some of the "crossroads" that arise in this context.

In any case, the picture (even if incomplete) seems to show a hybridisation effect between regulatory models, which leads to at least a different interpretation fundamental assumptions that characterise the two sectors, if not to change them. The "classic" view that characterises the matter in question and regulatory framework of CIUs is changing in order to take into account the specific needs of prudential supervision that characterise banks, and these changes affect essential elements. The same concept of "investment policy" (a key element in the definition of CIUs) must fit into the wider context of the prudential regulation of banks; it is no longer only characterised by the pursuit of a certain risk-return profile of the portfolio, or by the achievement of certain objectives, but it is characterised by the presence of 'third party' interests compared to that of the CIU, or of its investors, represented by the interest in the stability of and towards its sound and prudent management. This phenomenon is quite particular to the case in question and does not occur in the case of a CIU investing in a type of company that is not also a regulated company, as are the intermediaries subjected to forms of prudential supervision. This phenomenon involves, in some ways, a sort of "institutionalisation" of the role of the investing CIU and of the scope of interests towards which its activities are typically orientated

However, the regulatory framework for banks is also influenced by this hybridisation phenomenon: the presence of CIUs in the capital as, holders of qualifying shareholdings, entails the need to adopt a new approach in relation to fundamental issues such as the role of the reference shareholders of a bank, their objectives, the impact of the use of financial leverage, the strategic plan, risk management (once more withholding further issues that have deliberately not been addressed here and which relate to the profiles, *sensu lato*, of corporate governance).

Finally, all the cases discussed offer points for wider reflection, also in terms of policy decisions, as they are emblematic of the complexities that arise when "hybridisation" phenomena or overlaps between different sectors of the regulatory framework of the capital market occur. The financial crisis has seen the accentuation of situations that pose similar issues and within which it is possible to decipher the possible friction between various regulatory frameworks that, in the specific case, could overlap: for example, the pursuit of additional capital by the banking system has had to inevitably follow non-traditional channels, also turning to institutional investors, who made their entrance, with sometimes significant standing, and with the typical logic of the private equity sector, into the capital of banks. At the same time, the incessant legislative work that has characterised the regulatory framework of the European capital market after the financial crisis moves - still, and perhaps necessarily - with sectoral logics, however leaving many delicate issues that inevitably arise in a system which appears and operates in an increasingly integrated way unresolved. It is the responsibility of the interpreter to attempt to bring the system back to unity, in an interpretation that is as integrated as possible.

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