Italy Brings Clarity to Foreign Takeover Rules in Strategic Sectors

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Introduction

On 15 March 2012, the Italian Government chaired by Mario Monti introduced rules for the protection of companies’ operating in certain sensitive sectors from foreign takeovers, with the Law Decree No. 21 of 2012 (the "Strategic Sector Act"). This reform, which was urged by the outcomes of the proceeding initiated by the European Commission in 2009, responds to some of the concerns that the European Commission raised on the pre-existing regulation, which granted special powers to the shares held by the Italian Treasury in certain companies through so-called golden shares.

As of the date of issuance of the Strategic Sector Act, the Italian Government held such special powers in different formerly state-owned companies, such as Telecom Italia S.p.A., the defense contractor Finmeccanica S.p.A., and the energy key players Eni S.p.A. and Enel S.p.A.2

The Strategic Sector Act follows a new approach based on the identification of strategic industry sectors and assets, instead of specific entities, in respect of which the Italian Government is vested with a set of special powers ("Special Powers"), regardless of whether the Italian Government owns or participates in the target company. The Special Powers may be exercised by the Italian Government only in the event of the occurrence of certain specific situations that constitute a potential threat to the national interests (each an "Actual Threat").

To foster a positive environment for foreign investors, based on the predictability of the Government’s intervention, and to respond to the concerns of the European Commission, the Strategic Sector Act contains an articulated description of the situations of Actual Threat, with respect to each specific Special Power.

The Strategic Sectors Act creates a legal framework that brings clarity to what can be done by foreign investors, thus practically removing the risk from the Italian Government introducing ad-hoc measures to discourage foreign takeovers, as it did in 2001 in connection with France’s EDF building up a stake in Montedison (now Edison), and in 2011 when a group of foreign investors attempted to change Parmalat’s management and subsequently France’s Lactalis launched a bid for control of the company.
Background

The former Italian golden share law,\(^3\) No. 474 of 1994\(^4\) (the “Golden Share Act”), provided that the by-laws of certain companies, directly or indirectly controlled by the State, had to incorporate certain provisions that granted the Italian Government a wide and not entirely definite set of special powers\(^5\).

The EU Commission\(^6\) took steps against golden share laws implemented from time to time by European Member States,\(^7\) including Italy.\(^8\) In an attempt to mitigate such EU pressure, in 2003 the Italian Government passed a general reform of the Golden Share Act, which was, however, subsequently challenged\(^9\) by the European Commission.\(^10\) According to the European Court of Justice, laws aimed at safeguarding the national interests in strategic fields are consistent with EU law as long as their implementation is based on *objective and verifiable conditions*.

Arguably, the Golden Share Act coupled with a protectionist approach showed by the former Governments in recent occasions, such as in the Parmalat/Lactalis transaction, constituted a potential barrier for foreign investors. The Strategic Sector Act is indicative of the positive approach of the new Italian Government towards foreign investments and the EU common market principles.

The Strategic Sector Act

The approach of the Strategic Sector Act is differentiated between (i) companies operating strategic activities for the defense system and national security (“National Security Sector”); and (ii) companies operating strategic networks, plants, assets, and relationships in the field of energy, transportation and communications (“Energy, Transportation and Communications Sector”).

With implementing decrees,\(^11\) the Italian Government shall specify the strategic activities included in the National Security Sector, as well as the specific plants, networks, assets and relationships included in the Energy, Transportation and Communications Sector, in which respect it may be entitled to exercise one or more of its Special Power.

A. National Security Sector

With respect to companies operating in the National Security Sector, the Strategic Sector Act defines Actual Threat as an “*actual threat of a material prejudice to the essential interests of the defense and of the national security*”,\(^12\) and provides specific criteria on the basis of which the Government shall assess the existence of an Actual Threat with reference to each Special Power. The Government may exercise its Special Powers *vis-à-vis* any investor operating in the National Security Sector, whether from the EU or not, as follows.
1. Veto on Resolutions.

a) Veto Powers

Power to veto (as well as to impose specific terms and conditions on) material resolutions of the shareholders’ meeting, board of directors and other corporate bodies.

b) Actual Threat

Where the relevant resolution (and/or the underlying transaction) may trigger a situation affecting the safety of the Italian national and international defense.

c) Notice Procedure

A company envisaging a relevant resolution has to notify the Italian Government. The transaction is considered automatically approved, unless the Government exercises its veto rights within 15 days.

2. Block on Investments.

a) Block on Investments

Power to block the direct or indirect purchase (including through shareholders’ agreements) of participations with voting rights.

b) Actual Threat

Where the potential investor would hold participations and voting rights that would enable it to jeopardize the National Security Sector.

c) Notice Procedure

The purchase of a participation in a relevant company has to be notified to the Government within 10 days, and the purchase is considered approved unless the Government vetoes it within 15 days as of the day of the notice. The Strategic Sector Act clearly defines the thresholds for the notification obligations in case of purchase of participations in listed companies (2%, 3%, 5%, 10%, 15%, 20% and 25%) but apparently not in case of purchase of participations in non-listed companies.

3. Special Terms and Conditions.

a) Special Terms and Conditions

Power to impose special terms and conditions in order to safeguard supplies, security of information, transfer of technology and export controls in cases of any acquisitions of participations in companies in the National Security Sector.

b) Actual Threat

Same definition as in point 1(b) above.

c) Notice Procedure

Same notice procedure as in point 1(c) above.
**B. Energy, Transportation and Communications**

The power of the Italian Government *vis-à-vis* companies operating Energy, Transportation and Communications has a more limited scope. In fact, the Italian Government may exercise the Special Powers described below only *vis-à-vis* non-EU investors, provided there is an Actual Threat that may jeopardize a plant, network, asset or relationship, included in the Energy, Transportation and Communications Sector, on the basis of "objective and non discriminatory criteria."

1. **Veto on Resolutions.**
   
   **a) Veto Powers**
   
   Power to veto (as well as to impose specific terms and conditions upon) material resolutions of the shareholders’ meeting or of other bodies, including the board of directors, as well as any resolution, action or transaction, which may determine a change in the property rights, control and availability of the plant, network, asset or relationships included in the Energy, Transportation and Communications Sector.
   
   **b) Actual Threat**
   
   Where the transaction/resolution may jeopardize the public interest in the Energy, Transport and Communications Sector.
   
   **c) Notice Procedure**
   
   A company envisaging a relevant resolution has to notify the Government within 10 days of the date of the resolution and, in any event, before such resolution is implemented. If the Government does not exercise its veto right within 10 days, the transaction is automatically approved.

2. **Block on Investments.**
   
   **a) Block on Investments**
   
   Power to block (as well as to impose specific terms and conditions upon) the purchase of participations in relevant companies by a non-EU investor, subject to the condition of reciprocity.
   
   **b) Actual Threat**
   
   Where a non-EU investor may potentially acquire the control of a relevant company.
   
   **c) Notice Procedure**
   
   Anyone purchasing participations in a relevant company shall notify the Government within 10 days, and the purchase is considered approved unless the Government vetoes it within the following 15 days. During this period, only the non-financial rights of the purchased participation are suspended.
3. Special Terms and Conditions.

a) Special Terms and Conditions
The Italian Government may impose special terms and conditions to ensure Material Assets’ safety, when such special terms and conditions would suffice to eliminate the Threat and therefore avoid the use of the veto.

b) Actual Threat
Same definition as in point 1(b) above.

c) Notice Procedure
Same procedure as in point 1(c) above.

C. Sanctions
The Strategic Sector Act provides that any resolution taken in violation of the Government’s veto rights on resolutions, notice obligations and possible special terms and conditions imposed by the Government is null and void, and the Government may mandate the reinstatement of the situation at one’s expense. Moreover, the violators may be subject to a fine ranging from a minimum of 1% of the consolidated turnover of the companies involved in the transaction (as resulting from the latest financial statements), to a maximum of twice the value of the transaction.

Conclusions and Expected Next Steps
Pursuant to Italian constitutional law,20 the Strategic Sector Act is applicable as of 16 March 2012. However, the golden share under the Golden Share Act remains in force, and the Special Powers may not be exercised by the Italian Government before the approval by the Government of the implementing decrees21 mentioned above, with which the specific strategic relevant assets will be identified. Moreover, Parliament shall convert the Strategic Sector Act into a law within 60 days, possibly with amendments.

If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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On 16 February 2011, the European Commission “has requested Italy to modify legislation that grants the State special powers to intervene in ownership and management decisions in privatised companies operating in strategic sectors such as the telecommunications and energy sectors. The Commission considers that the special powers constitute unjustified restrictions on the free movement of capital and the right of establishment in the EU. The Commission’s request takes the form of a reasoned opinion, the second stage of an infringement procedure. If the Italian authorities fail to take satisfactory measures to remedy the infringement of EU law within two months, the Commission may decide to refer the case to the European Court of Justice” (IP/11/175).

European Commission IP/11/175.

In the early 90’s Italy, like other European states, such as France and the United Kingdom, started a process of privatizations of state-owned companies. In the context of this privatization process, the Italian Parliament passed its first golden-share law on 30 July 1994.

The Golden Share Act was approved as decree law No. 332 of 31 May 1994, converted (with amendments) into law No. 474 as of 30 July 1994, and subsequently further amended with law No. 350 as of 24 December 2003.

Notably, the power to veto material corporate resolutions and to appoint certain directors.

The European Commission took the initiative, which was then also backed by the European Court of Justice.

In 2002, the European Court of Justice ruled against the golden share laws enacted by Portugal (case C-367/98), Belgium (case C-503/99) and France (case C-483/99).

Case C-58/99. On 23 May 2000, the European Court of Justice for the first time ruled against the Italian golden share triggered by the Golden Share Act, for breach of the free movement of capital and the right of establishment in the EU. More precisely, a threshold (equal to 3% of the company’s share capital) was set in the by-laws of ENI S.p.A. (article 6(1)(a)) and of Telecom Italia S.p.A. (article 5(1)(a)). If any shareholder was to pass such threshold, his voting powers were automatically frozen until the Minister of Treasury had approved such ‘relevant shareholder’ and, should the Minister not grant such approval, the shareholder would have been legally bound to sell his shares. In 2003, the European Court of Justice then issued its famous ruling against the UK golden share rights held in the British Airports Authority (Case C-98/01).

Substantially on two main grounds: (i) the special powers thereunder constituted a breach of the free movement of capital and right of establishment principles; and (ii) its provisions were vague and vested the Italian Government with broad and unpredictable powers.

On 13 July 2007, the EU Commission started a new proceeding, which led on 26 March 2009 to another European Court of Justice ruling against Italy (Case C-326/07).

Such further implementing decrees are expected to be issued in the following months.

Strategic Sector Act, article 1, section 1.

Relevant resolutions would involve a merger, demerger, sale of business, sale of assets, transfer of the registered office abroad, change of the corporate purpose, dissolution of the company, transfer of property or usage rights on tangible and intangible assets, as well as the granting of any encumbrances.

More precisely, the Strategic Sector Act refers to an actual threat to the integrity of the defense system and national security, safety of the information relating to the military defense, the international interests of the country and the protection of the Italian territory, borders and strategic infrastructures. There is also a generic and not entirely clear cross-reference to the criteria set forth for the veto rights on investments.

Such notice does not trigger the public notice obligation of article 114 of legislative decree No. 58/1998 (the Italian unified financial law, “TUF”).

Days are calculated as of the day the notice was given. The Government may request clarifications and, in such case, the 15-days term is suspended, but such clarifications have to be provided within 10 days as of the request for clarification.

Relevant resolutions would involve a merger, demerger, sale of business, sale of assets, transfer of the registered office abroad, change of the corporate purpose, dissolution of the company, transfer of property or usage rights on tangible and intangible assets, as well as any encumbrances limiting their usage.

Such notice does not trigger the public notice obligation of article 114 TUF.

Days are calculated as of the day the notice was given. The Government may request clarification and, in such case, the 15-days term is suspended, but such clarifications have to be provided within 10 days as of the request for clarifications. Until such term has not expired, the validity of the relevant resolution (or act or transaction) is suspended.

In particular, Article 77 of the Italian Constitution.

Which, as discussed, are expected to be issued in the upcoming months.