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Controlling shareholders and minority protection: governance lessons from the case of Telecom Italia

by

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Controlling Shareholders and Minority Protection. Governance Lessons from the case of Telecom Italia*

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Abstract

In this paper, we study the history of Telecom Italia, the sixth biggest world telecommunication company for turnover, to evaluate how changes in control affected minority protection. Telecom Italia was privatized in 1997 and it has been the target of two takeovers in 1999 by Olivetti and 2001 by Pirelli. Recently, in 2008, control was ultimately passed over to a newco, Telco, owned by the Spanish Telefónica and a consortium of Italian banks. We analyze how the acquisitions of Telecom Italia were achieved and, in particular, who paid for the control, and what were the consequences for minorities**.** We show that, in the case of Telecom Italia, the implementation of pyramids is connected with the existence of large private benefits, measured both by the size of premium paid for the acquisition and by the voting premium. However, minorities constantly suffered a strong expropriation due to the acquisitions. Our analysis reveals that despite the introduction of the Draghi reform in 1998, aimed to strengthen investors' rights, minority protection is still inadequate in the Italian financial market.

JEL Classification: G32, G34.

Key words: Ownership structure; Minority protection; Wealth transfer; Business groups; Voting premium; Case Study.

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1. Introduction

The changes of control of Telecom Italia (TI henceforth), nowadays the sixth largest telecommunication company in the world by turnover, are a textbook case to learn on Italian corporate governance. Founded in 1994 as a state-owned company, TI was the first Italian public company to be privatised in 1997. In 1999, the company suffered a hostile takeover by Olivetti, controlled by Roberto Colaninno. In 2001 Colannino sold his stake to the Italian private group Pirelli. In 2007 The Italian conglomerate ultimately sold its control stake to a consortium of Italian financial companies and Telefónica, the Spanish major telecommunication company, now controlling TI through the newco Telco.

The history of Telecom Italia has already attracted the interest of researcher. Kruse (2007) analyses Olivetti's acquisition of TI, showing how Olivetti pursued several operations perceived to be detrimental to Telecom Italia's minority shareholders, but also how minority shareholders were atypically vigorous in fighting back. Meoli et al. (2008a) contrast the treatment of minorities through the first and second acquisition of TI. In this paper we revise what has now become the "long tale" of TI trying to develop some policy implications from the comparison of the three changes in ownership. In particular, our main aim is to evaluate the treatment of minorities in the acquisitions of TI. The history of TI does not involve a scandal due to bankruptcy or illegal activities, such as for instance the case of Parmalat recently considered in the literature by Melis (2005), but rather it is an exemplary case of expropriation of minorities carried out despite the Draghi reform in 1998, implemented to enhance minority protection.

The acquisitions of TI in 1999, 2001 share an important feature, because they were performed by groups with a pyramidal ownership structure. This structure may generate several concerns. First of all, when the separation between ownership and control is obtained via groups, high managerial agency cost may arise (Claessens et al., 2002; La Porta et al., 2002; Bekaert et al, 2003; Lins, 2003), and private control benefits are larger (Burkart et al., 1998; Nenova, 2003; Doidge, 2004; Dyck and Zingales, 2004). Secondly, recent studies in corporate finance underline how pyramids adversely affect the protection of minority shareholders (Bebchuck et al., 2000; La Porta et al., 2000). Third, a pyramid structure determines an underdeveloped market for corporate control and this point is commonly investigated in the literature by analysing how markets award voting rights (Nenova, 2003; Doidge, 2004). Although similar, these operations differed under important aspects, and in particular with regards to the acquisition process: in fact, Olivetti's takeover was carried out through a tender offer, while the following acquisitions were performed via a private purchase of a controlling block.

In this paper, therefore, we first analyse how Olivetti's, Pirelli's and Telco's takeovers were achieved and, in particular, who paid for the acquisition of control, by tracing down all operations performed in the market by all companies in the two groups. Second, we contrast the operations with regards controlling shareholder benefit and minority protection. We do this by testing the existence of private benefits extracted by controlling shareholders, and whether minorities were protected from expropriation during the acquisitions. Our results show that, on the one hand, in all acquisitions the controlling shareholder contributed with a small percentage of the total equity investment. On the other hand, the Pirelli's acquisition, obtained through a private purchase, had the worst effect for minorities, possibly due to an extraction of private benefits by part of the controlling shareholder. Our analysis reveals that despite the consistent improvement in Italian corporate governance law after the introduction of the Draghi reform in 1998 (see for instance Melis, 2000), the Italian legal framework is still weak in defending minorities' rights, and some recommendations to strengthen its efficiency are provided in this work.

The remainder of the paper is organised as follows. The following section contains a short description of the stylized facts on TI's history. Further we report a detailed analysis of the ultimate payer of the two acquisitions, and an analysis of the effects of controlling minority shareholders. We draw some governance lessons from the case in the following section and then we conclude. A description of the data used in this paper and details of the two acquisitions are reported in Appendix.

2. Changes in ownership in the history of Telecom Italia

This section provides a summary of the main events in recent history of TI, focusing in particular on changes of ownership in the history of the company as summarised in Table 1.

On 30 June 1994, the IRI Board[1] approved the "Telecommunications restructuring plan". Under this plan, the five companies in the IRI-Stet Group operating in the telephone industry (SIP[2], Iritel, Italcable, Telespazio and Sirm) were to merge in a new company, i.e. TI. On 28 June 1995, the rulings of the TI shareholders' meeting of the 5 May 1995 were implemented, and this brought to a partial split of the company subsequent to foundation of TI Mobile Spa (TIM), which started its operations in July, taking over mobile telecommunications-related services. On

30 January 1997, the TI Board of Directors started to undertake the incorporation of TI into Stet. On 18 July, TI merged with Stet, which subsequently changed its company name to TI.

In 1997 the Council of Ministers published the Law Decree for the privatisation of TI. The sale of shares held by the Treasury took place between October 20 and October 24. This was the first Italian public company with widespread public share ownership. This massive privatisation involved more than two millions of individual investors. The ownership structure was featured by a stable core of shareholders representing the 6% of the ordinary capital and among them there was the Italian Treasury, owning a golden share (granting the power of veto on particular operations such as mergers, etc).

In February 1999, Olivetti, run by Roberto Colannino but ultimately controlled by Bell, a non-listed company controlling the pyramid with a 17% stake in Olivetti, announced the launch of a takeover bid for TI's equity capital. After receiving Consob authorization, the offer was officially launched on 30 April, and was successfully concluded on the 21 May 2006. The offer, with a total value estimated in 59.9b Euro, was the first successful hostile takeover and the greatest financial operation in the history of Italian market. After the acquisition was accomplished, TI entered a group structure depicted in Figure 1.

At the end of July 2001 Olimpia Spa, a vehicle company owned by Pirelli Spa, Edizione Finance International SA (Benetton Group), Intesa Bci and UniCredito Italiano Spa[3], ultimately controlled by the Tronchetti Provera family, acquired approximately 27.7% of Olivetti's ordinary share capital[4], 21% directly from Bell and 6% from the market. Figure 2 and Figure 3 describe the position of TI immediately before and after Olimpia's acquisition of Olivetti. This new group represents a new form of ownership. First, the ownership chain involves several companies all traded on the stock market (except Olimpia). Second, the presence of relevant banking minorities at a crucial point of the ownership chain makes the banking endorsement a strategic component of the pyramidal structure.

After the acquisition, the Pirelli pyramid reshaped its financial structure by raising equity and transferring debt to the lower level of the ownership chain. In 2002 Pirelli Real Estate (Pirelli RE), a company dealing with real estate operations for Pirelli group since the beginning of the '90s, went public through an IPO. On 24 and 26 May 2003, TI and Olivetti Shareholders' Meetings approved the plan to merge TI into Olivetti. The move was completed on 4 August, when the shares of a new company, named TI, began trading on the market. At the same time the

Pirelli group's chain was shortened also at the top, with the merger between Pirelli & C. and Pirelli Spa into Pirelli & C. Spa. On 7 December 2004 the tender offer of TI on TIM was announced, and a merger followed. The new company was traded on the market since 1 July 2005.

At the end of 2006, TI announced a plan to split off and sell its mobile unit TIM in face of mounting debt that reached almost 50b Euro. The decision provoked a widespread outcry in Italy as the split off was seen as the last dismantling of a national asset that generations of Italian tax-payers helped to build. Following this widespread disapproval, TI's chairman and ultimate controller, Marco Tronchetti Provera, resigned on 16 September 2006. The new chairman to be nominated was Guido Rossi, who ironically held the same position at the time of privatisation.[5]

On 28 April 2007, a consortium of Italian financial companies (Mediobanca, Assicurazioni Generali, Intesa-Sanpaolo and Benetton, through the holding Sintonia) and Telefónica launched an offer to acquire Pirelli's control stake in TI by taking over the whole capital of Olimpia, by creating another newco, Telco. The sale was performed on 24 October 2007, and Telco now owns a 23.6% controlling stake in TI (18% coming from the acquisition of Olimpia, and the rest coming from former ownership). While Telco's control is currently held by the Italian consortium (summing up a 57.7% ownership share), the largest share is owned by Telefónica (42.3%). It has to be noticed that Telefónica is the first telecommunication company involved in the acquisitions of TI since its privatisation. The ownership structure of TI after this acquisition is represented in Figure 4. Note that Olimpia is now completely absorbed into Telco.

Key consolidated data for TI, reported in Table 2, show how company's revenue kept increasing until 2003. Profitability did not follow the same pattern, as from 2001 onwards, contemporary to Pirelli's acquisition, the group experienced relevant losses. Nevertheless the company did not abandon a generous dividend policy, but started a necessary restructuring activity involving also a notable reduction of employees. Benefits from this restructuring process appear from 2005 onwards.

3. Analysis of TI's acquisitions

3.1. Financial commitment

In this section we provide evidence of the "small" financial commitment of the controlling shareholders that took over Telecom Italia. The acquisitions of TI were carried out by companies with a similar ownership structures, but via different acquisition procedures.

We consider all operations that a pyramidal group carries out to raise financial resources on the market. We take the group as a single entity, but we split its financial resources according to the kind of resource (equity or debt) and the subject involved (controlling shareholder or minority). The choice of the "deal window", i.e. the period of time we consider the group operating to finance the operation, was dictated by the information provided in official statements and in financial newspaper. We set the "deal window" to (0;+2) years, i.e. over the period the company carried out major operations strategically linked to the acquisitions.

Therefore, when analysing an operation, we refer to the following definition:

$$Deal = E_{CS} + E_{MS} + D_{CS} + D_{MS} \qquad (1)$$

where *Deal* represents an operation involving an important financial commitment with reference to the group dimension, i.e. the total amount paid for the acquisitions; E_{CS} is the contribution of the controlling shareholder in equity and convertible bonds; E_{MS} is the contribution of minorities in the deal in equity and convertible bonds; D_{CS} is the contribution of the controlling shareholder in loans and bonds; D_{MS} is the contribution of minorities in the deal in loans and bonds. We can assume to allocate a fraction of the capital collected as equity or debt to the controlling shareholder and to the rest to minorities according to ownership shares at relevant time. As in both takeovers we are considering groups with a pyramidal structure, we repeat the analysis at higher levels of the ownership chain to evaluate the contribution of the ultimate shareholder.

After processing all operations carried out by the whole group in the "deal window", we evaluate a measure that represents the interaction between controlling shareholders and other sources. In particular, we define "controlling shareholder leverage" as the ratio between the whole amount of money needed for the deal, and the direct contribution by part of the controlling shareholder:

$$CS\ Leverage = \frac{Deal}{CS + D_{CS}} \qquad (2)$$

The higher this ratio, the higher the amount of money raised from the minorities per single currency unit invested by the controlling shareholder. In Table 3 we report the results of our analysis for the three operations. Details on the acquisitions are provided in the Appendix.

Consider Olivetti's acquisition (Table 3, Panel A). Since a public offer took place, all TI shareholders were given a chance to sell their stake in the company, or to reject the offer. The bid was carried out by Tecnost, a listed company controlled almost 100% by Olivetti[6], controlled by Bell, a non-listed company owned by Roberto Colaninno and other entrepreneurs. The value offered was 11.00 Euro per ordinary share, and as 51.86% of the capital was collected, it involved a total expenditure of 31,069m Euro. Further 2,530m Euro were collected in readjusting the financial structure of the group in the same period. Thus, the total amount of the deal sums up to 33,599m Euro. As we report in Table 3, only 4,035m Euro are a direct contribution of the ultimate controlling shareholder Bell, while a very relevant role is played by minorities both of Tecnost and Olivetti. In particular, Tecnost largely recurred to debt, while Olivetti's minorities contributed to the operations participating at different operations in equity. To summarise, Bell's investment equals a 12% share of the total investment, so that we get a value of the controlling leverage equal to 8.31, meaning that for each Euro invested in the group, Bell was able to acquire effectively a value corresponding to 8.31 Euro.

Telecom Italia was not controlled by Roberto Colaninno for long. In 2001 the majority shareholder Bell sold its ownership share in Olivetti to the Pirelli group, that carried out the takeover via Olimpia. This operation did not involve the market, as the ownership quote acquired was slightly lower than 30%, the legal threshold for a public offer. The acquisition from Olimpia created a complex pyramidal structure, with Marco Tronchetti Provera as the ultimate controller. In Table 3 (Panel B) we report evidence of the financial contributions to this acquisition from all companies in the Pirelli pyramid. The largest part is directly paid by Olimpia minorities[7] in equity and Pirelli Spa minorities in debt, while smaller contributions come from Pirelli & C. and Camfin minorities. The ultimate controller of the group, Marco Tronchetti Provera family, directly invested in the operation only 134m Euro in equity capital, and further 179m Euro in debt can be attributed to him, summing up to a 4% share of the total acquisition price. From our calculations the value of the controlling leverage is 26.25. This means that for each Euro invested by the controlling family, 26 Euro were raised from the market, almost four time as much as it was in the first operation, showing that the commitment of the controlling shareholder was much smaller that in Olivetti's acquisition.

Our interpretation here is that the implementation of a pyramidal group helped both controller to carry out the operation recurring to external financial funds, coming both from debt and equity, reducing his/hers direct investment, and generating a conflict with minority interests.

Telecom was lastly taken over via Telco in 2007 (Table 3, Panel C). This operation offers a third procedure, as the acquisition of TI was performed by acquiring Olimpia through the newco Telco. It has to be noticed that, in this operation, no single shareholder obtains an absolute control over Telco. Nevertheless, with a 42.3% share in the newco, Telefónica becomes the relative controller. Morever, Telefónica is the only non-financial entity with a ownership in the company. Notice how the controlling leverage is here limited to a 3.03 level: as Telefónica's ownership is diffused, there is not a pyramidal structure reducing the amount of cash needed for the acquisition. Besides, if we consider the consortium and Telefónica as a single shareholder, the controlling leverage is reduced to 1.28.

3.2. Effects for controlling and minority shareholders

The main conclusion from the previous section is that the control of TI was largely paid by minorities in both Olivetti's and Pirelli's acquisitions. Conversely, in the last acquisitions, financial companies and diffused equity are the instrument employed for the acquisition financing. In what follows, we focus on the main consequences of these takeovers on controlling and minority shareholders. We show that who takes control of Telecom Italia can extract a large flow of private benefit at the expense of minorities. Nevertheless, because of the different acquisition procedure, effects on controlling and minority shareholders are particularly interesting for the Olivetti's and Pirelli's acquisitions.

Private benefits. One of the reasons why the presence of complex group structures is detrimental to the development of markets is that they give rise to high managerial agency costs and therefore higher private benefits. We first focus on the two acquisitions looking for evidence on opportunities to extract private benefits. We then consider the whole period of control period of control, in order to understand whether the two controllers have actually been able to extract benefits. A first methodology to measure private benefits, pioneered by Barclay and Holderness (1989), focuses on privately negotiated transfers of controlling blocks in public traded companies, measuring the following acquisition premium (*AP*) and the adjusted acquisition premium (*adjAP*):

$$AP = \frac{P_{acq} - P_{after-offer}}{P_{after-offer}} \qquad (3)$$

$$adjAP = \alpha \left[\frac{P_{acq} - P_{after-offer}}{P_{after-offer}} \right] \qquad (4)$$

where P_{acq} is the price per share an acquirer pays to previous shareholders, and P_{post_offer} is the market price of a share after the change in control, and α corrects for the size of block to which the offer refers.. The first price represents the cash flow benefits from this fractional ownership and the private benefits stemming from his controlling position. By contrast, the second price reflects only the cash flow benefits that non-controlling shareholders expect to receive under the new management. Hence the difference between the price per share paid by the acquiring party and the price per share on the market after the announcement captures the differential payoff accruing to the controlling shareholder. A correction, through α, is needed because the two offers we are analysing refer to a different percentage of equity: we set the parameter to 1 in the case of a public offer on the whole equity, and to the correct percentage when considering a private offer on a controlling block.

We report the full set of results of our analysis in Table 4, Panel A. In Olivetti's acquisition, Tecnost acted as a bidder targeting TI. The amount paid by Tecnost was high (31.07m Euro), even if only a small amount was paid cash. The final offer for a single share was of 11.50 Euro, while the market price after the issue was of 9.86 Euro. The acquisition premium is therefore equal to 1.64 Euro per share, 16.63% of day-after-offer price. Since the operation involved the exchange of approximately 2.70bn of shares, the premium paid to the market is approximately 4,428m Euro. In the 2001 Pirelli's acquisition, Pirelli Spa acquired a block in Olivetti to gain control of TI. The offer was agreed to be equal to 4.17 Euro per share, while the relevant market value was 1.95 Euro per share (113.85% premium per share). As the offer regarded more than 1.97bn of share, the aggregate premium was 4,373m Euro. Rescaling this value on the 27.7% acquisition share, we get a corrected premium of 0.61 Euro, equal to 31.53%. In the case of

Telco's acquisition, notice that Olimpia is a non traded company. Nevertheless, according to the acquisition report, TI's share were paid 2.82 Euro each, with a current market value of 2.26 Euro and while the market price after the transaction felt to 2.09 Euro. We can therefore evaluate a 35% Acquisition Premium, that falls to 6% when rescaled for the acquisition share.

Note that Dyck and Zingales (1994) provide evidence regarding acquisition premium around the world between 1990 and 2000. Italian values are among the highest around the world, and distribution is described by a strongly skewed distribution, with median value of 0.16 and a mean of 0.37. The full set of results is reported in Table 4.

We now turn to analyse the voting premium to check whether controlling shareholders appropriated a flow of private earnings during their respective period of control. Following the methodology proposed by Rydqvist (1987), Zingales (1994, 1995) and Nenova (2001)[8], we consider the price difference between two classes of stocks, with similar or identical dividend rights and liquidity, but different voting rights. If control is valuable, then corporate votes should be valuable as well.

We calculate the voting premium (*VP*) as follows:

$$VP = \frac{P_{ord} - P_{sav}}{P_{sav}} \qquad (5)$$

where P_{ord} is the price of a ordinary share and P_{sav} is the price of a saving share[9].

Voting Premium represents the premium that the market assigns to an ordinary share for its voting power, as a percentage on the value of a saving one. We expect the voting premium to be at different levels under the five ownership schemes that the company experienced during its life: the era of public ownership, the post-privatisation era, the Olivetti's, the Pirelli's and the Telco's control (see Tables A1-A3 in the Appendix for details). In particular, since the market price represents the value of an ordinary share for minorities, but not for the controlling shareholder (whose share does not actually fluctuate on the market), we can observe the evolution of "minorities' importance" over time. In Figure 5, we report on the left the plot of the TI's ordinary and saving share, and on the right the behaviour of the voting premium.

Focusing on the voting premium trend, we can observe the importance of minority shareholders over the five periods. Before October 1997, TI was state-owned, and the role of voting rights was awarded by the market a 48.81% in average. A slight change can be seen after the October 1997 privatisation, when the Italian Treasury sells almost all its share in this company, allowing most of its capital to freely float on the market. We note an increase in the voting premium to 52%, as the market fixed a high value for the voting rights. This value had an erratic behaviour, that cannot be explained using micro- and/or macro-economic factors. It started its strongest rise after Olivetti's hostile takeover in May 1999, when ordinary shareholders were awarded by the market a voting premium over the 100%. When the ownership became more or less stable, the voting premium started a slow decrease, and with Pirelli's acquisition, in 2001, it slowly came back to the level prior to TI's privatization[10] . This result shows that the appropriation of benefit has been particularly high during Pirelli's control, justifying the high level of premium paid in the acquisition. The value of the Voting Premium shows a little reprise after the Telco's acquisition, but the data series is too short for a consistent comparison.

Expropriation of minorities. In this section we consider the position of minorities, looking for evidence of expropriation at their expense. We define expropriation as a persistent negative abnormal return in a window of time corresponding to the acquisitions under investigation. This negative abnormal return can be seen as expropriation at the expense of minorities shareholders for two reasons: a) in a pyramidal structure a controlling shareholder owns a share in a company by means of a series of ownership relationships, with a net effect being only a small percentage of the abnormal return; b) as shown in the previous section, a controlling shareholder may extract private benefits that offsets the negative effect on a share price.

We therefore employ an event analysis (as proposed in Brown and Warner 1985), to study the effects for minorities of both bidding and targeting company for the first and the second acquisitions. Considering the first acquisition, we take Olivetti (as a bidder, being Tecnost just a vehicle) and TI (target) minorities are clearly the objects of our analysis. Concerning Pirelli's acquisition, the choice is not trivial as Olimpia (the actual bidder) is a non-listed company. We therefore analyze consequences for Pirelli Spa, controller of Olimpia, to consider the bidder, and Olivetti and TI (the ultimate objective of the acquisition) to consider the target. With regards to the third acquisition we focus again on TI, target of the operation, and on Pirelli Spa, in order to evaluate whether the company acquiring the control suffer any abnormal effect.

We evaluate Abnormal Returns (AR) with a common market model, considering a short- (-1;+1) and a long-range (-30;+30) windows, choosing a 200-day estimation window one month before the two acquisitions. Results are reported in Table 5. As far as the first acquisition is concerned, we find that TI's share price performed an abnormal positive return both on a short- and a long-range windows, while effects on Olivetti's share price are not statistically significant. Results regarding Pirelli's acquisition are astoundingly different: a negative abnormal return is significant both for the target side, Olivetti's value, and for the bidding side, Pirelli Spa, while TI, the ultimate objective, does not benefit from the acquisition premium. When considering results on Telco's acquisition, impressively, we note that there is no positive reaction to the announcement for the Pirelli's stock, while TI's price reacts negatively. Again, the market incorporates an expropriation for minority shareholders.

The most important result, in our opinion, is that the first and second acquisitions had radically different consequences for minorities, as can also be seen from inspecting Figure 6.

The left figure reports abnormal returns for target and bidder in Olivetti's acquisition, while the right figure plots abnormal return for Pirelli Spa and Telecom, target and bidder of an operation only formally carried out by Olimpia as a bidder and Olivetti as a target. While in the first case we observe the positive effect of the public offer on the target's value, in the second case we detect a strong negative impact on the Pirelli Spa's public price. Since the controlling stake is firmly in the hands of a stable controlling agreement, we conclude that this acquisition was paid at minorities' expenses.

4. Lessons on Minority Protection

In this final section we summarize what are the most important lessons from the analysis of TI acquisitions. In particular we provide some recommendations on how to make the protection of minorities more effective in Italy, and suggest improvements in the regulation of financial markets. We first consider the specific influence on minority protection of the methods to separate ownership and control (1 and 2). Then we focus on two financial market rules that played a central role in this case (3 and 4). Last, we consider how external factors, such as media pressure, could also interfere with minority protection.

1. **Pyramid structure and dual class shares**

   Pyramid structure and dual class shares are used in Italy to separate ownership from control of the company. This framework allows company to face tough financial constraints to raise money from a wide set of channels, as reported in Nicodano (1998) and Bebchuck et al. (2000). For the case of TI, the pyramid structure and the dual-class structure allowed the controlling shareholder an excessive power that increased minority expropriation. We think that the actual legislation needs to be reinforced with the introduction of an option to exit for minorities when such a concentration of power takes place.

2. **Minority splitting**

   A high concentration of power is not unusual in corporate governance systems such as those in place in UK and USA, where though the controller (manager) owns a small number of shares, shareholders' meetings assess manager's decisions. By contrast, when a group is controlled by a pyramidal structure, the controlling shareholder keeps tight control of a series of shareholders' meetings at different levels of the pyramid structure, and thus (s)he can rely on a (usually) solid majority in all of them. Therefore the various shareholders' meetings cannot carry out an effective control: minorities are split at each level and thus they do not have the choice to reject the controlling shareholder decisions. In our view, in the presence of a pyramid structure, group shareholders' meetings need to be unified, so that group minorities may play an effective role in the corporate governance of the group.

3. **Rule on Public Offer**

   A very important form of protection for minorities is the mandatory public offer that a controlling shareholder must, according to Italian law, carry out when owning a share larger than 30%. In the case of TI, Colaninno's takeover took place via a public offer, but the Pirelli group acquisition avoided the public offer via a private 27% share acquisition from Bell, as reported in Figures 2 and 3 . Thus, the latter acquisition gives rise to doubts on the effectiveness of market enforcement law in Italy in a context where in general institutional investors do not play a substantial role and thus leaving minorities dispersed.

   We think that the 30% threshold, appropriated in other European countries, should be reconsidered for Italian big companies belonging to business groups. In this case, Consob, the financial market monitoring authority, should have the power to intervene when a minority expropriation is likely to happen.

4. **Equity issues with rights method (”enforced subscription”)**

   We have reported evidence that, for the case of TI, a controlling shareholder reduces her/his financial liabilities by using no just "debt leverage" but also ”equity leverage”, given that minority equity is collected through several rights issues. A contribution by Meoli et al.

(2008b) shows that, when private benefits are extracted, rights issues do not protect minority's value, but actually "enforce" minorities in exercising their pre-emptive rights. In fact, when the issuing is carried out at a substantial lower price than the market price, the right to subscribe has a high positive value, and it can be traded on the market, but at a price lower than its theoretical value, if an expropriation is expected. Once again, implications are more remarkable when considering a group of listed companies, that recur to minority equity through several companies.

5. **Media pressure**

   Dyck and Zingales (2004) show how media pressure can be a crucial factor to decrease the relevance of private benefits extracted by controlling shareholder. However, if media systems are strongly connected with industrial groups and politicians, as in Italy, this minority protection effect can be indeed limited.

5. Conclusions

We studied Telecom Italia, the sixth biggest world telecommunication company for turnover, to evaluate how the ownership structure and corporate governance have affected minority protection. Telecom Italia was privatised in 1997 and it has been the target of three takeovers: in 1999 by Olivetti, in 2001 by Pirelli and in 2007 by a consortium of Italian financial companies and Telefónica. We analysed how the acquisitions were achieved and, in particular, who paid for the control. The most strinking results regard the first and second acquisitions: in the 1999 Olivetti's hostile takeover, the controlling shareholder contributed with a 12% of the total equity investment, while in the 2001 acquisition, the family controlling Pirelli group paid less than 4% of the acquisition.

We also considered the consequences of the acquisitions for both controlling and minority shareholders. We estimated the expected private benefits for controlling shareholder by measuring the acquisitions premium, that was equal to 16.63% and 113.85% of the price after the Olivetti's and Pirelli's takeovers respectively. In order to compare the evolution of the private benefits during Olivetti's and Pirelli's control, we focused on the voting premium. When Colaninno was controlling the company, it increased to over 102%. It dropped to approximately 38% when company was acquired by Pirelli group, lower than the level experienced during the 1994-1997 state-ownership period. Afterwards we considered the effects on minorities during the two acquisitions. We showed that following the Pirelli acquisition, the market was strongly negative for the bidder companies (-48.70% in a two-month window for Pirelli Spa). This shows how, while the future of TI's control is still doubtful, minorities are constantly expropriated in all the operations involving a change in the control of the company.

This analysis provides clear evidence of the impact of changes in control, reflecting different corporate ownership schemes. We show that, due to the contemporaneous employment of several devices to device ownership and control, and to the inefficiency of governance rules regarding rights issues and tender offers, minority protection in Italy is still weak, and a special discipline is deserved with regards to groups owning several listed company.

There is a more general lesson to be learnt from the case of TI, of particular interest for those researchers dedicating their attention to the development of the Italian financial market and of the Italian economy. The "long tale" of TI regards a state-owned company that, after being privatized, quickly ended up in the hands of a stronger foreign partner. Is this process becoming a paradigm for the Italian capitalism? One can think of the case of Alitalia, another state-owned company currently involved in a troubled privatization process, and already involved in discussions regarding the necessity of a strong international partner. It will be another "long tale". *Repetita juvant*.

Appendix: Data description and takeover's details

In order to carry out the analysis provided in this paper, we have collected from several sources the following data:

1. Historical data

   We have collected information on the history of TI and other companies involved in Olivetti's and Pirelli's pyramids from two internet sites (www.telecomitalia.it and www.pirelli.com), providing a complete chronology of main events.

   A detailed information about all financial operations is provided by several issues of "Calepino dell'Azionista" and "Indici e dati", two annual publication edited by Mediobanca. In particular, every issue of "Indici e dati" provides in Table IX a list of all operations comporting a variation in equity capital of all listed companies (such as equity issues, convertible bond issues, acquisitions and so on).

   All event dates used in this paper are collected from "Il Sole 24 Ore", the most important Italian financial newspaper.

2. Ownership data

   We collected ownership data from Consob (Commissione Nazionale per le Societa' e per la Borsa), the Italian authority for the market.

3. Balance Sheet data

   All balance sheet data are collected from Datastream and official company's sources.

4. Market data

   All market data are collected from Datastream. All price series have been collected from 1 January 1997. Concerning market value on Datastream, it is defined as the share price multiplied by the number of ordinary shares in issue. The amount in issue is updated whenever new tranches of stock are issued or after a capital change.

5. Acquisition details

   All data regarding acquisitions are collected from official statements available online. In Table A1 below, we report the relevant details.

Notes

1. IRI was the holding company directly controlled by Ministry of Treasure, managing public ownership shares in industrial enterprises.
2. SIP was the state-owned listed company (owned via the holding STET) in charge of telecommunication.
3. Since 1993, in Italy banks have been able to acquire ownerships in industrial companies. Unicredito Italiano Spa and Intesa Bci are the two biggest Italian banks for market capitalisation with market value at the end of 2003 of 26.438m(illion) and 18.679m Euro, respectively.
4. According to Italian law, a public offer on the whole equity capital is mandatory only after the acquisition of a share above the 30% boundary.
5. In April 2007, TI controlling shareholder made public its intention to sell the company, so that another change in ownership is soon to be expected. Anyway, this paper limits its analysis to Olivetti's and Pirelli's acquisitions.
6. Six months before the deal, Tecnost was the target of a residual public offer aimed to delist the company, but actually it acted as a vehicle company for this takeover and was merged with Olivetti before being delisted.
7. It is worth mentioning that minorities in Olimpia are mainly banks, and therefore their status is to be considered partly different from that of other minorities in the group.
8. Note that the two methods to evaluate private benefits may suffer from a common bias (they capture only the ordinary pecuniary value component of private benefits, disregarding the non-financial, or psychic, aspect) and may underestimate the value of control (Dyck and Zingales, 2004). The non-financial component is to be considered relevant in this case, due to the implication of controlling TI in Italy.
9. Saving shares are labelled RNC ("Risparmio Non Convertibili") in the Italian market.
10. This result is robust even when we consider the decline of the average Voting Premium in Italy over the last decade (see Croci and Caprio, 2007): the abnormal Voting Premium falls from an average 53.14% in 2001 by almost 20% in the following two years.

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Tables

Table 1: The five ownership schemes of Telecom Italia

State-owned company period starts off when the company is founded, up to when the company is privatized. Diffuse ownership lasts until the Olivetti's acquisition of TI through Tecnost. Pyramidal group - Bell ends up on the day of official Pirelli's acquisition of TI through Olimpia. Pyramidal group - Pirelli ends up on the day of Telco's official acquisition of Olimpia.

Period	**Start**	**End**
State-owned company	30 June 1994	23 October 1997
Diffuse ownership	24 October 1997	20 May 1999
Pyramidal group - Olivetti	21 May 1999	27 July 2001
Pyramidal group - Pirelli	28 July 2001	23 October 2007
Consortium - Telco	24 October 2007	Nowadays

Table 2: Telecom Italia's consolidated data (m Euro)

All data refer to the consolidated balance sheets. Total revenues, Net earnings and Dividend paid are in millions of Euro. Ebitda and Ebit are in percentage on Total Revenues. Net Financial Position (NFP) is evaluated as (Financial Debt - Cash and liquidity).

	31.12.1998	**31.12.1999**	**31.12.2000**	**31.12.2001**
Total revenues	24,432	26,674	28,591	30,179
Ebitda %	45.9%	43.1%	41.2%	41.0%
Ebit %	23.7%	23.1%	21.5%	20.2%
Net earnings	1,978	1,737	2,028	-2,068
Dividends paid	751	1,096	2,324	2,309
NFP	8,287	8,187	20,080	22,496
Employees	123,966	122,662	114,669	116,020
	31.12.2002	**31.12.2003**	**31.12.2004**	**31.12.2005**
Total revenues	30,701	31,926	29,391	30,597
Ebitda %	41.1%	42.1%	45.5%	41.8%
Ebit %	22.0%	20.0%	26.9%	25.1%
Net earnings	-322	1,192	781	3,216
Dividends paid	2,307	2,291	2,780	2,342
NFP	18,518	33,809	29,525	39,858
Employees	106,620	93,187	91,365	85,484
	31.12.2006	**31.12.2007**		
Total revenues	31,881	31,703		
Ebitda %	40.2%	36.5%		
Ebit %	23.6%	18.1%		
Net earnings	3,003	2,455		
Dividends paid	2,997	2,831		
NFP	37,672	34,805		
Employees	83,209	83,429		

Table 3: Financial resources for the two acquisitions (m Euro)

Panel A reports the contributions of Tecnost minorities, Olivetti minorities and Bell (group's ultimate controlling shareholder) in the Olivetti's acquisition of Telecom Italia. Panel B reports the contribution of Olimpia minorities, Pirelli Spa minorities, Pirelli & C. minorities, Camfin minorities and Tronchetti Provera Family (group's ultimate controlling shareholder) in the Pirelli's acquisition of Telecom Italia. All figures are millions of Euro. Panel C reports the contribution of Telefonica and the consortium of Italian banks in the Telco's acquisition of Telecom Italia.

Panel A: Olivetti's acquisition (21 May 1999)			
Shareholders	**Equity**	**Debt**	**Total**
Tecnost minorities	4,602	12,704	17,306
Olivetti minorities	11,417	841	12,258
Controlling shareholder (Bell)	2,061	1,974	4,035
All shareholders	18,080	15,519	33,599
CS Leverage: (33,359/4,035)		*8.31*	
Panel B: Pirelli's acquisition (28 July 2001)			
Shareholders	**Equity**	**Debt**	**Total**
Olimpia minorities	3,286	-	3,286
Pirelli Spa minorities	1,084	2,584	3,668
Pirelli & C. minorities	840	-	840
Camfin minorities	110	-	110
Controlling shareholder (MTP family)	134	179	313
All shareholders	5,454	2,763	8,217
CS Leverage: (8,217/313)		*26.25*	
Panel C: Telco's acquisition (24 October 2007)			
Shareholders	**Equity**	**Debt**	**Total**
Banks' equity	1,874	-	1,874
Debt	-	913	913
"Strongest shareholder" (Telefónica)	1,374	-	1,374
All shareholders			4,161
CS Leverage: (4,161/1,374)		*3.03*	

Table 4: Evidence of private benefits

Panel A reports acquisition premium per share, adjusted acquisition premium per share and aggregate adjusted premium, as evaluated for the Olivett's, Pirelli's and Telco's acquisitions of TI. Panel B reports the average voting premium, for TI's shares, during the different ownership schemes in the history of TI.

Panel A: Acquisition premium for the two acquisitions			
	Olivetti's acquisition	**Pirelli's acquisition**	**Telco's acquisition**
Premium per share	€1.64 (16.63%)	€2.22 (113.85%)	€0.73 (35.93%)
Adj. Premium per share	€1.64 (16.63%)	€0.61 (31.53%)	€0.13 (6.28%)
Adj. Premium * N. shares	€4,428m	€4,373m	€315m

Panel B: Voting premium for the five "eras"	
State-owned company	48.81%
Diffuse ownership	52.18%
Olivetti's ownership	102.14%
Pirelli's ownership	37.08%
Telco's ownership	27.67%

Table 5: Expropriation of minorities

***, ** and * indicates statistical significance at 1%, 5%, and 10%, respectively

CAR	Olivetti's acq.		Pirelli's acq.			Telco's acq.	
	Olivetti	TI	Pirelli Spa	Olivetti	TI	Pirelli Spa	TI
-1;+1	-0.047	0.081 **	-0.242 ***	-0.155 **	0.015	0.024	0.002
	(0.047)	(0.024)	(0.028)	(0.036)	(0.024)	(0.016)	(0.003)
-30;+30	-0.067	0.177 *	-0.487 ***	-0.316 **	-0.116	0.006	-0.075 **
	(0.211)	(0.108)	(0.120)	(0.160)	(0.110)	(0.072)	(0.014)

Table A1: Olivetti's takeover details

Total value of takeover (100% of TI shares at final price)	€59,909m
Total market value of ordinary capital controlled (ord. sh.)	€47,769m
Total market value of equity capital controlled (all sh.)	€61,155m
% of the ordinary capital actually acquired	51.86%
Total value of the deal (% of shares bought at final price)	€31,069m
Ordinary Share Price before the Announcement	€8.12
Price offered per Share (final)	€11.50
Ordinary Share Price after the end of offering period	€9.86
% Acquisition Premium	16.63%
Offering period: from 21/04 to 21/05/99	
Bidder: Tecnost	
Payment: €6.92 cash + €2.90 Tecnost bonds + €1.68 Tecnost shares	

Table A2: Pirelli's takeover details

Total value of takeover (27% of Olivetti ordinary sh.)	€8,217m
Total market value of ordinary capital controlled (ord. sh.)	€15,984m
Total market value of equity capital controlled (all sh.)	€16,378m
% of the ordinary capital actually acquired	27%
Total value of the deal (% of shares at offer price)	€8,217m
Ordinary Share Price before the Announcement	€2.05
Price offered per Share	€4.17
Ordinary Share Price after the Transaction	€1.95
% Acquisition Premium	113.85%
Transaction date: from 28/07/01	
Bidder: Olimpia, non-listed company controlled by Pirelli Spa (60%)	
Payment: €4.17 cash	

Table A3: Telco's takeover details

Total value of takeover (100% of Olimpia)	€4,161m
% of the TI's ordinary capital actually acquired (via Olimpia)	18%
Total market value of TI equity capital controlled	€27,923m
Total market value of TI equity capital acquired	€6,728m
Ordinary Share Price before the Announcement	€2.26
Price paid per TI's share	€2.82
Ordinary Share Price after the Transaction	€2.09
% Acquisition Premium	€35.93%
Transaction date: 24/10/07	
Bidder: Telco	
Payment: cash	

Figures

Figure 1

Ownership Structure immediately after Colaninno’s hostile takeover (21/05/1999)

The figure shows the ownership and control structure of listed companies: each box represents a listed company; arrows represent control; the numbers above each box represent the percentage of voting rights directly owned by the controlling party; * represents dual-class structure; AD stands for “Amministratore Delegato”, equivalent to CEO, PCA stands for “Presidente del Consiglio d’Amministrazione”, equivalent to “Chairman of the Board”, (V)P stands for (Vice)President; the ultimate owner is represented at the top of the figure.

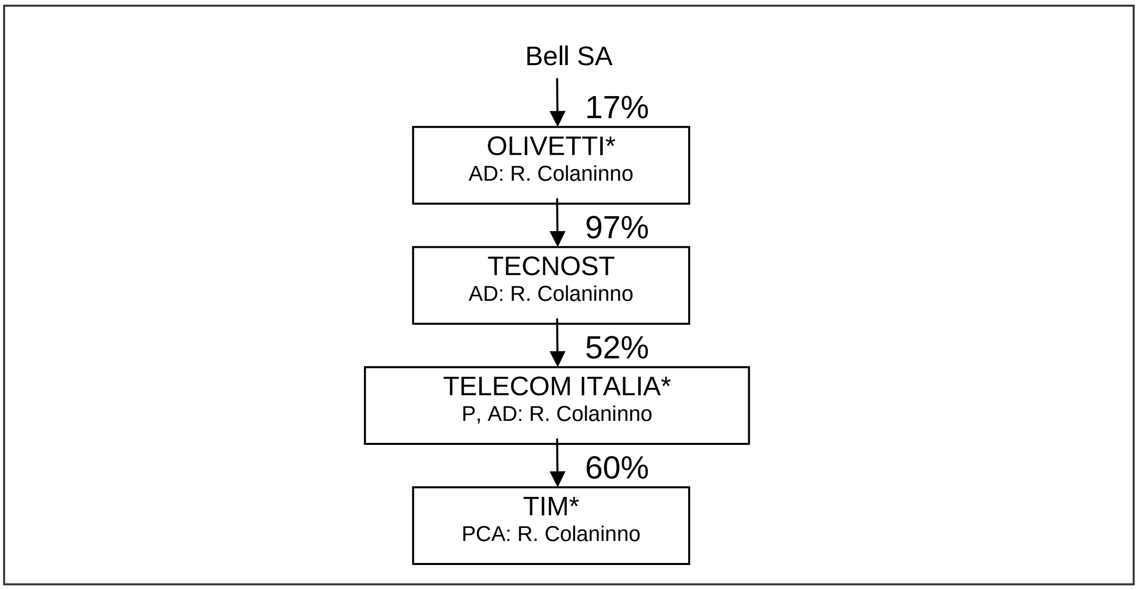

Figure 2

Ownership structure immediately before Pirelli’s acquisition (before 28/07/2001)

For explanation see notes to Figure 1.

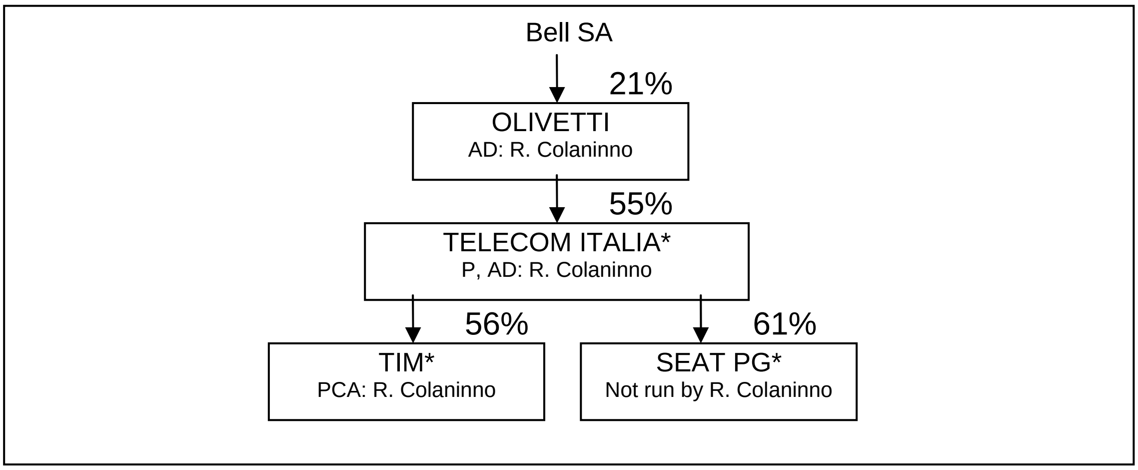

Figure 3

Ownership structure immediately after Pirelli's acquisition (after 28/07/2001)

For explanation see notes to Figure 1. In addition: the Figure reports also the position in the pyramid of Olimpia, a non-listed newco company, and of the voting pact controlling Pirelli & C.

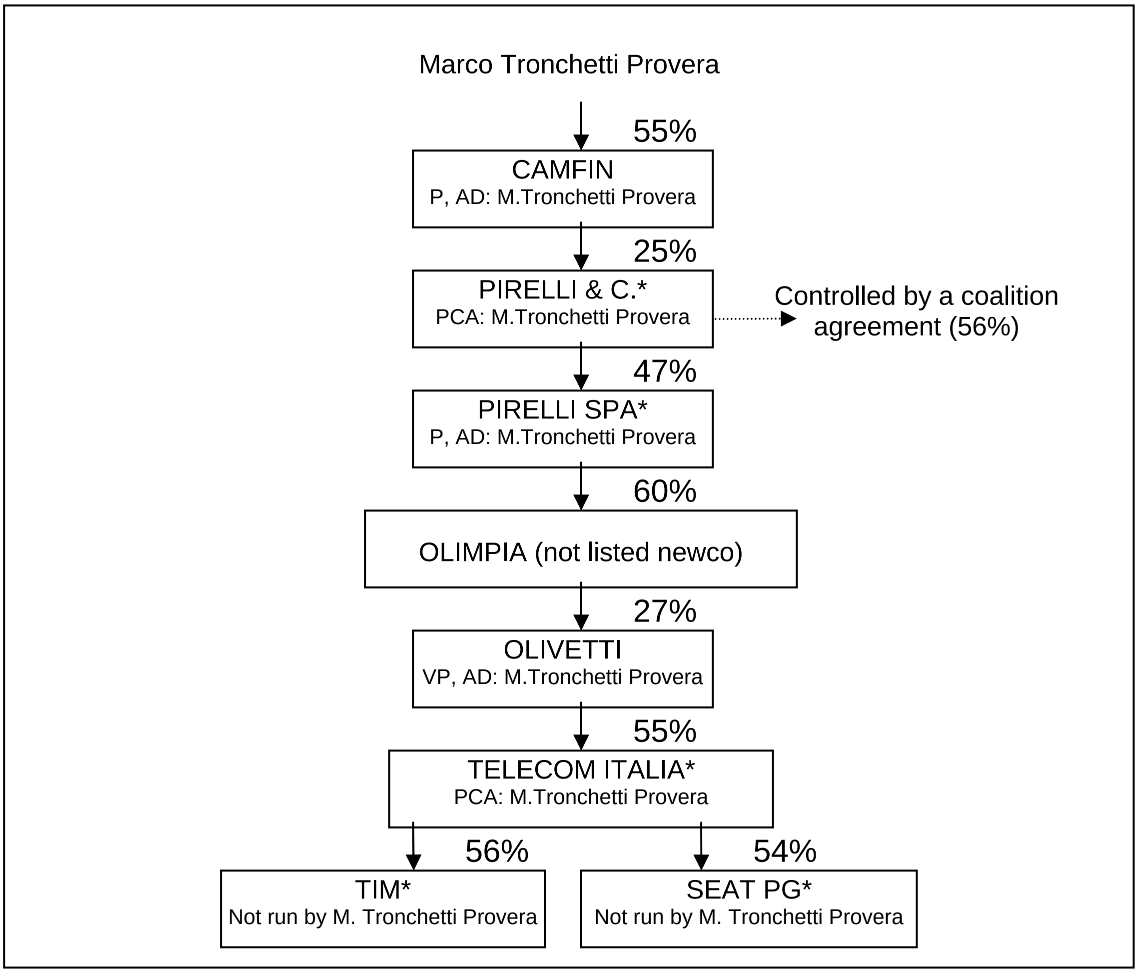

Figure 4

Ownership Structure immediately after Telco's acquisition (24/10/2007)

For explanation see notes to Figure 1.

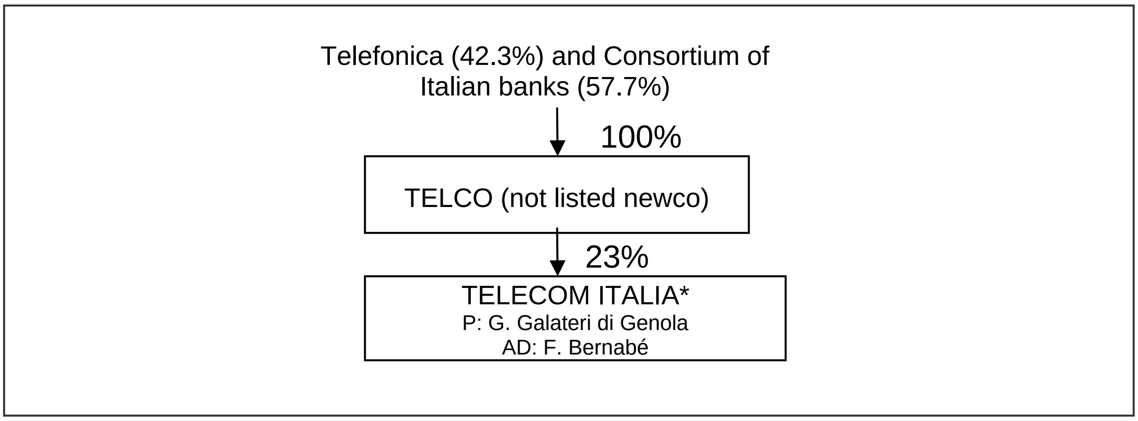

Figure 5

Telecom Italia's ordinary and saving shares trends; voting premium trend

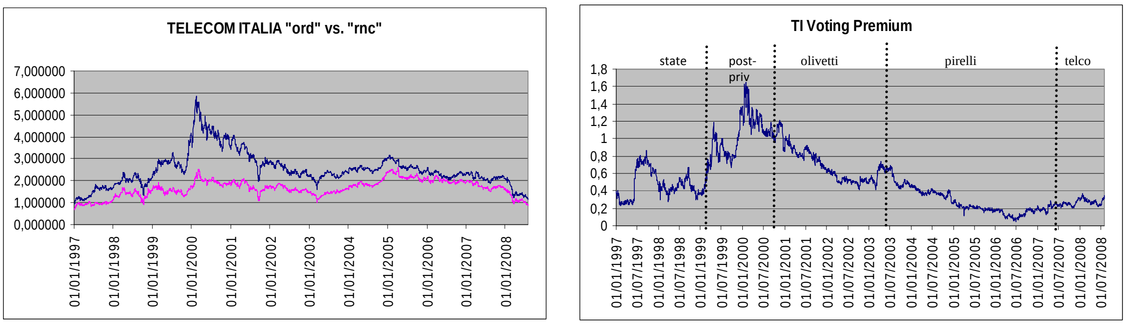

Figure 6

Relevant CAR across Olivetti and Pirelli acquisitions' announcements