Corporate Compliance Focus Team & Corporate Governance Focus Team

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Corporate Compliance Focus Team

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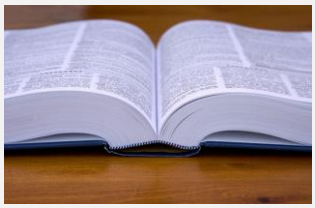
AMCs: DETERMINING LIABILITY FOR MANAGEMENT AND COORDINATION AND FOR ADMINISTRATIVE OFFENCES UNDER LEGISLATIVE DECREE NO. 231/01 FOR ACTIONS CARRIED OUT BY SUBSIDIARIES

Court of Milan (Division B, specialised in company law) Decision No. 90 of 9 January in effect extends liability for unlawful management and coordination under Art. 2497 of the Italian Civil Code to AMCs.

Art. 2497 of the Italian Civil Code



Companies and other entities that, in exercising **management and coordination** over another company, act **in their own or others'** interest in breach of the principles of sound management are **directly liable** to: a) the shareholders of the company for prejudice caused to the profitability and value of the corporate holding, and b) to the creditors for damage to the integrity of the company's assets. There is no liability when, based on the overall outcome of the direction and coordination, no damage resulted and when the damage is entirely eliminated (including as a consequence of transactions entered into to eliminate the damage). A person who contributed to the damage is jointly liable, as is – to the extent of the advantage gained – the person who knowingly obtained a benefit.

Only if a company subject to direction and coordination fails to satisfy the claims of its shareholders and creditors may they act against the company/other entity that exercises the direction and coordination.

In the event of bankruptcy, forced administrative liquidation or extraordinary administration of a company subject to direction and coordination, the (civil claim) action available to the creditors is exercised by the trustee, the liquidating commissioner, or the extraordinary commissioner.

Key facts of case

Two minority shareholders of a company in the services industry brought a liability action against an Italian joint-stock company (*società per azioni*) and two investment funds (as majority shareholders) seeking damages for the damage suffered as a result of the company's subsidiary being **managed and coordinated** in violation of Art. 2497 of the Italian Civil Code.

A key aspect was that the claimants brought the action against the asset management company 21 Investimenti Società di gestione del risparmio ("**21 Investimenti**") instead of the two mutual funds managed by it, **because the claimants held that it was the AMC that exercised the management and coordination** .

21 Investimenti's key defensive argument

From the outset, 21 Investimenti claimed it lacked legal standing to be sued because **its shareholding in the subsidiary was not held in its own interest but in the exclusive interest of two investment funds**. In other words, 21 Investmenti argued that Art. 2497 of the Italian Civil Code does not apply to AMCs because they do not legally own shareholdings but merely manage them on behalf of others.

The court's reasoning for dismissing 21 Investimenti's arguments

The court dismissed 21 Investimenti's defensive arguments based on the following:

- On the wording: The first paragraph of Art. 2497 of the Italian Civil Code, in identifying the persons covered by the the provision, refers without distinction to "**companies and other entities**" without leaving any room to exclude AMCs, which, as commercial entities, undoubtedly fall into the above broad category.

- The rationale behind the provision: The provision then specifies that liability falls on companies and other entities that exercise **management and coordination**, thus focusing attention on the material exercise of management and coordination. This means that legal standing to be sued is basically connected to establishing that a company or other entity called to account under Art. 2497 of the Italian Civil Code actually carried out unlawful **management and coordination**, regardless of the ownership of shareholdings in a subsidiary that suffered unlawful management conduct.

- The AMCs' legal standing to act: The difference and separation between the ownership strategy and that of management and coordination finds support in Art. 36 of the Italian Consolidated Law on Finance (TUF). The article stipulates that an AMC that establishes a mutual investment fund manages the fund **independently** in the fund investors' interest. It follows that the exercise of management and coordination over a subsidiary may well be considered as the power to manage being expressly attributed to AMCs by the abovementioned provision.

  On the other hand, it is precisely the granting to AMCs of management power to manage a mutual investment fund that implies **funds lack legal standing to act in any way**. Thus funds, which are unable to perform any managerial acts, cannot be held liable for exercising management and coordination over a subsidiary even though they are shareholders (which is entirely irrelevant for the purposes of establishing liability under Art. 2497 of the Italian Civil Code in accordance with the criterion of effectiveness under the provision).

The principle of established law

In brief, according to the Court of Milan, Art. 2947 of the Italian Civil Code may be applied only when a company's or another entity's exercise of management and coordination is concretely proved.

No obstacles exist in applying Art. 2947 to AMCs because they exercise management and coordination for the investment funds they manage and because funds do not have independent capacity to act: capacity is reserved to the AMCs that set the funds up.

Can AMCs be liable for crimes committed by subsidiaries under Legislative Decree No. 231/2001?

There is no doubt that Legislative Decree No. 231/2001 may be applied also to AMCs provided that the exceptions under the banking legal system are respected, which are justified by the need to guarantee investors protection.

It follows that the principles of caselaw, which are well established for **groups of undertakings**, apply also to AMCs. Indeed, the phenomenon of corporate groups, although not expressly regulated by the decree, is currently one of the main legal forms of large businesses, which normally operate under the management and control of a holding company.

Over time, caselaw has established that – if certain conditions are met based on the mechanism of origin of liability – holding companies may be held liable for the administrative offence under Legislative Decree No. 231/2001 also when the crime triggering the abovementioned liability is **committed by a subsidiary**.

This can happen in each of the following instances:

- the triggering crime was committed by a person from the subsidiary together with a person from the parent company;
- the parent company also acted in the interest of the holding company; and
- the representative member of the holding company is also recognised as the **de facto managing director** of the subsidiary.

The **objective-functional concept** of management and coordination carried out thus prevails also over the criteria for allocating administrative liability under Legislative Decree No. 231/2001.

Without prejudice to the principles established by the decree, regulatory gaps inevitably arise due to the speed with which new legal forms of do-

ing business arise. Caselaw thus constantly provides interpretations to fill the gaps until the law does.

The decision under discussion reaffirms and reinforces the need for companies that do business using legal forms not entirely already regulated by law to raise the level of compliance checks. Companies also need to bear in mind that courts, in determining liability (not only under civil law) of a company within a group are increasingly taking a more factual approach, whihc takes into account how exactly the company carries on its business rather than merely how the company is formally structured.

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