Expropriation, Unification, and Corporate Governance in Italy

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ABSTRACT

Extant literature has usually argued that firms that unify dual class shares are likely to increase shareholder value. We examine the universe of Italian dual class unifications over the 1974-2005 period and show that the unification process is considerably more complex than described in prior literature. In over half the universe, Italian voting shareholders are not compensated for allowing their voting rights to be diluted, and, not surprisingly, experience a price decline at the announcement of unifications. While non-voting shares appreciate in value at the announcement there is little evidence that the unification increases total firm value. We argue that share unifications are designed to benefit the *controlling* shareholders and, in several cases, controlling voting shareholders use the unification to expropriate wealth from minority shareholders.

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1.Introduction

A large number of corporations around the world issue different classes of common equity. Typically in these firms, one share of a given class has a claim to voting rights disproportionately different from its share of the firm's cash flow. The dominant view in the literature is that these deviations from the one-share-one-vote principle reduce shareholder value. Bebchuk, Kraakman, and Triantis (2000) for example argue that these deviations lead to distortions in investment decisions while Grossman and Hart (1988) argue that they lead to inefficiencies in the market for corporate control. The tunneling literature uses the deviation of cash flow from control rights as a proxy for the likelihood of expropriation. This measure has been shown to affect dividend policy (Faccio, Lang and Young, 2001), firm valuation (Claessens, Djankov, Fan, and Lang, 2002; Lemmon and Lins, 2003; Baek, Kang, and Park, 2004), firm profitability (Joh, 2003), and the propagation of earnings shocks within the firm (Bertrand, Mehta, and Mullainathan, 2002). The empirical implication from this stream of literature is that firms that unify their share classes should increase shareholder value.

Over the last few years, there has been a marked trend away from dual-class structures in European countries (Pajuste, 2005). Prior literature has examined why firms might choose to unify their shares into one share class (see for example, Amoako-Adu and Smith, 2001, or Hauser and Lauterbach, 2004). There is however little empirical evidence on whether such stock unifications benefit or harm shareholders.[1] In fact, Adams and Ferreira (2007), in surveying the literature on one-share one-vote rules, conclude that the question of whether such a structure improves shareholder value "*…has proven difficult to address empirically*".

In this paper, we examine the wealth effects of the universe of 46 share unifications in Italy between 1974 and 2005. The Italian market is appropriate for conducting this research for two reasons. The period we examine is characterized by two exogenous factors – changes in corporate governance laws in Italy in 1998 and the induction of Italy into the European Monetary Union in 1999 – that made non-voting shares potentially less useful to the majority shareholders. Half the unifications in Italy (23) occur in the 1998-2001 period. Italy therefore forms a (quasi) natural experiment to examine the wealth effects of share unifications.

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[1] While Dittmann and Ulbricht (2008) examine the wealth effects of German unifications, they do not analyze the potential for intra-shareholder wealth transfers.

More important, relative to non-voting shares, voting shares in Italy have traded at among the highest premiums in the world. By design, stock unifications involving shares with different voting rights will result in a dilution of the voting rights of superior voting shareholders and a corresponding strengthening of the voting rights of inferior or non-voting shareholders. Empirical research has found that voting shareholders are typically paid extraordinary dividends or new shares to compensate them for the loss of voting premium. In the U.K., Ang and Megginson (1989) report that, in 45 of the 49 stock unifications in their sample, voting shareholders received an extraordinary dividend equal, on average, to 12% of the voting share's stock price. Hauser and Lauterbach (2004) document that in 52% of share unifications in Israel, voting shareholders are assigned new shares to compensate for the dilution in their voting power.

In contrast, despite the high voting premiums for voting shares in Italy, over half of the dual class unifications (DCUs) are characterized by the absence of compensation for voting shareholders and by the presence of forced unifications. Why would voting shareholders opt for stock unifications in such cases? Consistent with the argument that these unifications do not offer benefits to voting shareholders, we find that while non-voting shares earn significantly positive market-adjusted excess returns of 11.7% on average in the three day period surrounding the announcement date, voting shares earn significantly negative excess returns of -1.6% over the same period. The overall firm value does not change significantly, suggesting that wealth is transferred from voting to non-voting shareholders.

The Italian firms that announce DCUs are not different from other Italian firms across most of their operating, accounting, or ownership characteristics. They are similar to their industry peers in size, market to book ratios, leverage and operating performance. Similar to other Italian firms, they are characterized by the presence of a majority shareholder, typically a family owning more than 50% of votes.

However, in at least 21 unifications (almost half of the whole population), the majority shareholder also owns a large block of non-voting shares before the unification decision. In these firms, the majority shareholder directly benefits from the unification when the non-voting shares he owns are converted into voting shares. Our results on the negative excess returns earned by voting shareholders are driven by this subsample. Specifically, voting shares in this subsample earn significantly negative three-day market adjusted excess returns around the announcement date of -3.7%, as opposed to an insignificant 0.47% for voting shareholders in the

remaining firms.

A probit analysis shows that non-voting share ownership by the majority shareholder is significantly positively related to the probability that the unification is forced and is negatively related to the probability of voting shareholders being compensated. A multivariate regression analysis shows that the abnormal return earned by voting shareholders around the unification date is significantly negatively related both to the proportion of non-voting equity as a fraction of total equity and to a dummy for ownership of non-voting shares by the majority shareholder.

In the last part of the analysis, we provide detailed case studies for two dual class unifications, illustrating the process through which expropriation occurs. In these cases, a few months before the unification announcement, the majority shareholder typically bought large blocks of non-voting shares, approved non-voting stock option plans and sold voting shares. Both the behavior of the controlling shareholders and the sharp drop of the voting share price at the announcement (ranging between -5% to -10%) support the hypothesis that dual class unifications can be a form of expropriation of wealth from minority shareholders.

Overall, we conclude that while dual class unifications have the potential to increase shareholder value, in practice they also offer opportunities for the majority shareholders to expropriate wealth from the minority shareholders in the firm. Our results suggest that public policy initiatives that seek to encourage dual class share unifications[2], without paying attention to such nuances as the terms of the deal, and prior insider trading activity of controlling shareholders, are unlikely to result in their desired objectives. Our paper contributes to the literature on corporate governance and share unifications by showing that testing the wealth effects of dual class share unifications is considerably more complex than it appears, depending upon, among other things, external minority shareholder protection statutes and the initial ownership stakes of controlling shareholders.

Our paper also contributes to the growing body of literature on tunneling and expropriation in publicly listed firms by showing that unifications can serve to expropriate wealth from minority shareholders particularly in settings characterized by the presence of majority control. Johnson, La Porta, Lopez-de-Silanes and Shleifer (2000), for example, discuss how controlling shareholders can tunnel resources away from minority shareholders by selling assets, goods, or

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[2] See for example, Buck, Tobias, "EU seeks to end bias among shareholders", *Financial Times*, October 16, 2005. In another example, the 1992 CIPE directives on Italian privatization stated that privatizing dual class companies in Italy, should favor solutions allowing conversion of non-voting shares into voting.

services to the company through self-dealing transactions, by obtaining loans on preferential terms, or by transferring assets from the listed company to other companies under their control. Investigating how expropriation happens is important because, as Stulz (2005) argues, the agency problems created when corporate insiders pursue their own interests ultimately may limit the economic growth and financial development of the country. The form of "tunneling" we document in this paper is unique and adds to the list of such activities described in prior literature.

While the Italian experience may be unique in sheer scale – both the voting premium and the wealth effects for voting shares are large compared to those documented in other countries – we argue that DCUs in other settings, particularly ones characterized by dominant shareholders, are potentially subject to similar abuses. Part of the reason why the effects we document have not been previously reported is because the limited extant literature on DCUs has focused chiefly why companies choose to unify their share classes and the announcement price effects. The literature has not focused on wealth transfers between non-controlling and controlling shareholders of the same class of (voting) shares. As we show in this paper, such wealth transfers are likely the norm given the concentration of ownership in most countries.

The rest of the paper is structured as follows. Section 2 discusses related literature on share class recapitalizations and unifications. Section 3 describes the institutional background and the main reasons for Italian stock unifications. Section 4 reports results for our empirical tests while Section 5 concludes.

2. Related literature

Faccio and Lang (2002) document that non-voting or limited voting shares are rarely used in Belgium, Portugal and Spain, while they are common in Italy, Germany, Switzerland and countries in northern Europe. The dominant view in the literature is that the presence of multiple share classes is detrimental to shareholder value. Grossman and Hart (1988) and Harris and Raviv (1988), for example, show that the one share-one vote rule is an optimal corporate governance scheme in that better management teams are more likely to be elected in takeover bidding contests. Bebchuk, Kraakman and Triantis (2000) argue that these deviations lead to distortions in investment decisions. The tunneling literature uses the deviation of cash flow from control rights as a proxy for the likelihood of expropriation (see among others, Faccio, Lang and

Young, 2001, Claessens, Djankov, Fan, and Lang, 2002, Joh, 2003 or Bertrand, Mehta, and Mullainathan, 2002). Some papers have also pointed out that multiple share classes may have benefits. Burkart, Gromb, and Panunzi (1998) for example, show that issuing non-voting shares may be optimal when it leads to higher takeover probabilities or increases security benefits in competitive takeovers.

Adams and Ferreira (2007) provide a comprehensive survey of this literature, and conclude that overall, the valuation effects of deviations from the one-share one-vote rule are likely negative, given the inefficiencies associated with private consumption. They also rightly point out the difficulty of interpreting the event study evidence, given that the decision to either recapitalize shares into two voting classes or to unify them into one voting class is surely endogenous to the attendant benefits. One implication of their argument is that the total benefit associated with eliminating dual voting class structures, as well as how the benefit is shared among controlling and minority shareholders, ought to depend on the control structure of the firm at the time of the unification decision.

In line with the Adams and Ferreira caution, the empirical evidence on the valuation effects of the creation of a second class of shares with differential voting rights is mixed. Partch (1987) finds no evidence that current shareholders are harmed by the creation of limited voting common shares for firms in the U.S. Cornett and Vetsuypens (1989) examine the wealth effects of the announcement of an issue of stock with differential voting rights. They document that their sample of 70 U.S. firms earned positive abnormal returns when they announced a dual class recapitalization. Ang and Megginson (1989) and Liljeblom and Rydqvist (1991) find similar results in the U.K. and Sweden. In contrast, Jarrell and Poulsen (1988) find significant negative excess returns for U.S. firms announcing dual-class recapitalizations while Jog and Riding (1986) find similar results in Canada.

In contrast to the research on the creation of multiple share classes, there is a more limited amount of research on stock unifications. Some of these papers document a recent trend towards share class unification in several countries, such as Canada (Amaoko-Adu and Smith, 2001) and across Europe (Pajuste, 2005). However, as mentioned in the introduction, most of this research has chiefly focused on the reasons behind the unifications and not on the potential for intra-shareholder wealth transfers. In contrast, we believe that intra-shareholder wealth transfer

possibilities are a prime motivation in understanding a wide array of corporate events, in particular, dual-class share unifications.

Amoako-Adu and Smith (2001) conduct a longitudinal study of Canadian dual class firms over the fifteen year period following their IPOs. They find 56 cases of stock unifications in the 1979-1998 period. Amoako-Adu and Smith (2001) report three main reasons why firms choose to re-capitalize into a single class of shares: they put into place a debt restructuring plan that requires elimination of dual class shares; they need to facilitate the sale of a control block and avoid coat-tail provisions[3]; or they need to increase liquidity and institutional investor appeal, especially prior to a seasoned equity offering.

Using a logistic analysis, Dittmann and Ulbricht (2008) examine a sample of 29 stock unifications in Germany and find that the probability of abolishing a dual class structure is higher for (i) firms that issue new equity in the same calendar year; (ii) larger firms; (iii) firms with a high proportion of voting shares; and (iv) firms where the largest block of voting shares is small. They interpret the strong correlation between a stock unification and subsequent equity offering as indicative of the presence of growth opportunities. In 29 of the 37 stock unifications from their 1990-2001 sample, Dittmann and Ulbricht (2008) find an average abnormal return in the five days around the announcement (day –4 to day +1) of 9.9% for non-voting shares, 3.9% for voting shares, and 5.4% for the firm as a whole.

Pajuste (2005) estimates a logistic regression on the determinants of 108 forced stock unifications from seven European countries (Denmark, Finland, Germany, Italy, Norway, Sweden and Switzerland) in the 1996-2002 period. She finds that the probability of a forced stock unification is positively related to the issue of new equity, the number of acquisitions, and the presence of growth opportunities, and negatively related to the presence of a high voting premium.[4]

Ang and Megginson (1989) report that, in the 1955-1982 period, 49 of 152 U.K. listed firms with restricted voting shares decided to extend full voting rights to restricted voting shareholders. In 45 of these 49 operations, voting shareholders received an extraordinary dividend equal, on

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[3] Coat-tail provisions are meant to provide equal treatment to all classes of shareholders upon a takeover involving an acquisition of at least 50% of the superior voting shares of a dual class company.
[4] Pajuste (2005) examines twelve Italian share unifications in her sample. In contrast, our sample contains 26 stock unifications announced over the same period, 13 of which were forced and 13 voluntary.

average, to 12.3% of the voting share stock price as a form of compensation for their surrender of special voting privileges.

Hauser and Lauterbach (2004) analyze 84 stock unifications in a sample of Israeli firms between 1990 and 2000, after a new regulation banned new issues of inferior voting shares at the Tel Aviv Stock Exchange. The typical Israel dual class shares structure involves a superior voting class (one share to one vote) and an inferior voting class (five shares to one vote). All stock unifications transformed inferior voting shares into superior voting ones. In 55% of their sample (46 out of 84 cases) voting shareholders were compensated for the loss in voting power through a new issue of superior voting shares distributed to superior vote shareholders free of charge. The authors use this compensation to infer the value of a voting right and find that the price of votes in unifications (as compensation for the vote dilution) is similar to the market price of votes. They find that family-controlled firms sell votes at higher prices and both stock classes respond positively to the unification announcement in a subsample of 44 observations.

Finally, Ehrhardt, Kuklinski, and Nowak (2006) analyze 43 German unifications in the 1987-2003 period. They report a dilution of the controlling block of votes due to the unification (on average, from 56% to 45%), a significantly positive market reaction at the announcement for both the voting and non-voting shares (of about 4% each) and an increase in the stock's liquidity after the unification.

To summarize, the extant literature on unifications has focused on why companies choose to return to a one share-one vote equity structure, and has ignored the control structure of the firm at the time of the unification decision. In contrast, we focus on a sample of firms characterized by the presence of a controlling shareholder, allowing us to examine the wealth effects of unifications on different classes of shareholders. The empirical evidence documented in section 4 is consistent with the hypothesis that Italian stock unifications adversely affect the welfare of minority voting shareholders. Ironically, such unifications have been warmly endorsed by the financial press.[5]

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[5] For example, *Il Sole 24 Ore*, a prominent financial newspaper, described the CIR unification announcement as a "market friendly" operation. At the announcement of the unification, voting shares dropped in price by about 9% around the announcement date. In addition, the CIR board approved three separate stock option plans involving non-voting shares a few months prior to the announcement of the unification. Over the same period, the controlling shareholder sold voting shares and purchased non-voting shares. (See *Il Sole 24 Ore*, *Finanza e Mercati*, page 1, September 14th 2000).

3. Italian non-voting shares

In this section, we describe the regulations governing Italian non-voting shares, and main factors driving the conversion to one-share one-vote equity structures, both across the world and in Italy.

3.1 Regulations governing Italian non-voting shares

Italian listed companies can issue non-voting shares for up to 50 percent of their equity capital. While these non-voting shares do not have any voting rights, Italian law (L. 216/1974) prescribes minimum privileges to holders of these shares (these privileges can be increased by corporate charter amendments). These include a minimum dividend payment equal to five percent of par value; dividend protection and priority provisions (e.g. if a dividend is paid to voting shares, the dividend to non-voting shares has to be greater by an amount equal to two percent of the par value or more); a mandatory replenishing of the firm's equity capital by voting shareholders when cumulative losses wipe out book equity; and priority of claims during bankruptcy proceedings.

Notwithstanding the dividend priority and protection, non-voting shares usually trade at deep discounts from the price for voting shares. This is largely due to the high value of the voting rights in Italy. For instance, Nenova (2003) computes the aggregate value of voting rights equal to 29% of total firm value based on the price difference between voting and non-voting Italian shares in 1997. Similarly, Dyck and Zingales (2004) estimate that the aggregate value of voting rights is 37% of the firm's total market capitalization, based on the higher price paid for controlling blocks of shares in Italy in the 1990-2000 period.

The number of Italian dual class listed firms has been declining in the past decade. At the end of 2005, there were only 38 dual class firms listed on the Milan stock exchange, out of 266 Italian listed companies (14%), versus 85 out of 233 in 1990 (36%). The market capitalization of non-voting equity as a fraction of total equity value has declined even more precipitously, from 15% in 1990 to only 3.4% at the end of 2005.

3.2 Why do Italian firms choose to unify their share classes?

Below we discuss some of the reasons underlying why Italian firms choose to unify their share classes. The first set of three factors is common to share unifications in other countries

while the second set is unique to Italy.

Over the last decade, as in other countries, Italian firms have experienced increasing internationalization of their investor bases. This internationalization, together with institutional investors' preferences for a one share-one vote equity structure, may have caused some Italian firms to choose to unify their share classes. Amaoko-Adu and Smith (1995) argue that direct institutional pressure towards a more desirable one share-one vote structure is one of the main reasons underlying Canadian unifications. Hauser and Lauterbach (2004) report that the trend towards unification in Israel was triggered by the Stock Exchange's decision to ban any new issue of limited voting stock in 1990. In Italy, in August 1998, Parmalat had to cancel a $500 million non-voting share issue targeting US investors due to an adverse market reaction.[6] This attempt to create new non-voting shares was the last made by an Italian blue chip firm. The belief that the stock market was likely to react negatively to the creation of new non-voting shares may have favored the conversion of the existing ones (as in Israel).

In addition, in order to be included in domestic or international stock indices, the two most common criteria are usually the firm's market capitalization and share turnover. Since a dual class unification increases both parameters, companies might find it easier to be listed on these indices following a share unification. As Dhillon and Johnson (1991) and Beneish and Whaley (1996) note, an inclusion in a major index, such as the S&P 500, increases the investor base, stock liquidity, and firm value. Since equity indexes typically use only voting shares to compute market capitalization and share turnover, an increase in the DCU firm's weight in the index or a higher probability of being included in the index, after conversion of non-voting shares into voting shares, may have motivated some firms to unify their shares.

Finally, Italian firms, similar to most continental European firms, use the rights offering method in equity offerings, involving a longer execution period and an issue price below market price.[7] The issue of new non-voting shares at prices below depressed market quotes could bind the company into paying a high minimum yield. This might provide an incentive for unification *prior* to the rights offering. This is probably the reason for at least one recent Italian stock unification (IFIL in 2003). This incentive is also consistent with the significant correlation

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[6] The Financial Times described the failed offering in an article beginning "Tired of milking cows? Try the shareholders". (See "Parmalat - Lex**",** *Financial Times***,** 14 August 1998, page 16).
[7] On average, new shares were pre-emptively offered at 42.1% of market price in the 1980-1994 period (Bigelli, 1998).

between unifications and equity offerings found by Dittmann and Ulbricht (2008) for share unifications in Germany.

In addition to these factors, in the 1998-1999 period, several changes occurred in the regulatory and economic environment in Italy that made the issuance of non-voting shares less favorable. First, in the aftermath of the European Monetary Union in 1999, Italian interest rates plunged to rates more in line with the average in the EMU countries. Unlike previous drops in interest rates, this sharp decrease (of more than 5% in 1998-1999) was structural, and affected the relative costs of debt and equity capital. Since non-voting shares involve a minimum dividend payment based on their par value, a general decline in interest rates resulted in dividend yields that sometimes exceeded the company's cost of debt, especially in the wake of market-wide depressed stock prices (as in 2001 and 2002) and large discounts on non-voting shares relative to voting shares. The higher mandatory dividend yield on non-voting shares may have made non-voting shares less favorable as a form of financing. For example, Cofide decided to convert non-voting shares into voting shares in December 2001 when non-voting shares were trading below par, forcing the company to pay a minimum legal dividend yield equal to 5.7% on these shares.

Second, Italian takeover regulations, introduced in 1998, reduced the threshold necessary to exercise control in two ways. When a bidder buys more than 30% of votes, he must launch a tender offer on *all* voting shares (coat-tail provision). In addition, the quorum to control extraordinary shareholders' meetings was increased to 66.67% of voting shares (from 50%). This means that a 34% voting block can stop any extraordinary meeting decision and thwart a hostile takeover. Because of this new regulation, unifications which would previously have significantly diluted the controlling voting blocks, could now take place without threatening the controlling shareholder. For example, the Cofide unification diluted the majority shareholder block (Carlo De Benedetti & Figli S.a.p.a.) to 34.7%, down from 43.2%. Third, the adoption of a new Italian financial code[8] in 1998 improved non-voting shareholders' rights, causing a decline in the attractiveness of dual-voting share structures to controlling shareholders.

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[8] D. lgs 58/1998.

4. Results

In this section, we describe the main results of our paper. We first report the incidence of dual-class share unifications in Italy from 1974 through 2005. We then report the reasons for unification as cited by the companies, describe the sample firms' characteristics, and report the wealth effects surrounding unification announcements. Finally, we conduct cross-sectional tests to shed light on the determinants of wealth effects to voting and non-voting shareholders.

4.1. *Types of Italian dual class share unifications*

We search Mediobanca's *"Indici e Dati"* and *Il Sole 24 Ore* for announcements of stock unifications made by Italian listed companies from 1974 (when non-voting shares were introduced) through 2005. Our hand-collected sample consists of 46 DCUs[9] announced by 41 firms, with half our sample, 23 DCUs, announced in the 1998-2001 period. This is consistent with the argument that the changes in the regulatory and economic environment in Italy in this period caused a significant decline in the attractiveness of non-voting shares in Italy.

Table 1 Panel A shows the frequency and type of dual-class share unifications approved by the sample firms' boards. Out of 46 unifications, 22 are classified as forced unifications. Most of the forced unifications (18 cases) are structured as one-for-one conversions without any direct or indirect compensation to voting shareholders. In the remaining four cases, either a cash payment is required from non-voting shareholders (the cash payment actually goes to the firm) or the unification sets a favourable conversion ratio based on the differential market prices of the two classes of shares. Most voluntary unifications (14 cases) do not involve any additional payment from non-voting shareholders to convert their shares into voting shares. In ten cases, non-voting shares needed to pay either cash or additional stock to convert into voting shares – and in these cases, the payment was invariably less than the price premium associated with voting shares prior to the unification announcement.

Overall, an overwhelming majority of unifications did not involve any explicit indirect compensation to the voting shareholders as part of the conversion. In one case, non-voting shareholders were even paid to convert their shares into voting shares. The absence of any compensation to voting shareholders, despite the high premium associated with voting rights, is

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[9] Four firms started with voluntary unifications, and used either a final compulsory offer to the remaining non-voting shares to complete the unification, or forced a delisting of the remaining hold-out non-voting shares.

unique to Italy, and indicates the potential for harm to minority voting shareholders during the unification process.

Table 1 Panel B compiles the reasons for the unification as stated in the company's press announcement or newspaper articles. Commonly cited reasons include a desire to improve the firm's attractiveness to international investors, increase the stock's market liquidity, and simplify the firm's equity structure. These reasons are similar to ones cited by firms undergoing dual-class share unifications in other countries (see Amoako-Adu and Smith, 2001, for Canada; Dittmann and Ulbricht, 2008, for Germany; and Pajuste, 2005, for a subset of E.U. countries).

Other reasons cited by firms in our sample appear to be unique to Italy. Four firms in our sample report that the reason for the unification was "to raise cash to finance new investments".[10] All cash raised through the DCU came from non-voting shareholders. Five firms unified their dual-class shares to comply with Italian privatization guidelines;[11] three firms unified their shares prior to a merger, and three firms announced unifications before a new equity issue.

4.2.   *Ownership structure for Italian DCU firms*

Table 2 reports data on the ownership structure of these firms in the period immediately before the announcement of the share unification. We obtained ownership data from *Il Taccuino dell'azionista* (1982-1995), the Italian Security and Exchange Commission (Consob) print database (1995-1997), and online data sources (1998-2005).

Since Italian non-voting shares are bearer shares, official ownership data is not available for these shares. In eight cases, however, the financial press or the company's press release reported the fraction of non-voting shares owned by the majority shareholder, with a mean holding of 41%. For all other unifications, we infer the largest shareholder's ownership of non-voting shares from ownership data for voting shares before and after the unification as well as from the unification characteristics (type of unification, acceptance rate, etc.). We restrict this procedure to cases when there is a relatively short period (6 months) before and after the unification date (to minimize the possibility of trading voting shares) and where ownership data is available from

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[10] Though Pajuste (2005) does have data on Italian unifications, her data does not include voluntary unifications. Consequently this motivation is not documented in her paper, as all unifications requiring a cash payment from non-voting shareholders are voluntary.

[11] The 1992 CIPE directives on future Italian privatization stated that future privatized dual class companies "will favor solutions which allow conversion of non-voting shares into voting". The five Italian unifications announced by privatized companies (Credit, Comit, Alitalia, BNL, Finmeccanica) followed the above guidelines.

the Consob online database (available since 1998). This reduces the sample to 33 observations with ownership estimates of non-voting shares prior to the unification. We further eliminate eleven observations due to potentially confounding events such as a change of control, a merger or an equity issuance. In 21 of the remaining 22 cases, we can infer the stakes of non-voting shares held by the majority shareholder prior to the unification. Using this conservative estimate, we find that in 21 unification announcements, the largest shareholders owned significant stakes of non-voting equity, equal, on average, to approximately 30% of all non-voting shares prior to the unification event. We divide our sample into firms where we are able to obtain data on non-voting share ownership by the largest shareholder and cases where we were unable to conclusively do so.

The ownership structure of a typical DCU firm is highly concentrated. The largest shareholder owns, on average, close to 60% of the voting rights before the unification. Such a concentration of voting control sets the Italian sample apart from other unification experiences in other countries, and provides for a unique setting to study the interaction of seemingly benign corporate governance prescriptions and concentrated control. Interestingly, the mean portion of total votes held by the largest shareholder is almost unaffected by the unification. These results contrast with the German evidence (Ehrhardt et al, 2006) where unifications reduced the average proportion of voting shares held by the largest shareholder from 56% to 45%. The largest shareholder is usually represented by a family (30 cases), followed by financial institutions (8 cases) and the Italian government (8 cases). The stake held by the second largest shareholder is typically less than a tenth of the stake held by the largest shareholder.

We also compute the degree of separation of ownership of all equity (cash flow ownership) from control (voting rights) before and after the unification for a subset of firms where we have ownership data (we do this for unifications occurring after 1995, since the Consob ownership database is only available after this year). Following Faccio and Lang (2002), we trace the ultimate shareholder of each firm and compute the ratio of cash flow ownership (Ownership) and voting control (Control). We find that the dual-class share unifications reduce the separation of ownership and control. The mean (median) value for the Ownership/Control ratio increases significantly from 0.762 (0.80) before the DCU to 0.873 (0.99) after the unification though there are no significant differences between the two sub-samples. The tunnelling literature uses the divergence between cash flow and voting rights as an indirect proxy for expropriation. Hence,

by eliminating this divergence, dual class unifications may reduce the potential for expropriation going forward and improve shareholder value. Our (unreported) results are qualitatively similar when we divide the sample into forced and voluntary unifications or into unifications where compensation was involved and where it was not.

In Table 3 we report financial characteristics such as leverage, profitability, and market-to-book ratio, for all dual-class unification firms in our sample. The table also reports mean and median statistics for industry-adjusted financial characteristics. Again, we divide the sample into cases when we can infer the non-voting ownership by the majority shareholder and cases when we cannot, and report characteristics for each separately. Our sample firms are unremarkable in terms of their financial and operating characteristics. There are no significant differences between these firms and their industry peers across leverage ratios, profitability, and market-to-book measures. In addition, there are no significant differences between the firms where the majority shareholder owned non-voting shares prior to the unification and firms where he did not. In unreported results, we divide the sample into forced and voluntary unifications and between unifications that involved compensation and unifications that did not. There are no significant differences between the two subsamples.

Table 4 reports voting and non-voting share characteristics of Italian DCU firms during the unification process. On average, non-voting shares represent 17.6% of total equity shares in Italian DCU firms. Three days before the announcement date of the DCU, voting shares traded at an average premium of 39% relative to non-voting shares. When differences in dividends (higher for non-voting shares) are taken into consideration, the mean value of the voting right is 54% of the non-voting stock price. The cumulative value of all voting rights represents 29.8% of the total equity value of the firm, almost identical to Nenova's (2003) findings based on 1997 Italian data (29.4%).

Based on pre-announcement market prices, non-voting shares earned a minimum dividend yield of 1.8% (median yield=1.1%). Both current yield (based on the most recent dividend) and expected yield (based on next year's dividend) averaged 2.9% and were about 3% lower than the 10-year Italian Treasury-bond gross yield.[12] Splitting the sample into firms where we can infer ownership of non-voting shares by the majority shareholder and firms where we cannot, we find that there are no substantial differences between the two samples.

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[12] In five cases, the dividend yield was higher than the T-bond yield.

When we split the sample into forced and voluntary conversions, and into compensated and non-compensated conversions, we find that the *process* of unification is different across the two resulting sub-samples (not reported in tables for brevity). In voluntary DCUs, on average, 83.8% (91% median) of the non-voting shares decided to convert their shares. One possible explanation for the acceptance rate not being 100% is that the largest shareholders do not convert all their non-voting shares in order to retain some say in non-voting shareholders' meetings. Alternatively, perhaps some shareholders simply miss the announcement. Voluntary unifications are associated with significantly higher voting premiums (33.8% at the median) than forced unifications (21.5%). Similarly, firms that offer compensation during the unification process have significantly higher voting premiums (51.9% at the median) than non-compensated unifications (15.5% at the median). Compensation also tends to be offered in the presence of a larger fraction of non-voting shares. The median fraction of non-voting shares to total equity is 19% for compensated unifications in comparison to 8.9% for non-compensated unifications.

4.3. *Announcement period returns around the announcement of a unification*

For every firm in the sample, we search the *Il Sole 24 Ore* financial newspaper for announcement dates. Market data information is obtained from the Italian Stock Exchange. Of the 46 sample firms, we are able to compute abnormal returns at the announcement date for 35 paired observations of voting and non-voting shares.[13] Table 5 reports abnormal returns for voting and non-voting shares separately, as well the change in the market value of the firm, for several event windows surrounding the announcement of the unification.

For non-voting shares, the mean (median) three-day return surrounding the announcement of DCUs is 11.66% (6.75%), while the mean (median) five-day return is 12.50% (6.53%). These results are broadly in line with the positive announcement date wealth effects of unifications from other countries such as Germany (Dittmann and Ulbricht, 2008, Ehrhardt, Kuklinski, and Nowak, 2006) though the Italian statistics are somewhat higher in magnitude.

However, what is unique to Italy is the announcement date wealth impact on voting shares. The voting shares for German firms announcing DCUs earn positive abnormal returns, and the overall wealth impact on the firm's market capitalization is positive. In contrast, voting shares in

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[13] Eleven observations were excluded due to a lack of the announcement date (4 cases); insufficient liquidity of the non-voting share (3 cases); non-voting shares not listed (1 case); voting shares not listed (2 cases); and lack of the stock market price series (1 case in 1982).

our sample earn a three day market-adjusted return of –1.56% (median –1.25%) and a five-day excess return of -1.94% (median –0.60%). The difference from the German evidence could be due both to the higher average level of the Italian voting premium, which translates in a bigger dilution in the value of a voting right, and due to the opportunistic behavior of Italian majority shareholder as described in the next section.

The total increase in market capitalization (in excess of the market) for the firm, $\Delta MktCap$, is computed as $\Delta MktCap = CAR_V \times MktCap_V + CAR_{NV} \times MktCap_{NV}$ where $MktCap_V$ and $MktCap_{NV}$ are the market capitalizations of voting and non-voting stocks prior to the DCU announcement, and CAR_V and CAR_{NV} are the cumulative market adjusted returns for voting and non-voting shares around the announcement of unifications. The mean (median) change in the total market value of the firm is 0.57% (0.03%), and is not statistically significant, suggesting that, in contrast to the literature on dual class recapitalizations, Italian unifications have little, if any, impact on firm value in Italy. We obtain similar results when we compute the market reaction over longer event windows (such as day –1 through day +30).

Our results appear to be driven largely by the sample of firms where we can infer ownership of a block of non-voting shares by the controlling shareholder prior to the unification. In these cases, voting shares earn significantly lower returns (more negative), both in the three and five days surrounding the announcement date, than firms where there is no information on non-voting ownership. Voting shares in the first sample earn negative excess returns of -3.72% in the three days and -3.33% in the five days around the announcement date. Total market capitalization is not affected around the unifications event, suggesting instead a wealth transfer from voting shareholders to non-voting shareholders.

4.4.   *Multivariate analysis*

Our analysis so far shows no significant differences between firms where the controlling shareholder owns non-voting shares prior to the announcement and firms where we cannot find such information. The two samples are similar in terms of ownership structure of voting shares, financial characteristics, operating performance, voting premiums, voting rights and dividend yields. About the only characteristic that separates the two samples is the ownership of non-voting shares by the majority shareholder.

However, our univariate analysis in section 4.2 also showed that the ownership structure and voting premiums varied significantly between forced and voluntary unifications and between compensated and non-compensated unifications. In Table 6, we investigate whether ownership of non-voting shares by the majority shareholder also explains the structuring of the unification process - specifically whether non-voting share ownership by the controlling shareholder explains the probability of a forced unification and whether it explains the probability of compensation being offered.

We find that, in fact, the probability of compensation being offered to voting shareholders during a unification event is almost solely driven by non-voting share ownership by the controlling shareholder. In addition, the higher the level of control of the largest shareholder, the less likely it is that compensation will be offered – the pre-unification stake of the largest shareholder is significantly negatively related to the probability of compensation being offered. Less surprisingly, we also find that voting shareholders in larger firms are more likely to be compensated.

Privatizations of government owned shares are more likely to be forced. In addition, consistent with the hypothesis that the changes in the regulatory and economic environment in Italy caused non-voting shares to become less attractive, the dummy variable for the post European monetary union period in 1999 is strongly related to the probability of a forced unification. Finally, even after controlling for all these variables, the probability of a forced unification is strongly positively related to the ownership of non-voting shares by the controlling shareholder.

We next estimate a set of OLS regressions to examine the effect of the indicator variable for non-voting share ownership on the cumulative abnormal returns (CARs) earned by the voting shareholders, non-voting shareholders, and on the total market capitalization of the firm. Coefficient estimates are reported in Table 7.

We first report the regression estimates using announcement period abnormal returns (day -1 to day +1) for voting shares as our dependent variable. The abnormal returns are inversely related to the fraction of equity represented by non-voting shares. This is not surprising since the larger the fraction of pre-unification non-voting equity, the greater the dilution of voting rights. There is also a significant positive relation between the abnormal returns and the size of holdings by the largest blockholders of voting shares. This is consistent with the interpretation that

shareholders with very large blocks of voting shares find hedging against the unification-related dilution more difficult. The pre-unification stake held by the second-largest blockholder is marginally significant at the 10% level in two models – at best weakly consistent with the hypothesis that the second largest blockholder exercises a monitoring role on the controlling shareholder. This is not surprising given the largest blockholder owns ten times the voting shares owned by the second-largest blockholder on average. Finally, the indicator variable for non-voting share ownership by the largest shareholder is significantly negative across all the models, implying that pre-DCU non-voting share ownership is associated with larger wealth losses for voting shareholders, and is consistent with our earlier univariate results.[14]

We next report regression results using the three-day announcement period abnormal returns for the non-voting shares as the dependent variable. Abnormal returns to the non-voting shares are almost solely driven by the pre-unification voting premium. In two models, they are significantly positively related to the indicator variables for a forced compensation and significantly negatively related to the presence of any form of indirect compensation for the unification (such as a cash payment, a conversion ratio based on the market price, or any limits on the amount of non-voting shares that can be converted). Ownership by the largest or second largest blockholder is not significantly related to the abnormal returns earned by the non-voting shares. The indicator variable for non-voting share ownership by the majority shareholder is not significantly related to the CARs earned by the non-voting shareholders.

Finally, we examine the effect on total market capitalization of the firm in the three-day announcement period. The voting premium is significantly positively related to the total market capitalization suggesting that wealth gains are greater where the *a priori* potential for abuse by controlling shareholders is higher. The proportion of non-voting shares as a fraction of total equity is significantly negatively related to firm value. This is not surprising since non-voting share fraction has a negative effect on both the voting as well as non-voting shares at the announcement of unifications. Ownership by the largest and second largest shareholder is unrelated to total firm value. Indicator variables for forced unifications, compensated

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[14] In unreported regressions, we also use alternate definitions for this indicator variable such as a variable for the actual % of non-voting shares held, and an indicator variable for the cases when non-voting shares were declared by the largest shareholder. Our results are qualitatively similar. In addition, the actual % of non-voting shares held by the largest shareholder is significantly positively related to the CARs earned by the non-voting shareholders.

unifications and non-voting ownership are marginally significant and only in some models, suggesting that the overall firm value is not affected by these variables.

4.5. *Wealth effects for the controlling shareholder*

Twenty-four of the unifications in Italy are voluntary and 14 of these require no additional compensation from the non-voting shareholders. It is unreasonable to believe that the controlling shareholder is worse off in these cases. To test the hypothesis that the controlling shareholder structures the unification process so that he is not adversely affected by the unification, we compute the raw returns earned by the controlling shareholder alone from two days prior to the unification announcement to two days after the completion of the DCU. We take into account unification characteristics such as whether the compensation was forced or voluntary, whether compensation was required or not, the terms of compensation, and the number of non-voting shares owned by the controlling shareholder, and examine the total effect on the wealth position of the controlling shareholder.[15] After eliminating six firms that announced a merger or an equity issue between the announcement and completion dates, we find that the controlling shareholder earns a raw return of 5.7% (median=1%) between the time the unification is announced and it is completed, suggesting that the unification process at worst leaves the majority shareholder unharmed.

4.6. *Two cases illustrating the process of expropriation*

In this section, we describe the process through which unification might occur through two case studies where controlling shareholders bought non-voting shares prior to the unification from the non-voting shareholders. The information for these cases is taken from articles published on *Il Sole 24 Ore*, the firms' financial statements, press releases and the Consob online ownership database.

4.6.1 Fin.part forced 1 :1 unification

Fin.part was a small financial company with holdings across several industries (its major brands include Moncler, Best Company, Marina Yachting, and Henry Cottons). The Fin.part

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[15] When we cannot infer the ownership of non-voting shares by the controlling shareholder, we set the ownership as zero.

unification was announced by the board on January 24th 2000. The unification involved a forced 1:1 conversion of non-voting and preferred shares[16] into voting shares. Since both preferred and non-voting shares were trading at deep discounts from the voting shares and represented about 40% of total equity, a 1:1 stock unification should have depressed the stock price of voting shares, as it indeed did.

Six months before the unification announcement, in July 1999, Miravan Luxemburg, a company based in Luxembourg, and controlled by the majority shareholders of Fin.part, had launched a voluntary tender offer for 100% of preferred and non-voting shares. About 66% and 59% of preferred and non-voting shareholders tendered their shares. Share trading volume was abnormally high in the three days immediately preceding the DCU announcement, suggesting some advance knowledge of the event.

An analysis of the tender offer prospectus shows that 54% of Miravan Luxemburg was controlled by a second firm, Valcor. In turn, Valcor was controlled by two Italian industrial families. Overall, Valcor controlled Fin.part through the direct and indirect control of 33.3% of the voting shares (12.06% directly and 22% through Miravan Luxemburg). To summarize the events before the unification, the controlling shareholder (Valcor), through Miravan Luxemburg, initiated a purchase of all preferred and non-voting shares via a tender offer. Six months later it converted them into the more valuable voting shares in a 1:1 forced unification.

The non-voting shareholders were certainly not harmed by this unification. This is not true for the minority voting shareholders of Fin.part. In the three-day announcement window, the price of voting shares declined by about -7% while the price of the non-voting shares rose by +26.8%. We also examine in detail post-unification events reported for Fin.part in the popular press. In 2001, after having bought out the remaining minority shareholders, Gianluigi Facchini became the sole majority shareholder. Fin.part eventually entered bankruptcy in October 2005 after a subsidiary, Cerruti Finance, defaulted on a bond issue in 2004. Facchini was arrested in May 2005, on charges of fraudulent bankruptcy, falsifying financial statements, and market manipulation. He had previously pleaded guilty to the charge of insider trading in relation with Fin.part equity warrants.

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[16] Italian preferred shares are generally non-voting, but can vote in extraordinary meetings. They are entitled to higher dividends than common shares.

4.6.2 CIR forced 1:1 unification

CIR is a mid-cap financial company in the second tier of a pyramidal group controlled by the De Benedetti family. CIR's immediate controlling company is Cofide (another financial listed company). The board proposed a 1:1 forced unification in September 2000, which was approved on October 27th 2000. Non-voting shares represented 22.5% of the firm's equity.

Three days before the announcement voting and non-voting stocks traded at €4.256 and €3.497. Following the announcement of the unification, the voting shares dropped by -6.73%, while non-voting shares gained +6.44%. The total market capitalization dropped by about 4%.

In this case, not only had the majority shareholder bought non-voting shares in advance of the unification announcement, but the board had assigned stock option plans to purchase non-voting shares before the unification. A year prior to the unification (in 1999), a stock option plan based on non-voting shares was approved by the CIR's board of directors. The first exercise date was set on December 22nd 1999, followed by additional exercise dates on March 31st, June 30th, September 30th, and December 31st through the end of 2003. All board members exercised their stock options on the first exercise date, i.e. December 22nd 1999. The CEO (a member of the controlling family) exercised his stock options for 2 million shares on that date. On March 7th, 2000, six months before the unification announcement, the board approved a new stock option plan based on non-voting shares. The stock market decline in April 2000 (after the collapse of the Internet bubble) meant that these new options remained out-of-the-money[17]. As noted above, CIR is controlled by another financial company, Cofide, which is controlled by the De Benedetti family. *Il Sole 24 Ore* reported that during the months of April and May 2000, Cofide had also bought CIR non-voting shares and sold CIR voting shares.[18]

5. Conclusions

Dual class share unifications are usually compensated either by an extraordinary dividend (Ang and Megginson, 1989) or by assigning new voting shares to voting shareholders (Hauser and Lauterbach, 2004). In Italy, where the price differential between voting and non-voting shares is one of the highest in the world (Nenova, 2003, Zingales, 1994, Dyck and Zingales, 2004), share unifications are typically forced and do not offer compensation to the voting

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[17] CIR is a financial company valued at the time, for its internet and media businesses.
[18] See Il *Sole 24 Ore*, September 14th, 2000, *Finanza e Mercati*, page 1.

shareholders. In addition, share unification announcements are associated with price increases for non-voting shares and price declines for voting shares, with little change in overall firm value. Italian dual class unifications thus present two puzzles – first, why do voting shareholders agree to such unifications, and second, why do they not increase firm value?

We examine the universe of 46 Italian unifications made in the 1974-2005 period and show that the unification process is driven by the preferences of the controlling shareholder. The negative returns earned by voting shareholders are largely driven by a subsample of firms where the controlling shareholder owned a block of non-voting shares prior to the unification. The ownership of this block of non-voting shares also explains why dual class unifications in Italy are sometimes forced and often do not include any compensation to voting shareholders for the loss of their voting premium. Italian controlling shareholders hedge or even take advantage of such unifications by buying blocks of non-voting shares prior to the unification announcement. In other cases, the terms of the unification process are set so that the controlling shareholder is unaffected by the unification.

In this sense, our paper adds to the extant literature on expropriation, documenting a new channel through which minority shareholders can be expropriated in publicly listed firms. It may seem puzzling that minority shareholders do not realize the potential for expropriation and drive down the voting premium prior to the unification decision. There is some evidence that they do. Croci and Caprio (2007) show that the average voting premium in Italy drops precipitously from 50% in 1997 to 21% in 2002. However, the negative excess returns for voting shares in the sample of firms where the controlling owner owns a large block of non-voting shares suggests that the voting premium does not drop nearly enough. This would be consistent with Cheung, Rau and Stouraitis (2006) who show that while the market seems to punish firms for tunneling episodes, there does not seem to be a systematic discount when they examine companies that have the potential to engage in such transactions. However, since the ownership of non-voting shares is hard to establish, it is not entirely surprising that minority shareholders do not anticipate the expropriation *a priori*.

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Table 1

Types of and stated reasons for Italian dual class share unifications

Panel A reports the types of Italian dual class share unifications carried out between 1974 and 2005. Forced unifications are defined as those where the non-voting shareholders are forced to convert their holdings into voting shares. Panel B reports the reasons companies cited for unifying the dual class share structure. The information was compiled from company disclosures and newspaper articles. Some firms provided multiple reasons for the unification.

Panel A: Types of Italian dual class share unifications

Type of conversion	1:1 conversion with no additional compensation	1:1 conversion with additional cash compensation paid by non-voting shares	N non-voting shares converted to 1 voting share	Limit on total number of non-voting shares that can be converted	Number
Forced	Yes	No	No	No	18
	No	No[*]	No	No	1
	No	Yes	Yes	No	3
Voluntary	Yes	No	No	No	11
	No	No	No	Yes	3
	No	Yes	No	No	7
	No	Yes	Yes	No	3
Total					46

[*] Required an additional cash payment made to non-voting shares since non-voting shares were trading at a premium to voting shares.

Panel B: Stated reasons for Italian dual-class share unifications

Stated reason	Number
Increase float and liquidity	9
Simplify equity structure	8
Before or after the firm's privatization by the government[*]	5
Raise cash for new investments	4
Improve attractiveness for international investors	4
Before a merger[*]	4
Before an equity issue[*]	3
Secure index membership	1
No reasons given	19

*Reason not declared but unification preceding or immediately following extraordinary event.

Table 2

Ownership characteristics of Italian DCU firms

This table reports ownership data calculated in the period immediately before the unification announcement date. All ownership variables are obtained from *Il Taccuino dell'Azionista* (1982-1995), the Italian Security and Exchange Commission (Consob) print database (1995-1997), and online data sources (1998-2005). The sample is divided into cases where the ownership of non-voting shares by the largest shareholder prior to unification can be inferred and into cases where it cannot. The ratio of control rights to cash-flow rights is computed using the methodology in Faccio and Lang (2002) and Consob ownership data since 1995. The p-value for the difference is computed using the median test.

	Overall			Controlling shareholder owns non-voting shares			No information on non-voting share ownership			P-value for difference in medians
	N	Mean	Median	N	Mean	Median	N	Mean	Median	
Fraction of votes held by largest shareholder										
Before unification	46	59.65%	59.90%	21	55.65%	57.40%	25	63.01%	61.90%	0.14
After unification	35	55.49%	55.94%	19	53.75%	54.19%	16	57.56%	56.70%	0.88
Dilution in vote ownership	35	-2.21%	0.00%	19	-1.21%	-3.29%	16	-3.40%	0.28%	0.20
P-value for difference		(0.28)	(0.44)		(0.62)	(0.09)		(0.33)	(0.79)	
Identity and fraction of shares held by largest shareholder										
Family	30	58.90%	55.99%	15	57.16%	59.65%	15	57.24%	56.76%	0.72
Government	8	69.60%	69.85%	2	62.25%	62.25%	6	72.05%	77.62%	0.13
Financial institutions	8	58.90%	55.99%	4	46.72%	52.84%	4	71.08%	67.14%	0.19
Fraction of votes held by second largest shareholder										
Before unification	46	4.72%	3.26%	21	4.79%	2.10%	25	4.65%	3.66%	0.77
After unification	34	5.20%	3.24%	19	5.39%	2.20%	15	4.95%	4.95%	0.31
P-value for difference		(0.33)	(0.77)		(0.78)	(0.45)		(0.08)	(0.06)	
Ratio of control rights to cash-flow rights										
Before unification	32	0.76	0.80	17	0.73	0.77	15	0.79	0.93	0.30
After unification	32	0.86	0.99	17	0.87	1.00	15	0.85	0.99	0.73
P-value for difference		(0.01)	(0.00)		(0.00)	(0.00)		(0.35)	(0.00)	
Fraction of non-voting shares owned by largest shareholder	21	30.56%	19.94%	21	30.56%	19.94%	-	-	-	-

Table 3

Financial characteristics of Italian DCU firms

This table reports accounting data calculated based on the last annual financial statement before the unification announcement date. All accounting variables are from Datastream, with the exception of data for the two earliest unifications (Fisac, 1982 and Reyna, 1986) which were obtained from "Il Taccuino dell'Azionista". All variables are computed as of the last financial statement before the unification announcement date. The market-to-book ratio is the market value of equity divided by the book value of equity. Market leverage is computed as total debt divided by total capital (debt plus market value of equity). Book leverage uses the book value of equity in place of the market value. ROA is computed as Earnings before interest and taxes (EBIT) divided by total assets. To compute industry adjustments, for each sample firm, we classify all the Italian companies belonging to the same industry in three industry definitions in increasing level of detail: INDC3 (SIC2), INDC4 (SIC3) and INDC5 (SIC4).To avoid the problem of an insufficient number of matching companies, we use the most detailed industry (INDC5) only if the number of companies in the industry is greater or equal to 3, otherwise we use the less detailed industry (INDC4) or the least detailed (INDC3). The industry average is used for the industry-adjusted variables. The p-value for the difference is computed using the median test.

	Overall			Controlling shareholder owns non-voting shares			No information on non-voting share ownership			P-value for difference in medians
	N	Mean	Median	N	Mean	Median	N	Mean	Median	
Total Assets, €millions	38	4,250	1,062	17	6,832	451	21	2,159	1,593	0.33
Market-to-book	38	2.79	1.64	17	3.04	1.66	21	2.59	1.45	0.75
Industry adjusted market-to-book ratio	38	-0.56	-0.51	17	0.35	-0.29	21	-1.29	-0.70	0.75
		(0.49)	(0.14)		(0.82)	(0.63)		(0.12)	(0.19)	
Market Leverage	38	0.40	0.39	17	0.41	0.40	21	0.39	0.38	0.75
Industry adjusted market leverage	38	0.03	0.01	17	0.05	0.02	21	0.01	0.01	0.75
		(0.60)	(0.87)		(0.58)	(1.00)		(0.89)	(1.00)	
Book Leverage	38	0.33	0.32	17	0.34	0.39	21	0.32	0.27	0.11
Industry adjusted book-leverage	38	0.04	0.00	17	0.61	0.63	21	0.04	-0.05	0.87
		(0.38)	(1.00)					(0.49)	(0.66)	
ROA	38	7.90%	6.40%	17	9.27%	6.96%	21	6.80%	6.34%	0.75
Industry adjusted ROA	38	-0.11%	-0.94%	17	0.81%	-0.18%	21	-0.85%	-1.62%	0.75
		(0.92)	(0.42)		(0.64)	(1.00)		(0.59)	(0.38)	

Table 4

Characteristics of voting and non-voting shares

This table reports mean and median statistics on voting and non-voting shares during the unification process. All variables are obtained from *Il Taccuino dell'Azionista* and *Il Sole 24 Ore*. The sample is divided into cases where the ownership of non-voting shares by the largest shareholder prior to unification can be inferred and into cases where it cannot. All values are computed three days before the unification announcement date. The voting premium is calculated as the price differential between a voting and a non-voting share divided by the price of a non-voting share. The value of the voting right is computed as the ratio of the voting right, adjusted for the higher dividend to non-voting shares, over the market price of non-voting shares. The regulated dividend yield for non-voting shares is defined as the ratio of minimum dividend (according to the company charter) over the market price of non-voting shares. The actual non-voting dividend yield is defined as the ratio of last dividend paid on non-voting shares over the market price of non-voting shares. The expected non-voting dividend yield is defined as the ratio of next DPS paid on non-voting shares over the market price of the non-voting shares. The excess yield over the 10-year T-bond yield is defined as the expected non-voting dividend yield minus 10-year Italian Treasury Bond gross yield in the same month of the announcement date (source: Bank of Italy).The p-value for the difference is computed using the median test.

	Overall			Controlling shareholder owns non-voting shares			No information on non- voting share ownership			P-value for difference in medians
	N	Mean	Median	N	Mean	Median	N	Mean	Median	
Ratio of non-voting to total shares	35	17.55%	18.01%	17	19.88%	18.69%	18	15.35%	9.47%	0.25
Voting premium	35	38.73%	29.50%	17	36.50%	31.43%	18	40.84%	29.39%	0.62
Value of voting right	35	54.20%	49.17%	17	51.11%	50.84%	18	57.12%	46.17%	0.62
Regulated dividend yield for non-voting shares	35	1.83%	1.11%	17	1.70%	1.05%	18	1.96%	1.96%	0.40
Actual non-voting dividend yield	35	2.89%	2.57%	17	3.29%	2.96%	18	2.52%	2.52%	0.62
Expected non-voting dividend yield	35	2.92%	2.57%	17	3.89%	3.42%	18	2.00%	2.25%	0.25
Excess yield over 10-year T-bond yield	35	-3.06%	-2.75%	17	-1.63%	-2.42%	18	-4.42%	-4.62%	0.25

Table 5

Stock price performance at the announcement of dual class unifications

This table reports cumulative market-adjusted returns measured over the window [x, y] for voting shares and non-voting shares, and the change in the total market capitalization of the firm. Unification announcements are collected from the *Il Sole 24 Ore* financial newspaper. The event date is defined as the unification announcement date or the first next trading date if the stock was suspended by the Italian exchange in the day of the information release. The p-value for the difference is computed using the median test.

	N	Overall Mean	Overall Median	N	Controlling shareholder owns non-voting shares Mean	Controlling shareholder owns non-voting shares Median	N	No information on non-voting share ownership Mean	No information on non-voting share ownership Median	P-value for difference in medians
CARs earned by voting shares										
Period [-1,+1]	35	-1.56%	-1.25%	17	-3.72%	-4.59%	18	0.47%	0.81%	0.03
		(0.09)	(0.23)		(0.01)	(0.05)		(0.70)	(1.00)	
Period [-2,+2]	35	-1.94%	-0.60%	17	-3.33%	-4.51%	18	-0.64%	0.16%	0.03
		(0.07)	(0.39)		(0.05)	(0.14)		(0.65)	(1.00)	
CARs earned by non-voting shares										
Period [-1,+1]	35	11.66%	6.75%	17	12.30%	9.37%	18	11.07%	6.43%	0.25
		(0.00)	(0.00)		(0.00)	(0.00)		(0.03)	(0.01)	
Period [-2,+2]	35	12.50%	6.53%	17	14.85%	11.29%	18	10.29%	5.00%	0.07
		(0.00)	(0.00)		(0.00)	(0.00)		(0.05)	(0.03)	
Effect on total market capitalization										
Period [-1,+1]	35	0.57%	0.03%	17	-1.05%	-1.62%	18	2.10%	2.18%	0.13
		(0.52)	(1.00)		(0.34)	(0.63)		(0.13)	(0.48)	
Period [-2,+2]	35	0.08%	0.01%	17	-0.34%	-1.39%	18	0.48%	1.03%	0.40
		(0.94)	(0.86)		(0.85)	(0.63)		(0.73)	(0.33)	

Table 6

Likelihood of compensated or forced unifications

This table reports the coefficients from a probit regression of the likelihood of a compensated or a forced unification. The dependent variable takes on the value 1 if compensation is offered to voting shareholders or if the unification is forced. The independent variables are the voting premium (the pre-unification difference in price of voting and non-voting shares), the fraction of shares represented by non-voting equity, pre-unification stakes of the largest and second largest shareholders of voting equity, and indicator variables that equal 1 when non-voting share ownership by the majority shareholder is inferred or declared, when a family, government or financial institutions own stakes in the firm and for the post EMU period in 1999. Controlling variables are the excess yield over the 10-year T-bond yield (defined as the expected non-voting dividend yield minus 10-year Italian Treasury Bond gross yield in the same month of the announcement date) and the size of the firm (log of total assets). P-values are reported in parentheses.

	Probability of compensated unification		Probability of forced unification			
N	35	35	35	35	35	35
Intercept	-10.96	-10.36	-1.28	-1.51	-0.39	2.48
	(0.09)	(0.11)	(0.76)	(0.72)	(0.93)	(0.69)
Voting premium	0.23	0.32	0.09	0.05	-0.94	-1.18
	(0.83)	(0.76)	(0.90)	(0.94)	(0.35)	(0.29)
Non-voting equity as fraction of total equity	13.71	14.68	-4.46	-4.40	-4.66	-4.85
	(0.09)	(0.08)	(0.14)	(0.14)	(0.21)	(0.22)
Pre-unification stake of largest shareholder	-11.60	-12.91	4.98	5.07	6.79	7.13
	(0.05)	(0.03)	(0.17)	(0.15)	(0.10)	(0.12)
Pre-unification stake of second-largest shareholder	-3.53	-6.18	1.73	1.38	3.75	5.41
	(0.86)	(0.78)	(0.83)	(0.87)	(0.71)	(0.61)
Non-voting share ownership dummy	-14.14	-14.98	4.81	4.99	7.24	8.32
	(0.02)	(0.02)	(0.10)	(0.09)	(0.05)	(0.06)
Pre-unification stake of largest shareholder × non-voting share ownership	19.06	19.83	-5.04	-5.30	-8.36	-9.91
	(0.03)	(0.03)	(0.26)	(0.24)	(0.13)	(0.13)
Post European Monetary union dummy	0.48	0.61	2.07	2.03	3.91	4.88
	(0.60)	(0.48)	(0.03)	(0.03)	(0.01)	(0.02)
Dummy for family ownership						-1.19
						(0.33)
Dummy for government ownership					3.90	4.38
					(0.06)	(0.05)
Dummy for financial institution ownership		1.10		-0.26		
		(0.39)		(0.72)		
Excess yield over 10-year T-bond yield	7.63	13.91	-35.62	-36.05	-52.31	-57.65
	(0.67)	(0.49)	(0.03)	(0.03)	(0.03)	(0.03)
ln(Total assets)	1.13	1.15	-0.32	-0.31	-0.61	-0.83
	(0.04)	(0.04)	(0.13)	(0.15)	(0.03)	(0.04)
Pseudo R^2	0.44	0.45	0.35	0.35	0.41	0.42

Table 7

OLS regression estimates

This table reports coefficients of OLS cross-sectional regressions of three-day abnormal returns on the independent variables defined in table 6. The dependent variables are the three-day market-adjusted abnormal returns for voting shares, the three-day abnormal return for non-voting shares, and the three-day total change in firm market capitalization. P-values are reported in parentheses.

	CARs earned by voting shareholders				CARs earned by non-voting shareholders				Effect on total market capitalization			
N	35	35	35	35	35	35	35	35	35	35	35	35
Intercept	-0.03	-0.03	-0.05	-0.06	0.07	0.09	0.21	-0.03	-0.04	-0.04	-0.03	-0.08
	(0.73)	(0.75)	(0.56)	(0.54)	(0.80)	(0.73)	(0.50)	(0.92)	(0.65)	(0.71)	(0.74)	(0.49)
Voting premium	0.02	0.02	0.02	0.02	0.29	0.30	0.28	0.30	0.06	0.07	0.06	0.06
	(0.34)	(0.35)	(0.40)	(0.31)	(0.00)	(0.00)	(0.00)	(0.00)	(0.01)	(0.01)	(0.01)	(0.01)
Non-voting equity as fraction of total equity	-0.28	-0.28	-0.25	-0.26	-0.37	-0.19	-0.46	-0.26	-0.20	-0.16	-0.18	-0.14
	(0.00)	(0.00)	(0.00)	(0.00)	(0.06)	(0.34)	(0.04)	(0.24)	(0.01)	(0.03)	(0.01)	(0.06)
Pre-unification stake of largest shareholder	0.12	0.12	0.12	0.11	-0.08	-0.11	-0.03	-0.12	0.09	0.08	0.10	0.08
	(0.05)	(0.05)	(0.03)	(0.04)	(0.63)	(0.50)	(0.89)	(0.50)	(0.14)	(0.17)	(0.10)	(0.19)
Pre-unification stake of second-largest shareholder	0.29	0.29	0.37	0.35	-0.66	-0.93	-0.66	-0.95	0.19	0.13	0.26	0.20
	(0.15)	(0.16)	(0.05)	(0.08)	(0.27)	(0.12)	(0.32)	(0.13)	(0.37)	(0.54)	(0.22)	(0.35)
ln(Total assets)	0.00	0.00	0.00	0.00	0.00	0.01	-0.01	0.01	0.00	0.00	0.00	0.00
	(0.60)	(0.58)	(0.80)	(0.88)	(0.92)	(0.65)	(0.60)	(0.57)	(0.74)	(0.88)	(0.67)	(0.76)
Indicator variables for:												
Post European Monetary union	0.01	0.01	0.03	0.02	0.00	0.04	0.02	-0.01	0.01	0.02	0.03	0.02
	(0.45)	(0.38)	(0.10)	(0.42)	(0.98)	(0.44)	(0.73)	(0.92)	(0.60)	(0.29)	(0.15)	(0.39)
Forced unifications	0.00			0.01	0.13			0.07	0.03			0.02
	(0.77)			(0.49)	(0.01)			(0.26)	(0.09)			(0.25)
Compensated unifications		0.00		0.00		-0.15		-0.10		-0.03		-0.02
		(0.98)		(0.95)		(0.01)		(0.14)		(0.09)		(0.36)
Non-voting ownership			-0.04	-0.04			0.05	0.03			-0.03	-0.03
			(0.02)	(0.02)			(0.31)	(0.60)			(0.13)	(0.06)
Family ownership				-0.01				0.06				0.00
				(0.59)				(0.37)				(0.96)
Government ownership				-0.03				0.04				-0.01
				(0.20)				(0.68)				(0.84)
Adjusted R^2	0.36	0.36	0.48	0.45	0.43	0.45	0.30	0.42	0.30	0.29	0.28	0.32