The new edition of Corporate Governance Code of companies listed on Borsa Italiana (the Italian Stock Exchange) was published on December 5th, 2011. The Code was presented by Gabriele Galateri di Genola and Domenico Siniscalco, respectively Chairman and Deputy Chairman of the Italian Corporate Governance Committee, during a press conference held at Palazzo Mezzanotte, headquarters of the Stock Exchange in Milan.

The first experience of self-regulation of companies listed in Italy was made in 1999, just a few years after the privatization of the Borsa. The main aim of the so-called Codice Preda (which took its name from the first Chairman of the private Italian Stock Exchange, Mr. Stefano Preda) was to regulate the decisional processes as well as the control system of issuers, taking particular care of the enterprise risk and the management of possible conflicts of interests between directors and shareholders (in particular, minority ones). This objective has always been taken in consideration in Italy, also in light of (i) the particular model of the local familiar entrepreneurship and (ii) the traditional administration and control system of limited companies, where shareholders elect a Board of Statutory Auditors (the Collegio Sindacale). Nevertheless, the Italian Code of Corporate Governance, from its first edition, has introduced the concept of “independent director”, which has then been adopted also by Italian legislator1, and has pushed issuers to have at least two Committees inside the Board, one dedicated to make proposals for remuneration of directors and top managers (the Remuneration C.) and the other to supervise their internal control system (the Internal Control C.). The creation of a Nomination Committee was also advised in the Code but not considered as “necessary” for the “comply or explain” rule, which is the core of the self-discipline.

As their authors wrote, the Codice Preda wanted to offer a «model of reference of organizational and functional nature» also in order to ease the international comparison of Italian corporate governance rules vis-à-vis international ones, permitting in this way a similarity between Italian listed companies with the international best practice which institutional investors feel as necessary for the creation of the “shareholder value”. After the first issue in 1999, the Corporate Governance Committee of Italian Stock Exchange made some minor modification to the Code in 2002.

In March 2006, the Corporate Governance Committee published a totally new release of the Code, which contained a set of updated recommendations for listed issuers2. In
particular, the structure of the Code itself did profoundly change: each article was divided into three distinct sections, (i) general “principles”, (ii) “application criteria”, containing detailed instructions for implementing the principles, and (iii) “comments”, aimed at defining the range of principles and criteria, also including suitable examples, if the case»3.

The main new features of the 2006 Code were substantially the following:

- Role of the Board of Directors: recommendations in the Code were modified in order to comply with the new regulatory framework (in fact, the Italian Civil Code had been amended between 2003 and 2004 in the part regarding the commercial companies), in particular with regard to the new discipline of groups; recommendations of limits to the number of roles held by each director and annual self-assessment by the board were also introduced as well as an improved definition of the role of non-executive directors. On this subject, one of the most important amendments was the introduction of the so called “lead independent director”, in case of concentration of roles of Chairman and CEO in the same person4;

- Independent Directors: the principle of “substance over form” (which is also the mainstream of the norms on the deals with related parties) was affirmed in assessing independence, also with examples of criteria based on which the Board of Directors must perform the assessment; the direct involvement of the Board of Statutory Auditors was required in verifying the correct application of said criteria; an yearly meeting to be attended only by independent directors was introduced;

- Internal Committees of the Board of Directors: general regulations regarding the composition, powers and methods of carrying out their mandate were put in place;

- Appointment of Directors: the principle of transparency principle in the procedure of appointment was restated and better specified and examples of possible duties of the Nominating Committee were foreseen;

- Remuneration of Directors: the Board was asked to define the structure and purposes of remuneration, providing a distinction between executive and non-executive directors; the duties of the Remuneration Committee were specified;

- Internal Control System: the concept of control was updated in order to comply with the evolution of international best practice; roles and relations between various persons/bodies involved in defining, monitoring and updating the system were reviewed, with particular regard to the relations between the Board of Auditors and the Internal Control Committee;

is nourished through a daily confrontation with the market and the stakeholders, of which the issuers are protagonists, not only those of a large size, naturally prone to liaise with investors, but also medium-small size companies, which are aware that they can find in good governance an effective instrument to increase value and to protect the investments of their shareholders. Essentially a continuously evolving regulatory context, among European Union directives and recommendations, reforms of the domestic legislation in the field of corporate law and the protection of savings».

3 This new formulation of the Code was so explained by the authors: «Each matter is handled having regard to principles, criteria and comments, in order to facilitate the implementation of the “comply or explain” principle and the full understanding, by the market, of the corporate governance model applied by each company. Moreover, the best efforts were used to avoid ineffective burdensome operating and administrative procedures for the issuers, introducing elements of flexibility that accommodates differences such as the size of the company, the shareholding composition and the economic sector involved».

4 Section 2.C.3 of the Code indicated that the designation of a lead independent director was also required in the event that the office of chairman was covered by the person controlling the issuer.»
- Directors’ Interests and Transactions with Related Parties: recommendations consistent with the new regulatory framework introduced by Articles 2391 and 2391-bis of the Italian Civil Code were set;
- Statutory Auditors: there were new rules regarding extension of the guarantee of their independence and the definition of measures aimed at guaranteeing efficient and effective performance of their role;
- Relations with Shareholders: the Code required the promotion of initiatives aimed at facilitating shareholders’ awareness of company information and favoring their participation in meetings and the exercise of their rights;
- Alternative Management and Control Systems: the Code had also to face with companies adopting the one-tier or two-tier system introduced by the amendment to the Civil Code: also said companies were invited to apply the Code’s recommendations, adapting themselves to the chosen system and providing ample disclosure of the adaptations used and the reasons for such choice.

In March 2010, the Corporate Governance Committee met again and approved a new text of the Code’s contents related to the remuneration of directors and strategic managers, in light of the Commission Recommendation of 2009.

As the previous editions, the 2011 issue of the Italian Corporate Governance Code sets out again the best practices of corporate governance, in line with the main international market experience; such practices are recommended by the Committee to all listed companies and they have to be applied according to the “comply or explain” principle, requiring the explanation of the reasons for any omitted compliance to one or more recommendations set forth by the principles or the criteria of the Code.

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5 The new text completely amended Article 7 of the Code. The companies were asked to comply with the new rule within fiscal year 2011. The complete compliance for the issuers on this chapter was uneasy, due to the fact that, in the meantime, Italian Parliament approved the new Article 123-ter of the Consolidated Law on Financial Intermediation which required the listed companies to yearly publish a Remuneration Report. Said report is divided in two parts: the first, containing the policy on the remuneration of directors and strategic managers, and the second with the complete indication of all the parts of remuneration paid in the previous fiscal year to directors and strategic managers and their compliance with the policy enacted. The first part of the Report is submitted to the non-binding vote of the shareholders. CONSOB, the supervising authority of the Italian financial markets, enacted its regulation on the matter at the end of 2011 and a large number of listed issuers complied with the mandatory rules during 2012.


7 Article 124-bis of the Consolidated Law on Financial Intermediation, introduced by Law No. 262/2005, required the issuers to yearly provide information on the “adhesion to codes of conduct promoted by companies managing regulated markets … motivating reasons of any failure”. Non respecting this rule might have the consequence of an administrative fine for members of the board of directors as well as board of internal auditors and general managers of the captioned company, pursuant to Article 192-bis of the same Law. As a consequence, in the Italian law for listed companies we have assisted to “external” consequences in case of lack of (information about) compliance to self-regulated rules. The Legislative Decree No. 173/2008 has deleted Article 124-bis and has modified Article 192-bis, which now is headed Corporate governance disclosures and punishes failures to issue disclosures pursuant to Article 123-bis, subsection 2, paragraph a) by means of a financial penalty ranging from 10,000 to 300,000 euro and the publication of the disciplinary measure, at the expense of the offender, in at least two daily newspapers having a national circulation. Article 123-bis requires listed companies to yearly issue a «Report on corporate governance and ownership structures» and subsection 2, paragraph a), substantially has the same contents of the deleted Article 124-bis: companies are also asked to provide information about corporate governance practices actually applied over and above any legal or regulatory obligations and where the adopted corporate governance code of conduct may be accessed by the public.
The Committee has significantly modified the 2006 version: the new Code, which is a now “decalogue” as it contains ten articles, was streamlined and, at the same time, boosted. As an introduction, it is recalled that adoption of, and compliance with, the Code is voluntary. Again, the structure of the each article is the same as in the 2006 version, with a division of each section in *principles, criteria and comments*. The *criteria* set out the recommended conduct typically necessary in order to reach the objectives set out in the *principles*. Instead, *comments* – as highlighted in the foreword of the Code – pursue two goals: *i)* clarification, also through examples, of the relevant *principles and criteria*; *ii)* description of additional positive conduct, intended as possible desirable methods to pursue the objectives set out in the *principles and criteria*. It has also to be said that the weight of these parts are different from the point of view of the “comply or explain” rule: in fact, issuers which adopt the Code shall provide in their Corporate Governance Report\(^8\) accurate, concise and easily understandable information on the way in which each single recommendation contained in the *principles and criteria* has been effectively implemented during the period covered by the report. As a consequence, each issuer shall supply adequate information with regard to the reasons for the omitted or partial application of just *principles and criteria*. *Comments* are not part of the “comply or explain” rule and issuers are not compelled to explain a lack of compliance to them. In case *principles and criteria* relate to optional conduct, a description of the conduct followed is required, though it is not necessary to provide the reasons for the choices made by the company.

In preparing the new issue of the Code, the Committee adapted it to several rules introduced by the Italian legislator as well as by CONSOB over the last years – also in order to implement European directives –: in fact, said changes made certain recommendations of the previous issue outdated. Furthermore, the Code was graduated in order to facilitate small and medium size listed companies\(^9\).

On the other hand, the Code was revised in order to increase the real effectiveness of the recommendations, also in light of the most recent national and international best practices: it has been emphasized, once again, the central position of the action to be carried out by the Board of Directors\(^10\), and the role of internal committees, as well as their “independent” components, was strengthened\(^11\).

As far as composition of the board of directors of the Board itself is concerned, it has been recommended that all directors should be adequately competent and professional\(^12\) and more details than in the previous issues have been provided in relation to the minimum number of independent directors, clarifying that at least 1/3 of the directors in the board of companies belonging to FTSE-Mib shall be independent\(^13\). The designation of a lead independent director, other than in the case of coincidence of Chairman and

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\(^8\) This report is mandatory – see footnote 7).

\(^9\) In fact, several principles are limited to the FTSE-Mib index companies. In the principle V of the introduction, it is clarified that an issuer is deemed to belong to the FTSE-Mib index «if its shares were included in the list of such an index (or of an index that might replace it in the future) in the last trading day of the fiscal year before the fiscal year covered by the annual report».

\(^10\) Article 1 is headed “Role of the Board of Directors” and the first principle, contained in section 1.P.1, is: «Listed companies are governed by a Board of Directors that meets at regular intervals, adopts an organisation and a *modus operandi* which enable it to perform its functions in an effective manner».

\(^11\) Both for Remuneration Committee and for Control and Risk Committee the Code asks that they have to be made up of independent directors or, alternatively, of non executive directors, the majority of which to be independent; in this case, the chairman of the committee(s) shall be chosen among the independent directors.

\(^12\) Principle 2.P.1: «The Board of Directors shall be made up of executive and non-executive directors, who should be adequately competent and professional».

\(^13\) All the companies shall have at least two independent directors, whichever is the total number of board members – see 3.C.3.
CEO and/or Chairman and controlling shareholder in the same person, is mandatory in companies belonging to FTSE-Mib index in case it is requested by the majority of independent directors (2.C.3)\textsuperscript{14}.

An application criterion discouraging cross directorship between CEO of listed issuers not belonging to the same corporate group has been introduced by Section 2.C.5, which has anticipated a similar rule introduced by the Italian legislator with regard to banks, insurances and financial institutions\textsuperscript{15}.

Again with particular regard to independent directors, in the comment to Section 5 the Committee «wishes that a director who has expressed his/her eligibility as independent undertakes to maintain it during his/her office and, if necessary, to resign, it being understood that the Board of Directors has the faculty to resolve upon immediate co-optation». It has also been suggested to consider the need to ensure management continuity, and mainly in relation to the activity of the committees set up within the board of directors, even through a diversification of the expiry of all or part of the board members (the so-called staggered board), provided that this does not jeopardize the different shareholders’ rights\textsuperscript{16}.

About the role of the board of directors, the Code specifies in Principle 1.P.2 that the main objective of the Board of Directors shall be to create value over a medium-long term period: the board has also the duty to define both the nature and level of risks in a way consistent with the issuer’s strategic objectives (1.C.1. b): the parallelism between risks to be run and targets to be reached is one of the relevant features of the 2011 Code. The need of self-assessment of the board have been stressed, highlighting the advantages that may derive from the presence of “different” directors in terms of experience (also international one), professional competence (including managerial experience) and gender\textsuperscript{17} (1.C.1. g).

The Code stresses also the need of prompt and complete information to be supplied before and during each meeting of the Board to the benefit of directors, with the faculty recognized to the chairman to require, also upon the other directors’ request, the managers in charge of the items on the agenda to attend the board meetings (1.C.6).

Also in its 2011 issue, the Code has focused its attention on the committees set up within the board and has dedicated particular care to their organization. In particular, it has been set forth that they have to elect a chairman (4.C.1. a), who will be an independent director both in the Control and Risks Committee and in the Remuneration Committee (7.P.4 and 6.P.3). Anyway, in view of making less heavy the compliance to the Code, it has been set out that the establishment of one or more committees may be avoided and the relevant duties may be assigned to the entire board of directors, that, in this case, should dedicate adequate time to “preliminary examination” under the coordination of the chairman (4.C.2). An alternative may be to combine the various duties of the committees to a sole

\textsuperscript{14} Pursuant to 2.C.4, the lead independent director:  
(a) represents a reference and coordination point for the requests and contributions of non-executive directors and, in particular, those who are independent …; (b) cooperates with the Chairman of the Board of Directors in order to guarantee that directors receive timely and complete information.

\textsuperscript{15} See Article 36 of Law Decree 201/2011, converted in Law No. 214/2011.

\textsuperscript{16} See comment to Section 2.

\textsuperscript{17} On this subject, the Code and the Italian law follow the same direction: in fact, the Law No. 120/2011, enforceable in August 2012, requires listed companies to have board of directors composed by at least 1/5 of members belonging to the least represented gender. This percentage will increase in the next years, arriving to 1/3.
For issuers having board of directors composed of no more than eight members, it has been set out the possibility to establish committees made up of two members.

One of the most important changes envisaged by the new Code is the recommendation of setting up a Nomination Committee, while, as already explained, so far issuers had been requested only to evaluate the opportunity to establish it. Even though pursuant to Principle 5.P.1 this committee should propose candidates for appointment to the position of director, the criterion 5.C.1 clarifies that it has (a) to express opinions to the Board of Directors regarding its size and composition and express recommendations with regard to the professional skills necessary within the Board and (b) to submit the Board candidates for directors offices in case of co-optation, should the replacement of independent directors be necessary. It has also been recommended to evaluate whether to adopt a succession plan, and, in the event of adoption of such a plan, to charge the Nomination Committee (or any other committee in charge for this task) of the relevant preparation and to disclose the choices made to the market.

The Code make another relevant step, after the 2006 edition, towards a complete rationalization of the internal control and risks management system in line with most recent trends. The central position of the “risk” in the control systems has been definitively underlined, and this turned into a different name of the system (that is now defined as “internal control and risk management system”). The name of the Internal Control Committee has also changed as it is now called “Control and Risk Committee”.

Principle 7.P.3 clarifies the relevant roles and duties of all the participants to the system of control and risk management:

- the Board of Directors shall provide «strategic guidance and evaluation on the overall adequacy of the system», identifying within the Board the “Director in charge of the internal control and risk management system” and the Control and Risk Committee, «to be charged with the task of supporting, on the basis of an adequate control process, the evaluations and decisions to be made by the Board of Directors in relation to the internal control and risk management system, as well as to the approval of the periodical financial reports»;
- the person in charge of internal audit is entrusted with the task to verify the functioning and adequacy of the internal control and risk management system;
- the Board of statutory auditors, also as “Audit Committee”, which is responsible for oversight of the internal control and risk management system.

The role of the internal audit function has been specially emphasized and, in order to safeguard its autonomy, it has been set out that any decision concerning the appointment,

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18 In any case, as usual, the Board is required to explain in its Corporate Governance Report the reasons leading to choose an alternative approach and how this approach permits to achieve anyway the goals fixed by the Code for each committee – see comment to Article 4.
19 In the previous editions, this rule was for issuers with boards of less than five members.
20 The criterion requires also the Committee to express opinions “with regard to the topics indicated by articles 1.C.3. and 1.C.4.”, i.e. maximum number of offices as director or statutory auditor that may be considered compatible with an effective performance of a director’s duties and cases of possible application of Article 2390 of the Italian Civil Code which prohibits Directors to perform activities in competition with the company.
21 It has to be noted that any reference to the “person in charge of internal control” (preposto al controllo interno) has been deleted, substituted by reference to the person in charge of the internal audit.
22 This is in line with Legislative Decree No. 39/2010, which implements in Italy the European Directive No. 2006/43/CE on statutory audits of annual accounts and consolidated accounts.
revocation and remuneration of the relevant officer in charge should be adopted by the entire Board of Directors with the opinion (which shall be considered as binding) of the Control and Risk Committee and after consultation with the Board of statutory auditor.

On the subject of the control system, the Code clarifies also that it is up to the entire Board the approval – at least once a year – of the audit plan prepared by the Chief Audit Executive, after consultation with the Board of statutory auditors and the director in charge of the internal control system.

To complete the landscape with regard to the control and risk management, the Code touches a sore point which concerns the “administrative-criminal” responsibility of companies pursuant to Legislative Decree No. 231/2001. In fact, in the comment to Article 7, it is suggested to issuers to “assess the opportunity” to entrust the Board of Statutory Auditors with the duties pertaining to the surveillance body pursuant to Article 6 of the said Legislative Decree. Also on this point, the Code and the Italian law follow the same path: in fact, Law Decree No. 212/2011, converted in Law No. 10/2012, has introduced the new subsection 4-bis to Article 6 of Legislative Decree N. 231/2001 with a content similar to the one of the Code on this subject.

Article 9 focuses its attention on the relations with shareholders, asking issuers – in continuity with previous versions of the Code – to «ensure that a person is identified as responsible for handling the relationships with the shareholders and ... evaluate from time to time whether it would be advisable to establish a business structure responsible for such function» (Criterion 9.C.1); Article 10 closes the Decalogue making reference to the alternative systems of administration and control of the companies (two-tier and one-tier) which, by the way, had chosen by a very limited number of issuers until now. With reference to the two-tier model, Criterion 10.C.1 clarifies that the articles of the Code which refer to the Board of Directors and the Board of Statutory Auditors, or their members, are applied, in principle, to the Management Board and Supervisory Board, or their members respectively, apart from cases where specific options of the by-laws adopted push issuers to different solutions.

Issuers have been invited to apply the amendments brought to the Corporate Governance Code by the end of the fiscal year beginning in 2012, providing information to the market in the Corporate Governance Report to be published within the following fiscal year. Amendments to the composition of the Board of Directors and the relevant committees may be postponed and the issuers may comply to the relevant rules in occasion of the election of new bodies.

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23 Some major Italian issuers, such as ENI and Fiat, have already disclosed the application of the new Code.
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