

Italian Corporate Governance Code Amended to Include Corporate Social Responsibility and Whistleblowing Provisions for Listed Companies

Italian Listed Companies should implement changes by the end of the 2016 fiscal year.

On July 10, 2015, the Corporate Governance Committee (the Committee)¹ approved certain amendments to the Corporate Governance Code of Italian Listed Companies (the Code). These amendments incorporate recommendations provided in the second annual report on the application of the Code, published on December 11, 2014 (the 2014 Report)², and introduce certain corporate social responsibility and whistleblowing principles.

This *Client Alert* details the main changes approved by the Committee. Listed companies are invited to implement such changes — with the exclusion of changes to article 8, regarding the statutory auditors — by the end of the fiscal year beginning in 2016 and to provide information about such implementation in the corporate governance report to be published in the following fiscal year. As far as the changes to article 8 are concerned, listed companies are invited to implement such changes starting from the first renewal of the Board of Statutory Auditors occurring after the fiscal year beginning in 2015.

Main Amendments

- Increased attention of the board of directors to the risks that may affect the issuer's business in the medium-long term perspective and to induction sessions
- Reiteration of the recommendation to independent directors to hold separate and periodic meetings
- Recommendation to draft minutes of each committee's meetings and focus on the corporate social responsibility
- Role of the nomination committee when the board of directors submits a slate for the renewal of the board
- Strengthening of the internal control and risk management systems in line with the best practices and the most recent whistleblowing provisions set out by Regulation (EU) No. 596/2014 on market abuse (so-called MAR) and Directive No. 2013/36/EU on prudential supervision and capital requirements of banks and credit institutions (so-called CRD IV)
- Statutory auditors – disclosure of the results of the verification of the independence requirements and remuneration criteria

Article 1 – Role of the Board of Directors

The amendments to Article 1 strengthen the recommendations regarding the role of the board of directors in relation to the determination of both the nature and the level of the risk that the listed issuer should take in meeting its own strategic objectives. To this end, the amendments to the Code outline that the board of directors should take into account any risks that may affect the sustainability of the issuer's business in a medium-long term perspective (criterion 1.C.1. (b)). In the comment section, the Committee highlights the essential role of the board of directors in evaluating the actual functioning of the internal control system and of the management of any risk that may affect the sustainability of the issuer's business in a medium-long term perspective. Furthermore, the Committee outlines that, under relevant circumstances, the board of directors should acquire any necessary information and adopt any suitable measure to protect the company and the information towards the market.

As already provided for in the 2014 Report, the updated Code recommended the corporate governance report should state the effective attendance of the executives of the issuer and its subsidiaries (executives responsible for the relevant corporate and management functions), if any are invited to the board of directors' meetings by the CEO upon request of either the chairman or other directors to provide any clarification and supplemental information on the items on the agenda (criterion 1.C.6.).

Article 2 – Composition of the Board of Directors

With regard to the induction sessions dedicated to directors and statutory auditors (which the Code recommends that the chairman organize periodically), and based on the findings of the 2014 Report, the Committee recommended that the corporate governance report should state the type and the organizational methods of any initiatives which occurred during the relevant fiscal year. Such initiatives — in addition to providing the directors and the statutory auditors with an appropriate knowledge of the issuer's business sector, corporate dynamics, development, and the relevant regulatory and self-regulatory frameworks — should now also address appropriate risk management principles (criterion 2.C.2.).

Article 3 – Independent Directors

The recommendation that the independent directors meet at least once a year separately from the directors (criterion 3.C.6.) has been expanded and clarified in line with the recommendations contained in the 2014 Report, providing that specific meetings should be called and held separately from the committees' meetings attended by the independent directors .

Article 4 – Establishment and Functioning of the Internal Committees of the Board of Directors

In the general recommendations on the establishment, composition and functioning of the internal committees of the board of directors, the Committee added two new recommendations. First, the recommendation that committees' meetings be recorded with specific minutes has been supplemented by the recommendation that the chairman should provide information about such recording to the board of directors at the first available meeting (criterion 4.C.1.). The second, more relevant amendment relates to the comment section of article 4 where the Committee has introduced the recommendation that the boards of directors of companies listed on the FTSE MIB index evaluate the opportunity to establish a committee in charge of corporate social responsibility matters. This committee would supervise the sustainability issues related to the business activities of the company and its interaction dynamics with all its stakeholders. As an alternative to the establishment of a dedicated committee, the board may decide to group or to allocate the tasks above among the other established committees.³

Article 5 – Appointment of Directors

Building on the experience gained in recent years with regard to appointment of the board of directors based on the slate system and the recommendations in the 2014 Report, the Committee has underlined and specified the importance of involving the nomination committee when a slate of candidates for the renewal of the board of directors is submitted by the board itself, to the extent permitted by the law.

Furthermore, if the listed issuer has adopted a plan for the succession of the executive directors, the Committee recommended that the plan's procedure should clearly define the plan's objectives, instruments and timeline. The involvement of the board of directors and a distinct allocation of the relevant tasks, starting from the preparatory activities which, according to the Code, should be assigned to the nomination committee or to any other internal committee in charge of such tasks, should also be clearly defined.

Article 7 – Internal Control and Risk Management System

The amendments to Article 7 are primarily aimed at strengthening the internal control and risk management systems and at aligning such systems with domestic and international best practices. The amendments also seek to align with recent regulatory reforms concerning whistleblowing with regards to listed issuers, introduced by Regulation (EU) No. 596/2014 on market abuse (abrogating Directives No. 2003/6/CE/, 2003/124/CE, 2003/125/CE and 2004/72/CE as of July 3, 2016⁴), as well as by the so-called CRD IV (Directive No. 2013/36/UE), which relates to access to the business of credit institutions and the prudential supervision of credit institutions and investment firms.⁵ In this respect, the Committee:

- Recommended that the control and risk committee be granted the specific task of supporting, with adequate preliminary and structuring activities, the assessment and decisions of the board of directors on the management of risks deriving from abuses which the board may have become aware of (criterion 7.C.2. (g))
- Outlined the importance of an internal control and risk management system, usually covered by the legal and compliance corporate functions — with particular emphasis on the protective measures to be applied against the legal and non-compliance risks, including the risk of performing criminal offences to the prejudice or in the interest of the company — which are relevant for the purposes of legislative decree No. 231/2001 on criminal liability of companies
- Specified that — at least in the listed companies belonging to the FTSE MIB index — an adequate internal control and risk management system includes a system allowing the company employees to report any irregularity or breach of the applicable laws and internal procedures (the so-called whistleblowing systems) in accordance with the domestic and international best practices, thus ensuring a specific and confidential communication channel as well as the anonymity of the reporting person

Article 8 – Statutory Auditors

The last amendments to the Code approved by the Committee concern the recommendations applicable to statutory auditors. Per these amendments, the results of the verification of the independence requirements of the statutory auditors, to be performed after their appointment and subsequently on an annual basis, shall be submitted to the board of directors. The board will then disclose such results through a press release relating to the first verification conducted after the first appointment and in the relevant corporate governance report with reference to the annual verification (criterion 8.C.1.).

Finally, it is worth noting the addition of a new principle that, in line with the recommendations already set forth for directors' remuneration, states that the remuneration of statutory auditors should be proportionate to the commitment required from each of them, to the importance of their office and to the size and business sector of the company (criterion 8.C.3.).

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Endnotes

- ¹ The Committee was set up, in its current composition, in June 2011 on the initiative of the main Italian associations representing corporations and institutional investors (ABI, ANIA, Assonime, Confindustria, Assogestioni) and Borsa Italiana S.p.A. The Committee is in charge of promoting, approving and updating the Corporate Governance Code of Listed Companies.
- ² The 2014 Report is available on the Committee's website: <http://www.borsaitaliana.it/comitato-corporate-governance/comitato/relazione2014.pdf>
- ³ For an analysis of the application of the corporate social responsibility principle by Italian listed companies, see the research "*C.d.A. e politiche di sostenibilità. Come sostenibilità e CSR entrano nell'agenda dei consigli di amministrazione delle imprese quotate italiane*" (BoD and sustainability policies. How sustainability and CSR crept into the items on BoD's agendas of Italian listed companies) promoted by CSR Manager Network, in collaboration with Assonime and Nedcommunity, conducted between May 2013 and May 2014 with the research team of Alta Scuola Impresa e Società (ALTIS) of the Università Cattolica del Sacro Cuore.
- ⁴ July 3, 2016 is the final deadline for the entry into force of the MAR and for the amendments of the national legislation to comply with the new regulatory provisions. Article 11 of the 2014 European proxy law, approved on July 2, 2015, delegated the government to adopt the legislative measures necessary to implement in Italy both the MAR and Directive No. 2014/57/UE, regarding the criminal penalties in case of market abuse (the so-called MAD II).
- ⁵ Directive No. 2013/36/UE was transposed in Italy with legislative decree No. 72 of May 12, 2015.