2019 Hot Corporate Governance Topics - 2019 shareholders' annual meeting of Italian listed companies

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The season for shareholders' annual general meetings is fast approaching, and we would like to take this opportunity to provide our clients and friends with some suggestions that we believe provide strategic flexibility and reflect best practices in corporate governance.

1. Treasury shares for strategic transactions

The annual shareholders' meeting of a listed company generally authorizes the Board of Directors to buy back the company's own shares and to dispose of them in compliance with applicable law, including, in particular, (i) the safe harbor (provided under Article 5 of MAR[1]) providing protection from MAR prohibitions on insider dealing, unlawful disclosure of inside information and market manipulation and (ii) the so-called "accepted market practices", as applicable from time to time (which set forth market practices that are deemed not to constitute market manipulation) pursuant to Article 13 of MAR ("**AMPs**").

Consob has previously put into effect AMP No. 1, concerning purchases of a company's own shares to support market liquidity, and AMP No. 2, aimed at building a reserve of shares ("*magazzino titoli*") to be used as consideration for extraordinary transactions and/or in stock option or stock granting plans. In 2018, many listed companies in Italy purchased their own shares in order to support liquidity and use them as consideration in strategic transactions.

However, in September 2018 Consob started a review of the compatibility of the Italian AMPs with MAR, which may result in a repeal of AMP No. 2. If AMP No. 2 is repealed, the repurchase of shares to build a reserve of shares would still be permitted, but would no longer benefit from the protection granted by Article 13 of MAR in relation to market manipulation.

We would recommend including specific language in corporate resolutions and reports for the 2019 annual shareholders' meetings relating to the purchase of a company's own shares that contemplates possible future changes to the AMPs and keeps the scope of the authorization flexible enough to reflect such changes.

2. Diversity

Issues of diversity have recently garnered an increasing amount of attention.

1 Market Abuse Regulation, i.e. EU Regulation No. 596/2014.

As you know, pursuant to the Italian Consolidated Financial Law[2], listed companies must approve a diversity policy or explain their reasons for not doing so.

Moreover, under the Corporate Governance Code (*Codice di Autodisciplina*), the board of directors must provide instructions and criteria to any shareholders' meeting called to appoint new members of the board of directors and statutory auditors in order to ensure compliance with diversity recommendations in the composition of such corporate bodies (in relation not only to gender but also to professional and managerial skills, international experience, age and professional seniority), or explain in the corporate governance report published in advance of the annual shareholders' meeting the reason for the company's lack of compliance with such provision. However, only a number of Italian listed companies have adopted a diversity policy or have a board of directors that has provided instructions to the shareholders' meeting in relation to diversity requirements.

Gender has been and continues to be one of the key focal points of diversity: according to public data made available by Consob, female representation in boards of directors increased to 33% in 2017 and further to 36% as of June 2018, with an average of 4.6, 4.1 and 3.3 female directors sitting on the boards of directors of Ftse-Mib, Mid Cap and STAR listed companies, respectively, as of June 2018. However, the same data show that 68.6% of such women serve as independent directors and rarely do they act as chief executive officer or chairperson of the board of directors.

Absent an extension of currently applicable provisions[3], the gender diversity requirements will no longer apply after the third renewal/appointment of the board of directors following the adoption of the Italian gender diversity law in 2011. In expectation of the gender diversity law's expiration, on July 18, 2018 the Corporate Governance Committee approved a revised version of the Corporate Governance Code (*Codice di Autodisciplina*), introducing various diversity requirements for listed companies' boards of directors and boards of statutory auditors, including the gender diversity requirements set out under the gender diversity law.

We would recommend paying increased attention to adopting a diversity policy in line with best practices in preparation for the implementation of the new provisions of the Corporate Governance Code.

3. Non-financial information

Recent reporting provisions[4] require large companies (including listed companies)[5] in the EU to include non-financial information in their public disclosures.

The Italian 2019 Budget Law[6] broadened the scope of non-financial information that companies are required to make public with regard to key social and environmental issues. In particular, listed companies are now required to include descriptions of the management procedures they have adopted in order to (i) manage and mitigate key environmental, social risks and risks relating to personnel, (ii) ensure the promotion of human rights and (iii) fight against corruption.

2 Italian Legislative Decree No. 58/1998, as amended most recently in 2016Pursuant to Italian Legislative Decree No. 254 of December 30, 2016.

3 Italian Law No. 210/2011.

4 Directive 2014/95/EU of October 22, 2014 amending Directive 2013/34 EU as regards disclosure of non-financial and diversity information by large companies has been implemented in Italy by Legislative Decree No. 254 of December 30, 2016.

5 Large companies are defined as groups of companies (i) having more than 500 employees in average in a single financial year and (ii) whose consolidated financial statements reports (a) aggregated assets for more than Euro 20 million or (b) aggregated revenue for more than Euro 40 million.

6 Italian Law No. 145 of December 30, 2018.

The 2019 Budget Law entered into force on 1 January 2019, therefore its provisions should only affect non-financial information prepared in relation to 2019 and subsequent financial years.

We would recommend that companies implement or improve processes for the collection, validation and disclosing of non-financial information and structuring of risk management procedures, in order to ensure future compliance and even to try to be - a market leader by being among the first to institute practices compliant with the 2019 Budget Law.

4. Internal control measures

Based on the new Italian Bankruptcy Law[7], starting from March 16, 2019, Italian companies (including listed companies) must have in place "*an organizational, administrative and accounting structure that is adequate to the nature and size of the company*" and is "*aimed at overcoming crisis and restoring corporate continuity*"[8]. The legislator has not provided additional guidelines on the establishment of said adequate structure, which we believe shall be coordinated with the issuers' internal control procedures.

In 2018, Consob paid increased attention to listed companies' internal control procedures, issuing sanctions to 11 companies in 2018 due to inadequacy of the companies' internal control procedures.

While listed companies already have in place corporate governance procedures and an internal control and risk management system, we would recommend that companies assess whether their internal policies, procedures and SCG meet the new requirements.

5. Minority Shareholders' Rights

The Shareholders Rights Directive II[9] is aimed at encouraging long-term shareholders engagement and must be implemented in Italy by 10 June 2019. According to the draft decree approved by the Italian government on 7 February 2019, key changes will relate to:

- *Shareholders' identification*: issuers would have the right to request that intermediaries identify any shareholder owning more than 0.5% of its share capital, thus allowing a clearer and more transparent picture of the shareholding structure[10].

- *Shareholders' binding vote on remuneration policy*: the company's remuneration policy would need to be presented to the shareholders at least every three years or whenever a change to such policy is proposed by the board of directors; however, their vote remains non-binding under the draft decree and therefore if the remuneration policy is not approved by the majority of the share capital represented at the annual general meeting, a new remuneration policy would have to be presented by the directors at the following shareholders' meeting.

- *Shareholders' right to ask questions*: in connection with the shareholders' right to submit questions ahead of the shareholders' meeting, a new deadline would be introduced for submitting such questions (corresponding to the record date[11]), with longer time

7 The new Code for Corporate Crisis and Insolvency introduced by Italian Legislative Decree No. 14 of 12 January 2019, implementing Italian Delegated Law No. 155/2017.

8 Art. 375 of the new Italian Bankruptcy Law amending art. 2086 of the Italian Civil Code.

9 EU Directive No. EU/2017/828, amending EU Directive No. 2007/36/CE.

10 As of today, an issuer may identify its shareholders owning less than 3% (or 5%, as the case may be) of its share capital if such right is provided in the company's bylaws and the relevant shareholder does not refuse to be identified, without prejudice to the identification procedure carried out by issuers in connection with shareholders' meetings.

11 The sevent[h] trading day prior to the date of the shareholders' meeting.

provided for listed companies to prepare answers in advance of the shareholders' meetings (applicable starting from 1 January 2020).

- *Related parties transactions*: Consob would have the right to set out total or partial exemptions from the applicability of related party transactions rules.

- *Sanctions*: Consob's sanctioning powers would be extended, as the number of sanctioned actions would be increased (particularly in relation to transactions with related parties and remuneration policy).

As the Shareholders Rights Directive II has not been implemented in Italy yet, we are assessing the impact that the above provisions may have on issuers, particularly in relation to minority shareholders' rights and future annual shareholders meeting, we would recommend that companies start considering the potential impact of the Shareholders Rights Directive II on their internal procedures.

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