



## **CONSOB ISSUES A CONSULTATION DOCUMENT ON THE REGULATION OF RELATED PARTY TRANSACTIONS**

### **Executive Summary**

Consob has issued for consultation a draft regulation on disclosure and fairness requirements for related party transactions entered into by Italian listed companies and companies with a high number of shareholders (hereinafter together referred to as issuers).

Following a legislative mandate to adopt general principles that issuers must follow in setting out their internal codes on related party transactions, Consob is proposing a comprehensive new framework for such transactions, both providing for ongoing and periodic disclosure requirements and introducing procedural steps issuers must comply with in order to ensure the entire fairness of related party transactions.

The draft regulation greatly enhances disclosure on related party transactions, by requiring their immediate disclosure when they are above some specified thresholds, and enlists independent directors to ensure the entire fairness of related party transactions.

An unofficial translation of the draft regulation, together with a summary of the consultation document, will shortly be available on Consob's website ([www.consob.it](http://www.consob.it)).

The following are the key features of the draft regulation:

1. Consob Regulation on Issuers already provides for the on-going disclosure of material related party transactions, but materiality is now defined narrowly to comprise only transactions that, “for their contents, consideration, conditions or time of execution may have an impact on a company’s solvency or on the completeness and faithfulness of available information pertaining to the issuer” (Article 71-2). The draft regulation, drawing inspiration from the UK Listing Authority approach, identifies material related party transactions as those above some specified thresholds in terms of consideration (as a percentage of market capitalization, assets, and profits). Material related party transactions

have to be promptly disclosed to the market by issuing a circular describing the transaction, how it was entered into, and its impact on the issuer.

- a. Material related party transactions between an issuer and a 100 percent subsidiary need not be disclosed on an on-going basis, provided that no other related party has an interest in the subsidiary;
  - b. for issuers posing a higher threat of minority shareholder expropriation due to the presence of control enhancing mechanisms such as pyramids, issuance of non-voting shares or voting caps, the threshold is 1 percent (as opposed to 5 percent for other companies).
2. Drawing inspiration from US case law on fiduciary duties, Consob has identified the following general principles that issuers have to abide by in devising their own internal codes on related party transactions are the following:
- a. for material related party transactions, a committee of independent directors is to play a key role in the decision-making process. Such a committee should conduct, or at least take part to, the negotiations with the related party and may obtain the advice of legal and/or financial advisers of their own choice. It should also be entrusted with the power to finally approve the transactions, unless by law or corporate charter approval should be made by the whole board, in which case they should give the board their advice on the transaction;
  - b. for related party transactions other than material ones, issuers may provide for a simpler procedure, in which independent directors are only required to give their advice on the transactions, but still may obtain independent advice;
  - c. small caps, newly listed companies, and issuers other than listed ones may adopt the simpler procedure also for material related party transactions. This is the first instance in which Consob differentiates its rules on listed issuers based on their size or other criteria;
  - d. as for the related party transactions which have to be approved by the shareholder meeting, the issuers must adopt specific mechanisms that guarantee alternatively that they are not approved by the vote of related parties (whitewash mechanisms) or that independent directors play a determining role in the approval of the proposals to be submitted to the shareholder meeting.

3. Finally, a new corporate governance requirement has been introduced to address minority shareholder protection concerns within pyramidal groups. For listed companies that are under the control of another listed company, first, a majority of the directors must be independent. Second, the audit committee and the other committees a listed company establishes in compliance with the Italian Corporate Governance Code must be comprised exclusively of independent directors.