



corporate governance

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CONTENT AND STRUCTURE OF ANNUAL CORPORATE GOVERNANCE REPORTS AND ANNUAL REMUNERATION REPORTS AND OF OTHER DISCLOSURE INSTRUMENTS

1. INTRODUCTION

The Sustainable Economy Law (Law 2/2011, of March 4, 2011) and the legislation on governing bodies and other components of the legal rules on savings banks (Royal Decree-Law 11/2010, of July 9, 2010) laid down new corporate governance obligations each for listed companies (*sociedades anónimas*) and savings banks (*cajas de ahorros*). Principally to implement those obligations, Order ECC/461/2013 was published on March 23, 2013 in the Official State Gazette, after being approved by the Ministry of Economy and Competitiveness on March 20, 2013, an order determining the content and structure of the annual corporate governance reports, of the annual remuneration reports and of the other disclosure instruments of listed companies, of savings banks and of other institutions issuing securities admitted for trading on official securities markets.

The order's main aims are as follows:

- Update the content of annual corporate governance reports and group together in a single ministerial order all of the obligations in connection with this report for listed companies, savings banks and other institutions issuing securities admitted for trading on official securities markets.
- Implement the content of the annual remuneration report, established as an obligation in the Sustainable Economy Law, also jointly for listed companies and savings banks.
- Update the information that listed companies and savings banks must include on their websites.

The order came into force on the day following the date of its publication in the Official State Gazette, although (to prevent distortion of the shareholders' meeting period that has already started) in a transitional provision it determines that the reporting obligations it contains will not apply in the fiscal year commenced on January 1, 2012, which will be governed by the legislation previously in force.

This order repeals Order ECO/3722/2003, of December 26, 2003, on the annual corporate governance reports and other disclosure instruments of listed companies and other institutions and Order ECO/354/2004, of February 17, 2004, on the annual corporate governance reports and other information of savings banks that issue securities admitted for trading on official securities markets.

It also amends Order EHA/1421/2009, of June 1, 2009, implementing article 82 of the Securities Market Law (Law 24/1998, of July 28, 1998), to add a provision on the dissemination of significant facts on websites, a provision that had already appeared in Order ECO/3722/2003 which has been repealed.

The Spanish Securities Market Commission (“**CNMV**”) has been authorized so that, within three months, it can detail the content and structure of annual corporate governance reports and annual remuneration reports. Until then, the CNMV Circulars hitherto in force on this subject will apply (Circulars 1/2004, 4/2007 and 2/2005).

In relation to annual corporate governance reports, this publication summarizes the key new provisions in the order, without describing therefore the information already being included in annual corporate governance reports on the forms approved by the CNMV, or in an attachment to them with the new information required by the Sustainable Economy Law.

2. GENERAL PROVISIONS

The order contains general provisions establishing:

- **The principle of information transparency:** the information to be included in annual corporate governance reports and annual remuneration reports must be clear, complete and truthful, and no information may be included that may create error or confusion for investors.
- **How the reports must be sent:** they must be submitted remotely on the CIFRADO/CNMV system or any other similar system that may be put in place by the CNMV. Exceptionally, the CNMV may, with just cause, give authorization for them to be submitted on paper on the required form.
- **Responsibility for the preparation and content of the reports:** lies with the institution’s managing body.

3. PRINCIPAL AMENDMENTS CONCERNING THE ANNUAL CORPORATE GOVERNANCE REPORTS OF LISTED COMPANIES

The order has introduced the following new provisions:

- In relation with the functioning of the shareholders’ meeting, inclusion of any decisions implying structural modifications at the company which, although there is no legal requirement, must be submitted to the shareholders’ meeting .

- The key new provisions concerning the structure of company management are:
 - The proportion of nominee directors and independent directors on the committees must be specified as part of the board composition.
 - In the case of directors who, despite receiving payments from, or engaging in business dealings with, the group, have been classed as independent directors, a reasoned declaration by the board must be included on the reasons why it considers that director can act as an independent director.
 - It must be reported whether the board has performed in the fiscal year an assessment of its activities, mentioning any significant changes that have taken place as a result in its organization or procedures.
 - Details must be given of the number of female directors present at board meetings and at committee meetings and changes in the past four years.
- The main changes concerning transactions with related parties are:
 - The board must report on both the competent body and on the procedure for approving transactions with related parties, with an obligation to explain whether that power has been delegated.
 - An additional section has been added for transactions with other related parties.
 - A new obligation has been added to report on any intragroup transactions performed with companies established in countries or territories classed as tax havens.
- Further specification has been added on the content of the section on risk control systems, in which information must be given on the principal risks that may affect the achievement of business objectives, the risks that have taken place in the year, the scope of the management systems, the responsible bodies, the level of tolerance and a description of the response and supervision plans.
- Concerning the internal risk management and control plans in relation to the process for issuing financial information (new section under the Sustainable Economy Law, which introduced the obligation to describe the main characteristics of those systems), it has been specified that the information must be broken down into the following basic components: control environment, risk assessment, control, disclosure and communication activities, and supervision.
- Lastly, in relation to the obligation to specify how far the company follows the recommendations of the Unified Good Governance Code, it emphasizes that if the company does not follow, or partially follows, these recommendations, its explanations should give shareholders, investors and the market generally sufficient information to assess the company's modus operandi. The CNMV is also authorized to update the Code's recommendations.

4. PRINCIPAL AMENDMENTS CONCERNING THE ANNUAL CORPORATE GOVERNANCE REPORTS OF SAVINGS BANKS ISSUING SECURITIES ADMITTED FOR TRADING ON OFFICIAL SECURITIES MARKETS

The new changes concerning the annual corporate governance reports of savings banks are expectably in keeping with those concerning listed companies.

- Concerning the structure and duties of the governing body:
 - Information must be included on the number of female members on the board, on board committees and on the control committee, on the same terms as for listed companies.
 - It must be reported whether the board has performed in the fiscal year an assessment of its activity, mentioning any significant changes that have taken place as a result in its organization and procedures.
- Requirements have been added to mention the percentage that *cuotas participativas* (“equity units”) bear to the savings bank’s equity and to indicate the members of the control committee (in addition to the board members) that hold equity units.
- Detailed information must be provided, in relation to received remuneration, on the agreements between the savings banks and those with responsibility at them for management and control, or their employees, which provide for severance if they resign or are dismissed in an unjustified dismissal or if the employment relationship comes to an end.
- A new section has been added on conflicts of interest existing between the members of the governing bodies or, the holders, if any, of equity units, and the savings bank’s community outreach arm.
- Further specification has been added on the risk control systems, on the same terms as for listed companies and the same obligation has been added to describe the internal risk management and control systems in relation to the process of issuing financial information.
- Lastly, the order has eliminated for the annual corporate governance reports of savings banks the provision regarding how far they follow the good governance recommendations.

5. PRINCIPAL AMENDMENTS CONCERNING THE ANNUAL CORPORATE GOVERNANCE REPORTS OF INSTITUTIONS ISSUING SECURITIES TRADED ON OFFICIAL SECURITIES MARKETS

The main changes in relation to their minimum content are:

- Concerning the structure of ownership of the institution, there is a new obligation to provide information on any restrictions on transfers of securities and on voting rights.
- Concerning the structure of management of the institution, information must be included on the female directors on the same terms as for listed companies.
- A description of the internal risk management and control systems in relation to the issue of financial information must be included on the same terms as for listed companies.
- The provision regarding how far they follow the good governance recommendations has been eliminated.

6. TYPES OF DIRECTORS

The order contains definitions of the various types of directors (executive, nominee and independent) which, to date, had been provided in the Unified Good Governance Code. The fact of including them in this order implies that a breach will be subject to the provisions in the Securities Market Law.

Apart from the changes mentioned in the following two paragraphs, the definitions are the same as those provided in the Unified Good Governance Code.

The most important change, which triggered a wide debate in the approval process for this order, is that the directors that have been in office uninterruptedly for a period of over twelve years cannot be classed as independent. A transitional period has been established, however, in which (i) independent directors who, as of June 30, 2013, have been in office for longer than 12 years, will not lose their independent director status until the end of their current mandate; and (ii) in the annual corporate governance report for 2013, it is allowed to class directors who in that fiscal year have been in office for longer than twelve years as independent directors.

In relation to directors who are significant shareholders, executive directors or senior managers of an institution who is receiving, or has received in the past three years, donations from the company or from its group, the adjective “significant” referring to those donations has been eliminated and so, in principle, it appears that any donation would prevent the director concerned being classed as independent.

The annual corporate governance reports of listed companies must be prepared in line with the established definitions. If there is an external director who cannot be classed as either nominee or independent, the company must explain this circumstances and that director's ties, with either the company or its shareholders.

The board, subject to a prior report from the nominations committee, is responsible for determining, each year upon preparing the annual corporate governance report whether the directors have complied uninterruptedly with the independence conditions contained in the order.

7. PUBLIC DISCLOSURE

The order contains detailed provisions on the public disclosure required of annual corporate governance reports and the related time periods, in addition to the following special cases:

- Entities domiciled in Spain whose voting rights are held entirely by another institution whose securities are listed on Spanish official secondary securities markets.
- Foreign entities whose securities are listed on Spanish official secondary markets.
- European companies domiciled in Spain that have chosen the dual system.

8. ANNUAL REPORT ON DIRECTORS' REMUNERATION

The order has introduced the minimum content of the annual remuneration reports required for the directors of listed companies, and for the members of the board and of the control committee of savings banks that issue securities admitted for trading on official securities markets (for these last-mentioned institutions, with the necessary adaptations required for this type of institution).

This minimum content is based on the content that had already been recommended in the Unified Good Governance Code, but the order has considerably broadened the scope of some contents.

Thus, annual remuneration reports must have the following minimum content:

- Remuneration policy in the current year.
 - Amount of the fixed components and attendance fees, and of the variable items of remuneration, with the performance evaluation criteria chosen for the remuneration design and the methods in place to determine fulfillment of those criteria. The director classes that have variable remuneration, plus an explanation of the relative size of variable remuneration items with respect to fixed items. Added to this in the order is the requirement for a significant breakdown.

- Principal characteristics of the welfare systems with an estimate of their amount or equivalent annual cost.
- Conditions that must be satisfied by the contracts of those carrying on senior management activities as executive directors.
- Most significant changes in the remuneration policy with respect to that applied in the previous year.
- Information on the preparatory work and the decision-making process that have taken place to determine the remuneration policy and the role played, if any, by the remuneration committee and other monitoring bodies in the remuneration policy structure.
- Information on action adopted by the company in relation to the remuneration system to reduce exposure to excessive risk and adjust it to the company's long-term objectives, values and interests.
- Sufficient information on the periods set for the availability of shares following the acquisition of absolute ownership of them.
- Remuneration policy in place for future years.
 - General outline of provisions.
 - Information on the decision-making process and role played by the remuneration committee.
 - Information on the incentives created to reduce exposure to excessive risks.
- Overall summary of the remuneration policy for the previous year.
- Detail of the remuneration received in the previous year.
 - Breakdown of the remuneration received by each director.
 - Breakdown of any awards of shares to directors, stock options or any other instrument linked to share prices.
 - Information on the ratio between directors' remuneration and earnings or other measures of the company's performance.
 - Information on the results of the consultative ballot of the shareholders' meeting, stating the number of negative votes in relation to the annual remuneration report.

Annual remuneration reports must be published as a material event and notified to the CNMV, in addition to being submitted to a consultative ballot of the shareholders' meeting set out as a separate item on the agenda for the shareholders' meeting (or general assemblies in the case of savings banks), as required by article 61 ter of the Securities Markets Law.

In all other respects, the rules on public disclosure and times limits for annual remuneration reports are the same as for annual corporate governance reports.

9. ANNUAL CORPORATE GOVERNANCE REPORTS AND ANNUAL REMUNERATION REPORTS OF OTHER SAVINGS BANKS

In an additional provision, the order provides that:

- Savings banks, regardless of whether their business is conducted directly or indirectly, that do not issue securities admitted for trading on official securities markets are required to publish an annual corporate governance report and an annual remuneration report every year, and send it to the CNMV, which in turn will send them to the Bank of Spain and to the competent autonomous community government bodies.

Their contents and structure must be in line with the provisions of this new order and any forms required by the CNMV for issuing savings banks, with the relevant adjustments.

- In the case of savings banks that carry on the activities in their corporate purpose as a credit institution through a banking institution to which they have contributed all of their financial business, the provisions in this order will apply to the institutions through which those savings banks conduct their business as a credit institution.

In cases where the institutions mentioned in this last paragraph are not listed companies, the content and structure of their annual corporate governance reports and annual remuneration reports must be adapted, with the adjustments required for non-issuing institutions, to the provisions in this order and the forms and printed matter that the CNMV may have in place for listed companies.

- Their annual corporate governance reports and annual remuneration reports must be sent to the CNMV, which in turn will send them to the Bank of Spain (and, at savings banks not issuing securities, to the competent bodies of the autonomous community governments).
- These annual corporate governance reports and annual remuneration reports will be governed, concerning the rules on public disclosure, authority for approval and responsibility for their preparation, by the general rules in the order.

10. DISCLOSURE INSTRUMENTS

Concerning the information that must be included on the website of listed companies, the order sets out the disclosure obligations contained in various pieces of legislation, with clarification that the annual financial reports to be included are those relating to the past five fiscal years.

The changes regarding the information to be included (now as an obligation) on the websites of savings banks issuing securities admitted for trading on official securities markets are the requirements to include the annual corporate governance reports, annual remuneration reports, annual financial reports for the last five years and the half-yearly reports on the first six months of the fiscal year.

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