INFORMATIVE NOTE

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CORPORATE GOVERNANCE

CORPORATE GOVERNANCE CODE OF THE IPCG

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The Corporate Governance Code of the *Instituto Português de Corporate Governance* («IPCG Code») was published on 30 January 2013. For the first time, commercial companies have access to a corporate governance best practice code prepared by civil society which is an alternative to the existing corporate governance code of the Portuguese Securities Market Commission (CMVM).

Although it is intended for general application (that is, application to all commercial companies), the IPCG Code recognises that its natural targets are companies with shares admitted to trading on regulated markets («Issuers») because the regulations that govern such companies require them to adopt a corporate governance code.

The IPCG Code is based on a presumption of flexibility and adaptability and it uses a set of principles and recommendations with content that is elastic and adjustable to the situation of each one of the companies it is targeted at. The objective the IPCG Code's approach is for Issuers to adopt corporate governance practices that enable them to comply with the principles and recommendations, but without imposing a one size fits all content.

For this purpose, the IPCG Code opted for a division between principles and recommendations and this is something new compared to governance codes that have existed to date in the Portuguese jurisdiction. With this structure, the IPCG Code seeks, among other things, to give a new relevance to the exercise of explaining, allowing Issuers to consider certain principles as having been complied with, even without observing all the recommendations that constitute them.

In this way if Issuers adopt practices that do not conform to the content of a certain recommendation, but they provide a grounded explanation for their choice that demonstrates that, in terms of purpose and function, they are apt to comply with the justifying principle, such an explanation will be deemed equivalent to compliance by the Issuer.

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The IPCG Code is divided into the following seven chapters which feature a number of variable principles and recommendations:

(i) A general part containing provisions on the relationship of the company with investors and information on and operation of the corporate bodies and their inter-relationship and conflicts of interest;

(ii) Shareholders and the general meeting;

(iii) Executive management;

(iv) Monitoring and supervision;

(v) Performance appraisals and remuneration;

(vi) Risk management; and

(vii) Financial information.

Without any claim to being exhaustive, we will now highlight some of the recommendations of each one of these chapters which will, perhaps, contribute to drawing a distinction between this and the CMVM Corporate Governance Code.

Right away in the introductory chapter, the IPCG Code addresses the problem of conflicts of interest and recommends that, by means of internal regulation, any director that finds himself in a situation of conflict must inform the body or committee to which he or she belongs about the facts that may amount to such a conflict, and this director must not interfere in the decision-making process. What is new in this respect is the fact that the supervisory body has to confirm the existence of the conflict whenever the director requests, or whenever the decision of the body or committee on the existence of a conflict of interests has not been unanimous.

In the chapter on shareholders and the general meeting, what merits special attention is the recommendation on the establishment of criteria and terms under which the management body asks the general meeting to decide on management matters within its power. This is the first time this issue has been addressed in a corporate governance code on a national level.

As regards executive management, the IPCG Code recommends that the internal regulation of the management body provides that the exercise of executive duties in companies outside the group by executive directors must be authorised by the board of directors or the supervisory body. Therefore, the IPCG Code has responded to the discussion on the accumulation of duties by executive directors by requiring authorisation from the Issuer, without establishing any strict number that might not be appropriate for all.

In monitoring and supervision, one of the areas of great sensitivity lies in the notion of independence and the establishment of the number of independent non-executive directors. In this area, the IPCG Code chose to adopt the criterion of independence that is legally established for members of the supervisory body, but it admitted that, if it is justified by the size of the company, the percentage of independent non-executive directors may be lower than 25% of the total number of directors.

Also in this respect, the IPCG Code recommends that information on the relationship of directors with shareholders to whom more than 2% of the votes may be attribuited, or suppliers or clients with whom the company has significant commercial relationship, must be made available.

In respect of performance appraisal and remuneration, there are, in particular, two new features: (i) the composition of the remuneration committee – a majority, not all, of independent members of the management – and (ii) the possibility for non-executive directors to be given executive duties from time to time, which might be reflected in their remuneration (notably by the possibility of attributing variable remuneration to any director in this situation).

The issue of risk management is the area in which the IPCG Code made less ground-breaking choices and the recommendations it has laid down are very close to those that already exist.

Finally, in the chapter on financial information, it should be noted that recommendations are made on external auditing and here the IPCG Code chose not to recommend limits on the number of «terms of office» of the external auditor, and not to limit the provision of non-auditing services by it. Instead it preferred to provide that Issuers establish, by internal regulation: (i) which services other than auditing services, should not be provided by the external auditor and (ii) that the supervisory body should issue an opinion on whether or not the external auditor should be maintained at the end of each term of office.

As our analysis has been carried out immediately after the appearance of the new code, it is preliminary and, as of necessity, it does not address every issue. We must now wait and see what the reaction of Issuers and the CMVM will be to this new code. It is still early to draw any conclusions, but it seems we are now on a path to the existence and implementation of a corporate governance code other than that of the CMVM with all the advantages such a code brings to the functioning of commercial companies and, in particular, Issuers.

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