



ITALY

DETAILED ASSESSMENT OF OBSERVANCE OF IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION

December, 2013

This Detailed Assessment of Observance of IOSCO Objectives and Principles of Securities Regulation on Italy was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed in March 2013. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of Italy or the Executive Board of the IMF.

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ITALY

FINANCIAL SECTOR ASSESSMENT PROGRAM

March 2013

DETAILED ASSESSMENT OF OBSERVANCE OF IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION

Prepared By
**Monetary and Capital
Markets Department**

This Detailed Assessment Report was prepared in the context of an IMF Financial Sector Assessment Program (FSAP) mission in Italy during March 2013, led by Dimitri G. Demekas, IMF and overseen by the Monetary and Capital Markets Department, IMF. Further information on the FSAP program can be found at:

<http://www.imf.org/external/np/fsap/fssa.aspx>

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GLOSSARY

| | |
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| AIFMD | Alternative Investment Fund Managers Directive |
| AMC | Asset Management Company |
| BI | <i>Banca d'Italia</i> |
| BoS | Board of Supervisors |
| CEREP | Central Repository |
| CL | Consolidated Law on Finance |
| CC&G | <i>Cassa di Compensazione e Garanzia</i> (the Italian central counterparty) |
| CCP | Central Clearing Counterparty |
| CDS | Credit Default Swaps |
| | <i>Comitato Interministeriale per il Credito e il Risparmio</i> |
| CIS | <i>Collective Investment Schemes</i> |
| Consob | <i>Commissione Nazionale per le Società e la Borsa</i> |
| COVIP | The <i>Commissione di Vigilanza sui Fondi Pensione</i> (pension regulator) |
| CRAs | Credit Rating Agencies |
| EC | European Commission |
| ECB | European Central Bank |
| EMIR | European Market Infrastructure Regulation |
| ESAs | European Supervisory Authorities |
| ESMA | European Securities and Markets Authority |
| ESRB | European Systemic Risk Board |
| FNG | <i>Fondo Nazionale di Garanzia</i> |
| HF | Hedge Funds |
| IAS | International Auditing Standards |
| IASB | International Accounting Standards Boards |
| IF | Investment Firm |
| IFRS | International Financial Reporting Standards |
| IOSCO | International Organization of Securities Commissions |
| IOSCO MMoU | IOSCO Multilateral Memorandum of Understanding |
| IVASS | <i>Istituto per la Vigilanza sulle Assicurazioni</i> (IVASS) (the insurance regulator) |
| KIID | Key Investor Information Disclosure |
| MEF | The Minister for Economy and Finance |
| MiFID | Market in Financial Instruments Directive |
| MoJ | Ministry of Justice |
| MTFs | Multilateral Trading Facilities |
| MTS | <i>Mercato Telematico dei Titoli di Stato</i> |
| NCA | National Competent Authorities |

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| PIEs | Public Interest Entities |
| RAM | Risk Assessment Matrix |
| RMs | Regulated Markets |
| SICAV | <i>Società di investimento a capitale variabile</i> (investment company) |
| SMEs | Small and Medium Enterprises |
| SRTs | Suspicious Reporting Transactions |

EXECUTIVE SUMMARY¹

1. Italy exhibits a high level of implementation of the IOSCO principles. Overall the legal and regulatory framework is sound and the regulatory authorities have developed extremely sophisticated arrangements for off-site supervision that have resulted in a robust system of supervision. These arrangements have been developed using extensive data reporting obligations that allow the *Banca d'Italia* (BI) and the *Commissione Nazionale per le Società e la Borsa* (Consob) to have a much more precise understanding of intermediaries and products and their characteristics than is currently available to regulators in many advanced jurisdictions. Staff uses these tools to the fullest to target their supervisory interventions. Furthermore, analysis at a system-wide level by the BI complements microprudential supervision and helps in the identification of risks arising from the securities market.

2. However, these arrangements need to be complemented by additional on-site inspections to make the system more effective, although the current coverage of inspections (measured by assets and number of clients) is very high. While the robustness and sophistication of such off-site tools allow adjustments in the use of on-site inspections and altogether the current approach of Consob and BI has delivered an adequate level of supervision, on-site work remains a key tool to identify weaknesses in conduct practices, which cannot easily be detected via reporting. The same applies to operational risk, and more generally to poor governance, internal controls and risk management systems.

3. In addition the enforcement strategy should be continuously monitored to ensure that there is the right mix of tools to affect behavior, and tools available to the regulators should be strengthened. In this regard, remedial actions are necessary components of any enforcement program, but they are not sufficient. Stronger use of pecuniary sanctions is a natural complement to corrective actions. To this end, it is critical that the powers to impose pecuniary sanctions on licensed entities be strengthened, both in terms of the ability to impose penalties on legal entities and individuals, as well as in the level of fines that can be imposed. Finally criminal sanctions, in particular imprisonment, should be used sparingly but strategically to punish the most egregious violations and send clear deterrence messages to the market. The assessors acknowledge that criminal enforcement is a challenging area for both advanced and emerging economies.

4. Consob has done very effective work on identifying conflicts of interest across a range of areas in the securities markets. This is particularly important in the Italian context, where banks dominate the securities industry. It is critical that policy and supervisory actions, including enforcement, continue to be taken to address these issues.

5. Finally, strengthening of the licensing framework is required and a few refinements to the current allocation of responsibilities between BI and Consob are encouraged. On the

¹ This assessment was prepared by Ana Carvajal, from the Monetary and Capital Markets Department, IMF, and Malcolm Rodgers, MCM expert.

former, it is necessary that the definition of fit and proper be strengthened and the regulatory authorities be given the power to remove individual directors. On the latter, the mission recommends that a consultation process with Consob be established for the review of applications by banks seeking to provide investment services. In addition, the current framework could benefit from a streamlining of the chosen twin peak structure, aimed at eliminating possible ambiguities or inconsistencies and strengthening the functional approach.

INTRODUCTION

6. An assessment of the level of implementation of the IOSCO Principles in the Italian securities market was conducted from January 18 to 31, 2013 as part of the Financial Sector Assessment Program (FSAP) by Ana Carvajal, Monetary and Capital Markets Department (MCM) and Malcolm Rodgers, MCM expert. An initial IOSCO assessment was conducted in 2004. Since then significant changes have taken place in the Italian market, in terms of market development as well upgrading of the regulatory framework. In addition IOSCO approved a new set of Principles in 2010 and a revised Methodology in 2011.

INFORMATION AND METHODOLOGY USED FOR THE ASSESSMENT

7. The assessment was conducted based on the IOSCO Objectives and Principles of Securities Regulation approved in 2010 and the Methodology adopted in 2011. As has been the standard practice, Principle 38 is not assessed due to the existence of a separate standard for securities settlement systems. A technical note on the oversight framework for clearing and settlement of securities markets will be delivered during this mission.

8. The IOSCO methodology requires that assessors not only look at the legal and regulatory framework in place, but also at how it has been implemented in practice. The recent global financial crisis has reinforced the need for assessors to take a critical look at supervisory practices, to determine whether they are effective enough. Among other things, such judgment involves a review of the strength of off-site monitoring, as well as of the inspection programs for different types of intermediaries, the cycle, scope and quality of inspections as well as how the agency follows-up on findings, including the use of enforcement actions.

9. The assessors relied on: (i) a self-assessment prepared by the *Commissione Nazionale per le Società e la Borsa* (CONSOB) and the *Banca d'Italia* (BI); (ii) the review of relevant laws and reports; (iii) review of supervisory files; (iv) meetings with staff from Consob, the BI, the Minister for Economy and Finance (MEF), and prosecutorial authorities; as well as (v) meetings with market participants, including issuers, banks and their association, securities firms, fund managers, and their associations, as well as with the exchange, trading venues, external auditors, credit rating agencies and law firms.

10. The assessors want to thank Consob and BI for their full cooperation as well as its willingness to engage in very candid conversations regarding the regulatory and supervisory

framework in Italy. The assessors also want to extend their appreciation to all other public authorities and market participants with whom they met.

INSTITUTIONAL STRUCTURE

11. The regulation and supervision of securities markets in Italy follows a “modified” twin peaks structure, whereby overall the BI is responsible for prudential supervision and Consob for market transparency and conduct supervision. The mandates and responsibilities of the regulators are set out in legal provisions, mainly the Consolidated Law on Finance (CL). However, the specific allocation of responsibilities between the two authorities is very complex and stems from historical reasons.

12. The CL requires BI and Consob to cooperate in a coordinated manner, with a view to minimizing costs for market participants. The CL states that they may not invoke professional secrecy in their mutual relationship. The BI and Consob have entered into arrangements, via memorandum of understandings (MoUs), to make this obligation operational.

13. The decision making bodies for Consob and BI (the latter in exercising its supervisory role) are collegial bodies. In the case of Consob, decisions are taken by its board of three members.² For the BI, the organ responsible for its supervisory functions is the Directorate or Governing Board. It is a collegial body composed by the governor, the director general, and three deputy directors general.

14. Overall they both have independent sources of funding. Consob’s funding stems primarily from levies on market participants; by 2012 Consob’s budget was no longer dependent on funds from the general budget of the Government. In the case of BI, the operating expenses are mainly financed by the income derived from BI’s own assets as well from the income coming from net financial assets not related to monetary policy.

15. The MEF retains limited powers over securities markets regulation and supervision. In particular pursuant to the CL, the MEF is responsible for (i) issuing regulations in very specific cases; (ii) imposing certain extraordinary measures on securities intermediaries, such as the special administration and compulsory liquidation of intermediaries on a proposal from the BI or Consob; (iii) intervening in sovereign debt markets pursuant to the short selling regulation upon a proposal from the BI, after consulting Consob; (iv) and regulating and recognizing wholesale government bond markets, after consulting the BI and Consob; and (v) recognizing investor compensation schemes, after consulting the BI and Consob.

16. Regulated Markets (RMs) and Multilateral Trading Facilities (MTFs) have a limited role in market surveillance, thus they are not considered self-regulatory organizations for the

² A recent reform reduced the number of commissioners from five to three. Currently there are four commissioners, but once the period of the fourth commissioner expires, the seat will not be filled.

purposes of this assessment. The RMs and MTFs are the front line supervisors for the purpose of ensuring orderly trading, and they have a complementary role to that of Consob in regard to market abuse. Neither the RMs nor the MTFs have a role in securities intermediaries' supervision beyond ensuring that the rules of the market are being complied with. Listing is a function of the trading platforms. Listing requirements are set up via market rules subject to regulatory oversight (approval for RMs, ex-post supervision for MTFs). Issuers' obligation to comply with them stems from their contract with the market, rather than by law.

MARKET STRUCTURE

A. Issuers

17. As of December 2012 there were 323 companies listed on *Borsa Italiana*, compared to 328 in 2011. Market capitalization amounted to EUR 365,466 million or roughly 232 percent of GDP, compared to EUR 425,099 or 27 percent of GDP for 2011. There were four new listings as of October 2012, compared to five listings in 2011. The number of new listings has declined over time.

18. The ownership structure of listed companies in Italy is highly concentrated; although it has decreased slightly over time. Control is exercised through different mechanisms including (i) dual class shares, (ii) formal coalitions; (iii) pyramidal groups; and (iv) control enhancement mechanisms.

| | | Ownership concentration (as a percentage of total number of shares) | | | | |
|--------------------|-----------------|--|------|------|------|------|
| | | 1990 | 1998 | 2003 | 2007 | 2011 |
| Largest | Average | 54.7 | 47.1 | 47.5 | 45.7 | 44.8 |
| Shareholder | Weighted | 47.8 | 33.8 | 33.5 | 27.8 | 33.9 |
| Floating | Average | 28.4 | 39.2 | 37.0 | 37.0 | 37.0 |
| Capital | Weighted | 40.7 | 56.5 | 52.6 | 57.4 | 54.1 |

19. The bond market is dominated by banks' issuance and exhibits a high degree of retail participation. There is significant retail participation in the bond markets. To some extent this is due to a preferential tax treatment of bonds vis-à-vis deposits. Such preferential treatment was eliminated last year. Currently the bulk of instruments are plain vanilla bonds issued by banks; however some more complex bonds were placed among retail investors earlier in the crisis.

B. Collective Investment Schemes (CIS)

20. There are 1,235 CIS in Italy. Almost all Italian CIS are investment funds, rather than *Società di investimento a capitale variabile (SICAVs)*, and in particular open ended funds. As included in the table below, open-end funds amount to almost 76 percent of AUM; closed-end funds to 21 percent (the majority in real estate funds); and hedge funds (HFs) amount to 3.27 percent of AUM. In the past years AUM by open-end funds have plummeted, due to sizeable

redemptions, especially in 2008. Such flows in turn were captured by banks mainly via the issue of bonds. The trend for real estate funds—most of which are reserved for qualified investors—is the opposite.

| Number of CIS (as of December 2012) | | | |
|-------------------------------------|--------|-----------------|------------|
| Type of CIS | Number | AUM EUR million | Percentage |
| Open-end funds | 644 | 143,568 | 75.58 |
| Harmonized (UCITs) | 555 | 129,462 | 68.16 |
| Non-harmonized (non-UCITs) | 89 | 14,106 | 7.43 |
| Closed-end funds | 492 | 40,157 | 21.14 |
| Private Equity Funds | 139 | 8,070 | 4.25 |
| Real estate funds | 353 | 32,087 | 16.89 |
| Hedge Funds | 99 | 6,325 | 3.27 |
| TOTAL | 1,235 | 189,950 | |

C. Trading Platforms

21. The Italian markets have not faced as deep challenges in connection with market fragmentation as other European markets. Trading in equity markets continues to be concentrated in *Borsa Italiana*. There is more fragmentation in the bond markets, where systematic internalizers (SIs) compete with trading venues, but they are subject to pre and post trade transparency (although not required by EU law), including public transparency on OTC transactions and market solutions are available to consolidate prices.

D. Intermediaries

22. At end 2012, there were 740 Italian firms authorized to carry out investment services in Italy, out of which 97 were investment firms (IFs) and 643 were banks. The majority of IFs have simple business models. Only 14 of them are authorized to carry on proprietary trading activities, and out of them only two are “large” though their business model is also simple, as they do not have large trading desks. Roughly 5–6 percent of them are experiencing losses, mainly as a result of current conditions in the securities markets; thus a consolidation of the sector is expected. Investment services activities are bank dominated; furthermore banks dominate the distribution of financial products either through their platforms or through tied agents. They are also issuers of securities, mainly bonds.

23. At the end 2012, there were 172 asset management companies (AMCs). Almost all AMCs whose core business is the management of open-ended funds are owned by banks. The five largest companies manage almost 65 percent of the industry’s total AUM as of December 2012.

PRECONDITIONS FOR EFFECTIVE SECURITIES REGULATION

24. The preconditions for effective regulation and supervision of securities markets appear largely to be in place. Foreign issuers can tap the markets under similar conditions to domestic issuers. The same authorization requirements apply to both domestic and foreign corporations that want to provide investment services, including CIS management, or to operate an RM or an MTF in Italy. The tax system has created some distortions for the development of capital markets. For example a favorable treatment of bonds versus deposits prompted banks to be active in the issuing of bonds, which in practice were considered quasi-deposits; this favorable treatment was eliminated last year. The implementation of a financial transaction tax could potentially distort the development of capital markets as it is only applicable to equity transactions and equity derivatives transactions. The company law is modern, and the insolvency framework includes restructuring procedures, but insolvency procedures are very protracted. The judiciary's independence, specifically capacity and resources, in connection to criminal enforcement of securities regulations needs to be strengthened. Italy has implemented International Financial Reporting Standards (IFRS), and auditing standards do not have major differences with international standards.

MAIN FINDINGS

25. Principles for the regulator: Overall the legal framework for BI and Consob is sound and provide each of them with a clear mandate. Arrangements are in place to ensure coordination and cooperation. There is also a strong framework of transparency, independence and accountability, both to the government and the public. The rights of third parties are adequately protected via the imposition of due process obligations. BI and Consob are subject to ethical rules. However, the framework for independence for both Consob and BI should be further strengthened, in particular in regard to the protection of staff during the course of legal actions, as well as their respective code of ethics in regard to securities transactions. In addition, strengthening of the licensing and enforcement powers in the specific areas discussed in this assessment is needed. Finally a few refinements in current allocation of responsibilities between Consob and BI are encouraged.

26. Principles for enforcement: Both Consob and BI have broad investigation and inspection powers in line with their respective mandates. There is a wide range of enforcement tools available including sanctions. However, in the areas of intermediaries and CIS Consob and BI can only impose pecuniary sanctions on the individuals involved and not on the regulated entities (although regulated entities are severally liable for payment) and the level of such sanctions (other than for market abuse/short selling offences) appears low. The supervisory approaches of BI and Consob, which altogether have delivered an adequate level of supervision, rely heavily on robust off-site monitoring, and a more limited use of on-site inspections, although their coverage by market share (in terms of assets and investors covered) is high. The enforcement approach relies more on remedial actions, which while necessary might not be sufficient, and pecuniary sanctions for breaches other than market abuse/short selling violations are low mainly due to the limitations in

the legal framework as stated above and judicial practices. Criminal enforcement faces challenges, as there is a preference for settlements and even when convictions take place conditional execution is given; all of which affects the deterrent effect of the criminal system.

27. Principles for issuers: Issuers of securities subject to public offerings and products admitted to trading on an RM are subject to robust disclosure obligations at the moment of registration and on a periodic and on-going basis. Consob has developed a robust program to monitor their compliance with their disclosure obligations. Basic rights of shareholders are imbedded in company law. Additional protections exist in connection with issuers listed in an RM, including the obligation to launch a mandatory tender offer, and notification obligations for substantial and insider holdings. Issuers admitted to trading only in MTFs are not subject by law to these additional disclosure and fairness obligations. However the listing rules of *Borsa Italiana* do impose requirements in both areas, although less stringent than for issuers admitted to trading in a RM. AIM market is currently not significant in size. There is an additional category of issuers widely held which is subject to less stringent requirements than issuers admitted to trading in a RM; however currently it does not appear to be significant in size.

28. Principles for auditors, credit rating agencies (CRAs) and other information service providers: Auditors of public interest entities (PIEs) are subject to oversight by Consob. Such oversight is mainly exercised through a quality control review, conducted via on-site inspections that are carried out on a three year cycle. The inspections program appears robust. CRAs that provide services in Italy were subject to a thorough registration process by cross-European colleges of supervisors. They are now under the supervision of the European Securities and Markets Authority (ESMA), which is in the process of implementing its supervisory program for CRAs. There is a framework in place for all persons who provide recommendations on securities, which is based on fair disclosure; in addition, regulated entities are subject to organizational requirements to minimize potential conflicts of interest.

29. Principles for collective investment schemes: The authorization framework for AMCs and SICAVs includes capital requirements, fit and proper and organizational requirements and the process to review applications by BI is thorough. However there are limitations on the definition and verification of fit and proper requirements and BI cannot order the removal of individual directors except in narrow circumstances. CIS that are offered to the public are subject to similar disclosure obligations as issuers. Consistently with the EU legislation, only the prospectuses of closed-end funds are subject to pre-authorization by Consob; however the fund rules of any CIS other than a hedge fund or reserved fund must be pre-approved by BI. In addition, through its off-site monitoring Consob conducts ex-post checks of prospectuses. The supervisory program for AMCs and CIS relies heavily on robust off-site monitoring, and a more selective use of on-site inspections, although the coverage of the latter in terms of market share (measured by assets and investors) is high. Rules concerning custody of assets are robust including the requirements that assets must be entrusted to a depositary bank which is required to hold a separate license by BI and is under its supervision, including through on-site inspections. In addition, external auditors are required to submit annual reports on compliance with segregation obligations. BI has developed guidance for

the valuation of assets of CIS, including in connection with illiquid assets, which are consistent with IFRS. Conditions of suspensions of redemptions must be disclosed in the offering documents. Suspensions must be notified to Consob.

30. Principles for securities intermediaries: The authorization framework for IFs includes capital requirements (initial and ongoing), fit and proper, and organizational requirements and the process to review applications is thorough. However there are limitations on the definition and verification of fit and proper requirements and neither BI nor Consob can order the removal of individual directors except in narrow circumstances. The supervisory program for IFs by both Consob and BI relies heavily on robust off-site monitoring and a more selective/targeted use of on-site inspections, although the market coverage (measured by assets and clients) is high. The legal framework provides the authorities with robust crisis management and resolution tools in connection with banks, IFs and AMCs. In particular special administration is available to deal with troubled firms, and their liquidation can be done on an administrative basis via a compulsory liquidation. An investor compensation scheme is in place.

31. Principles for secondary markets: RMs operators are subject to authorization requirements, which include financial, fit and proper, and organizational requirements; and the process to review applications is thorough. MTFs must hold a license of IF or market operator and therefore are subject to strong authorization requirements. Trading venues are subject to pre and post trade transparency requirements, including in relation to financial instruments other than shares (although not required by EU law), and SIs are also subject to post-trade transparency. These obligations are complemented by obligations on intermediaries to report off market transactions. Consob and BI, as for wholesale markets in government securities, have developed robust arrangements for market surveillance, which are complemented by the RMs and MTFs. Consob and BI have also developed both formal and informal arrangements to oversee Borsa Italiana, MTS and the MTFs. *Cassa di Compensazione e Garanzia* (CC&G) monitors clearing members' exposures on a daily basis and has powers to request members to post additional margins intraday. Default procedures are transparent. There are reporting obligations in connection with short selling, as well as in connection with failed settlements.

Table 1. Summary Implementation of the IOSCO Principles

| Principle | Grade | Findings |
|--|-------|--|
| Principle 1. The responsibilities of the Regulator should be clear and objectively stated. | FI | BI and Consob mandates are clearly defined by the CL. The specific allocation of responsibilities between the authorities is complex and requires a significant amount of cooperation and coordination. Arrangements for such coordination and cooperation are in place. |
| Principle 2. The Regulator should be operationally independent and accountable in the exercise of its functions and powers. | BI | Overall, the framework for independence and accountability is robust; however, for both BI and Consob it is important that arrangements concerning the defense of staff during the course of law suits be strengthened. |
| Principle 3. The Regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers. | BI | Both BI and Consob have broad powers to carry out their functions. A few limitations apply in the area of intermediaries and CIS, in particular (i) they do not have the power to remove individual directors except when they no longer meet the fit and proper criteria of MEF regulations which are narrowly defined or they are sanctioned for market abuse or a public offering violations, and (ii) they can only impose pecuniary sanctions on individuals of such regulated entities but not on the legal entities, although the latter are jointly and severally liable for payment. And the level of the sanctions for breaches different from market abuse/short selling violations is low. Both BI and Consob appear to have sufficient resources. |
| Principle 4. The Regulator should adopt clear and consistent regulatory processes. | FI | Development of regulations is subject to a consultation process. Requirements for licensing are clear and available in the websites of BI and Consob. Decisions that can affect third parties are subject to due process, including the right to appeal to the judiciary. |
| Principle 5. The staff of the Regulator should observe the highest professional standards, including appropriate standards of confidentiality. | FI | Staffs of both BI and Consob are subject to ethical rules, derived from the general rules for the public administration. Such general rules are complemented by the codes of ethics and terms of employment. In general in both cases there is a duty to notify conflict of interest, and in the case of Consob there is the specific requirement to notify securities |

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| | | transactions. The rules of each authority contain specific provisions regarding the use of information and the obligation of staff to keep the confidentiality of the information they have. The internal audit units are in charge of monitoring compliance with ethical obligations. |
| Principle 6. The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate. | FI | There are processes in place at both BI and Consob to identify systemic risk. They both exchange information on a regular basis. In addition, a financial stability committee has been set up with a view to support risk identification and monitoring and crisis management cross-sectorally. |
| Principle 7. The Regulator should have or contribute to a process to review the perimeter of regulation regularly. | FI | There are processes in place at both BI and Consob to support the identification of risks to the perimeter of regulation. In addition, they are obliged to review their regulations on a three year cycle. They both actively support MEF in the discussion of EU directives and regulations. |
| Principle 8. The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed. | FI | There are important conflicts of interest in the Italian market that relate to i) the ownership structure of issuers, and ii) banks' role as issuers and distributors of securities. Consob has adopted policy measures to tackle these conflicts of interest, and review of their compliance is part of the supervisory program of Consob. |
| Principle 9. Where the regulatory system makes use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, such SROs should be subject to the oversight of the Regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities. | NA | RMs and MTFs play a limited role in market surveillance and listing of issuers. As a result they have not been considered SROs for the purposes of this principle. |
| Principle 10. The Regulator should have comprehensive inspection, investigation and surveillance powers. | FI | Both BI and Consob have been given broad powers to supervise, and inspect regulated entities, conduct surveillance of authorized securities markets, and conduct investigations in connection with breaches to securities laws. To this end, they both have been given compulsory powers commensurate to their |

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| | | respective mandates. |
| Principle 11. The Regulator should have comprehensive enforcement powers. | BI | Consob has been given broad powers to request information from third parties, including the use of compulsory powers in connection with breaches to securities laws. A wide range of enforcement tools are available to Consob and BI, except that for breaches different from market abuse, short selling and issuers related violations, pecuniary sanctions in the areas of intermediaries and CIS can only be imposed on the natural persons and not on the legal entities –although the latter are jointly and severally liable for their payment– and the level of such sanctions for breaches other than market abuse/short selling violations appears low. |
| Principle 12. The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program. | PI | The supervisory approach of BI and Consob relies heavily on robust off-site monitoring and a more limited use of on-site inspections, although the coverage by market share (measured in terms of assets and clients) is high. The enforcement approach relies more on remedial actions, which while necessary might not be sufficient. Furthermore pecuniary sanctions imposed for offences other than market abuse/short selling violations are low to a large extent due to the limitations in the law and judicial practices. Criminal enforcement faces challenges, including a strong reliance on settlements and conditional execution which can detract from the deterrent effect that criminal enforcement should have. |
| Principle 13. The Regulator should have authority to share both public and non-public information with domestic and foreign counterparts. | FI | Consob and BI are required to cooperate with each other, including by sharing information. Consob is the point of contact for request for information from international regulators. The CL empowers Consob to share information with them, even if it is confidential. |
| Principle 14. Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts. | FI | Several MoUs govern cooperation between Consob and BI. There is also a protocol for coordination in relation to financial stability signed by BI, Consob, IVASS and the MEF, which established the financial stability committee. Consob is signatory of the IOSCO MMoU. |

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| <p>Principle 15. The regulatory system should allow for assistance to be provided to foreign Regulators who need to make inquiries in the discharge of their functions and exercise of their powers.</p> | FI | <p>Consob regularly collects information on behalf of foreign regulators. Under the IOSCO MMoU no request for assistance has been refused.</p> |
| <p>Principle 16. There should be full, accurate and timely disclosure of financial results, risk and other information that is material to investors' decisions.</p> | FI | <p>Issuers of securities subject to public offerings and issuers of securities to be admitted to trading in an RM must submit a prospectus. In addition, issuers with securities traded in an RM are subject to robust on-going and periodic requirements. Issuers whose securities are widely held are subject to ongoing and periodic disclosure obligations, however periodic financial obligations are more limited than for issuers admitted to trading in a RM. Nevertheless currently this category does not appear to be significant in size. Issuers with securities admitted to trading on AIM are subject to on-going obligations and periodic obligations by virtue of their contract with the exchange, which are more flexible than those of the RM. The AIM market caters to SMEs and is currently not significant in size.</p> |
| <p>Principle 17. Holders of securities in a company should be treated in a fair and equitable manner.</p> | FI | <p>Issuers with securities admitted to trading in an RM are subject to, among others, tender offer and related party transactions rules and notification of substantial and insider holdings is required. Issuers whose securities are widely held are subject to many, but not all these obligations (e.g., they are not subject to notification of substantial and insider holdings, although change of control must be notified and insider information disclosed). However, as indicated in Principle 17, this category is currently not significant in size. Issuers admitted to trading on AIM Italia, the only equity MTF, are subject to similar obligations than those of issuers admitted to trading in A RM, although under more flexible rules. AIM caters to SMEs and is currently not significant in size.</p> |
| <p>Principle 18. Accounting standards used by issuers to prepare financial statements should be of a high and internationally acceptable quality.</p> | FI | <p>Issuers with securities admitted to trading in an RM must submit their annual financial statements prepared according to IFRS. Consob monitors compliance via a risk-based approach. Issuers with widely held securities must apply IAS/IFRS. Issuers admitted to</p> |

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| | | trading on AIM can also use local GAAP or US GAAP. AIM is currently not significant in size. |
| Principle 19. Auditors should be subject to adequate levels of oversight. | FI | Auditors of PIEs are subject to oversight by Consob conducted via onsite inspections on a three year cycle. On-site inspections appear robust. Preference has been given to remedial measures, but disciplinary actions have been taken. |
| Principle 20. Auditors should be independent of the issuing entity that they audit. | FI | There are robust rules on independence of auditors of PIEs that apply not only at the audit firm level but also at the level of its network. There are also rotation requirements. |
| Principle 21. Audit standards should be of a high and internationally acceptable quality. | FI | Domestic auditing standards apply. Such standards are of high quality and consistent with ISAs. |
| Principle 22. Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision. | BI | This grade is that given ESMA, as the direct supervisor of CRAs in Europe. All CRAs that provide services in Italy were subject to a thorough registration process, through colleges of European regulators, including Consob. ESMA has conducted on-site inspections of the large CRAs and is in the process of finalizing the implementation of a risk framework to support its supervisory program. Additional resources are necessary for ESMA to carry out its functions effectively. |
| Principle 23. Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them. | FI | There are rules on fair disclosure including disclosure of conflicts of interest that apply to any person who provides recommendations. In addition, regulated entities are subject to organizational requirements to avoid, mitigate and manage conflicts. |
| Principle 24. The regulatory system should set standards for the eligibility, governance, organization and operational conduct of those who wish to market or operate a collective investment scheme. | BI | AMCs are subject to authorization requirements which include capital, fit and proper and organizational requirements. The review of applications is thorough. However the definition of fit and proper is very narrow and the process for its verification relies mainly on self-certification. The supervisory programs at Consob and BI to ensure compliance with such obligations rely heavily on robust off-site arrangements and a more limited use of on-site inspections, though their market coverage (measured by assets and clients) is high. |

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| <p>Principle 25. The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.</p> | FI | <p>Rules on segregation are robust, including the requirements that assets must be placed in custody with a depositary bank, which is required to obtain a separate license from BI. In addition external auditors are required to submit an annual report on compliance by AMCs with segregation obligations. Changes to fund rules must be approved by BI. Significant changes to the fund rules must be notified to investors.</p> |
| <p>Principle 26. Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme.</p> | FI | <p>CIS are required to submit a prospectus. Only the prospectuses of closed-ended funds are subject to pre-approval by Consob, consistently with the EU legislation. However the BI pre-approves the fund rules for every CIS and through its risk-based program Consob reviews on an immediate basis the disclosure documents of CIS where the risks to misleading disclosure are higher (i.e. new or complex products), and on an annual basis a selected but significant number of disclosure documents for other CIS based on risk criteria. CIS are subject also to robust periodic disclosure obligations towards investors.</p> |
| <p>Principle 27. Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme.</p> | FI | <p>BI has developed rules for the valuation of CIS assets, including illiquid assets, which are consistent with IFRS. External auditors must verify valuations done by AMCs in their annual reports.</p> |
| <p>Principle 28. Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight.</p> | FI | <p>AMCs that manage HFs are subject to the same authorization requirements and periodic reporting obligations to the regulators as any other AMC. HFs are part of the regular supervisory program of BI and Consob, and Consob and BI can share confidential information with other regulators in the terms described under Principle 13.</p> |
| <p>Principle 29. Regulation should provide for minimum entry standards for market intermediaries.</p> | BI | <p>IFs are subject to authorization requirements which include capital, fit and proper and organizational requirements. The review of applications is thorough. However, the definition of fit and proper is narrow and the process for its verification limited.</p> |

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| <p>Principle 30. There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.</p> | FI | <p>IFs are subject to minimum and ongoing capital requirements that reflect the risks they undertake. They are subject to periodic reporting of capital (monthly or quarterly depending on their activities) and must submit annual audited financial statements. BI monitors closely prudential requirements.</p> |
| <p>Principle 31. Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters.</p> | BI | <p>IFs are required to put in place robust internal controls and risk management mechanisms. A risk management function, an internal compliance function and an internal audit function must be established. Reports from the three units must be submitted on an annual basis to BI and Consob. IFs are also subject to information disclosure obligations to clients, as well as to suitability obligations in connection with investment advice. Consob's and BI's supervisory programs to ensure compliance with such obligations rely heavily on robust off-site reviews and a more limited use of on-site inspections although their coverage by market share (measured in terms of assets and clients) is high. In the last years Consob has conducted thematic inspections on MiFID implementation by banks.</p> |
| <p>Principle 32. There should be procedures for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.</p> | FI | <p>The legal framework provides the authorities with robust crisis management and resolution tools in connection with banks, IFs and AMCs. In particular special administration is available to deal with troubled firms, and their liquidation can be done on an administrative basis via a compulsory liquidation. An investor compensation scheme is in place.</p> |
| <p>Principle 33. The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.</p> | FI | <p>There are authorization requirements for RMs and MTFs that include financial, fit and proper and operational requirements. The process to review applications by Consob and BI is thorough. RMs and MTFs are also subject to periodic reporting, including an annual audit report on their IT systems.</p> |
| <p>Principle 34. There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of</p> | FI | <p>RMs and MTFs are required to have market surveillance mechanisms in place. Such systems complement BI and Consob's own market surveillance systems. In connection with their respective responsibilities and duties, Consob and BI have developed robust</p> |

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| different market participants. | | supervisory programs to oversee <i>Borsa Italiana</i> , MTS and the operators of MTFs, which include on-site inspections. |
| Principle 35. Regulation should promote transparency of trading. | FI | There is pre and post trade transparency imposed not only in equity markets but also in bond markets (although not required under EU law), and SIs. In addition, securities intermediaries are obliged to report off-market transactions in financial instruments admitted to trading in a RM. The challenges brought by fragmentation in the equity markets appear to be much more limited in the Italian context. There is more fragmentation in the bond markets; however market solutions seem to be in place to consolidate prices. |
| Principle 36. Regulation should be designed to detect and deter manipulation and other unfair trading practices. | FI | Market abuse constitutes both an administrative infraction and a criminal infraction. Italy allows both administrative and criminal actions to proceed at the same time. The level of sanctions is high. Consob has robust systems in place to detect market abuse, and is active in investigating cases. It has imposed sanctions, as well as referred cases to the criminal prosecutors. |
| Principle 37. Regulation should aim to ensure the proper management of large exposures, default risk and market disruption. | FI | CC&G monitors clearing members' exposures on a real time basis and has powers to request members to post additional margins on an intraday basis. Default procedures are transparent. There are reporting obligations in connection with short selling, as well as in connection with failed settlements. |
| Principle 38. Securities settlement systems and central counterparties should be subject to regulatory and supervisory requirements that are designed to ensure that they are fair, effective and efficient and that they reduce systemic risk. | N/A | Not assessed |
| Fully Implemented (FI), Broadly Implemented (BI), Partly Implemented (PI), Not Implemented (NI), Not Applicable (NA) | | |

Table 2. Recommended Action Plan to Improve Implementation of the IOSCO Principles

| Principle | Recommended Action |
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| Principle 1 | <p>A mandatory consultation process with Consob should be established for the review of applications of banks that wish to be authorized to provide investment services.</p> <p>The current framework could benefit from a streamlining of the chosen twin peak structure, aimed at eliminating possible ambiguities or inconsistencies and strengthening the functional approach.</p> <p>Consideration should be given to transferring to Consob the approval of fund rules.</p> |
| Principle 2 | <p>Stronger arrangements for the legal protection of staff should be pursued, such as an arrangement that allows the regulatory authorities to provide financial support for staff defending legal actions throughout the course of the action rather than only after its conclusion.</p> |
| Principle 3 | <p>Although the legal entities to which the authors of the violations belong are jointly and severally liable for payment, the legal framework should be reformed to provide the regulatory authorities with the power to impose pecuniary sanctions on regulated entities as well as individuals in the areas of intermediaries and CIS where this is currently not possible. In addition the level of sanctions for breaches different from market abuse/short selling violations should be increased.</p> <p>The legal framework should be reviewed to provide the authorities with the power to remove individual directors from boards of financial intermediaries in cases where this is currently not possible. The legal framework should be reformed to consolidate the compulsory powers given to Consob by different provisions of the CL into one single provision, applicable to all areas under Consob's mandate.</p> <p>The legal framework should be reformed to transfer residual functions currently vested in the MEF to the regulatory authorities.</p> <p>Allocation of resources should be reviewed in particular the allocation of resources between on-site and off-site functions.</p> |
| Principle 5 | <p>The current regulations and/or terms of employment should be reviewed and strengthened, in particular in connection with transactions in securities, as described in this assessment.</p> |
| Principle 11 | <p>The legal framework should be reformed to provide the regulatory authorities with the power to impose pecuniary sanctions on regulated entities as well as individuals in the areas where this is currently not possible. In addition the level of sanctions for breaches different from market abuse violations should be increased.</p> |

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| Principle 12 | <p>Although altogether the current approach of Consob and BI has delivered an adequate level of supervision, it should be complemented by a more intensive use of on-site inspections. It is acknowledged that BI has developed a new model for short on site visits more suited for smaller intermediaries that is currently being tested. In addition the strategy towards enforcement should be kept under monitoring to ensure a good balance in the use of remedial (corrective) actions and sanctions.</p> <p>Consob should work together with the criminal authorities to identify mechanisms to strengthen criminal enforcement.</p> |
| Principle 16 | The current framework should be reviewed to ensure that issuers of widely held securities are subject to an adequate level of periodic and ongoing disclosure, consistent with the Principles, in particular if this category were to expand. |
| Principle 17 | The current framework should be reviewed to ensure that equity issuers of widely held securities are subject to requirements for the protection of investors that are consistent with the Principles, in particular if this category were to expand. |
| Principle 24 | Regulations from MEF should be amended to include a more comprehensive definition of fit and proper requirements and give the regulatory authorities more comprehensive mechanisms to verify compliance. |
| Principle 29 | Regulations from MEF should be amended to include a more comprehensive definition of fit and proper requirements and give the regulatory authorities more comprehensive mechanisms to verify compliance. |
| Principle 31 | Consob and BI should make more use of on-site inspections. It is acknowledged that BI has developed a new model for short on site visits more suited for smaller intermediaries that is currently being tested. In addition the strategy towards enforcement should be kept under monitoring to ensure a good balance in the use of remedial (corrective) actions and sanctions. |
| Principle 35 | The level of fragmentation in both the equity and bond markets should be kept under monitoring, to assess the potential need for measures to ensure the existence of a consolidated tape. |
| Principle 37 | Prompt implementation of the European Market Infrastructure Regulation (EMIR) should allow for portability of clients margins and positions |

Authorities Response

32. The Italian authorities wish to express their appreciation to the FSAP mission for its assessment of the Italian Security regulatory and supervisory structure. The Authorities welcome the recognition of a high level of compliance with the IOSCO Principles and of a positive track record in the implementation of a robust system of supervision. The authorities also wish to recall that the evaluation has been conducted with the new release of the IOSCO principles, which is more demanding and more oriented towards the quality and outcomes of supervision.

33. The Assessment has provided a number of recommendations for further improvement.

Authorities will duly consider all recommendations and, in particular, will implement those needed to achieve Fully Implemented status for all principles.

| Table 3. Detailed Assessment of Implementation of the IOSCO Principles | |
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| Principles Relating to the Regulator | |
| Principle 1. | The responsibilities of the regulator should be clear and objectively stated. |
| Description | <p>Structure of the securities regulation regime</p> <p>The Consolidated Law on Finance (Legislative Decree 58 of February 24, 1998—henceforth CL) makes two authorities responsible for securities markets regulation and supervision in Italy: the <i>Commissione Nazionale per le Società e la Borsa</i> (Consob) and the <i>Banca d'Italia</i> (BI).</p> <p>Consob's mandate and responsibilities are set out in Consob's foundation law (Law 216/1974) and the CL. BI's mandate and responsibilities are set out in its by-laws (approved by the Decree of the President of the Republic December 12, 2006), the Consolidated Law on Banking (Legislative Decree 385/1993) and the CL.</p> <p>Overall Consob has responsibility for transparency and proper conduct of business by intermediaries (Article 5(3) of the CL); the orderly functioning of regulated markets (Article 73 and 74 of the CL); the protection of investors; and the efficiency and transparency of the market in corporate control and the capital market (Article 91 of the CL). The BI has responsibility for risk limitation, capital adequacy and the sound and prudent management of intermediaries (Article 5(2) of the CL).</p> <p>From an operational perspective Consob and BI share regulatory, supervisory and enforcement competences over financial intermediaries, wholesale markets for government bonds and for the operation of post-trading facilities. Consob has sole responsibility for financial salespersons; regulated markets and MTFs (other than wholesale markets for government securities); issuers; and auditing firms.</p> <p>Supervision of credit rating agencies (CRAs) has been transferred by the European legislation solely to the European Securities and Market Authority (ESMA).</p> <p>The Minister for Economy and Finance (MEF) retains limited competences, in some cases shared with BI and CONSOB:</p> <p>The MEF has the power to issue regulations in certain specific cases.</p> <p>The MEF, after consulting Consob and the BI, regulates and authorizes wholesale markets in government securities and approves their rules; and identifies the minimum operating requirements for wholesale MTFs in government securities.</p> <p>The MEF is the authority responsible for recognizing investor depositor compensation schemes.</p> <p>The MEF has the authority to take certain exceptional measures on securities intermediaries and market operators, including placing them under special administration and compulsory liquidation, and in the case of market operators revoke their authorization in particularly serious cases. In these cases the MEF acts on a proposal of Consob or BI.</p> |

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| | <p>The MEF is the competent authority for the exercise of the extraordinary measures on short selling affecting sovereign bonds and on sovereign credit default swaps (CDS). It exercises these powers acting on a proposal from the BI, after consulting Consob.</p> <p>Discretion to interpret authority</p> <p>The CL contains a number of general principles defining the objectives of the securities regulation regime that guide the exercise by Consob and the BI of their regulatory discretions. For example, Article 5(1) of the CL states that the aims of supervision are:</p> <ul style="list-style-type: none"> • the safeguarding of trust in the financial system; • the protection of investors; • the stability and proper functioning of the financial system; • the competitiveness of the financial system; • compliance with financial provisions. <p>Article 6 of the CL requires BI and Consob to observe the following principles:</p> <ul style="list-style-type: none"> • recognition of the decision-making autonomy of authorized persons; • recognition of proportionality as a criterion to exercise powers; • recognition of the international character of the financial market and safeguarding of the competitive position of Italian industry; • facilitation of innovation and competition. <p>Article 74 of the CL provides that the purpose of supervision of RMs is to ensure the transparency of the market, the orderly conduct of trading and the protection of investors. Further, Article 91 of the CL states that Consob must exercise its powers with respect to issuers having regard to the protection of investors and the efficiency and transparency of the market in corporate control and the capital market.</p> <p>Article 2 of the CL as amended provides that Consob and the BI must exercise the powers conferred on them in harmony with the provisions of the European Union, apply the regulations and decisions of the European Union and act on their recommendations.</p> <p>Article 23 of Law 262/2005 requires resolutions of a general nature made by Consob and the BI to be fully substantiated and that relevant acts must be accompanied by a report on the expected consequences for persons and entities subject to the act, and for the protection of savers and investors.</p> <p>Gaps or overlaps</p> <p>The division of tasks between Consob and BI in the field of securities is laid down in article 6 of the CL according to the following guiding criteria:</p> <p>BI regulates (after consulting with Consob) and controls issues which are directly material under a prudential perspective only (e.g., capital ratios) (see article 5, para. 2, and article 6, para. 1);</p> <p>Consob regulates (after consulting with BI) and controls issues which are directly material under an investor protection perspective only (e.g., rules on conduct of business) (see article 5, para. 3, and article 6 para. 2).</p> |
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| | <p>BI and Consob regulate jointly a number of issues, mentioned in article 6, para. 2-bis of the CL, which are directly material under both a prudential and an investor protection perspective: (a) corporate governance, general requirements on organization remuneration and incentive systems, (b) business continuity, (c) administrative and accounting organization, (d) procedures for the correct provision of investment services, (e) monitoring of the compliance function; (f) company risk management, (g) internal audit, (h) top management responsibilities, (i) complaint handling, (j) personal transactions, (k) outsourcing of essential or important operations, (l) management of conflicts of interest, (m) recordkeeping, and (n) procedures for the receipt or payment of incentives.</p> <p>While regulatory power is jointly granted to BI and Consob, the supervisory powers necessary to ensure the compliance with these rules are allocated by law taking into account which perspective is the most relevant for each issue. According to this principle, for investment services BI is the competent authority for supervising aspects related to (a), (b), (c), (f), (g) and (h), while Consob is the competent authority to supervise aspects related to (d), (e), (i), (j), (l), (m), and (n), and they have joint supervision on (k) (see article 6 para. 2-ter).</p> <p><i>Cooperation and coordination</i></p> <p>Pursuant to article 5 para. 5 of the CL the two authorities are under an obligation to cooperate closely. Cooperation is required even when there is a clear definition of the respective powers.</p> <p>In order to avoid a duplication of the activity of supervisors and with a view of limiting administrative burdens for regulated entities, article 5, para. 5-bis of the CL provides for BI and Consob to enter into an agreement aimed at coordinating their respective functions. The Memorandum of Understanding (MoU), which is in place since 2007, regulates a number of issues, such as information exchange between the two authorities, management of queries as well as the (reciprocal or external) provision of opinions; the MOU also contains safeguards to ensure the proper involvement of both authorities in the supervision of regulated entities. Based on such MoU, the authorities have exchanged information and cooperated through different mechanisms, described below.</p> <p><i>Strategic and Technical Committees</i></p> <p>More general themes, on which a joint analysis is advisable, are discussed by the Technical Committee and, if necessary, submitted to the Strategic Committee, both set up by the MoU.</p> <p><i>Periodical meetings</i></p> <p>The supervisory units of the two authorities meet periodically to exchange information concerning banks providing investment services, investment firms and asset management companies, with specific regard to problems identified by on-site or off-site analyses (basically related to the internal control system) and critical issues highlighted by complaints.</p> <p><i>On-site inspections</i></p> <p>According to the MoU, when performing on-site inspections both authorities are subject to information duties (see point (i) above). For example, in 2011 and 2012, this obligation generated the following interventions.</p> |
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| Type | 2011 | 2012 |
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| Notifications of inspections sent to the Consob | 94* | 104* |
| Notifications of inspections received from the Consob | 7* | 8* |
| Extensions of the scope of the inspection at the request of the Consob | 5 | 3 |
| Joint Inspections | 1 | 2 |
| Excerpts of inspection reports sent to the Consob | 15 | 16 |

* All examinations regarding banks performing investment services, IFs and AMCs, as required by the MOU.

Ad hoc interaction

In case of significant or urgent issues concerning single institutions Consob is informed (via letter and/or meeting), without having to wait for the next periodical meeting. Three recent examples of this kind of interaction were given. In some occasions, mainly referred to IFs and AMCs, BI and CONSOB have also jointly convened directors, members of the board of auditors and managers of intermediaries.

Consistent regulation of like services and products

Italian legislation conforms to the "same business, same rules" principle. Banks authorized by the BI that provide investment services are subject to the same rules for those services as investment firms authorized by Consob, asset management companies (AMCs) that provide individual portfolio management services are subject to the same rules that apply to investment services providers and banks providing the same services. In addition, Consob has regulatory responsibility under Law 262/2005 for both disclosure and conduct of business obligations in relation to insurance products (unit linked products) with investment characteristics.

Arrangements involving other authorities

Article 4(1) of the CL provides that Consob, the BI, the *Istituto per la Vigilanza sulle Assicurazioni* (IVASS) (the insurance regulator) and the *Commissione di Vigilanza sui Fondi Pensione* (COVIP) (the pension schemes authority) must cooperate by exchanging information or otherwise for the purposes of facilitating their respective functions. Law 262/2005 provides that the BI, Consob, IVASS, COVIP and the antitrust authority must cooperate, including by exchanging confidential information, to facilitate the performance of their respective functions (Article 21). These authorities are required to establish ways to coordinate the exercise of their respective duties, including through the signing of protocols or the setting up of coordination committees. They must meet at least once a year (Article 20).

In this regard, the BI and Consob are members of the special Committee for the protection of financial stability (see under Principle 6) and the special Committee for preventing use of the financial system and the economy for the purpose of money laundering and terrorist financing.

Both BI and Consob have entered into MoUs with the finance police; which allow them to use its assistance for their investigations.

Finally BI, Consob and ISVAP (now IVASS) have entered into a MoU (whose contents are shared by the Competition Authority) in connection with the implementation of the

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| | prohibition of interlocking directors in financial institutions. |
| Assessment | Fully implemented |
| Comments | <p>The CL defines the mandate, responsibilities, powers and authority of Consob and the BI in clear terms. From an operational perspective, the specific allocation of responsibilities between the two authorities is complex and requires a significant degree of coordination and cooperation. The evidence provided leads to conclude that such cooperation and coordination is taken place in practice.</p> <p>Vis-a-vis regulated entities there are no important areas outside of the regulation or supervision of one of the two authorities. The assessors recognize that from the perspective of regulated entities there are benefits in a system that seeks to minimize overlap between the two competent authorities, and that the system has created mechanisms to ensure cooperation and coordination. At the same time, if both authorities are to be effective it is critical that they both have the “independent” authority to supervise areas that could have a direct impact on their respective mandates.</p> <p>In this context, a critical question posed to the authorities has been the extent to which article 6–2ter of the CL could be interpreted as to limit Consob’s independent authority to conduct supervisory activities including on-site inspections on ISPs for issues related to the areas under the supervisory responsibility of BI (such as for example corporate governance), or from imposing enforcement actions on ISPs if shortcoming on such areas were found to have affected the capacity of the ISP to fulfill their market and/or conduct obligations, as this would result in a suboptimal outcome of the current structure.</p> <p>The assessors have been told that such provision needs to be interpreted along with article 5 of the CL, which sets out the mandate of the two authorities. This means that Consob does have independent authority to conduct inspections on issues related to the areas under the supervision of BI, as long as they have an impact on market or conduct obligations which are under Consob’s mandate, and that Consob would have the authority to impose enforcement actions derived from such inspections. The review of Consob’s inspections files in connection with the implementation of MiFID showed that in practice Consob inspections have indeed covered these issues. The current framework could benefit from a streamlining of the chosen twin peak structure, aimed at eliminating possible ambiguities or inconsistencies and strengthening the functional approach.</p> <p>There is one area where the current approach of the legislation has the potential to result in a suboptimal outcome, which relates to the consultation process in connection with the licensing function. Under the current framework Consob is required to consult with the BI in the authorization of non-bank IFs, and the BI is required to consult with Consob in the authorization of AMCs. But the BI is not obliged to consult Consob on the authorization of banks that want to provide investment services, except where they involve the operation of an MTF. The assessors acknowledge that Consob and the BI are under a general obligation to cooperate and coordinate with one another and that the BI’s regulation establishing the information that banks must submit along with their application was issued in consultation with Consob. However the absence of a formal requirement for BI to consult with Consob when it assesses such applications means that Consob’s expertise in conduct of business issues is not applied in a more direct manner into the authorization process. Thus the assessors encourage the authorities to</p> |

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| | <p>implement a consultation process also in connection with banks.</p> <p>Finally, the assessors encourage the authorities to review the current allocation of responsibilities in connection with the approval of fund rules. The fund rules frame the relationship between investors and the fund manager, in particular in connection with investment objectives, policies and limits. Given that investors bear the risk of such investment, the prevailing objective of the review of fund rules is to ensure that the rules are clear—and in line with the regulations established for CIS—and that adequate disclosure is made to investors. From that perspective it seems sensible that the approval of fund rules be under Consob, rather than under BI, while the need for a prudential framework for CIS, as appropriate, can be dealt with via regulations.</p> |
| Principle 2. | The regulator should be operationally independent and accountable in the exercise of its functions and powers. |
| Description | <p>Independence</p> <p>Consob is an independent agency established as a legal person under public law, and can make decisions on areas within its competence as an autonomous body.</p> <p>BI is a public law entity with private and public shareholders. The ownership structure of the BI reflects its past history and the evolution of the Italian banking regulation. It was established, under the 1893 Banking Law, as a private company as a result of the merger of three institutions. Afterwards, the 1936 Banking Law explicitly declared the public nature of the BI, defining it "a public law institution". Shareholdings were expropriated and equity was reserved to financial institutions of public relevance (banks, insurance firms and social security institutions). Since then, a high number of mergers and acquisitions within the Italian banking system has led to the current distribution of shares. Its capital (amounting to EUR 156,000 and divided into 300,000 registered shares with a par value of EUR 0.52 each) is held by 54 privately-owned banks, 5 insurance firms, the National Social Security Agency and the Italian Workers' Compensation Authority. The Statute establishes that the distribution of shares among the shareholders must be balanced and the power exercised in voting cannot exceed certain limits: the votes any shareholder may cast in a shareholders' meeting are limited to a maximum of 50 (out of a total, as of 8.2.2013, of 535), regardless of the minimum of shares held, in order to prevent individual shareholders from exercising a preponderant influence (article 9(3)). The scope of issues under the decision/intervention of shareholders is rather limited. They approve the annual accounts; the allocations of profits, the distributions of the income earned on the reserves, and appoint the members of the Board of Directors.</p> <p>The Board of Directors is charged with the general administration, management, supervision and internal control of the Bank, but is explicitly excluded by article 5(1) of Legislative Decree 691/1947 from all tasks relating to banking and financial supervision. Besides deciding on the dividends to be paid by shareholders, the Board approves the budget, internal regulations, and determines the staffing levels.</p> <p>The Director is the governing body of the BI. Art 19 (4) of Law no. 262/2005 establishes that the BI has autonomy to take supervisory actions or decisions. The law explicitly states the principle of independence from "public or private-sector entities".</p> <p><i>Governance</i></p> <p>Consob's Commission is a collective body comprising the chairman and members. Decisions are taken by a majority of the members in attendance.</p> |

The Commission currently consists of a Chairman and three Members, all of whom hold office for seven years; they may not stand for re-election. Recent legislation has reduced the number of Commission members to three, including the Chairman. This will be achieved as current members reach the end of their term of office.

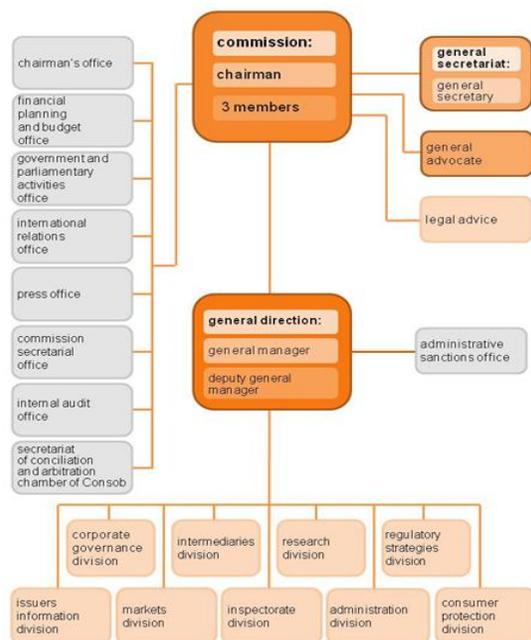
All Commission members are appointed by a Decree of the President of the Republic acting on a proposal submitted by the Prime Minister and approved by the Council of Ministers. The special Parliamentary Commissions of the House of Representatives and of the Senate of the Republic are required to issue an opinion on the proposed nominees but their opinion is not legally binding on the Government.

The criteria for the selection of the nominees are established by law 216/1974. The Chairman and the members of the Commission must be chosen from among persons with specific expertise and experience and of unquestionable integrity and independence. The law also requires that the members of the governing body cease any previous private or public activity to work exclusively for Consob. Commissioners are obliged to resign if the requisites for their appointment cease to be fulfilled.

The removal of the Commission is possible, according to the law, only for proven non-functioning or for inactivity. The procedure to be followed is also established by law. The Prime Minister, after hearing the MEF, communicates the proposal, and the reasons justifying it, to Parliament. The dissolution of the Commission can be declared by Decree of the President of the Republic following a decision by the Council of Ministers. This Decree must appoint an administrator to continue the activity of the Commission. Within 45 days, a new Commission must be appointed, following the procedure described above (including the opinion of the Parliamentary Commissions). There is no mechanism for the removal of individual members of the Commission.

The rules on incompatibility, declaration of interests, and like matters for the Chairman and Commissioners are set out in legislation (mainly Law 216/1974 and Law 14/1978) and are specified in Consob's internal organization regulations.

Consob's organization structure is as follows:



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| | <p>For the BI, the organ responsible for its supervisory functions is the Directorate or Governing Board (Article 19 of Law 262/ 2005), which is an organ different from the board of directors of the BI. It is a collegial body made up of the Governor, the Director General, and three Deputy Directors General and is authorized to adopt measures regarding the exercise of the public functions given to the BI by legislation.</p> <p>The appointment of the Governor, his/her reappointment and his/her removal from office must be enacted by means of a decree issued by the President of the Republic, acting on a proposal from the President of the Council of Ministers, following the adoption of a resolution by the Council of Ministers, after hearing the opinion of the BI's Board of Directors. The Governor proposes the appointment of the other members of the Directorate to the Board of Directors. The appointment, reappointment and removal must also be approved by a decree of the President of the Republic acting on a proposal from the President of the Council of Ministers in agreement with the Minister for the Economy and Finance after consulting the Council of Ministers.</p> <p>Pursuant to article 24 of the Statute of the BI the Governor's term of office is six years; and it may be renewed only once. Same rules apply to the other members of the Directorate.</p> <p>According to the statute of the BI (article17.3) the reasons for removal of the Governor or other members of the Directorate are those provided for by Article 14(2) of the statute of the ESCB, i.e. only if they no longer fulfil the conditions required for the performance of their duties or if they have been guilty of serious misconduct. According to the principles of Italian public law, the formal decision by the President of the Republic, which is published as described above, must acknowledge the reasons for removal. No member of the Directorate has been removed under this framework, so far. In the last five years, three members of the Directorate, including a governor, resigned before their term, in all cases to assume presidency positions in Italian or European public entities.</p> <p>At Directorate meetings, resolutions are passed by a majority of those present; where the numbers of votes on a decision are equal, the Governor has the casting vote. Minutes are kept of meetings.</p> <p>Supervision of the securities market functions of banks and banking groups is carried out by the Banking Group Supervision Department. IFs, AMCs and the funds they administer are supervised by special units within the Specialized Intermediaries Supervision Department. A separate Supervision Inspectorate is responsible for on-site inspections of all supervised entities, including securities market intermediaries. Authorizations, including of AMCs, is the responsibility of the External Relations and General Affairs Department.</p> <p><i>Areas where the Government retains responsibilities</i></p> <p>There is no consultation to the MEF on day to day decisions taken by BI or Consob. However, there are a few areas where the Government, mainly through the MEF, retains responsibilities.</p> <p>Regulations</p> <p>There are a few cases in the CL where regulations must emanate from the MEF. One important case is the fit and proper requirements for board members of ISPs. In two cases, the regulations must emanate from the Ministry of Justice (MoJ) in concert with the MEF and with consultation with the financial supervisors.</p> |
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| | <p>Powers of intervention of the MEF</p> <p>(a) Financial Intermediaries</p> <p>The MEF acting on proposal of Consob or of the BI is empowered to issue measures with respect to intermediaries in crisis situations. In particular:</p> <p>Special administration (Article 56 of Consolidated Law)</p> <p>The MEF, acting on a proposal of Consob or the BI within the scope of their respective authority, may issue a decree dissolving the administrative and control bodies of an Italian IF, AMC or <i>Società di investimento a capitale variabile</i> (SICAV) where certain circumstances occur (serious violations, serious capital losses, etc.).</p> <p>Withdrawal of the authorization and compulsory administrative liquidation (Article 57 of Consolidated Law)</p> <p>The MEF, acting on a proposal of Consob or the BI within the scope of their respective authority, may issue a decree withdrawing the authorization to carry on business and ordering the compulsory administrative liquidation of an Italian IF, AMC or SICAV where the administrative irregularities or the violations of laws, regulations or bylaws or the capital losses are exceptionally serious.</p> <p>(b) Compensation schemes</p> <p>The MEF is entitled to recognize, after consulting Consob and the BI, compensation schemes for the protection of investors. Only systems recognized by the Minister can operate (Article 59 Consolidated Law).</p> <p>(c) Regulated Markets</p> <p>Wholesale markets in government securities</p> <p>The MEF, after consulting Consob and the BI, regulates and authorizes wholesale markets in government securities; approves their rules (Article 66(1) Consolidated Law); and identifies the minimum operating requirements for wholesale MTFs in government securities (Article 77-bis(6)).</p> <p>Extraordinary measures—Market management companies</p> <p>In the event of serious irregularities in the management of markets or in the administration of market management companies and wherever it is necessary for the protection of investors, the MEF, acting on a proposal made by Consob, can dissolve the administrative and internal control bodies of the management companies. In case of exceptionally serious irregularities, the MEF, acting on a proposal made by Consob, can revoke the authorization. The proposal is made by Consob in agreement with the BI where the company is a management company of markets for the wholesale trading of private and public sector bonds other than government securities and markets for the trading of money market instruments and financial derivatives based on government securities, interest rates and foreign currencies (Article 75 Consolidated Law). Pursuant to Article 76 (3) of the CL, for wholesale markets in government securities Article 75 applies with the BI having Consob's powers and duties.</p> <p>Crises of Central Depositories</p> <p>If serious irregularities are ascertained, the MEF, acting on a proposal from Consob or the BI, may order the dissolution of the administrative bodies of central depositories or their compulsory liquidation (see Article 83 of the Consolidated law).</p> |
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| | <p>(d) Extraordinary measures on short selling affecting sovereign bonds and on sovereign credit default swaps (CDS)</p> <p>The MEF is the competent authority for the powers of intervention in exceptional circumstances and of temporary suspension of restrictions with regard to sovereign debt and sovereign CDSs. It exercises these powers acting on a proposal from the BI, after consulting Consob, pursuant to Article 4-ter, para. 4 of the Consolidated Law establishing the competences for the implementation of European Union (EU) regulation no. 236/2012.</p> <p>The authorities point out that, where a regulatory or supervisory action by the Minister requires a proposal from the BI or Consob, no measure proposed by the regulator has been rejected by MEF. It is accepted that the Minister can accept or reject the proposal, but not make any other decision.</p> <p><i>Funding</i></p> <p>Consob manages its expenditure autonomously on the basis of an annual budget approved by the Commission. Its annual accounts must be approved by 30 April of each year and are audited by the Court of Accounts (<i>Corte dei Conti</i>) which audits the accounts of the State and of all entities belonging to the public sector.</p> <p>Since 1995 (Article 40 of Law 724/1994) Consob has been funded partly through a specific allocation from the central government budget and partly through fees collected directly from markets and market participants for the activities performed. By July 31 of each year, Consob informs the MEF of its funding needs and forecast revenues for the following year. On the basis of this information the MEF sets the annual allocation from the State budget. Over the years the amount of revenues from the State budget has decreased consistently. In 2011, it was equal to 0.3 percent of the total income; in 2012, following the entering into force of new provisions of law concerning the rationalization of State expenditure, it was reset to zero. In 2012 Consob did not receive any contribution from the Government. Overall Consob's budget has increased over the years.</p> <p>Consob fixes the types and amounts of fees in resolutions rendered effective by a decree signed by the Prime Minister after checking their legality and consulting the MEF.</p> <p>Changes to Consob's budget are subject to a special internal procedure and are published in the same way as the original budget.</p> <p>BI is autonomous in setting its yearly budget for operating expenses. The yearly budget is approved by the Directorate and endorsed by the board of directors. It is not subject to external controls made by the government or by the Italian Court of Accountants. The operating expenses are mainly financed by the income derived from BI's own assets as well from the income coming from net financial assets not related to monetary policy. As further described in principle 3 resources allocated to supervision have increased overtime.</p> <p><i>Legal protection</i></p> <p>Under Italian constitutional principles, any person is entitled to seek a judicial decision to protect their rights and legitimate interests including against public entities or the State. Under the Italian Constitution (Article 28) civil servants cannot invoke exemption from liability where they commit acts in violation of rights. This is clarified in the Civil Code (Article 2043), which provides that an act which causes unjust harm to someone</p> |
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| | <p>must be either deliberate or culpably negligent.</p> <p>Conditions for the implementation of this principle are set out in the Decree of the President of the Republic 3/1957 which regulates civil servants. Pursuant to this law, civil servants are liable only in cases of serious or gross negligence, fraud, deceit or willful wrong. So in practice for regulatory authorities and their staff to be liable the Italian courts require either bad faith or culpable negligence. (See also Article 24 (6bis) of Law 262/2005, which expressly provides that Consob and the BI, the members of their internal boards and their employees are liable only for damages caused by fraudulent or willful acts or gross negligence). In practice there have been a few actions against BI staff.</p> <p>Judicial authorities are ultimately responsible for sanctioning misbehavior and provide for compensation of damages suffered by persons injured by the actions of Consob and BI's staff.</p> <p>Consob has adopted an internal resolution to provide for reimbursement of legal expenses paid by staff (including former staff) sued by third parties in connection with the performance of their duties. However, legal expenses can only be reimbursed after a final verdict exonerating a staff member from liability. This means that the staff member must personally bear the costs of defending an action until such a verdict is reached.</p> <p>For the BI, the same provisions as to the liability of members of the Directorate and BI staff apply as for Consob, as do the provisions relating to the reimbursement of staff expenses in defending legal actions. Staff highlighted that BI is developing a proposal to provide financial support to staff members during the course of an action rather than only after its conclusion.</p> <p>Accountability</p> <p>Article 1 (13) of Law 216/1974 requires Consob to submit a report at least once a year to the MEF who, in turn, is required to present it (with comments if any) to the Parliament. The annual report must explain the activities performed by Consob and indicate the policy lines for the following year.</p> <p>Once a year, the Chairman of Consob presents the activity of the Commission to market participants in an official ceremony. The document submitted on that occasion summarizes the activities carried out and highlights the policy for the following year.</p> <p>The Chairman of Consob is required (see Article 1, (12) of Law 216/74) to keep the MEF informed about major developments on the markets and the operation of the Commission. MEF staff indicated that these types of communications are conducted via formal letters where Consob outlines major issues occurring in the market. They indicated that on average Consob sends six to eight letters a year—although during the current crisis letters have been sent more frequently. The type of events on which Consob must inform the MEF is understood to be major events, in particular potential threats to stability which can require action by the Government (for example, legislative changes).</p> <p>The Minister is entitled to communicate his views to the Commission, informing Parliament at the same time about these initiatives and their content. The Minister can comment at any time to Parliament about the activities of Consob.</p> <p>The Minister can also ask Consob for confidential information, provided the information is needed in order to perform his statutory functions. This provision does not give the Minister access to the information obtained through international cooperation (see</p> |
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| | <p>Article 4(4) of the Consolidated Law).</p> <p>Regulations issued by Consob are sent to the MEF for information except in specific cases when enactment by Decree of the MEF is required.</p> <p>Parliament and Parliamentary Commissions are entitled to call the Chairman of Consob or the other Commissioners for special hearings. However, Parliament is not entitled to ask for confidential information or to judge the operation of Consob. Only special Parliamentary Committees created by law and acting as judicial authorities can ask for the disclosure of confidential information. These Committees, as judicial authorities, are subject to compliance with the rules concerning judicial secrecy.</p> <p>Only judicial authorities are entitled formally to review Consob's activity. Government and the Parliament may express a political opinion but it has no legal impact.</p> <p>The BI publishes an annual report on its supervisory activity (Article 4(4) of the Consolidated Law on Banking). Article 8 of the Consolidated Law on Banking also provides for the publication of a bulletin by the BI, containing general measures it has issued and other significant measures concerning persons subject to supervision.</p> <p>Pursuant to Article 19(4) of Law 262 of 2005, the BI submits an annual report every year to Government and Parliament describing the activities carried on during the previous year.</p> <p>At the BI General Shareholders' Meeting, the Governor presents the Annual Report, which contains a section on the supervisory activity performed by the BI during the previous year and sets out the criteria and methods followed. This section of the Report fulfills the BI's obligation to publish an annual report on its supervision of banks and other intermediaries pursuant to Article 4 of the Consolidated Law on Banking. A similar section of the Annual Report is devoted to the description of supervisory activities on market infrastructures. The Annual Report submitted to the General Shareholders' Meeting is publicly available on the BI's website as is the Financial Stability Report which is issued twice a year.</p> <p>Parliament and Parliamentary Commissions are entitled to call the Governor or the senior management of the Bank for special hearings. The BI publicly reports on questions within the scope of its authority in parliamentary hearings and on other occasions.</p> <p>Procedural safeguards</p> <p>By Law 241/1990 and Article 24 of Law 262/2005, all decisions by Consob and BI must state the legal grounds for decisions and the reasons they were adopted. Article 23 of Law 262/2005 requires Consob and BI resolutions that have a general or regulatory character (other than those relating to internal administration) to be subject to public consultation, be duly motivated, and be accompanied by an illustrative report. Consob publishes and makes available on its website a monthly bulletin setting out the resolutions it has adopted. Article 4(3) of the Consolidated Law on Banking requires the BI to provide reasons for its decisions.</p> <p>Article 4(2) of the Consolidated Law on Banking requires the BI to give prior public notice of the principles and methods it uses for its supervisory activities, and to publish an annual report on its supervisory activity. Article 8(1) provides for the BI to publish a bulletin setting out the general measures it adopts and other significant measures about persons subject to its supervision.</p> |
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| | <p>Consob's accounts are audited by the Court of Accounts, an independent court of law. As a consequence of its participation in the European Central Bank (Article 27 of the ESCB Statute), BI's annual accounts must be audited by an external firm and an internal board of auditors oversees its internal administration and compliance with the law and the ESCB Statute.</p> <p>Decisions taken by Consob and the BI are subject to judicial review, normally by the Administrative Courts. Decisions relating to sanctions are reviewed by the ordinary courts rather than the Administrative Courts.</p> <p>Confidentiality</p> <p>The confidentiality of information supplied to the regulatory authorities is provided for in the relevant legislation.</p> <p>As a general principle all non-public information and data gathered by Consob while discharging its functions is protected by official secrecy, including with respect to other government authorities, except the MEF (Article 4(10) of the Consolidated Law). Information obtained from foreign regulators is specifically protected by Article 4(4), which provides that information received pursuant to international cooperation cannot be transmitted to any other Italian authority, including the MEF or a third party without the consent of the authority supplying it. Information included in the reports delivered by Consob to the Government or to Parliament must contain only data in aggregate form. The MEF is entitled to ask for confidential information from Consob only for the purpose of performing his/her functions under the law. With regard to Parliament, only special Committees created by an <i>ad hoc</i> law and acting as judicial authorities are entitled to obtain confidential information.</p> <p>Similar provisions apply to the BI pursuant to Article 7 of the Consolidated Law on Banking and Article 4 (4) of the Consolidated Law. The MEF is entitled to ask for confidential information from the BI only when the Minister acts as Chairman of the Interministerial Committee for Credit and Savings, <i>Comitato Interministeriale per il Credito e il Risparmio</i>, (CICR) (Article 7 of the Consolidated Law on Banking). By express legislative provision, such information must be strictly related to the tasks performed by the CICR, which is mandated to establish rules and adopt decisions of a general nature; on matters specified by the Consolidated Law on Banking, acting on proposals from the BI.</p> |
| Assessment | Broadly implemented |
| Comments | <p>In general, the legal framework provides both the BI and Consob with sufficient independence and the assessors did not find evidence of interference. As Consob staff highlighted the lack of provisions for the removal of individual Commissioners does not raise concerns related to independence; however from a governance perspective it is important that such provisions be in place, and that—in line with those established for the directors of BI—they require the existence of due cause for removal.</p> <p>The one area of concern is the degree of protection available in practice to the staff of both authorities where they are subject to legal action challenging decisions or actions taken in connection with the performance of their duties –especially considering that there have been a few actions against BI staff. The legal framework limits the liability of a staff member to cases involving bad faith or gross negligence and provides for reimbursement of legal expenses paid by a staff member after a final verdict exonerating him from liability. But in practice a staff member is required to bear his or her own legal costs in defending an action until finally exonerated. A suit may go</p> |

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| | <p>through a number of stages (for example including a number of appeals) and take considerable time to reach finality.</p> <p>It is undesirable that staff should be exposed to the risk of having to bear costs in this way. It may have a chilling effect on them in making necessary decisions, and be a disincentive to their taking robust action, especially in difficult or complex situations. The assessors stress that the concern is about potential and they are not aware of any decisions or actions by Consob or the BI that have been affected in this way. They also understand that the BI has recently implemented a proposal to provide financial support to staff members during the course of an action rather than only after its conclusion. Such a development would be welcome and should be followed by Consob.</p> |
| Principle 3. | The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers. |
| Description | <p>Power and authorities</p> <p>Consob and the BI have power to make binding rules in the form of regulations on matters specified in legislation. In practice the legislation typically expresses the power to issue regulations in broad terms and the only practical limitation is that Consob and the BI cannot make regulations on matters reserved for the MEF or other Ministers. There is therefore ample scope for each authority to make regulations to deal with emerging problems. The areas in which regulation making is reserved for the MEF are described under Principle 2.</p> <p>Consob and the BI have licensing, supervisory, and enforcement powers over regulated entities. Both for purposes of day to day supervision as well as to investigate breaches by them to their obligations, Consob and BI can request information from them as well as from entities and individuals associated with them, as described in Principles 10 and 11. Certain limitations and differences in powers must be noted, in particular:</p> <p>Except in connection with market abuse and short selling, BI and Consob can only impose pecuniary sanctions on the individuals (board members, top management, employees) involved in breaches to the provisions of the CL relating to market intermediaries and CIS, but not to the legal entities, although the legal entities are jointly and severally liable for payment, and level of the pecuniary sanctions that can be imposed for breaches other than market abuse violations/short selling is low.</p> <p>Neither BI nor Consob have the power to remove individual directors from boards of financial intermediaries except if the board member ceases to meet the criteria established in MEF regulations—which are narrowly defined—or is subject to a pecuniary penalty for market abuse and public offering violations that attracts automatic disqualification. They do have the power to replace the whole board in the event of serious administrative irregularities or serious violations of the legislative regime.</p> <p>BI has more limited compulsory powers than Consob. Consob can use all its compulsory powers in connection with authorized persons, short selling, supervision of markets and market operators, market abuse, takeovers and issuers, while BI can only require data and information, carry out inspections, hold hearings and take testimony, but does not have the other powers afforded to Consob by article 187 octies of the CL (although it can perform them through the Finance Police); except in connection with short selling, pursuant to articles 4 ter and 8 of the CL.</p> <p>As indicated in principle 2, in a few limited cases “recognition” authority has been bestowed in the MEF, in particular in connection with the wholesale government</p> |

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| | <p>markets and investor depositor schemes. Finally the power to impose certain extraordinary measures also corresponds to the MEF, at the request of BI or Consob.</p> <p>In connection with issuers' Consob has broad powers in connection with the authorization of public offerings, as well as for purposes of monitoring compliance by issuers with their periodic and ongoing obligations established in the CL. In addition, it can exercise its compulsory powers over issuers admitted to trading in a RM and third parties pursuant to articles 114, 115 and 187-octies of the CL.</p> <p>In connection with market abuse and short selling, Consob has been given broader investigative and enforcement powers. In this case its compulsory powers can be exercised over third parties (non regulated entities). In addition the pecuniary sanctions in connection with market abuse, short selling and issuers related violations can be applied to both the natural persons and legal persons, and the level of the sanctions is significantly higher.</p> <p>Funding and resources</p> <p>Both Consob and the BI appear to have adequate resources to carry out their securities regulatory functions.</p> <p>As described under Principle 2, Consob has effective budget autonomy and is dependent only to a very small extent on an allocation from the Government budget, with most of its funding deriving from fees levied on regulated entities. It is free to allocate operational resources as it sees fit.</p> <p>Consob's budget for 2012 was EUR 126 million. Supervision fees amounted to EUR 106 million. The largest share of annual supervision fees came from fees paid by issuers, intermediaries and auditing firms. The remaining EUR 20 million came from Consob's interest earnings and previous years' surpluses. As indicated under Principle 2 government supplementation of Consob budget has declined progressively and in 2012, following the entering into force of new provisions of law concerning the rationalization of State expenditure was reset to zero.</p> <p>Also as noted under Principle 2, the BI is wholly independent of government in relation to both revenues and the budget process. Except for asset management activities, the BI budget is not broken down between its banking supervision functions and its supervision of other areas such as supervision of securities intermediaries or wholesale market.</p> <p>Staff resources</p> <p>At December 2012, Consob had 627 staff members. An upper limit on the number of staff it can employ is set in its foundation legislation (Law 216/1974). The limit was amended by Law 262/2005 and is currently 750.</p> <p>Remuneration of Consob staff is pegged to that of BI staff and is substantially higher than that of public sector employees generally. There is uncertainty however on whether certain measures adopted for government employees apply also to Consob, in particular a cap on salaries (EUR 300,000). There are actions pending against such interpretation. Staff highlighted that this salary scale has allowed Consob to hire and retain skilled personnel. Turnover is low, although from the data provided it appears higher than for BI (for example in 2011 nine staff left the institution). About half of Consob's supervisory staff have legal training, with the other half having qualifications in economics and finance.</p> |
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| | <p>Training programs for Consob staff focus mainly on technical and vocational courses, with training directed to tasks that employees actually perform.</p> <p>As for BI at September 9, 2012, there were 1,168 resources employed in supervision activities (705 in the Head Office and 463 in the Branches; professionals were 542 and 313 respectively). Since 2008, resources employed in the Banking and Financial Supervision Area have increased by 190 units, mainly professionals, even though the overall staff has been steadily decreasing (from 7,400 at the end of 2007 to 6,990 at the end of 2011). Heads of department and units stated that staffing levels are currently adequate, although intensively used.</p> <p>Staff highlighted that BI has had no difficulties attracting skilled professionals. BI also promotes training and secondment with international institutions. Turn-over rate is low, about 8 percent. In the last 5 years, 18 people resigned to take positions in the private sector.</p> <p>Internal governance arrangements</p> <p>Almost all Consob's supervisory decisions, including decisions about sanctions, are taken by the Commission, on a proposal from the relevant supervision area. The Commission met 103 times in 2012 and adopted 377 formal resolutions. There are extensive internal coordination arrangements to ensure input from relevant areas on supervisory and enforcement issues.</p> <p>Consob issues non-public internal staff policies on the performance of specific activities. These include manuals on procedures for on-site inspections, detecting market abuse, the sanctioning process, calculating the amount of pecuniary penalties and a procedure for handling investor complaints.</p> <p>Consob Commissioners and staff are subject to a Code of Ethics, as further explained in Principle 5.</p> <p>In the BI, decisions about financial regulation and supervision are taken by the governing board (the Directorate). The Directorate usually meets weekly. Staff proposals may be accepted, rejected, modified or sent back to staff for reconsideration. Prior the formal decision, the Directorate usually hears the Managing Director responsible for Supervision and the General Counsel (Head of the Legal Research and Services Area).</p> <p>A code of conduct for members of the Directorate was introduced in May 2006. It relates to the standards for conduct of personal affairs, conflicts of interest, disclosure of conflicts of interest and the definition of circumstances that require any member of Directorate to abstain from voting. There is also a code of ethics for BI staff, as further discussed in Principle 5.</p> <p>Investor Education</p> <p>Consob's strategic objectives include investor education and a special section of its website is devoted to the topic. It includes "Dos and Don'ts" for investors and education initiatives, as well as a warnings section notifying investors about unauthorized activities and fraudulent investment services. A system on the website assists investors to assess complex products. Consob publishes investor pamphlets (for example on investment funds). The website also includes a list of persons authorized to provide investment services. Consob also has a unit devoted to relations with the public and a telephone help desk.</p> |
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| | <p>In 2010, Consob signed a protocol of understanding with the BI, COVIP, ISVAP (now IVASS) and the Competition and Market Ombudsperson to promote and create joint initiatives on the investor protection, to strengthen the existing reciprocal cooperation tools and to coordinate future activities.</p> <p>The BI has a financial education unit responsible for promoting and coordinating initiatives directed to financial education. It also plays a significant role in promoting financial literacy in line with the OECD framework on financial education. Its website contains a section devoted to financial education. The BI has an MoU with the Ministry of Education dealing with financial education in school curricula and has been active in disseminating basic financial information at all school levels.</p> |
| Assessment | Broadly implemented |
| Comments | <p>There are a few areas where the powers of the regulatory authorities need to be strengthened. Therefore the broadly implemented grade. Such limitations are described below.</p> <p>Neither BI nor Consob can remove individual members from board of financial intermediaries, except in the narrow circumstances described above. The assessors acknowledge that the two authorities have the power to remove the whole board. Also, in practice the two authorities have used their convening powers to request changes in board composition, and in the majority of the cases those requests have been complied with. However, in some circumstances the appropriate regulatory response to the conduct of an individual director is to ensure that director no longer plays a role in the management of an investment firm or AMC, and the regulators need the power to bring about this result. Neither BI nor Consob can impose pecuniary sanctions on legal persons for infractions established in the CL other than market abuse (see for example Article 190). In the assessors' view, the power to impose sanctions on regulated entities (as well as individuals) is a valuable tool to ensure compliance at the entity level as well as the individual one. It can be used to send clear signals to the entity that it is responsible for the conduct of its officers and employees, and is a necessary adjunct to the regulator's power to require remedial action for deficiencies in compliance. The assessors acknowledge that, by article 195 of the CL, employing entities are jointly and severally liable for the payment of sanctions imposed on their employees and agents. But in their view this is conceptually different from the power to impose sanctions on an entity as well as an individual, and this distinction is important especially for setting of penalty amounts and their potential deterrent effect.</p> <p>Finally, the assessors note the differentiated approach of the CL to compulsory powers.</p> <p>The assessors discussed with BI staff whether the lack of broad compulsory powers of BI other than in connection with short selling could hinder BI's ability to carry out its mandate. BI staff highlighted that in light of its prudential mandate such powers are not necessary. In addition, they highlighted the possibility that BI has to request the assistance of the finance police in its investigations. Finally they also highlighted that the unauthorized provision of banking services is a criminal offense and therefore in such case the judicial authorities can act. The assessors were satisfied with this explanation.</p> <p>The situation is different with Consob which as indicated above has been given broader compulsory powers, including towards non regulated entities. However, in its case such powers derive from several different provisions scattered throughout the CL. The question in this case, is the extent to which this patchwork approach has left any</p> |

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| | <p>significant gap vis-à-vis Consob's mandate. Consob staff considered that current provisions have been sufficient. Furthermore similar to BI, they also highlighted the possibility that they have to request the assistance of the finance police. The review of enforcement files seems to validate this opinion. However, the assessors encourage the authorities to strengthen the CL by consolidating in one single provision the compulsory powers of Consob, which should be available for all aspects of its mandate.</p> <p>As included in the description, the assessors noted that the recognition of certain entities and the imposition of certain extraordinary measures are in the hands of the MEF. However, in the current context these issues do not raise major concerns for the reasons discussed below. In the first case, the recognition requires consultation with the regulatory authorities, which have indicated that the MEF has not deviated from the technical opinion given by them. In the latter case, Consob and BI themselves can take a series of injunctive and remedial measures in protection of investors. In addition, extraordinary measures must be taken upon request of BI or Consob. Furthermore, the authorities stated that there has not been any case where the MEF has deviated from the technical opinion of Consob and BI. However, the assessors recommend that these powers be assigned to the regulatory authorities.</p> <p>Consob and BI appear to have adequate resources, and their staff are professional and skilled. However, it might be worth analyzing whether the most effective allocation of resources has been achieved. In this regard, in particular the assessors' note the potential that limits on resources in the specialist on-site units may have on the organizations' capacity to conduct on-site inspections. For example, Consob has more limited resources in its on-site inspectorate than it has in other supervisory divisions. This issue has not been taken into consideration for the grade.</p> |
| Principle 4. | The regulator should adopt clear and consistent regulatory processes. |
| Description | <p>Clear and equitable procedures</p> <p>Consob and the BI are both subject to the general principles for public administration (such as impartiality) established by Article 97 of the Italian Constitution and by Law 241/1990 (transparency, efficiency and effectiveness). These provisions require staff to act impartially and to be transparent, efficient and effective in carrying out their roles.</p> <p><i>Procedures rules and regulations</i></p> <p>Consob is required by law to adopt internal rules for its activities, including rulemaking, hearings, on-site inspections and enforcement. Consob Regulation 8674/1994 as amended governs its overall organization and functions and is published in Consob's official journal and on its website. Its Codes of Ethics (Resolution 17444 of 4 August 2010 for Commissioners and Resolution 17832 of 22 June 2011 for staff) set standards for the independence, impartiality and confidentiality required of Commissioners and staff.</p> <p>The supervisory activities of BI staff are governed by a comprehensive Supervisory Guide, which is available in the website.</p> <p><i>Consultation and transparency</i></p> <p>As noted under Principle 2, both Consob and the BI are obliged to consult publicly on measures of general application. In addition, article 23 of Law 262/2005 obliges both Consob and the BI to carry out a cost benefit analysis of any regulations they issue. Consob and the BI have specialist units for this purpose.</p> <p>Consob includes in its website the consultation document, responses received, the</p> |

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| | <p>impact statement and feedback statements at the close of public consultations.</p> <p>In addition Consob explains its activities in a weekly newsletter that summarizes main activities and decisions taken during the week. It issues guidance or instructions on interpretation and publishes recommendations and responses to specific questions of general application on its website and its official journal (<i>Bollettino Consob</i>). Consob also organizes consultations on documents and proposed standards issued by ESMA.</p> <p>All Consob regulations and rules are published in Consob's Official Journal and on its website. Regulations are also published in the Official Journal (<i>Gazzetta Ufficiale della Repubblica</i>). BI publishes its rules and regulations in the Official Journal and in its Bulletin, and on its website.</p> <p>Similar to Consob, the BI publishes in its website the consultation document, responses received, the impact statement and a feedback statement at the close of public consultations. In addition, the BI issues interpretative recommendations, guidance or instructions for the application of its regulations, either in response to requests for clarification or on its own initiative. This is done through communications to the relevant intermediaries.</p> <p>Measures applying generally are published, in accordance with Article 8 (1) of the Consolidated Law on Banking, in the BI's Bulletin, as well as in the <i>Gazzetta Ufficiale della Repubblica Italiana</i> (Official Journal) and on the BI's web-site.</p> <p>Procedural fairness</p> <p>As noted under Principle 2, Consob and BI are obliged to provide reasons for decisions taken. Consob regulations (Regulation 9641/1995 and Regulation 9642/1995) give persons affected by its administrative procedures the right to obtain documents and be heard before the decision is made. Article 4(3) of the Consolidated Law on Banking gives persons affected by BI decisions the right to obtain relevant documents, submit written briefs and receive notice of the commencement of a process.</p> <p>Consob and the BI have adopted rules to be applied to the authorization process for intermediaries (Consob Regulation 11522/1998; BI Regulation of July 1, 1998, replaced on May 8, 2012). Authorization conditions for regulated markets, central depositories and securities settlement systems are set out in the Consolidated Law and its implementing regulations and in Supervisory Instructions jointly adopted by Consob and the BI. A party that may be negatively affected by a licensing decision of Consob or the BI can ask to be heard in the licensing process.</p> <p>Confidentiality</p> <p>As a general principle, all the information and data in possession of Consob and BI by virtue of their supervisory activity is covered by professional secrecy (Article 4 (10), Consolidated Law and 7 (3) of the Consolidated Law on Banking).</p> <p>Pursuant to its obligation to explain decisions and the reasons for them, the outcome of investigations is (in part) made public. Under certain circumstances, Consob makes public statements about on-going investigations even before closing the investigation. In this case, special care is taken not to disclose confidential information.</p> <p>Review of material actions by the regulator</p> <p>Decisions of Consob and the BI are subject to judicial review by the Administrative Courts.</p> |
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| Assessment | Fully implemented |
| Comments | |
| Principle 5. | The staff of the regulator should observe the highest professional standards, including appropriate standards of confidentiality. |
| Description | <p>Conflicts of interest</p> <p>BI and Consob staff are bound by general provisions on conflict of interest applicable to all public servants. In addition, each authority has established more specific rules through their codes of ethics and the conditions for employment.</p> <p>Consob Regulation 13859/2002 provides specific rules on staff conflicts of interest. These require staff:</p> <ul style="list-style-type: none"> • to notify Consob of any interests, whether financial or non –financial, that they and their relatives may have and that could give rise to conflicts (even if just apparent) vis-à-vis the function that the staff performs in the organization (Article 19); • to abstain from any decision or from carrying out any act in relation to matters that may entail a conflict of interest (Article 19); • not to perform any activity other than their functions with Consob unless they are duly authorized to do so and the external activity does not interfere with their Consob work. <p>Articles 12/I and 17/II of the BI's Conditions of Employment govern conflicts of interest and contain specific duties of reporting of conflicts and refraining from work involving conflicts. Violation of the Conditions of Employment can involve disciplinary sanctions. These provisions are enhanced by the Code of Conduct adopted in 2006 which requires employees:</p> <ul style="list-style-type: none"> • to avoid any situation liable to give rise to any type of conflict of interest; • to report any potential conflict of interest to the employee's direct superiors; • neither to use nor disclose confidential information for the purpose of gaining an advantage for themselves, the members of their families or any other individuals. <p>Securities trading by Consob and BI members and staff</p> <p>Consob employees are obliged by Article 20 of Consob Regulation 13859/2002 to notify Consob of any transactions, carried out directly or indirectly, involving financial instruments other than securities issued by the State. Such transactions must be notified to the Human Resources Department, which reviews them and decides whether any follow up action is needed. In such case, the Head of the Department to which the staff belongs is notified first. In case of a decision to launch a formal investigation, the Internal Audit Department is then involved.</p> <p>There are no general provisions governing securities trading of BI staff; other than a provision in the internal regulations which states that staff can trade instruments "only in cash". The conditions of employment and the internal rules lay down specific provisions on insider trading and conflict of interest, and clearly prohibit employees from gaining any advantage, economic or otherwise, by trading on or in any way using or divulging confidential information.</p> <p>Use of information</p> <p>Article 19 of Consob Regulation 13859/2002 obliges employees to ensure the proper use of information obtained in the course of their activities. Article 20 requires</p> |

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| | <p>employees to refrain from exploiting information that comes to their knowledge by virtue of the functions performed and prohibits misuse of information. Consob's employees, when performing their functions, are regarded as public officials and therefore are also bound by general provisions applicable to Italian civil servants (including legal privileges).</p> <p>By Article 5(3) of the BI's Code of conduct, BI staff must refrain from taking advantage of information obtained while performing activities for the BI.</p> <p>BI staff are also subject to a specific code of conduct issued by the European Central Bank (ECB) for the use of all personnel within the ECB, when carrying out activities or operations involving the foreign reserve assets of the ECB. The code requires staff to observe the principle of confidentiality concerning any information relating to specific deals or to the instructions given by the ECB.</p> <p><i>Confidentiality and secrecy</i></p> <p>All information gathered by Consob is covered by official secrecy (see Article 4(10), of the Consolidated Law). Employees of Consob and consultants and experts engaged by Consob are bound by official secrecy (Article 4 (12) of the Consolidated Law).</p> <p>Article 7 (3) of the Consolidated Law on Banking provides that employees of the BI are bound by professional secrecy. The duty to abide by professional secrecy obligations is also provided for by Article 12(2)/I and 17(2)/II of the Conditions of Employment and by Article 5 of the BI's Code of conduct.</p> <p>Violation of official secrecy is punishable as a criminal offence.</p> <p><i>Procedural fairness</i></p> <p>Article 19 of Consob Regulation 13859/2002 obliges employees to behave with diligence and fairness. They must observe in respect of persons affected by their activities the rules of procedure set out by the law and by Consob (which provide for right of information of affected persons, etc.). Consob commissioners and staff are also subject to the Codes of Ethics resolved in 2010, aimed at ensuring fair, independent and collaborative practices.</p> <p>Under Article 2 of the BI's Code of conduct, BI employees must perform their activity with independence, impartiality, loyalty, honesty, and fairness. The Director General oversees application of and compliance with the Code by the staff, to this end making use of the Evaluation team set up within the Legal Department. The Evaluation team also examines requests of the employees concerning the application of the Code. The observance of these rules may be verified in the course of internal inspections carried out by the Internal Audit Department.</p> <p><i>Sanctions</i></p> <p>Consob staff who breach their professional obligations are subject to the following administrative sanctions:</p> <ul style="list-style-type: none"> • written reprimand; • reduction in salary; • suspension (including of the payment of the salary) up to one year; • dismissal. <p>The following disciplinary sanctions are provided for in the BI's staff regulation:</p> <ul style="list-style-type: none"> • censure; |
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| | <ul style="list-style-type: none"> • reduction in salary; • suspension (including of the payment of the salary) up to six months or up to one year; • dismissal. <p>Processes for monitoring and dealing with violations</p> <p>For both Consob and the BI, responsibility for ensuring compliance with integrity requirements for staff rests with in the first instance with the staff member’s line manager. Compliance with these requirements and with procedural requirements is also subject to review by the internal control function for Consob or internal audit function for the BI. It is important to note also that in both authorities the Legal Department has a supportive role by providing opinions in connection with correct behavior.</p> <p>Consob Regulation 13859/2002 establishes a special procedure for dealing with staff violations. A special body called “<i>Collegio di Disciplina</i>” decides cases against staff. Charges against an employee must be justified and notified to the employee. The employee is allowed 20 days to present briefs in response. Once the preliminary phase of evaluations of the allegations has been concluded and the briefs presented, the <i>Collegio di Disciplina</i> must issue a decision and, if appropriate, indicate to the Chairman of Consob which sanction should be imposed. The Chairman proposes the final decision to be taken to the Commission.</p> <p>If the outcome of the investigation indicates possible criminal violations, the administrative internal procedure is suspended, and the case is reported to the public prosecutor. Precautionary measures can be adopted where necessary.</p> <p>The BI Conditions of Employment govern the procedure relating to the application of disciplinary sanctions. A special organ “the <i>Commissione di disciplina</i>” proposes the disciplinary sanctions to be applied in the case of staff violations. The members of <i>Commissione di disciplina</i> are designated by the Governor. They are one Deputy Director General who acts as chairman, the head of the Personnel Management Department and three other members chosen among senior staff. Disciplinary sanctions are decided, on the basis of a proposal of the Governor and prior consultation of the <i>Commissione di disciplina</i>, by the Directorate, except for censures or fines which are decided by the Governor, in the case of high ranking staff, and by the Director General, in the other cases).</p> |
| Assessment | Fully implemented |
| Comments | <p>The assessors acknowledge that under the current framework, composed of both general provisions for the public administration, and the respective regulations and terms of employment for Consob and BI, staff have a general obligation to notify conflicts of interest, as well as general obligations on confidentiality. In addition there is an internal unit in each entity in charge of monitoring compliance with these obligations. However the current regulations and terms of employment are not aligned with best practices, in particular in connection with securities transactions. In this regard the assessors encourage the authorities to strengthen their codes, in particular BI, by establishing a robust framework for this type of transactions. The framework should include at a minimum notification of all transactions, but consideration should also be given to including prohibitions or at least preclearance of certain transactions where the conflict of interest is more acute. In addition, an internal unit in the organization should be assigned to provide periodic reports to management on compliance by staff with these obligations. It is customary in other countries to require senior staff (usually board</p> |

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| | and heads of departments at a certain level) to submit annual statements of assets to the general comptroller body of the country. If that were not the case in Italy, the assessors would recommend that consideration be given to establishing such obligation. |
| Principle 6. | The Regulator should have or contribute to a process to monitor, mitigate and manage systemic risk, appropriate to its mandate |
| Description | <p>Consob</p> <p>The CL does not provide Consob with the direct mandate to contribute to financial stability; rather in the context of the current division of responsibilities between the BI and Consob such mandate mainly corresponds to BI. In this regard BI has responsibility for risk limitation, capital adequacy and the sound and prudent management of intermediaries. Consob is responsible for transparency and proper conduct of business by intermediaries.</p> <p>As a result of such allocation of responsibilities the role of Consob in the identification of systemic risk is complementary to that of BI. Still Consob has made a significant effort to upgrade its skills in risk identification and monitoring.</p> <p>The Research Division, composed of 35 staff, supports Consob's efforts to identify risks on securities markets. In addition, there is an ad-hoc unit in charge of the performance of quantitative analysis to support supervisory functions. With the collaboration of different departments, Consob produces daily and weekly reports on the markets for internal consumption. It also produces a bi-annual risk outlook which describes the macroeconomic environment, the equity markets and the situation of intermediaries. It also includes a risk dashboard. This report is public and can be found in the website.</p> <p>BI</p> <p>The Specialized Intermediaries Supervisory Department and the Markets and Payments Department conduct microprudential supervision of securities intermediaries and market infrastructure providers, which provides a first layer of work on risk identification in the non-banking sector.</p> <p>At a system wide level there are two different bodies that support BI's identification of risk in the securities markets area: (i) the Analysis of Risks and Financial Innovation Division and the (ii) Task force on risks</p> <p>The Analysis of Risks and Financial Innovation Division conducts system-wide analysis on non-banking entities and products under the supervision of BI. The Unit was created in 2008. Since then it has produced reports on (i) consumer credit intermediaries, (ii) small investment banks, (iii) private equity funds, (iv) AMCs, (v) HFs, (vi) real estate funds, and (vii) ETFs. A report on investment firms is forthcoming. The Unit uses an array of methodologies/tools, including stress tests and sensitivity analysis.</p> <p>The reports that followed such analyses have generated different types of actions, including (i) firm specific interventions, (ii) enhancements of the methodology used by the supervision analysts, (iii) expansion of supervisory data; (iv) system-wide interventions; (v) proposals for regulatory and legal changes, and (v) cooperation with Consob and the MEF.</p> <p>In addition, the division supports the development of a risk assessment matrix for the Specialized Intermediaries Supervision Department, which provides a prospective view of the risks faced by each type of intermediary, via a risk assessment matrix (RAM). The</p> |

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| | <p>RAM describes the main risks, the impact that each risk could have on the sector; and the potential actions to address it. Such RAM is used by the supervisory department as an input to shape its interaction with different participants.</p> <p>The Task force on risks is coordinated by the Head of the Macroprudential Department, and is composed by the heads of different departments, including the supervision and the research departments. This group produces a risk report outlook, which then supports the development of the Financial Stability Report.</p> <p>Coordination for purposes of financial stability</p> <p>A special Committee for the protection of financial stability, the <i>Comitato per la salvaguarda della stabilita finanziaria</i>-CSSF, was set up in March 2008 between the MEF, Consob, BI and the ISVAP in accordance with a protocol signed by the authorities.</p> <p>The objective of the committee is twofold: (i) to prevent financial crisis with potential systemic effects, through the identification of main risks and vulnerabilities of the financial system; the evaluation of possible measures to limit such risks and the risk of contagion to other systems; the preparation of contingency plans; and the performance (twice a year) of simulation exercises and stress tests, and (ii) facilitating coordination of actions for the management and resolution of a crisis. The protocol requires bi-annual crisis simulation exercises.</p> <p>The parties to the protocol are required to exchange all information necessary to achieve such objectives. The Committee must meet at least twice a year, and extraordinary meetings may be convened. Public authorities interviewed expressed different views about the work performed by this committee so far. There is agreement that it has been useful to coordinate actions in connection with crisis, but there is less agreement on whether it has also been a useful vehicle for risk identification and monitoring. In any case, authorities have highlighted that given the persistence of the current crisis, it is reasonable that the work of the committee has focused on crisis responses.</p> <p>EU context</p> <p>The Italian supervisory authorities also participate in EU bodies which have a role in identification of risks at the EU level, including ESMA, the Joint Committee, and the European Systemic Risk Board (ESRB). Both Consob and the BI are required to consider, in case of crisis or tensions on financial markets, the effects of their actions on the stability of other EU Member States' financial systems (see article 2 of the CL).</p> |
| Assessment | Fully implemented |
| Comments | The assessors note that in the context of the ESRB Recommendation, the Italian authorities will need to assign an explicit macroprudential mandate to one authority. In the context of such decisions, it will be necessary to decide on the role of the Committee of Financial Stability. |
| Principle 7. | The Regulator should have or contribute to a process to review the perimeter of regulation regularly |
| Description | <p>Perimeter of regulation</p> <p>The perimeter of regulation in Italy covers a wide variety of entities, including some that in many jurisdictions would be outside of the perimeter of regulation (such as servicers of securitizations) or only recently were brought to the perimeter of regulation (hedge</p> |

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| | <p>funds). In practice this means that the supervisory authorities have access to a broad range of information that can help them to better identify risks.</p> <p>Pursuant to article 23 of Law 261/2005 the BI and Consob must periodically review the contents of their regulations in order to adapt them to the evolution of market conditions and the interest of investors. As a result this review takes into consideration whether there is a need to expand the perimeter of regulation to unregulated products, markets, market participants and activities. This review must take place at least every three years. In practice this review has been integrated into the annual planning of the respective institutions, as will be further discussed below.</p> <p>Finally article 18.5 of the CL provides that via regulation adopted after consulting BI and Consob the MEF has the authority to establish new categories of financial instruments, new investment services and activities and new accessory services, indicating which persons subject to certain forms of prudential supervision may exercise the new services and operations. This authority has to be exercised via regulation in compliance with the provisions of community law.</p> <p>Identification of risks and changes to regulations</p> <p>As discussed under Principle 6, both Consob and BI have processes in place to identify risks arising from the activities performed by different market participants and regulated entities, as well as from products offered in Italy. Such identification of risks feeds into the strategic planning activities of the institutions.</p> <p>In the case of Consob the Strategic Planning process is a key vehicle for the identification of regulatory and supervisory actions needed. The process starts with the analysis of the external environment, followed by the identification of the main risks that can affect regulated entities and their potential impact, as well as the risk that such external environment and the triggering of such risk on regulated entities could have on the regulatory objectives. The final outcome of it is a set of strategic priorities for the following three years. The Strategic Plan is updated on a yearly basis. Specific timing, roles, responsibilities, activities and resources to achieve such strategic priorities are defined in an annual Operating Plan, which is prepared with the contribution of all operating Divisions (bottom-up approach). The Operating Plan also includes a plan of regulatory actions that the authority intends to undertake during the year.</p> <p>A recent example of enhancements of regulations as a result of the detection of risks took place in 2009. Consob detected cases of mispricing of financial instruments that lack a liquid secondary market, or where products were not engineered, selected and marketed in view to meet the best interests of clients. Consob issued a communication on the distribution of illiquid assets to retail investors.</p> <p>BI has issued a Regulation implementing article 23 of the Law 262/2005. Pursuant to such regulation each year BI publishes the Program of regulatory activity planned for the following 12 months. The program specifies the areas where regulatory actions are envisioned, and the priorities of activities to be conducted. This Program follows a process of consultation process, whereby the banking industry as well as any other interested party may contribute through comments and suggestions.</p> <p>Changes to legislation</p> <p>The strategic planning conducted by both institutions can lead to proposals to the MEF for changes in legislation.</p> <p>For example, in order to limit regulatory and product arbitrage and enhance investor</p> |
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| | <p>protection in relation to complex products, in 2005 the scope of application of prospectus related requirements was extended to any offer of financial products to the public. Moreover the same financial instruments related distribution and disclosure rules were applied horizontally also to financial products issued or distributed by banks and insurance undertakings.</p> <p>However, the new architecture of financial market supervision in the European Union has led to increased centralization of legislative activity at the European level. At the European Level, the European Commission plays a key role in supporting the review of legislation, with a view to identifying areas where the perimeter of regulation needs to be reviewed. In such context the EC issues papers for consultation through which the EC gathers information and evidence on the need to regulate specific areas previously unregulated. For example, recently the EC issued a paper on shadow banking, which highlights potential areas where the perimeter of regulation might need to expand or where regulatory requirements and/or intervention might need to be strengthened.</p> <p>Consob and BI are actively involved and cooperate with the MEF in the negotiations on proposals for new directives and regulations. Consob is also involved in the “regulatory” activities of ESMA. In this regard, it is important to mention that ESMA has two permanent Units which help in risk identification, including areas not currently covered by the perimeter of regulations. Such Committees are the Standing Committee for Economics and Market Analysis and the Financial Innovation Standing Committee.</p> |
| Assessment | Fully implemented |
| Comments | |
| Principle 8. | The Regulator should seek to ensure that conflicts of interest and misalignment of incentives are avoided, eliminated, disclosed or otherwise managed. |
| Description | <p>Regulated entities</p> <p>The supervisory programs in place for the on-going supervision of securities intermediaries (described in Principle 31), CIS operators (described in Principle 24), auditors (described in Principle 19), and sell side analysts (described in Principle 23) are a key mechanism to identify, monitor and when necessary take regulatory actions to address conflicts of interest either on an individual entity or for the whole sector (through interpretations, guidelines, etc).</p> <p>In all cases the current regulatory framework requires regulated entities to put in place mechanisms to identify, monitor and mitigate conflicts of interest. As in other countries in Europe, the approach to mitigation is mixed: in some cases, certain activities are banned to prevent the conflict. Examples of this approach are the limitations on non-audit services for audit firms and credit rating agencies. In others, disclosure to investors, rather than elimination of the conflict, is required. Examples of this approach are the obligations on IFs to inform clients before acting on their behalf, on the nature and sources of conflict of interest that have been identified, so that they can make an informed decision on the services to be provided. Another example relates to the remuneration for sell-side analysts based on a firm’s investment banking activities; in such case the regulatory framework requires that appropriate disclosure to the public be made. However as mentioned in Principle 23, the practice has been that analysts’ remuneration is not tied to transactions.</p> <p>Monitoring of compliance with obligations in the area of conflicts of interest is carried out through a combination of extensive off-site reviews and on-site inspections. As</p> |

explained in Principles 24 and 31 Consob has developed robust data bases with very granular information for both CIS and IFs, which serves as the basis for its off-site monitoring. The analysis of such granular information allows Consob to identify potential issues of concern, including in relation to management of conflicts of interest. Such concerns could in turn prompt an additional request for information, convening of the management of a regulated entity to highlight weaknesses and the request to correct them, or an on-site inspection.

In the Italian context, one area of significant conflicts of interest has been the role of banks both as issuers and distributors of financial products. This potential for conflicts of interest was increased during the recent crisis when capital withdrawn from CIS was reinvested with banks in bank bonds and deposits.

Consob is aware of this area of risk and has taken some measures to better monitor it and address it. In this regard, in 2009 it implemented a thematic program of inspections that covered the nine largest banks with the objective of verifying their compliance with the Markets in Financial Instruments Directive (MiFID). Remedial actions were requested from these banks and in some cases pecuniary sanctions have also been imposed.

In addition, in 2011, it changed its organizational structure and “moved” the review of prospectuses of bonds issued by banks to the intermediaries division, so that it could link better the information on the type of products being issued with the distribution leg. This has triggered supervisory actions on specific banks, including pecuniary sanctions.

Issuers

In the case of issuers, overall the main mechanism used to address misalignment of incentives is disclosure to the public. For example, the current framework for issuers who offered securities to the public requires that the prospectus includes information on related party transactions, and compensation arrangements for the board.

However, as will be further explained in Principle 17, listed companies in Italy are subject to certain specific obligations tailored to the specific challenges brought by the ownership and governance structure of Italian companies. Examples of such regulatory requirements are (i) the regime applicable to related party transactions which requires the constitution of a special committee to review and in certain cases approve related party transactions in addition to the disclosure obligations explained above, and (ii) the slate system, which seeks to ensure representation of minority shareholders in the board. In both cases the measures have improved the system, although as will be further explained in principle 17, challenges remain.

In terms of the supervisory approach, there is a specific office within the Consob’s Corporate Governance Department, the Shareholders Rights Office, the mandate of which includes the monitoring of issuers’ obligations vis-à-vis fairness. Key issues in the supervisory program of this office are the issuers’ (i) internal controls system, (ii) implementation of related party transaction rules; (iii) slate system; and (iv) shareholders’ meetings. Based on the review of the information provided by issuers, Consob has taken supervisory actions against specific issuers, including sanctions.

The crisis highlighted the need for many countries to look at misalignment of incentives in connection with securitization products. Certain features of the Italian legal framework appear to have allowed for more scrutiny of securitization products. In this regard, the BI supervises servicers (banks or financial intermediaries enrolled in the “Special Register” article 107TUB) which have the legal duty to check compliance of

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| | each single securitization with the provisions of the Securitization Law and with the contents of the prospectus. In addition consolidation rules are strictly enforced. Also, the Italian legal framework has discouraged (though not eliminated) the issuance of the most complex structures such as synthetic CDOs through Italian special purpose vehicles. Finally, EU legislation has imposed retention requirements on originators (via obligations on banks and institutional investors). |
| Assessment | Fully implemented |
| Comments | It is key that Consob continues to devote sufficient resources to the analysis and monitoring of conflicts of interest in the areas mentioned above, and that supervisory actions, including enforcement if necessary, be taken. |
| Principles for Self-Regulation | |
| Principle 9. | Where the regulatory system makes use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, such SROs should be subject to the oversight of the Regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities. |
| Description | <p>As will be further explained in Principles 34 and 36, under the current framework, RMs and MTFs have a market surveillance role, in ensuring orderly trading and a complementary role to that of Consob in market surveillance for purposes of detecting market abuse.</p> <p>In addition, as explained in Principle 16, RMs and MTFs have a role in ensuring compliance by issuers with their listing obligations. Listing obligations include disclosure obligations, which in this case are imposed by virtue of the contract of the market with the issuer. In the cases of issuers admitted to trading in an RM, overall such obligations replicate disclosure requirements included in the CL, which monitoring has been entrusted by the CL to Consob. As a result, in connection with issuers admitted to trading in a RM, the RMs have a complementary role to that of Consob in ensuring compliance by issuers with disclosure obligations. In the case of issuers listed in AIM the exchange has sole responsibility for ensuring compliance with listing obligations. However, as explained in the introduction, in such case disclosure obligations stem from the contract with the exchange rather than the law. Currently the AIM market is not significant in size.</p> <p>Given the limited role of RMs and MTFs, the assessors' would not assess them under the SRO principles.</p> |
| Assessment | NA |
| Comments | |
| Principles for the Enforcement of Securities Regulation | |
| Principle 10. | The regulator should have comprehensive inspection, investigation and surveillance powers. |
| Description | <p>Information gathering and inspection powers</p> <p><i>General powers</i></p> <p>Consob and the BI have broad powers under the CL to gather information, and to carry out supervision and inspection of regulated entities and other persons and entities</p> |

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| | <p>carrying on securities market activities.</p> <p>These powers include powers to require the production of data and information from, and carry out inspections of:</p> <ul style="list-style-type: none"> • authorized persons—which include IFs, AMCs, SICAVs, financial intermediaries entered in the register referred to in Article 107 of the CL on Banking and banks authorized to engage in investment services—and their external auditors (Articles 8(1) and 10(1) of the CL); • natural person stockbrokers (Article 201(12) of the CL); • entities that, while not engaging in regulated activities, are linked to an Italian investment firm or management company by a shareholding relationship (Articles 12(3) and (5) of the CL); • financial salespersons (Article 31(7) of the CL); • market management companies (Article 74(2) of the CL); • wholesale markets in government securities (Article 76(2) of the CL); • central depositories and persons who administer clearing, settlement and guarantee systems (Articles 77(1) and 82 of the CL); • partners, directors, members of the board of auditors and general managers of auditing firms (Article 162(2) of the CL); • issuers of securities traded on regulated markets or that are widely held by the public, persons who control them and companies controlled by them, corporate officers, external auditors, and significant shareholders and parties to shareholder agreements (Articles 114, 115 and 116 of the CL); • persons who make public offers or require the admission of securities to trading, persons who control them and companies controlled by them, corporate officers, external auditors and intermediaries entrusted with the placement (Articles 97 and 113 CL); • persons who make public offers to buy or exchange financial instruments (Article 102 of the CL). <p>In exercise of their supervisory authority, Consob and the BI can ask all the persons and entities listed above to transmit reports, data and any other relevant information on a periodic or routine basis, as well as in response to particular inquiries, with no limitations or conditions as to when these powers can be exercised.</p> <p>Inspections can be carried out without giving prior notice to the inspected entity and in practice Consob and the BI do not normally give advance notice of inspections. Inspections are carried out in accordance with internal procedures manuals or guides (for Consob the <i>Inspection Manual</i>, for the BI the <i>Guide to Supervisory Activity</i>).</p> <p>In addition, pursuant to articles 4-ter, 8, 73, 74, 76, 115, 116 and 187-octies of the CL, Consob can make use of all the compulsory powers listed in 187-octies of the CL, in connection with authorized persons as well as in connection with short selling, supervision of markets and market operators, takeovers, issuers and market abuse. The list of such powers is included under Principle 11. In the case of BI use of compulsory powers over regulated entities is limited to the request of information and documents, hearings and testimony, inspections. Moreover the BI can ask the Finance Police to make use of further investigating powers.</p> <p>Consob and the BI may also request the competent authorities of EU States to carry out on-site verifications of branches of IFs, AMCs and banks established within the territory</p> |
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| | <p>of that State or agree on other methods of verification (Article 10(3) of the CL).</p> <p>Article 7 of the CL empowers Consob and the BI to convene (summon) the directors, members of the board of auditors and managers of regulated intermediaries. Convening powers are used by Consob in cases where they have found serious weaknesses in a regulated entity, and the purpose of convening a meeting is to inform the entity of the weaknesses found as well as of the corrective actions required. BI uses its convening powers more often, as they usually follow an on-site inspection, whereby BI convenes (summons) the entity to inform of the results of the inspection as well as of any corrective actions imposed on it.</p> <p><i>Trading activity on RMs</i></p> <p>Consob (and BI for wholesale markets in government securities) has real time access to trading activity on RMs. Market supervision powers and techniques are described under Principle 34.</p> <p>Consob is also part to the TREM system (Transaction reporting mechanism) set out under MiFID and managed by ESMA. Through this system, Consob receives reports from all EU IFs and banks concerning transactions in financial instruments listed on Italian RMs.</p> <p><i>Record keeping requirements</i></p> <p>Brokerage accounts and banking accounts can be opened only with intermediaries subject to authorization and prudential supervision. Consob and the BI have access to documents and information kept by supervised entities and makes it possible to track all flows of cash, funds and financial instruments for investigative and enforcement purposes. Under Law Decree 201/2011, transfers of cash, funds or financial instruments over EUR 999.99 must be made through authorized entities. These operations must be registered separately and the person responsible for ordering the transaction identified.</p> <p>Investment services providers (ISPs), including AMCs and SICAVs, are subject to detailed record keeping obligations relating to client identification and client subscriptions, orders and transactions (see EU Commission Regulation 1287/2006, implementing MiFID). Further information on intermediaries' record keeping obligations is set out under Principle 31.</p> <p>Records about client orders and transactions must be kept for five years (Article 29 of BI and Consob Regulation of 29 October 2007).</p> <p>Article 15 of Consob Regulation 11768/1998 requires market management companies to establish electronic procedures for each of the markets they manage to record the transactions carried out on them. Records must be preserved for at least eight years, and must make it possible to establish full details of transactions taking place on the market.</p> <p><i>Customer identity</i></p> <p>Legislative Decree 231 of 2007 and related regulations, which implement the EU Anti-money laundering Directive, require IFs, banks and other financial intermediaries to carry out identity checks for any person who carries out transactions or opens an account (including a deposit account) or establishes other continuing relationships which could entail the transfer of cash or financial instruments, such as custody services. The identification must take place face to face. For on-line transactions, a previous identification must be made by an eligible introducer (another financial intermediary who has already identified them in person).</p> |
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| | <p>Records relating to the opening of accounts must be kept for 10 years.</p> <p>Inspections outsourced to SROs and other third parties</p> <p>Neither the BI nor Consob outsource the performance of supervision functions or inspections.</p> <p>Consob and the BI may request another authority to carry out inspections on its behalf. In particular, under Article 22 of Law 262/2005, Consob and the BI can request the Italian Finance Police to collect information on their behalf. This can include performance of on-site inspections. In practice, Consob made 17 such requests in 2012. If this occurs, Consob and the BI remain the ultimate authority responsible to evaluate the findings obtained from the other authority or the Finance Police.</p> <p>Consob, pursuant to Article 10-(1)bis of the CL may request auditing firms to carry out ad hoc verifications and charge the investment firm of the relevant expenses. In practice, this power is rarely used.</p> |
| Assessment | Fully implemented |
| Comments | See comments on compulsory powers under Principle 3. |
| Principle 11. | The regulator should have comprehensive enforcement powers. |
| Description | <p>Investigative powers</p> <p>Consob</p> <p>As indicated in Principle 10, Consob has the power to require information and documents, to conduct inspections and to exercise the other compulsory powers referred to in Article 187-octies of the CL</p> <p>in relation to:</p> <ul style="list-style-type: none"> • IFs, banks providing investment services, AMCs and SICAVs (Article 8(5bis) of the CL); • stock exchange companies and market operators (Articles 73(1), 74(4-bis) and 76(2-4) of the CL); • issuers admitted to trading in a RM (Article 115(1)(c bis) of the CL); • issuers of securities widely distributed among the public (Article 116(1) of the CL); • takeover bidders (Article 102(7)); • market abuse (Article 187-octies of the CL) and • short selling and certain aspects of credit default swaps (Article 4-ter (7) of the CL). <p>According to article 187 octies of the CL, Consob has the power, against anyone who may be informed about the facts under investigation, to:</p> <ul style="list-style-type: none"> • require information, data or documents; • require telephone records; • conduct personal hearings and take statements; • seize property that may be confiscated under Article 187-sexies; • carry out inspections; and • conduct searches. |

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| | <p>In addition, Article 187-octies(4) of the CL enables Consob to:</p> <ul style="list-style-type: none"> • access the information system of the taxpayers' register in accordance with the provisions of Articles 2 and 3 of Legislative Decree no. 212 of July 12, 2001; • require telecommunication providers to provide telephone traffic records; • require the communication of personal data, notwithstanding the restrictions provided under the Data Protection Code. This power can be exercised in relation to persons that are not subject to Consob's direct supervision; • access information in the register of accounts and deposits; • access information contained in the anti-money laundering register (<i>archivio unico informatico</i>); • gain direct access, through a dedicated electronic connection, to the data contained in the BI's Central Credit Register. Access to this information is the subject of a memorandum of understating that was entered into by Consob and the BI on October 31, 2007. <p>Authorization by the prosecutorial authorities is required before Consob can:</p> <ul style="list-style-type: none"> • carry out inspections at the premises of persons which are not subject to its supervision or require any such person to provide existing telephone records or personal data, including by derogation to the prohibitions set by the Privacy Law; • require a telephone provider to furnish details on phone traffic records; • conduct searches according to the procedures established by the law in connection with the assessment of VAT and income taxes; • seize assets of any person who could be acquainted with the facts under investigation. <p>For (i), (ii) and (iii) Consob must submit a request to the prosecutorial authorities explaining the facts and the reasons why this information is needed. Consob explained that the use of this power is well established, and there are no cases where the prosecutorial authorities have refused to provide such authorization.</p> <p>In the case of hearings, a <i>procès-verbaux</i> (record of interview) must be drawn up noting the statements given by the summoned person. The summoned person must be requested to sign the <i>procès-verbaux</i> and is entitled to obtain a copy thereof. Under the Italian legal system, as a general principle witnesses are obliged to testify and cannot refuse to answer except in the case of self-incrimination (see Article 198 of the Code of Criminal Procedure) or when specified privileges (such as those for spouses, lawyers and others) apply. A judge can, in some circumstances, require persons claiming privilege to give testimony. However, as per interpretation of the Vienna Convention on Human Rights, a person cannot be forced to provide testimony under oath.</p> <p>For inspections, searches and seizures, a <i>procès-verbaux</i> must be drawn up noting the data and information obtained, the findings and the seizures carried out. The concerned person must be asked to sign the <i>procès-verbaux</i> and is entitled to obtain a copy of it.</p> <p>Seizure of assets is a precautionary measure in anticipation of confiscation under Article 187-sexies of the CL. Assets that may be seized are the product of the offence or the profit from the offence and the property used to commit it or, if this is not possible, a sum of money or property of equivalent value. Consob must provide the Public Prosecutor with evidence of the purported illegal behavior. The interested person may file opposition with Consob against the seizure and a decision on the opposition must be given with reasons within 30 days from the day of the filing of the opposition proceedings.</p> |
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| | <p>The decision to gather information by making use of its compulsory powers is a decision taken autonomously by Consob. It does not have to be endorsed by any other Italian authority.</p> <p>BI</p> <p>Similar to Consob, BI has broad supervisory powers over regulated entities, which include the power to request information and data from them, as well as to conduct inspections on them, as described under Principle 10. In addition, pursuant to article 8(5 bis) of the CL. BI has the power to conduct personal hearings and take statements over authorized entities.</p> <p>BI has the same compulsory powers provided to Consob by article 187-octies in connection with the short selling Regulation.</p> <p>Regulatory intervention measures</p> <p>Consob and the BI have extensive powers of supervisory intervention on regulated entities. The regulators' powers of supervisory intervention are described under the relevant principles for issuers, auditors and information providers, collective investments, intermediaries and markets.</p> <p>Consob can order the suspension of trading in securities. In particular, it can request the RM operator to suspend financial instruments or intermediaries from trading (Article 64 of the CL); it can order, in case of necessity and as a matter of urgency, that trading be halted in a given securities or in all the securities traded in a RM (Article 74 of CL); it can require the operator of an MTF to halt trading in securities (Article 77-bis); it can require SI to suspend trading in securities admitted to trading on RM(Article 78 of the CL); and it can suspend or prohibit public offers of securities and related advertisement (Articles 99 and 101 of CL); it can suspend or prohibit takeovers or exchange tender offers (Article 102 of the CL) .</p> <p>Administrative sanctions</p> <p>Overall, pursuant to article 190 of the CL individuals carrying out administrative or managerial tasks and employees of licensed entities (including market intermediaries and CIS) who do not comply with obligations contained in the CL are subject to pecuniary sanctions from EUR 2,500 to 250,000.</p> <p>Additional administrative infractions exist in connection with markets and issuers, and therefore, under Consob's remit, including:</p> <ul style="list-style-type: none"> • insider dealing (187bis); • market manipulation (187ter); • public offerings (Article 191); • takeovers bids or exchange tender offers (Article 192); • disclosure of corporate information, including notification of relevant holdings and shareholders agreements, and duties of auditing firms and members of the board of auditors (Articles 192bis and 193); • proxies (Article 194); • admission to trading (192 ter). <p>Pecuniary administrative sanctions are provided for under Article 193-ter for violations of the obligations deriving from the Short Selling Regulation (Regulation 236/2012/EU).</p> <p>The highest pecuniary administrative sanctions are for insider trading—up to EUR 15 million or up to 10 times the product of the offence or the profit from it</p> |
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| | <p>(Article 187 bis)—and market manipulation—up to EUR 25 million or up to 10 times the product of the offence or the profit from it (Article 187 ter). In the cases of insider trading and market manipulation, in addition to pecuniary sanctions on the individuals, Consob can also make the legal entity liable. In such case the employing entity is liable to a sanction which is the sum of sanctions imposed on managers and employees for the same offence, unless the firm can show the violator acted solely in his or her own interests or for third parties (Article 187 quinquies).</p> <p>By Article 187-sexies of the CL, the imposition of pecuniary administrative sanctions for market abuse offences also entails the confiscation of the product of the offence or the profit from it and the property used to commit it. If it is not possible to execute the confiscation, a sum of money or property of equivalent value may be confiscated.</p> <p>Under Article 196 of the CL, Consob can sanction financial salespersons directly by imposing:</p> <ul style="list-style-type: none"> • a reprimand in writing • a pecuniary administrative sanction • suspension from the register • deletion from the register. <p>Finally any person who fails to comply with a request from the BI or Consob within the prescribed time or delay the performance of their supervisory functions is subject to a pecuniary sanction of between 50,000 and 1,000,000 euro (Art. 187-quinquiesdecies of the CL).</p> <p>Fines are paid to the government and do not form part of the budget of the regulators.</p> <p>Sanctioning Procedures</p> <p>Under Article 195 of the CL, sanctions may be imposed within 180 days from the investigation or within 360 days if the interested party resides or is headquartered abroad. Sanctions must be imposed within 240 days from the notification of charges.</p> <p>To apply these provisions both Consob and BI have issued an internal regulation setting out step-by-step the sanctioning proceeding. Appeal against the decision to the relevant court is available.</p> <p>Sanction decisions are made by Consob's Commission and the Directorate in the case of the BI based on a proposal from:</p> <ul style="list-style-type: none"> • the administrative sanctions office or a sanctions committee (in the case of complex cases) in the case of Consob; • the sanctioning division or a collegial body (in complex cases) in the case of BI. <p>The decision on the sanction must state the relevant grounds, after notifying the charges to the interested parties. Sanctioning proceedings must afford all parties the opportunity to state their case and have access to the investigation file. Transcripts must be taken of the proceedings. Investigatory and adjudicatory functions must be separate.</p> <p>The general principle is that sanctions are made public except if such publication places the financial markets at serious risk or cause disproportionate damage to the parties involved. Resolutions imposing sanctions are published in abridged form in the Bulletin of the BI or Consob. Taking into account the nature of the offences and the interests involved, the BI or Consob may establish further methods of publicizing the measure.</p> |
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| | <p>Companies and entities with which offenders are connected shall be jointly and severally liable with them for payment of the sanction and shall be held to the exercise of the right of recourse against those responsible for the offences.</p> <p>Criminal investigations and sanctions</p> <p>Part V of the CL sets out a range of violations of the legislation that make the perpetrator subject to criminal prosecution. They include offences relating to:</p> <ul style="list-style-type: none"> • intermediaries and markets, including unauthorized activity, intentional breach of duty to clients, or obstructing Consob's and BI's supervisory functions (Articles 166–171); • issuers, including irregular acquisitions of shares and false statement in a prospectus (Articles 172–174); • insider trading and market manipulation (Articles 184 and 185). <p>Penalties including imprisonment and fines apply to criminal offences created by these provisions. The most severe criminal penalties are for insider trading (Article 184(1) and (2) of the CL) and market manipulation (Article 185(1), which carry a penalty of up to six years imprisonment, and for unauthorized provision of investment services (up to four years, Article 166).</p> <p>If Consob and BI have grounds for suspecting that criminal violation may have been committed, they must report the matter to the public prosecutor. The decision to report to the public prosecutor is taken by the Commission or Governor of the BI. The decision as to whether to lay criminal charges belongs to the criminal prosecutors.</p> <p>Under Article 187 <i>decies</i> of the CL, if a public prosecutor receives notice of the commission of an insider trading or market manipulation offence, he or she must without delay inform the Chairman of Consob. The Chairman of Consob must provide the public prosecutor with documentation gathered during its own inquiries with a reasoned report where there are grounds for suspecting that a crime may have been committed. Consob and the judicial authorities must cooperate with each other, including through the exchange of information on market abuse cases, including in cases where the conduct does not amount to a criminal offence.</p> <p>For market abuse offences, when the matter is taken before the Court, Consob acts as the injured party and has the rights and powers the Code of Criminal Procedure gives to entities and associations representing the interests injured by the offence (Article 187 <i>undecies</i> of the CL).</p> <p>Private rights of action</p> <p>Under the Italian Constitution, any person can seek remedies before a court of law when his or her rights or legitimate interests have been violated. This provision would therefore allow an injured person to seek civil remedies for breaches of securities laws.</p> <p>In actions for damages for injury caused to a client in the performance of investment services or non-core services, the burden of proof of having acted with due diligence lies on the regulated intermediary (Article 23(6) of the CL).</p> <p>Information sharing between authorities competent to impose enforcement actions</p> <p>Article 5(5) of the CL requires Consob and the BI to notify each other about the measures adopted and the irregularities discovered in carrying out their supervisory activities. Article 10(2) provides that Consob and the BI are to notify each other of the inspections they undertake. Each regulator may request the other to carry out</p> |
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| | <p>verifications on its behalf. In practice, the BI and Consob share plans for inspections and the results of those inspections.</p> <p>Consob may cooperate with the Financial Police and with other national authorities, including the judicial authorities in case of market abuse. Consob has an MoU with the Finance Police governing the use of the police in its supervision and inspection activities.</p> <p>The BI closely collaborates with public authorities performing law enforcement functions and especially with the national agencies in charge of investigations into organized crime (DIA- <i>Direzione investigativa antimafia</i> and DNA-<i>Direzione nazionale antimafia</i>), with which it exchanges information. In addition under the law in force, the judicial authority must report to the Governor of the BI any money laundering activities carried out through banking channels (Article 4 of Law 82/1991).</p> <p>Finally, pursuant to article 4.13 of the CL in the case of Consob and 7(cl) of the CL on Banking for BI governmental authorities and public entities must provide the information, documents and every further cooperation requested by them in accordance with the laws governing each authority or entity.</p> <p>Consob and BI cooperate with EU and non-EU competent authorities according to Article 4 of the CL.</p> |
| Assessment | Broadly Implemented |
| Comments | <p>Overall the authorities have been given sufficient investigative powers in connection with their respective mandates. However, as indicated under Principle 3, the assessors recommend that the CL be strengthened by consolidating in one single provision the compulsory powers of Consob which should exist in connection with all areas of its mandate.</p> <p>The framework for pecuniary sanctions is strong for more serious violations such as insider trading and market manipulation. However, as stated under Principle 3 there are a few limitations in connection with the use of pecuniary sanctions for all other violations to the CL, as they can only be imposed on the individuals not the legal entities (although the legal entities are jointly and severally liable), and their level appear low. Thus, the assessors encourage an overall review of the level of sanctions in areas other than market abuse/short selling to ensure they are sufficient to act as an effective deterrent to individuals' behavior and entity conduct. They recognize that any change would require amendment to legislation. These limitations in the enforcement framework are the reason for the broadly implemented grade.</p> |
| Principle 12. | The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program. |
| Description | <p>Inspection, surveillance and compliance monitoring</p> <p>Consob and the BI use a systematic approach to the monitoring and supervision of regulated activities. Details of the processes used are set out under the relevant Principles.</p> <p>Both authorities produce annual plans which indicate the main areas of focus for their regulatory and supervisory activities in the coming year. Each supervisory department produces a plan for the year which is approved by the Commission (for Consob) and the Directorate (for the BI). These internal plans identify the regulated entities that will be subject to on-site inspections and the off-site work each department will carry out.</p> |

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| | <p>Consob and the BI use a risk-based approach to their supervisory work. Sophisticated systems, drawing on extensive quantitative data and qualitative information, are used to identify higher risk entities for entities subject to the regulators' authority. The explanations below summarize the supervisory approach for different parts of the securities markets, as required by Principle 12. More detailed discussions are included in the sectoral principles.</p> <p><i>Off-site supervision</i></p> <p>For issuers of securities and other financial instruments, Consob reviews all prospectuses before approval, other than prospectuses for open-end harmonized CIS which are reviewed ex-post on a risk-based selection process. Issuers' obligations to keep the market informed of material information are monitored and corrective action, including the use of sanctions, is taken when failures to comply are detected. Issuer's compliance with financial reporting requirements is monitored using a combination of risk-based and sampling techniques. Particular attention is paid to corporate control issues (such as the conduct of major shareholders and the use of shareholders agreements that may have an effect on corporate control). This is necessary in view of the ownership structure of Italian companies whose securities are traded on regulated markets.</p> <p>In its off-site supervision of IFs and banks providing investment services, Consob uses the very detailed information available to it to monitor firm performance and potential compliance risks. Because of its ability to request and access relevant information and analyze it using its systems, Consob places much emphasis on the off-site supervision process.</p> <p>A similar approach is taken to Consob's ongoing off-site monitoring of AMCs.</p> <p>In its market supervision work, Consob has well developed processes for monitoring the conduct of markets and especially for identifying potential market misconduct.</p> <p>In its areas of responsibility, the BI has a systematic approach to off-site supervision. It uses the flow of information from AMCs and ISPs to analyze conduct which may indicate the need for intervention. It uses sophisticated systems and databases, linked to its risk scoring and supervisory processes, to monitor compliance by all firms. The assessors reviewed files that show the BI acts effectively, for example on deficiencies in regulatory capital, or shortcomings in governance, organization and control systems.</p> <p>Off-site monitoring can trigger different types of interventions, including letters and meetings with board and management of registered firms. In this regard, Consob highlighted the meetings with management and board of registered firms are used frequently, as an ordinary tool for supervision. For example, since 2009 Consob has held 541 meetings with senior officers (112 banks, 126 investment firms, 172 asset management companies and 131 other market operators) and has convened 124 meetings at Consob's offices (43 banks, 27 investment firms, 49 asset managers, and 5 other market operators).</p> <p><i>Thematic reviews</i></p> <p>Consob's risk rating system and robust off-site monitoring databases allows it to analyse firms on a group ("family") basis as well as on an individual basis. This enables it to identify firms carrying on similar business activities and to focus on conduct which may be common across a number of firms. This supports a thematic approach to potentially problematic conduct. The same applies to supervision of CIS.</p> <p>Thematic work is mostly conducted off-site. However, in 2009–2010 Consob conducted</p> |
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| | <p>thematic on-site inspections on the nine largest banks to verify compliance with MiFID.</p> <p><i>On-site inspections</i></p> <p>Consob and the BI both use on-site inspections in their supervision of regulated entities.</p> <p>Both organizations use separate inspection department to perform these inspections, but line supervisory staff are often part of an inspection team. A risk based approach is endorsed, so that neither Consob nor BI have an approach towards on-site inspections that requires putting all regulated entities under a fixed schedule of on-site inspections—although the coverage of inspections (in terms of assets and clients) is very high; and in the case of prudential supervision of banks, the current approach has ensured that the bulk of the banks are inspected. Rather on-site inspections are used as a complement to the extensive off-site monitoring which includes different type of interventions (meetings with the board of directors and the board of auditors, and letters and thematic reviews).</p> <p>On-site inspections are planned as part of the annual planning cycle and the selection of firms to be inspected is decided by the relevant supervision department on the basis of their risk analysis systems, which give significant weight to the size of firms. In practice, this means that there tends to be a focus on those firms that account for a significant market share, in terms of assets and number of customers. However small firms could be selected for on-site inspection, as a result of the off-site monitoring and both Consob and BI provided a few specific examples to that effect.</p> <p>Both Consob and BI inspections are typically broad in scope (and for AMC and IF BI inspections are full scope) and focus on a number of specific topics, which are decided based on the information available via off-site. For Consob, the final decision on the scope of an inspection must be taken at the Chairman level, based on a recommendation from the Inspectorate Division. This decision is translated into a formal letter which establishes the scope and time of the inspection.</p> <p>Consob and BI inspections are intensive and typically take many months to complete.</p> <p>Ad hoc inspections may be undertaken if the circumstances of a particular firm or entity warrant such a process, for example because of emerging problems or on the basis of investor complaints and tips and complaints from other sources.</p> <p>In both BI and Consob, inspections result in detailed written reports which are factual in nature. These are provided to the relevant line supervision area, which analyzes them, draws conclusion about compliance issues and decides on actions to be taken.</p> <p>In the case of BI, the results of the inspections are usually communicated to the entity in a meeting convened by BI to that effect. In such meeting the BI states the key deficiencies found and the main corrective actions expected, along with a deadline for the implementation of such actions. In the case of Consob, the results of inspections are communicated via a formal letter which also states any corrective action that is required. Regulated entities are given opportunity to provide explanations, which might affect the corrective actions requested.</p> <p>The review of files and conversations with the authorities also showed that there is follow up by both Consob and BI on the implementation of corrective actions by the corresponding entity. In this regard regulated entities must submit progress report along with the corresponding supporting information. Depending on the case, Consob and BI might decide to conduct follow up inspections to verify implementation. The</p> |
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assessors were provided evidence to that effect.

BI on-site inspections commenced in 2009–2012

| | 2009 | 2010 | 2011 | 2012 | Total |
|--|------|------|------|------|-------|
| Non-bank investment services providers | 15 | 12 | 10 | 16 | 53 |
| Asset managers | 9 | 10 | 15 | 13 | 47 |
| Total | 24 | 22 | 25 | 29 | 100 |

Source: BI

Consob on-site inspections commenced 2009–2012

Storyline goes here

| Regulated Entity | 2009 | 2010 | 2011 | 2012 | Total |
|---|------|------|------|------|-------|
| Investment Service Providers (Other than AMCs and SICAVs) | | | | | |
| Directly by Consob | 12 | 8 | 8 | 11 | 39 |
| Extensions of BI inspections at the request of Consob (Banks) | 4 | 1 | 1 | 3 | 9 |
| Extensions of BI inspections at the request of Consob (IFs) | 2 | 6 | 1 | 2 | 11 |
| Total for ISPs | 18 | 15 | 10 | 16 | 59 |
| Asset managers | 1 | 4 | 1 | 3 | 9 |
| Regulated markets, MTF, and financial intermediaries (short selling and market abuse) | 3 | | 9 | 4 | 16 |
| Issuers | | | | 1 | 1 |
| Audit firms | 9 | 8 | 3 | 3 | 23 |
| Listed companies (and controlling/controlled entities/related parties) | 3 | 13 | 1 | 16 | 33 |
| Total: | 34 | 40 | 24 | 43 | 141 |

Source: BI

Mechanisms to detect and investigate insider trading and other forms of market abuse

As further explained in Principle 36, Consob uses its IT systems to identify unusual transactions on the markets for which it has regulatory responsibility. Consob also uses a purpose-built system to detect anomalous trading trends in securities markets. If these trends indicate the possibility of market abuse the Market Supervision area refers the matter to the Market Abuse Office (which has a staff of 21) which is responsible for the investigations.

In addition, as will be further explained under Principle 34, RMs and MTFs have also developed market surveillance arrangements to detect market abuse.

Finally, the CL (Article 187 novies), as implemented in Consob Regulation on Markets, requires IFs, AMCs, other authorized entities and market operators to detect and report to Consob suspicious transactions which may indicate market abuse violations. These entities must have adequate internal systems and procedures to enable them to comply with this obligation.

As far as wholesale markets for Government securities are concerned, in addition to market surveillance functions performed by the market management companies, the BI has an autonomous system which stores all market data in order to check market conditions and the orderly conduct of trading.

| | <p>Investor complaints</p> <p>Consob has a Division for Consumer Protection to deal, among others, with investors' complaints. This Division performs a preliminary analysis of the complaints and of the possible action to be taken by Consob. Following that analysis, the complaint is forwarded to the operational unit in charge of the subject matter to follow up the case. It is up to the competent unit to decide whether or not to open an inspection, issue a cease and desist order, etc. While not automatically included in the database that supports its risk-scoring systems, complaints are another input for such scoring.</p> <p>The BI receives numerous complaints about investment services, especially where offered by banks. In some cases, it forwards these complaints to Consob, but more typically responds to investors by providing information about the applicable laws and the competencies and powers of the BI and Consob.</p> <p>Administrative sanctions by Consob and BI</p> <p>Usually the identification of weaknesses via either off-site and on-site supervision prompts a request to the regulated entity to take remedial actions.</p> <p>In the case of Consob the enforcement approach places more emphasis on remedial actions. Consob staff explained that in practice the costs of remedial actions can be even more expensive than any pecuniary sanction that Consob can impose. In egregious cases, however, a sanction can follow the on-site inspection and a couple of cases were provided to that effect. In addition, in such type of cases, Consob may also impose some type of injunctive relief and one case was provided to the assessors where this was done. More often a pecuniary sanction or other type of disciplinary sanction, such as suspension of a person, follows a second on-site inspection.</p> <p>In 2012, Consob completed 172 sanction processes. Of these, 159 resulted in pecuniary sanctions totaling EUR 9.26 million.</p> | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
|---|--|---|---------------------|----------------------------|--------------------|----|-----------|-------------------|---|-----------------------|-----------------------|---|-----------------|---|--|-------------------------------|---------|---|--|----------------------|-----|--|-----------------------|----|---|---|----|-----------|-------------|---|---|-----------------------|---|---------|--------------------------|---|--------|----------------|--|--|
| | <p>Consob Sanctions 2012</p> | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | <table border="1"> <thead> <tr> <th style="text-align: left;">Regulated entity</th> <th style="text-align: center;">Number of sanctions</th> <th style="text-align: center;">Total sanctions (EUR 000s)</th> </tr> </thead> <tbody> <tr> <td>Market abuse total</td> <td style="text-align: center;">11</td> <td style="text-align: center;">EUR 2,570</td> </tr> <tr> <td>• Insider trading</td> <td style="text-align: center;">5</td> <td style="text-align: center;">Plus confiscations of</td> </tr> <tr> <td>• Market manipulation</td> <td style="text-align: center;">6</td> <td style="text-align: center;">total EUR 5,890</td> </tr> <tr> <td>Investment services providers including AMCs and SICAVs</td> <td></td> <td style="text-align: center;">Corporate officers: EUR 1,470</td> </tr> <tr> <td>• Firms</td> <td style="text-align: center;">5</td> <td></td> </tr> <tr> <td>• Corporate officers</td> <td style="text-align: center;">26]</td> <td></td> </tr> <tr> <td>Financial salespeople</td> <td style="text-align: center;">85</td> <td style="text-align: center;">71 disqualifications 13 suspensions 1 pecuniary penalty</td> </tr> <tr> <td>Issuers, shareholders, members of issuers board of statutory auditors</td> <td style="text-align: center;">49</td> <td style="text-align: center;">EUR 4,329</td> </tr> <tr> <td>Audit firms</td> <td style="text-align: center;">5</td> <td style="text-align: center;">EUR 145 Plus 2 suspensions from audit work</td> </tr> <tr> <td>Unauthorized activity</td> <td style="text-align: center;">2</td> <td style="text-align: center;">EUR 230</td> </tr> <tr> <td>Unregistered salesperson</td> <td style="text-align: center;">1</td> <td style="text-align: center;">EUR 15</td> </tr> <tr> <td colspan="3">Source: Consob</td> </tr> </tbody> </table> | Regulated entity | Number of sanctions | Total sanctions (EUR 000s) | Market abuse total | 11 | EUR 2,570 | • Insider trading | 5 | Plus confiscations of | • Market manipulation | 6 | total EUR 5,890 | Investment services providers including AMCs and SICAVs | | Corporate officers: EUR 1,470 | • Firms | 5 | | • Corporate officers | 26] | | Financial salespeople | 85 | 71 disqualifications 13 suspensions 1 pecuniary penalty | Issuers, shareholders, members of issuers board of statutory auditors | 49 | EUR 4,329 | Audit firms | 5 | EUR 145 Plus 2 suspensions from audit work | Unauthorized activity | 2 | EUR 230 | Unregistered salesperson | 1 | EUR 15 | Source: Consob | | |
| Regulated entity | Number of sanctions | Total sanctions (EUR 000s) | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
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| Unregistered salesperson | 1 | EUR 15 | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| Source: Consob | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |

Below are details of sanctions imposed by BI. The main reasons for sanctions were shortcomings in internal controls and in the activity of the board of auditors, supervisory capital deficiencies and incorrect data reporting.

BI sanctions 2009–2012—AMCs

| Year | Number of AMCs | Number of managers and internal auditors | Total sanctions (€ 000s) |
|------|----------------|--|--------------------------|
| 2012 | 7 | 59 | 1,299 |
| 2011 | 6 | 42 | 638 |
| 2010 | 7 | 59 | 1,082 |
| 2009 | 5 | 59 | 764 |

Source: BI

BI sanctions 2009–2012—Nonbank IFs

| Year | Number of Firms | Number of managers and internal auditors | Total sanctions (€000s) |
|------|-----------------|--|-------------------------|
| 2012 | 4 | 33 | 166 |
| 2011 | 5 | 43 | 865 |
| 2010 | 6 | 55 | 713 |
| 2009 | 4 | 32 | 451 |

Source: BI

Criminal prosecution

Prosecution of market abuse (like prosecution of other crimes in Italy) is not centralized in one single office; rather all prosecutors have the authority to hear market abuse cases, if the facts occurred in their jurisdictions or are connected in other ways to their jurisdiction. In practice, most cases are heard by the Office of Milan, due to the fact that the *Borsa Italiana* is located in Milan. Official estimate that roughly 95 percent of market abuse cases are prosecuted by the Milan Office.

The Office has more than 100 prosecutors to cover all type of cases. There is a section specialized in economic crime, which includes market abuse cases. Twelve prosecutors are dedicated to such type of cases.

The bulk of the “complaints” received by this office are tax related and a significant number are also AML related. The number of “complaints” related to market abuse is more limited. For example in 2011 they had 128 cases. Referrals by Consob are a very important source to start an investigation. In 2012, nine reports were made to prosecutorial authorities as part of investigations into insider trading (two reports) and market manipulation (seven reports). Twenty-seven arraignments followed from these referrals.

Below is a list of criminal cases related to insider trading and market manipulation. It includes cases where Consob has been party to the procedure; thus it might not constitute a full list of cases. As can be seen in the information below, the criminal authorities indicated that settlement is used frequently, as officials focused on getting

the money back. The settlement is on the penalty not the evidence. In the case of convictions, the years of imprisonment are kept at a level that allow for conditional execution (i.e., the person does not suffer jail).

Criminal Cases in Connection to Insider Trading and Market Manipulation

| Criminal cases in connection to insider trading and market manipulation | | | |
|---|-----------|------------------------------|--|
| Year | No. cases | Crime | Outcome as of 31 December 2012 |
| 2004 | 2 | Market man. | 2 settlements 1 judgment of conviction 1 acquittal for "prescrizione" (statute of limitation/lapse of time) |
| 2005 | 6 | Insider Trad. Market man. | 4 judgments of conviction 3 settlements 3 judgments of non-suit |
| 2006 | 9 | Insider Trad. Market man. | 4 judgments of conviction 6 settlements 3 judgments of acquittal 1 acquittal for "prescrizione" (statute of limitation/lapse of time) |
| 2007 | 12 | Insider Trad. Market man. | 4 judgments of conviction 5 settlements 2 acquittal for "prescrizione" (statute of limitation/lapse of time) 1 judgment of non-suit 2 judgments of acquittal |
| 2008 | 5 | Insider Trad. Market man. | 1 judgment of conviction 1 settlement 1 acquittal for "prescrizione" (statute of limitation/lapse of time) 3 judgments of acquittal |
| 2009 | 1 | Market man. | 1 judgment of conviction |
| 2010 | 3 | Insider Trad. Market man. | 1 judgment of conviction 1 judgment of acquittal |
| 2011 | 6 | Market man. | 1 settlement 1 acquittal for "prescrizione" (statute of limitation/lapse of time) |

Source: Consob

Officials mentioned the need to preserve the independence of the prosecution function vis-à-vis the government, including in regard to its self-organization, as a key issue to ensure effective enforcement. Resources are also mentioned as a challenge, in particular a lack of support staff.

Compliance Systems

As indicated under principle 31, BI and Consob Regulation of October 28, 2007 provides for specific rules on ISPs governance, internal audits, compliance and internal controls. Intermediaries must establish and maintain permanent, effective, independent functions controlling conformity with regulations and in line with the principle of proportionality, business risk management and internal audit. These functions must have the authority, resources and competence necessary to carry out their duties; the managers must not be hierarchically subordinate to the managers of the department being controlled and must be appointed by the management body.

Pursuant to the allocation of responsibilities between Consob and BI, supervision of obligations related to the monitoring of compliance with regulations corresponds to Consob. Such supervision is conducted via a mix of off and onsite activities.

Measures against regulated entities for failure to supervise employees

Consob and BI have broad enforcement powers over regulated entities, including the power to order corrective actions and impose sanctions. Directors, managers and

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| | <p>controllers (responsible for the surveillance function) are responsible for ensuring that intermediaries comply with securities laws. Therefore they can be held responsible in the event of breaches of laws and regulations. As indicated under Principle 11, legal entities cannot be subject of pecuniary sanctions, although they are jointly and severally liable for payment of a sanction imposed on an employee.</p> |
| Assessment | Partly Implemented |
| Comments | <p>The grade stems mostly as a result of concerns regarding the effectiveness of the current enforcement framework, as will be described below.</p> <p>The limited use of on-site inspections, and how this can affect both supervision and enforcement, is also an issue of consideration; however the concerns of the assessors in this area are mitigated by the robust off-site arrangements, not only because of their sophistication (in terms of the granularity of the information received), but in terms of the type of interventions that they have triggered. Moreover, it is noted that the coverage of on-site inspections (in terms of assets and clients) is very high and that altogether the authorities' current approach has delivered an adequate level of supervision.</p> <p><i>Enforcement</i></p> <p>The assessors' review of files shows that, when material misconduct is detected, both Consob and the BI are thorough in the investigation of it and follow a detailed process to ensure evidence is gathered in a way that supports enforcement action. Comments from market participants support this perception.</p> <p>Because of the intensity of the process, Consob's on-site inspections take a considerable time (there are examples of inspections lasting up to a year). This means that there can often be a long time between the commencement of an inspection and the time decisions are made to order remedial actions or impose sanctions. The files reviewed suggest that Consob's general approach has been to provide ample time to banks and IFs to take remedial actions (sometimes a year during which there is a back and forth of letters) and to impose sanctions only if, after a second inspection, the findings from the inspection show that remedial actions have not been appropriately implemented. Overall this means that both remedial and sanctioning actions take a long time. This raises the question of whether sanctions at an earlier time might have been a more effective way of bringing to the attention of the firm the need for prompt action.</p> <p>In addition, the sanctions imposed are low. This is an issue that is outside of the control of Consob, as in areas of Consob's exclusive competence such as market abuse the amount is high and, in any case, the range of the sanctions stem from the law. Furthermore, the review of enforcement files showed that the courts have in some cases reduced the amount of the fines originally imposed by Consob. However, the level of sanctions does have a clear impact on their effectiveness as a deterrent tool.</p> <p>In the case of BI, the cases discussed also revealed that BI provides ample time for entities to take remedial actions. BI staff explained that in a prudential setting, such time is necessary as actions usually require finding a new shareholder to provide additional capital, which can be difficult especially in the current environment of distress in the financial sector. In the case of BI, however, the cases discussed suggest that it can impose sanctions as a result of a first inspection, and therefore within tighter deadlines.</p> <p>As for criminal enforcement, the conversations with the criminal authorities and data</p> |

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| | <p>provided showed a strong preference to settle cases. Even when convictions take place imprisonment is rare, as in most cases the sanctions stay within the range that allows for conditional execution, which altogether detract from their deterrent effect.</p> <p>The assessors acknowledge that the ultimate objective of an enforcement framework is to affect behavior. To this end, supervisory authorities should have at their disposal a wide variety of tools from corrective actions to sanctions, including criminal offenses. Furthermore there is no ex-ante formula in regard to what should be the appropriate balance on the use of such tools.</p> <p>In the assessors' view, however, use of the sanctioning power is critical for maximizing the deterrent effect of regulatory intervention, and signals the regulator's willingness to pursue breaches to the market as a whole in a clear and effective way. Remedial actions by themselves may not provide sufficient incentives for intermediaries to adjust their behavior at an early stage, and may result in firms waiting until the regulators formally intervene to adjust their practices. This is the area where pecuniary sanctions on both legal entities and individuals play a key role, and in particular criminal enforcement.</p> <p>For this purpose, sanctions need to be of sufficient significance; otherwise they could be subsumed easily in the cost of doing business. That is why criminal convictions, in particular imprisonment should also be part of an effective enforcement regime. However as explained above the current enforcement regime has important limitations that detract it from delivering this deterrent effect, as pecuniary sanctions for breaches other than market abuse/short selling violations are limited both in the number and the level, and criminal sanctions, in particular imprisonment is not used. The assessors acknowledge however, that the majority of these limitations are outside of the control of the regulatory authorities and stem from the law and judicial practices. Thus strengthening of the legal framework should help to address some of these limitations.</p> <p>The assessors encourage the authorities to continuously monitor their approach to enforcement, to ensure that the right mix of tools is used. Finally, the authorities should work with the Government and prosecutorial authorities to identify and remove obstacles to effective use of the criminal law in the securities markets.</p> <p><i>Supervision</i></p> <p>Off-site supervision by both Consob and the BI is very robust as are the information and analysis systems that support it. Risk analysis in both authorities is sophisticated and draws on extensive quantitative and qualitative information. This enables much supervision work to be done off-site, to a greater extent than can be achieved in many other jurisdictions. The information provided to assessors showed that off-site work leads to active intervention from the authorities, mainly in the form of letters and convening of meetings with the board and management of regulated entities. In addition, the off-site scoring systems are a key input to select the firms that are subject to on-site inspections.</p> <p>Inspections are used on a more limited basis. The tables included in the description showed that vis-à-vis the number of regulated entities the coverage is limited; however, in terms of market share (measured by assets and number of clients) the coverage is very high. In addition, the information provided by the authorities showed that in both cases firms classified as high risk (even if they were not big) were selected for inspection. Where on-site inspections occur, the assessors saw good evidence that they are carried out in a very thorough and professional way and often result in the ordering of corrective actions. From the files reviewed and conversations held, it seems that on-</p> |
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| | <p>site inspections lead more frequently to sanctions, though cases were shown where off-site work has led directly to sanctions.</p> <p>The assessors acknowledge that no system is expected to achieve a zero risk environment, which in the context of supervision and enforcement means that no system is expected to eliminate the risk of breaches of laws or even fraud. Therefore, the balance between off-site and on-site work is a reflection of the risk appetite of the regulatory agencies. However, in the assessors' view, on-site inspections are a critical tool for ensuring that the regulator has an active presence in the market place, and that poor conduct both at firm and industry level is detected and dealt with. Signals of such poor conduct do not usually manifest in regular reporting by firms, and emerge only in a partial way through indirect means such as complaints or other intelligence. On-site inspections are a better tool to uncover poor conduct practices, as supervisors are able to look through individual investors' files to see how obligations are being complied with in practice. A similar argument could be made in connection with prudential requirements, as on-site inspections are a better tool to detect operational risks, including weaknesses in governance, internal controls and risk management. This also applies to the connection between prudential requirements and conduct obligations, as on-site inspections can reveal to what extent internal compliance and other control procedures are in fact working in accordance with a firm's formal documented procedures. This is particularly important in critical conduct areas such as selling practices and compliance with suitability requirements, and transparency to clients. The experience of Consob and BI with on-site inspections fully supports this argument, as in both cases on-site inspections have been effective in revealing weaknesses and irregularities, and therefore have more often been followed by sanctions than off-site work. In the discussions held, BI staff concurred on the desirability of an expansion of the coverage of their on-site inspection program, for similar reasons as those stated above; they maintained however that the current balance between off and on site controls is able to ensure an effective supervision.</p> <p>As a result, the assessors consider that although altogether the current approach has delivered an adequate level of supervision, it needs to be complemented with additional on-site inspections. Furthermore, the assessors note that both Consob and the BI have plans to introduce shorter, more sharply focused, inspections as a way of increasing the number of inspections they carry out. BI carried out the first two short visits in march 2013. This would be a welcome development if it is used alongside the current practice of intensive, broad scope inspections.</p> |
| Principles for Cooperation in Regulation | |
| Principle 13. | The regulator should have authority to share both public and non-public information with domestic and foreign counterparts. |
| Description | <p>Domestic information sharing and co-operation</p> <p>Article 4 of the CL requires Consob, BI, COVIP and IVASS to cooperate and exchange information and otherwise for purpose of facilitating their respective functions. Such authorities may not invoke professional secrecy in their mutual relations.</p> <p>As described under Principle 1, the CL emphasizes the need for effective cooperation between Consob and the BI as the authorities responsible for securities markets regulation. It requires the BI and Consob to co-operate in a co-ordinated manner, with the view to minimizing the costs incurred by supervised intermediaries.</p> <p>There are no limitations on the type of information that can be shared with other</p> |

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| | <p>domestic financial regulators insofar as the information is necessary to enable the recipient regulator to perform its functions and all information held by an authority can be shared with the other authorities.</p> <p>No external approval is required for information to be shared in this way.</p> <p>International information sharing and cooperation</p> <p>Under Article 4(2) and (3) of the Consolidated Law, Consob and the BI may exchange confidential information they hold or search for information at the request of a foreign regulator (this applies to both EU and non-EU regulators). Article 4(7) provides that Consob and the BI may also exercise the powers conferred on them by law for the purpose of co-operating with other authorities and at their request. This means that Consob and BI may activate their own compulsory powers, if necessary, to collect information or the documents required by a foreign authority without the need for them to have an independent interest in the matter. There are no limitations on the subject matter of information that Consob and the BI may provide to foreign regulators. This means that information about surveillance, investigation and enforcement activities, authorization, regulated entities, markets and listed companies can be provided to foreign regulators.</p> <p>Consob's ability to provide information to foreign regulators has been assessed as part of the screening process under the IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (IOSCO MMoU). Consob is a signatory to that agreement.</p> <p>No external approval is required in order to exchange the information. The decision whether to accept a request for cooperation and the ways in which the information is collected (on a voluntary basis, by activating compulsory powers, etc.) is entirely a matter for Consob and the BI.</p> <p>Unsolicited information</p> <p>Information can be provided on an unsolicited basis. The provision of unsolicited assistance is also a principle under EU legislation (see in particular Directive 2003/6/EC and Directive 2004/39/EC).</p> <p>No requirement for breach of domestic laws</p> <p>There are no pre-conditions to the provision of information under Article 4 (2) and (3) of the Consolidated Law and no requirement that that conduct that is the subject of a request for information be treated as a crime or an illegality under Italian law; that is, there is no dual criminality or dual illegality requirement.</p> <p>Bank account information</p> <p>Any information held or acquired in response to a request can be provided, including information about bank accounts.</p> <p>Confidentiality</p> <p>Article 4(4) provides that information received by the BI and Consob through an exchange of information with a domestic or foreign regulator must not be transmitted to third parties or other Italian authorities, including the Minister of the Economy and Finance, without the consent of the authority that originally supplied it.</p> |
| Assessment | Fully implemented |

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| Comments | |
| Principle 14. | Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts. |
| Description | <p>Power to enter into information sharing agreements</p> <p>There are no restrictions imposed by domestic law on the ability of Consob and the BI to enter into information-sharing agreements, in application of Article 4 of the Consolidated Law and Article 7 of the Consolidated Law on Banking.</p> <p>Information sharing mechanisms</p> <p>Consob is a signatory to the IOSCO MMoU. It is also a signatory to the Committee of European Securities Regulators (now ESMA) Multilateral MoU and the Boca Raton Declaration on the supervision of futures markets. In addition, it has entered into a large number of bilateral MoUs with other securities and financial services regulators dealing with the exchange of information for enforcement purposes.</p> <p>Confidentiality</p> <p>Under Article 4, paragraph 5 bis, of the Consolidated Law, the exchange of information with authorities of non-EU countries is subject to the existence of provisions concerning professional secrecy. The recipient authority may use the information provided to perform its own supervisory functions including assisting or conducting administrative, civil or criminal proceedings for enforcement purposes.</p> <p>Consob verifies that the recipient authority is able to maintain confidentiality of the information transmitted by Consob consistent with the permissible use of the information under the relevant MOU.</p> <p>There are no other specific or general provisions of Italian laws rules or regulations, which restrict or limit the use by foreign authorities of information and documents provided by Consob in so far they are used to perform supervisory or enforcement functions as referred to above.</p> <p>Practice</p> <p>All requests for cooperation go through Consob's International Relations Office. There is good evidence of Consob's exchange of information with foreign regulators. For example, in 2011 it received and acted on 95 requests from foreign authorities (91 in 2010). It devotes significant resources to meeting these requests. In turn, Consob made 85 requests for information to foreign counterparts (77 in 2010).</p> |
| Assessment | Fully implemented |
| Comments | |
| Principle 15. | The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers. |
| Description | <p>Assistance to foreign regulators</p> <p>Any information that Consob holds or can acquire through the use of its powers (described under Principle 10) can be shared with foreign regulators. This includes books and records that permit the reconstruction of securities and derivatives transactions and records of funds and assets transferred into and out of banks accounts</p> |

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| | <p>relating to securities and derivatives transactions.</p> <p>If documentary evidence has to be acquired, Consob will use its power to require persons or entities which hold the information to produce the necessary records. It can also obtain records by means of an on-site inspection.</p> <p>It can also use its power to formally interview persons and can share the written record of these interviews with foreign counterparts.</p> <p><i>Court orders</i></p> <p>Consob can assist a foreign regulator to obtain court orders on behalf of a foreign regulator. It has done so, for example, in relation to the freezing of assets requested by a foreign regulator.</p> <p>No requirement for independent interest</p> <p>As noted under Principle 13, the use of Consob’s powers to compel the production of documents or to require persons to provide information does not require Consob or any other domestic authority to have an independent interest in the subject of a foreign regulator’s request for information.</p> <p>Information on regulatory processes</p> <p>Consob can provide information about regulatory processes, including the authorization process, investigations in progress and sanctions imposed.</p> <p>If information is held by other domestic authorities, Consob assist by asking the relevant authority on a foreign counterparty’s behalf or by facilitating contact with the relevant authority.</p> <p>Financial conglomerates</p> <p>Article 12 of the CL governs the supervision of groups. It enables Consob and the BI (within the scope of the respective authority) to request information and perform on-site inspections of persons and entities belonging to the same group. The information gathered through these processes can be shared with foreign regulators.</p> <p>Information from other domestic authorities</p> <p>Consob can seek information requested by a foreign regulator from other domestic authorities and as noted under Principle 10, the legislation requires cooperation between them. In addition, Consob can ask the Finance Police (the <i>Guardia di Finanza</i>) to seek information and conduct inspections on its behalf. It has on several occasions used this route to obtain information on behalf of foreign regulators.</p> <p>Practice</p> <p>Based on the files examined and cases discussed, the assessors conclude that CONSOB has been active in collecting information on behalf of foreign regulators that is not in its files. CONSOB staff estimates that roughly ten percent of its resources from the enforcement division are dedicated to meet international cooperation requests.</p> |
| Assessment | Fully implemented |
| Comments | |
| Principles for Issuers | |
| Principle 16. | There should be full, accurate and timely disclosure of financial results, risk and other |

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| | information that is material to investors' decisions. |
| Description | <p>General approach to disclosure obligations</p> <p>Overall the Italian legal framework differentiates disclosure obligations based on three categories:</p> <p>Issuers of securities subject to public offering: they are subject to a first level of disclosure requirements, which comprise the submission of a prospectus in accordance with EU legislation;</p> <p>Issuers of securities widely distributed among the public: in addition to the prospectus, these issuers are subject to a set of periodic and ongoing disclosure obligations;</p> <p>Issuers with securities admitted to trading in a RM: in addition to the prospectus, these issuers are subject to a more comprehensive set of disclosure obligations on a periodic and ongoing basis in accordance with EU legislation.</p> <p>Issuers with securities admitted to trading in a MTF that do not satisfy any of the conditions listed above would be subject to the disclosure obligations concerning inside information and to the additional obligations imposed by the listing requirements of such MTF.</p> <p>Finally it is important to note that by virtue of the Italian Civil Code all companies are required to prepare an annual report, which includes financial statements.</p> <p>Consob staff informed that in practice there are virtually no issuers that have made a public offering and do not fall under one of the categories under (ii) and (iii) above. Furthermore most of the issuers that have made a public offering fall under category (iii). In this regard, staff informed that at the time of the assessment there were 73 issuers on the category of "widely held," 71 of them were equity issuers (and 8 of them also had issued debt) and 2 were debt issuers. The list is available in Consob's website. The staff also emphasized that 90 percent of issuers of widely held securities are small "cooperative banks" and, thus, the outstanding amount of widely held securities is very limited compared to the amount of securities traded on RMs.</p> <p>As for the corporate bond issuers, Consob staff indicated that the vast majority of them were either (i) large corporations listed themselves on RMs or (ii) banks listed themselves on RMs (more than 90 percent or, in very limited cases, (iii) widely held banks subject to additional obligations stemming from the banking regulation. In addition, from a distribution perspective, banks (and more generally distributors of illiquid products) were also subject to disclosure obligations vis-à-vis the clients to which they placed their bonds, in particular the obligation to explain the product, and to provide them at least once a year with the fair value of the bond even if not listed.</p> <p>Finally staff indicated that in the context of Italy securitization offerings take place through private offerings.</p> <p><i>Public offerings of securities</i></p> <p>Rules applicable to public offers and admissions to trading are set out in the CL and Consob Regulation 11971/1999 which transpose EU Directive 2003/71/EC (the Prospectus Directive).</p> <p>Persons who intend to make a public offering must give advance notice to Consob attaching the prospectus to be published (Article 94 of the CL), unless one of the exemptions in Article 100 of the CL applies. These exceptions include: (i) offers</p> |

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| | <p>exclusively aimed at professional investors, (i) offers made to a very limited number of persons defined by Consob, (ii) offers that do not exceed the amount established by Consob by regulation, (iii) offers involving Italian government debt or of EU member countries, or the EC, or central banks of EU countries, (iv) debt offers issued in a continuous or repeated manner by banks but only if they are covered by the depositor guarantee scheme, and (v) money market instruments issued by banks with a maturity of less than 12 months.</p> <p>The prospectus must be drawn up in accordance with detailed models set out in the European Prospectus Regulation (for financial products other than securities, models are set out in Consob Regulation 11971/1999). The prospectus must contain all the information necessary for investors to make an informed assessment of the issuer's assets and liabilities, profit and losses, financial position and prospects and of the financial products and related rights (Article 94 of the CL).</p> <p>All prospectuses must contain a brief summary in non-technical language of the key information, highlighting the risks associated with, and the essential characteristics of, the offering.</p> <p>A prospectus must contain the information required by the European prospectus regulation (809/2004/EC), including full details about the issuer and its activities and the risks of investing in the securities offered.</p> <p>The EC prospectus regulation and Consob Regulation 11971/1999 provide that financial information included in prospectuses must be up to date. Audited financial information in the prospectus cannot be older than 18 months from the date of the prospectus; unaudited information cannot be older than 15 months. Any quarterly or half yearly information since the date of the last audited financial statements must be included in the prospectus.</p> <p>Pursuant to article 94 bis Consob must verify the accuracy, the consistency and comprehensibility of the information contained in the prospectus. After the filing of the draft prospectus by the issuer or offeror, Consob has ten days to respond if the issuer has securities already listed or offered to the public, and twenty days in other cases (Article 8 of Consob Regulation 11971/1999). Consob may:</p> <ul style="list-style-type: none"> • approve the prospectus; • require issuers, offerors and other persons and entities involved or who are intermediating the placement to provide additional or different information; • refuse to approve the prospectus when it does not comply with regulation and when additional information required has not been provided; • suspend the public offering as a precautionary measure (for a maximum of ten consecutive working days in case of offering concerning EU financial instruments or ninety days in case of other financial products) in the event of a well-founded suspicion of violation of the applicable regulations; • prohibit the public offering in the event of ascertained violation of the applicable regulations, or if there are grounds to suspect such violation • make public the fact that the offer fails to meet obligations • request the exchange to suspend trading on a RM for as period not exceeding 10 days if there are grounds to suspect violation of the applicable regulations or request the exchange to prohibit trading on a RM in the case of confirmed violation. <p>An approved prospectus must be filed with Consob and made available to the public as</p> |
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| | <p>soon as possible on the web site of the issuer or distributors, by publication in newspapers, or on the premises of the offeror, of the issuer and of the financial intermediaries involved in the placement. In any case, it must be provided free of charge if requested by investors (Article 9 of Consob Regulation 11971/1999).</p> <p>Any significant new factor, material mistake or inaccuracy relating to the information included in the prospectus requires a supplement to the prospectus (Article 94(7) of the CL). A supplement must be approved by the Consob in a maximum of seven working days and published by the same means adopted for the publication of the original prospectus.</p> <p><i>Responsibility for information in prospectuses</i></p> <p>Under Article 94 (8) of CL, the issuer, offeror, any guarantor (as applicable) and the persons responsible for the information contained in the prospectus, is liable, each in relation to the extent of their own duties, for damages caused to the investor placing reasonable faith in the truth and accuracy of information contained in the prospectus. A due diligence defense applies.</p> <p>The Italian Civil Code also provides general provisions permitting anyone who suffers an “unjust damage” to obtain restitution in a civil court (Article 2043). Article 2621 provides criminal penalties for false corporate disclosures.</p> <p>Violation of disclosure obligations can be dealt with by imposing administrative sanctions (see article 191 of the CL).</p> <p>Article 173 bis of CL provides for criminal sanctions for intentional false disclosures in prospectuses or otherwise in connection with a public offering or admission to trading.</p> <p><i>Derogations of disclosure obligations</i></p> <p>Article 7 of Consob Regulation 11971/1999 stipulates that only in exceptional cases and without prejudice to the general disclosure obligation in Article 94(2) of the CL, Consob may, at the request of the issuer or the offeror, exclude the publication of some of the information otherwise required. The circumstances are limited to the following:</p> <ul style="list-style-type: none"> • communication of the information is against the public interest; • communication of the information would cause serious damage to the issuer, provided that the omission would not be likely to mislead the public; • the information is less important for the specific offer and is not such as to influence the assessment of the financial position and prospects of the issuer, offeror, or any guarantors. <p>These exceptions are in line with the European prospectus directive. In practice, Consob uses its exemption power only on rare occasions.</p> <p><i>Advertising</i></p> <p>Under Article 101 of the CL requires documentation relating to any form of advertisement concerning a public offering to be filed with Consob at the same time of its dissemination. Advertisements must comply with provisions set out in Consob Regulation 11971/1999 requiring advertisements to be accurate and be consistent with prospectus contents. Article 34 <i>octies</i> of the Regulation requires advertising to be clearly recognizable as such. The information contained in the advertisement must be accurate and not be misleading about the features, nature and risks of the financial products</p> |
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| | <p>offered and the related investment.</p> <p>Consob has the power to:</p> <p>suspend further dissemination of an advertisement as a precautionary measure (for a maximum of ten consecutive working days in case of offering concerning EU financial instruments or ninety days in case of other products) in the event of a well-founded suspicion of violation of the provisions of the article or the related regulations;</p> <p>to prohibit the further dissemination of an advertisement in the event of an ascertained violation; and to prohibit the making of the public offering in the event of failure to comply with the above precautionary measures.</p> <p>Violations can be dealt with by imposing administrative sanctions (see article 191 of the CL).</p> <p><i>Periodic and Ongoing Obligations for issuers admitted to trading on a RM (Equity and Debt)</i></p> <p><i>Annual reports</i></p> <p>The Italian Civil Code requires all companies to approve and publish annual financial statements, including consolidated reports where applicable. According to article 154 ter of the CL, implementing Transparency Directive, the issuer of securities admitted to trading in an RM and that have Italy as their home state, must present their annual report to the annual meeting within 120 days of the end of each financial year and make it public at least 21 days before the meeting. The annual report must contain:</p> <ul style="list-style-type: none"> • audited financial statements; • a management report prepared by the directors; • a statement from those responsible about the accuracy of the financial and management reports. <p><i>Half yearly reports and quarterly reports</i></p> <p>Issuers of shares or debt admitted to trading on RMs must also prepare and publish half-yearly reports and quarterly statements (Article 154 ter of the CL).</p> <p>Half-yearly financial reports covering the first six months of the financial year must be prepared within 60 days of the relevant period. Reports contain:</p> <ul style="list-style-type: none"> • a condensed set of financial statements, prepared in accordance with the rules governing annual and consolidated accounts; • an interim management report prepared by the directors; which must include at least information on the more significant events occurring during the period and their impact on the semi-annual statements, together with a description of the main risks and uncertainties. Information on significant related party transactions must also be included; • a statement of responsibility. <p>Quarterly interim management statements must be published within forty-five days of the end of the first and third quarters of the financial year. They must contain:</p> <p>(i) a general description of the financial position and economic outlook of the issuers and its subsidiaries; (ii) an explanation of material events and transactions that have taken place during the relevant period and their impact on the financial position of the</p> |
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| | <p>issuer and its controlled undertakings.</p> <p><i>Material event disclosure</i></p> <p>Article 114 of the CL (implementing the European Market Abuse Directive) and Article 66 of Consob Regulation no 11971/1999 require issuers admitted to trading in a RM and their controlling shareholders to disclose promptly to the market inside information. "Inside information" is information of a precise nature which has not been made public and which, if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivative financial instruments.</p> <p>Consob Regulation (Article 66) requires issuers admitted to trading in a RM and their controlling shareholders to promptly publish a press release containing the essential information in a form permitting a complete and accurate assessment of the effect the information is likely to have on the price of the issuer's securities. The press release must be delivered simultaneously to:</p> <ul style="list-style-type: none"> • the market management company of the relevant RM, which must immediately disseminate it to the public, • the media and the issuer's website, and • Consob. <p>The Borsa Italiana S.p.A disseminates the information to market participants via a centralized system managed called NIS (Network Information System). The NIS also stores the information.</p> <p>Consob may require the issuer, the controlling shareholder, the holders of major holdings and corporate officers to disseminate to the public additional information, if necessary. Normally these additional requests are aimed at clarifying the characteristics and the financial impact of the price sensitive events announced to the public.</p> <p>Under article 114(3) of the CL, issuers admitted to trading in a RM and their controlling shareholders may under their own responsibility delay the public disclosure of inside information in the cases and under the conditions established by Consob in a regulation, provided that such delay would not be likely to mislead the public with regard to essential facts and circumstances and that such persons are able to ensure the confidentiality of the information.</p> <p>Article 66 bis of Consob Regulation 11971/1999 sets out the circumstances where such a delay may be permitted. Delay may occur where the public disclosure of inside information may jeopardize the carrying out of an operation by the issuer or may, for reasons connected with the insufficient formulation of the events or circumstances, lead to incomplete assessments by the public. Such circumstances must comprise at least the following:</p> <ul style="list-style-type: none"> • negotiations in process, or related elements, where the outcome or normal pattern of those negotiations would be likely to be affected by public disclosure; • decisions taken or contracts made by the management body of an issuer which need the approval of another body of the issuer, other than the shareholders' meeting, in order to become effective. <p>Issuers must inform Consob of the delay, indicating related circumstances. Consob may</p> |
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| | <p>require an issuer to disclose the information if the reasons for the delay are not well grounded.</p> <p><i>Periodic and Ongoing obligations for issuers whose securities are widely held (Equity and Debt)</i></p> <p>Securities that are not listed in a RM but are widely distributed to the public are subject to the provisions of article 116 of the CL (described below). The definition of issuers of financial instruments widely distributed among the public is based on quantitative criteria.</p> <p>In particular for issuers of bonds, the definition is based on the number of bondholders (greater than 500) and the aggregate denomination for bonds (at least 5 million euros).</p> <p>For issuers of shares the definition is based on the number (more than 500) of minority shareholders representing at least five percent of the share capital and other quantitative thresholds related to the average number of employees, the total balance sheet turnover, and the shares must comply with other requirements.</p> <p>Such issuers are subject to the following obligations:</p> <p>Submit a prospectus with the same content that an issuer admitted to trading in a RM. The Prospectus must include a special reference to the effect that the issuer does not aim at listing the financial instrument.</p> <p>Make available to the public and Consob their annual audited report, which should have the same content than for issuers admitted to trading in a RM. They are not subject to semi-annual nor quarterly reporting.</p> <p>Disclose to the public and CONSOB inside information. This obligation applies in the same way than for issuers admitted to trading in a RM.</p> <p>Inform the market on the allocation of financial instruments to their corporate officers and employees.</p> <p>Provide information required for the holders of their financial instruments to exercise their rights.</p> <p>Comply with the provisions on related party transactions.</p> <p>CONSOB can exercise on them the same extensive powers than can be exercised against an issuer of securities admitted to trading in a RM under articles 114 and 115 of the CL. This includes the power to require information and documents and to carry out on-site inspections of those issuers, the persons who control them and companies controlled by them, the issuer's corporate officer and the audit firm, and the other powers available to CONSOB under article 187 <i>octies</i> of the CL.</p> <p><i>Periodic and Ongoing Disclosure Obligations for issuers admitted to trading in MTFs</i></p> <p>Disclosure obligations established in the CL do not apply to issuers who are admitted to trading in an MTF only. In such cases disclosure obligations stem only from the listing rules of the respective market.</p> <p>In the case of AIM, the only MTF for equity markets, the main disclosure obligations are:</p> <ul style="list-style-type: none"> • an admission document, which is more abbreviated than a prospectus, but must which overall must be prepared following Annex I,II and III of the Prospectus Regulation; • annual audited financial statements which must be submitted not later than six |
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| | <p>months after the end of the fiscal year. The accounts must be prepared according to (i) national GAAP, (ii) International Financial Reporting Standards (IFRS) or (iii) US GAAP;</p> <ul style="list-style-type: none"> • half yearly financial statements which must be submitted not later than three months after the end of the period; • inside information. <p>Shareholder voting decisions</p> <p>The rules relating to information to be made available before shareholders' meetings have been recently amended to transpose EU laws (in particular Directive 2007/36/EC). Under revised Article 125 <i>bis</i> and 125 <i>ter</i> of the Consolidated Act, when a shareholders' meeting is called the directors of the company must publish a prior notice and issue a report on each item on the agenda. The notice and report must be available to the public (including on-line) at least 30 days before the date fixed for the meeting. The CL and Consob Regulation 11971/1999 specify the information that these reports must contain.</p> <p>The Civil Code requires minutes of shareholders' meetings that involve decisions about major transactions (such as mergers and spin-offs, changes to bylaws, capital increases) to be filed with the Company Register, which is publicly accessible. In case of mergers and spin-off additional disclosure requirements apply in accordance with the relevant EU Directives. For issuers admitted to trading in a RM the provisions of the Civil Code are supplemented by further disclosure requirements. In addition, Article 77 of Consob Regulation no. 11971/1999 requires listed issuers to make the minutes of the vote on the annual accounts available to the public. Special rules <i>apply</i> to the decisions concerning related parties transactions (see under Principle 17).</p> <p>Regulatory supervision—Measures available to the Consob</p> <p>As noted above, in the case of public offerings, Consob may suspend the public offering as a precautionary measure and prohibit the offering in case of ascertained violation of the relevant provisions or if there are grounds to suspect such violation (Article 99 of the CL). It may also suspend or prohibit the dissemination of advertisements not in compliance with Consob's regulations and it can prohibit the making of the public offer (Article 101 of the CL). Consob can also impose a range of pecuniary sanctions under the CL.</p> <p>In addition, Consob has a range of other intervention powers in connection with issuers admitted to trading in a RM and issuers whose securities are widely held including:</p> <ul style="list-style-type: none"> • if an issuer fails to disclose inside information or any other information that issuers must publish pursuant to a request from Consob, the relevant information can be published by Consob, at the expense of the issuer (Article 114 of the CL). This provision applies both to issuers of securities listed on RMs and issuers of financial instruments widely distributed among the public. <p>Under Article 115 of the CL Consob can:</p> <ul style="list-style-type: none"> • require issuers admitted to trading in a RM and MTF and issuers of financial instruments widely distributed among the public, the persons that control them and companies controlled by them to provide information and documents • gather information from directors, members of the board of auditors, auditing firms |
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| | <p>and managers of companies listed in paragraph a) above;</p> <ul style="list-style-type: none"> • carry out inspections at the offices of the persons listed in paragraph a) above; • exercise all investigatory powers provided for under Article 187-<i>octies</i>. <p>Article 115 of the CL applies also to issuers of securities of financial instruments widely distributed among the public.</p> <p>Consob can challenge the resolution of the shareholders' meeting or meeting of the supervisory board approving the annual accounts of a listed company on the ground that the accounts fails to conform with the provisions governing their preparation or may request the court verify the conformity of the consolidated accounts with the provisions governing the preparation thereof (Article 157(2) of the CL). Without prejudice to these powers, where it is ascertained that documents comprising the financial statements pursuant to article 154 of the CL do not comply with regulations, Consob may request that the issuer publishes this fact and arrange publication of supplementary information as necessary in order to reinstate correct market information.</p> <p>By virtue of the listing contract, operators of MTFs have "disciplinary" powers over issuers admitted to trading in a MTF. They can suspend or revoke their listing, and they can also impose pecuniary sanctions on them. Consob may request operators of MTFs to provide it with all information deemed useful for the purposes of revoking or suspending financial instruments from trading (article 77-bis of the CL).</p> <p><i>Suspension of trading</i></p> <p>Consob can order the suspension of trading in securities. In particular, it can order that trading be halted in a given securities or in all the securities traded in a RM (Article 74 of CL); it can prohibit organized trading of securities on non-RM (Article 78 of the CL); and it can prohibit public offers of securities (Article 99 of CL). Consob may request operators of MTFs to exclude or suspend financial instruments from trading (article 77-bis of the CL).</p> <p><i>Restrictions on trading by persons with inside information</i></p> <p>The prohibition on insider trading (described under Principle 36) makes it an offence for insiders to trade on the basis of inside information. Consob may exercise all the powers set forth by article 187-<i>octies</i> of the CL for the purposes of investigating and prosecuting market abuse. The provisions on market abuse also apply to financial instruments admitted to trading on Italian MTFs. Moreover, the obligation to disclose inside information also apply to issuers whose securities are widely distributed among the public</p> <p>Consob practice</p> <p><i>Prospectus reviews</i></p> <p>Prospectuses for listed and non-listed equities are reviewed by the Issuers Information Division. This office consists of 8 staff. IPO prospectuses are reviewed by the IPO Office in the Market Division (11 staff). Prospectuses for debt securities issued by regulated intermediaries (primarily banks) are reviewed by the Non-Equity Prospectuses Office in the Intermediaries Division (18 staff).</p> <p>All prospectuses are reviewed in detail before approval. The review focuses on the completeness, consistency and comprehensibility of prospectuses. A prospectus review</p> |
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| | <p>for a listed issuer takes on average about 20 days.</p> <p>In practice, there are comparatively few equity prospectuses (in 2012, 15 equity prospectuses and 3 shelf registrations were approved). By contrast, there were over 1,000 issues of debt products by Italian based issuers in the six months from July to December 2012.</p> <p><i>Material event disclosures</i></p> <p>Compliance with material event disclosure obligations is monitored by the Market Information Office in the Market Division. The Office monitors information about issuer (such as press reports and analysts' reports) and trading on the markets to identify cases where there may be a failure to comply with material event disclosure requirements.</p> <p><i>Review of periodic information</i></p> <p>See Principle 18.</p> <p>Cross border matters</p> <p>Public offerings by non-Italian EU issuers can use the European passport arrangements.</p> <p>Public offerings by non-EU issuers are subject to the regime set out in the Prospectus Directive. The prospectus drawn up in accordance with the legislation of a third country is approved in the EU provided that:</p> <ul style="list-style-type: none"> • the prospectus is in accordance with IOSCO guidance for cross border offerings • the information requirements, including information of a financial nature, are equivalent to the requirements under the Prospectus Directive. <p>The EU Commission is responsible for assessing whether a third country ensures the equivalence of prospectuses drawn up in that country with the Prospectus Directive, by reason of its national law or of practices or procedures based on IOSCO international standards. In 2011, ESMA issued a framework for ensuring consistent application across the EU of the EU Prospectus Directive's third country regime (ESMA/2011/36).</p> |
| Assessment | Fully implemented |
| Comments | <p>The IOSCO Principles require that issuers of public offering or admitted to trading be subject to periodic and ongoing disclosure obligations. The Principles do not impose the condition that the issuer be traded to be subject to periodic and ongoing requirements, nor to be traded in a RM. This contrasts with the current European framework which only subjects issuers admitted to trading on RMs to such disclosure obligations. The assessors note, however, that the Italian legal framework has subjected issuers whose securities are widely held to some ongoing and periodic disclosure requirements.</p> <p>Conceptually this category does not cover all issuers of public offering which are not listed in a RM. However, in practice, the data provided by Consob suggests that all issuers are subject to some level of periodic disclosure. That is because:</p> <p>On the equity side: the issuers would be either admitted to MTA or would be covered by the widely held definition (and there are currently 71 issuers in this category)</p> <p>On the corporate bond side: the bulk of the issuers are (i) large corporations listed in a RM (either for bonds or shares), or (ii) banks also listed themselves in MTA as equity issuers (90 percent) or (iii) a very limited number of banks that would be subject to</p> |

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| | <p>some additional obligations stemming from the banking regulation, and that from the distributions side would be subject to Consob's guidance on illiquid securities discussed above.</p> <p>As per the information above, the category of bond issuers that would not be listed themselves would be extremely limited in number (much smaller than the category of issuers widely held). Thus, it has not been considered significant for the purpose of this assessment.</p> <p>On the other hand the category of issuers whose securities are widely held is largely composed of cooperative banks, i.e., very small banks participated by their clients. In this regard, Consob staff estimated that 90 percent of the issuers in this category are such cooperative banks. Thus, the amount of outstanding shares in this category is limited when compared to the RMs. Therefore this category is not considered significant in size for the purpose of this assessment. The assessors also note that the prospectus of such issuers include a warning stating that the issuer does not intend to list. However, the assessors encourage the authority to align the requirements for this category with the IOSCO Principles, in particular if it were to expand.</p> <p>As for AIM, this market was not considered significant at the time of this assessment due to its size. Therefore it was not taken into consideration for the grade. In any case the assessors note that these issuers are subject also to disclosure of inside information and to both annual and semiannual reporting. However if this market were to grow, then the regime applicable to them should be revisited. In this regard, in the context of the EU proposals in connection with markets for SMEs, the assessors encourage the authorities to review what should be the appropriate balance between investor protection and easing of access to capital for SMEs.</p> |
| Principle 17. | Holders of securities in a company should be treated in a fair and equitable manner. |
| Description | <p>General approach to fair treatment of shareholders</p> <p>Overall three differentiated categories can also be found in the Italian legal framework in connection with the provisions that govern the treatment of shareholders:</p> <p>A basic framework required for all companies. This framework is established in the Civil Code. As will be further described below such framework covers all the obligations established under Principle 17. The only exceptions vis-a-vis the Principles are the rules on notification of substantial and insider holdings, which do not apply to all companies in general but to a subset of them (in any case, they are required to disclose the full list of shareholders on an annual basis pursuant to the Civil Code). The CL sets forth certain provisions on tender offers which apply also to issuers of securities that are not listed on regulated markets or other financial products.</p> <p>A more strict framework which applies to issuers admitted to trading in a RM in accordance with EU legislation: these issuers are subject to stricter requirements in connection with many of the obligations covered by the Civil Code, as well as to additional obligations, including for example in connection with related party transactions and notifications of substantial and insiders' holdings, as well as to the provisions on mandatory tender offers.</p> <p>Companies with widely held financial instruments are subject to only a subset of the stricter obligations that apply to issuers admitted to trading in a RM, such as in connection with related party transactions and disclosure of information necessary to enable the holders of financial instruments to exercise their rights. In this regard the</p> |

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| | <p>notification of insider holdings does not apply to them. Notification of substantial holdings applies but only when there is a change of control. In addition, they are subject to certain provisions on tender offers, but not to the mandatory tender offer obligation, and they are required to disclose the full list of shareholders on an annual basis.</p> <p>Issuers admitted to trading in AIM, the only equity MTF, are subject to a set of additional obligations beyond those established in the Civil Code. <i>Vis-à-vis</i> the IOSCO methodology, they include provisions on tender offer, and notifications of insider and substantial holdings although in a more flexible manner than for issuers admitted to trading in a RM.</p> <p>Accordingly, the description will explain the basic framework that applies to all companies, and in cases where stricter obligations apply to a subset of issuers, the relevant explanations will be made. Requirements for issuers listed in AIM will be included separately.</p> <p>Finally as explained above 71 equity issuers fall under the category of issuers whose securities are widely held. However, the category mostly includes small “cooperative banks”, thus outstanding amount of widely held securities is limited compared to Borsa Italiana’s market capitalization.</p> <p>Rights and equitable treatment of shareholders</p> <p>Article 2348 of the Civil Code establishes that all shares of the same class must confer equal rights. For listed companies, Article 92 of the CL requires listed issuers to guarantee the same treatment to all holders of listed financial instruments whose conditions are identical.</p> <p><i>Voting</i></p> <p>Article 2351 of the Italian Civil Code establishes the one-share-one-vote principle, but company by-laws can depart from that principle up to 50 percent of the issued shares. In cooperative companies each shareholder has only one vote, irrespective of the number of shares owned (Article 2538 of the Italian Civil Code). Consob staff informed that derogations to the principle of one share one vote are not common. The derogation mostly applies to banks set up as <i>banche popolari</i>, which have the legal nature of a cooperative, and therefore follow the one head one vote principle. Currently there are seven cooperative banks listed and one insurance company. There are also a limited number of securities still denominated as “<i>azioni di risparmio</i>” which are basically hybrid form of debt securities (even if called shares they do not grant voting rights but the grant returns).</p> <p>When shares have different rights from those of ordinary shares, the Civil Code (Article 2376) requires that resolutions adopted by the general meeting of shareholders that prejudice the rights of their holders must also be approved by a special meeting of the holders of these shares.</p> <p><i>Elections of directors</i></p> <p>Pursuant to the Civil Code, the approval of directors is a decision that must be made by shareholders. To be elected to the companies governing and control bodies candidates must satisfy integrity and experience criteria.</p> <p>Special rules apply under the CL to issuers admitted to trading on a RM:</p> |
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| | <p>Articles 147-ter and 148 and the relevant implementing Consob Regulation (11971/1999) specify ineligibility and disqualification criteria for directors and members of the internal control body (<i>collegio sindacale</i>) and require that at least one board member (two for bigger boards) and all members of the internal control body meet the independence standards set out in Article 148 of the CL;</p> <p>Special rules apply also to the election of members of the board to ensure that at least one of them is appointed by minority shareholders. In particular, Articles 147-ter and 148 of the CL mandate a “slate voting” mechanism (<i>voto di lista</i>) for the appointment of board members and internal auditors. Under these procedures a least one board member—the chairman, in the case of the internal control body—is selected from a list prepared by minority shareholders and may not linked in any way, even indirectly, to majority shareholders. Companies’ bylaws may establish a higher number of board seats to be reserved to minorities.</p> <p>Italian Law now also provides minimum gender quotas for company boards (Law 120/2011). At least one third (one fifth for the first term) of board seats must be held by directors of the less represented gender. Such provision is subject to a three board terms sunset clause.</p> <p>Special rules apply also to the composition of the board when the issuer is controlled and directed by another issuer admitted to trading in a RM (art. 37 of Consob Regulation n. 16191/2007): at least the majority of the directors of the former issuer shall be independent.</p> <p>The appointment of independent directors is also recommended by the Italian Corporate Governance Code, requiring that an adequate number of directors, and in any case at least two of them, should be independent according to its criteria, which are in line with those set out in the EC Recommendation No. 162/2005. For large caps (companies in the Italian FTSE MIB Index) independent directors should represent at least one third of the board. Borsa Italiana rules require listed companies to report, on a comply or explain basis, with the Code. Furthermore, the CL and Consob Regulation on Issuers impose disclosure obligations on the compliance with the code and the reasons for non-compliance (article 123-bis of the CL and article 89-bis of Consob Regulation on Issuers).</p> <p><i>Fundamental corporate changes</i></p> <p>Changes to the by-laws and other fundamental corporate changes are subject to the approval by an extraordinary shareholders meeting and are determined by special majorities that differ depending on the nature of the resolution (Articles 2368, 2369, 2441, 2443, 2420-ter of the Italian Civil Code).</p> <p>Article 2437 of the Italian Civil Code gives shareholders who did not vote in favor of the corresponding decision, the right to withdraw from the company, to be exercised in the manner and within the time limits established by law, when decisions in particularly important topics are taken, including:</p> <ul style="list-style-type: none"> • significant amendments of the corporate objectives; • transformation of the legal form of the company; • transfer of the registered office abroad; • changes to the criteria for the value assessment of the shares in the event of |
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| | <p>withdrawal;</p> <ul style="list-style-type: none"> • amendments to the by-laws concerning the voting or participation rights; • delisting. <p>Unless the by-laws provide otherwise, a right of withdrawal is also granted to the shareholders who did not concur with the approval of resolutions extending the life of the company; or introducing or removing limitations on share transfers.</p> <p>Moreover, qualified shareholders may challenge shareholders meeting's resolutions before the Court.</p> <p><i>Related party transactions</i></p> <p>Shareholders' approval of related party transactions is not required.</p> <p>However, Consob Regulation 17221/2010 provides rules for these transactions which are applicable to companies admitted to trading in a RM and widely held. In both cases companies must establish their own internal codes for entering into related party transactions and codes must comply with Consob principles. The Regulation covers both disclosure and fairness of related party transactions. Related party transactions must be reviewed by independent directors and different rules apply according to the size of the transactions.</p> <p>Material transactions (in general those that exceed a five percent threshold) must be reviewed by a committee of independent directors, who must be directly involved in the negotiations and receive adequate information from executives. The committee must express its view and the board can only approve a transaction if the committee agrees to it. A circular describing the transaction, its terms and the reason for it must be issued within seven days.</p> <p>Minor transactions must be reviewed by independent directors, but they do not have a veto power. Quarterly disclosure is required for transactions approved despite a negative opinion of the committee.</p> <p>A waiver from procedures and disclosure is provided for related party transactions in the ordinary course of business and entered into on terms equivalent to those that prevail in arm's length transactions. When material, they must be notified to Consob and described in the half year or annual report.</p> <p>Direct involvement of shareholders is limited and residual. Provided that the bylaws allows for it, a material related party transaction which has been rejected by the independent committee can be submitted to the approval of shareholders. The interested party may vote, but for the resolution to be effective it must be approved by the majority of the minority shareholders.</p> <p>The internal control body is in charge of monitoring compliance with this Regulation.</p> <p><i>General meetings</i></p> <p>Under the general law applying to companies, shareholders' meetings can be held only after the publication, at least fifteen days in advance with respect to the date of the meeting, of a notice specifying the day, time and place of the meeting and the agenda.</p> <p>Special rules apply to companies admitted to trading in a RM (Article 125-bis of the CL):</p> |
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- notice of the shareholders' meeting must be published at least 30 days in advance of the meeting on the company's website and disclosed by issuing a press release;
- notice of shareholders' meetings regarding the election of corporate boards must be given 40 days in advance, in order to allow for the presentation of the slates of candidates (by the 25th day before the meeting);
- 21 days' notice must be given for meetings regarding special situations (reduction of capital as a consequence of losses and below the minimum legal threshold, liquidation of the company).

The Civil Code allows companies to make provision in their bylaws for persons to take part in shareholders' meetings by distance communication or postal or electronic votes.

In the case of companies admitted to trading in a RM, if such voting systems are provided for in companies' bylaws, further implementing provisions are specified in the CL and in Consob Regulation 11971/1999, which give effect to of the European Shareholders' Rights Directive (Article 127 of the CL and Articles 140–143-ter of Issuers Regulation).

In companies admitted to trading in a RM, a proxy solicitation which is defined as a request to more than 200 shareholders for proxy to be conferred in relation to specific voting proposals or accompanied by recommendations, statements or other indications capable of influencing the vote are subject to the special provisions of the CL. Article 138 of the CL provides that the proxy solicitation must be performed by a promoter through dissemination of a statement and a proxy form. Articles 135-139 of Consob Regulation 11971/1999 establish rules regarding the transparency and correctness of proxy solicitation.

The proxy statement and the proxy form must be filed with Consob which reviews them all in detail. Article 144 of the CL authorizes Consob to intervene with respect to the proxy statement and the proxy form and to request the insertion of additional information or to establish special procedures for their distribution; it can also intervene with respect to the carrying out of the solicitation/collection of proxies and can suspend or prohibit the activity in case of suspected or ascertained violations of the applicable legislation.

For companies admitted to trading in a RM article 130 of the CL on a general basis for shareholders to have the right to view all the documents filed at the registered office for shareholders' meetings that have been convened and to obtain a copy at their own expense. The minutes of the shareholders' meeting pursuant to Article 2375 of the Civil Code shall in any event be made available on the web site within thirty days of the date of the meeting.

Ownership registration and transfer of shares:

Basic ownership registration and transfer rules exist in the Civil Code.

Under Article 80 and following of the CL and Legislative Decree 213/1998, financial instruments that are traded or are to be traded on a RM must be dematerialized. Transfer of these instruments and of rights attached to them is carried out by means of a book entry system operated by the authorized intermediaries and central securities depositories. This also applies to issuers of financial instruments that are widely

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| | <p>distributed among the public.</p> <p><i>Receipt of dividends and information for the exercise of rights</i></p> <p>Basic provisions in relation to the distributions of dividends and interim dividends exist in the Civil Code (articles 2433 and 2433bis).</p> <p>Article 83 terdecies of the CL provides that, for financial instruments registered in securities accounts, shareholders entitled to receive the payment are those holding the shares at the end of the accounting day indicated by the issuer (the record date), and establishes the methods by which the related payment is made.</p> <p>Consob Regulation no. 11971/1999 (articles 84 and 111) requires companies with financial instruments admitted to trading in a RM or widely distributed to the public to provide the public without delay with information needed for the holders of their financial instruments to be able to exercise their rights. Moreover, issuers of financial instruments admitted to trading on a RM must disclose information on any changes to the rights attached to the financial instruments (article 83 bis of Consob Regulation no. 11971/1999).</p> <p>Tender offers (takeovers)</p> <p>Takeovers are regulated by the CL and Consob Regulation 11971/1999 as amended.</p> <p>In general, a person who makes a cash or exchange tender offer of financial products (including non-listed financial instruments) is required under Article 103(1) of the CL to make the offer at the same conditions to the holders of all financial instruments that are subject to the offer. Article 42 of Consob Regulation 11971/1999 requires the interest parties (the offeror, the issuers, persons linked to them by relationships of control directors, board of auditors and general managers) to act in compliance with principles of proper conduct and equal treatment of those whom the offer is addressed and to refrain from carrying out transactions on the market with a view to influencing acceptances and to abstain from conduct and agreement aimed at altering the circumstances affecting the conditions of the mandatory tender offer.</p> <p>In addition, Italian issuers of financial instruments admitted to trading on Italian RM are subject to the provisions on mandatory takeovers provided for by articles 105 and following relevant provisions of the CL. In particular, pursuant to article 106 of the CL any person who comes to hold, as a result of purchases, an interest of more than 30 percent of the voting shares in an Italian company with ordinary shares listed on an Italian RM must make a tender offer for all remaining shares. The offer must be made within 20 days of the acquisition.</p> <p>Article 106(2) provides that the price offered must be no less than the highest price paid by the bidder, and by persons acting in concert with the bidder, in the twelve months prior to issue of the notice of takeover for securities of the same class. If no purchase against payment of securities of the same class was made in the period indicated, the takeover bid is implemented for that class of securities at a price no less than the weighted market average over the previous twelve months or shorter available period.</p> <p>A similar obligation to make a complete tender offer exists in the case of consolidation of a holding between 30 percent and majority control of the company concerned, as well as an obligation to acquire the outstanding shares (upon request of the relevant holder) in any person who comes to hold more than 90 percent if the issuers shares and</p> |
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| | <p>does not intend to restore the free float to ensure regular trading in the shares.</p> <p>Article 40 of Consob Regulation 11971/1999 provides that the offer period must be between 15 to 25 for mandatory offers, and between 15 and 40 days for voluntary offers. Consob can extend the time by up to 25 days.</p> <p>Article 102(1) of the CL—applicable to all takeovers, including voluntary takeovers—requires the bidder to give notice to Consob and the public of the bid. Article 37(1) of Consob Regulation 11971/1999 specifies the information that must be given to the market and the issuer, including:</p> <ul style="list-style-type: none"> • the bidder and its parent companies; • the persons acting in concert with the bidder on the offer; • the issuer; • the category and quantity of financial products in the offer; • the price offered for each category of financial products in the offer, as well as the overall consideration of the offer; • the reasons for the bid and, where applicable, the event from which the obligation to make a bid arose; • the intention of revoking the financial instruments concerned by the offer from trading; • the conditions the bid is subject to; • the shareholdings, including derivative financial instruments conferring a long position in the issuer held by the bidder and by the persons acting in concert; • the website where the press releases and documents relating to the bid will be published. <p>Consob has prescribed a model bid statement setting out the details that the offeror must include.</p> <p>Consob approves the bid document prior to the offer and may require supplementary information to be provided (Article 38(1) of Consob Regulation 11971/1999).</p> <p>Article 103(3) of the CL—applicable to all takeovers, including voluntary takeovers—requires the board of the target issuer to publish a notice containing all information useful to evaluating the bid and its own evaluation of the bid. For companies with a two-tier structure, the notice must be approved, jointly if necessary, by the control body and supervisory council. Article 39 of Consob Regulation 11971/1999 sets out the minimum content of the target company's statement. Consob reviews the target company statement ex-post.</p> <p>For companies admitted to trading in a RM, article 104 of the CL prohibits Italian companies whose shares are the subject of a tender offer from taking action that may hinder the achievement of the objectives of the offer unless authorized by the competent shareholders' meeting. This rule may be derogated through a specific</p> |
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provision in the target's by-laws.

Mergers and other change of control transactions

In the event of a transfer of control occurring as a consequence of extraordinary corporate actions (such as increases in capital, mergers and spin-offs), the equal treatment of shareholders—without prejudice to the general principle referred to in Article 2348 of the Civil Code mentioned earlier—is ensured by various provisions of the Civil Code, including: (i) that, except in special circumstances, extraordinary corporate actions must be approved by the shareholders' meeting with a larger majority than is required for ordinary business; (ii) that, where the increase in capital is to be effected with the exclusion of the right of pre-emption (applicable on a proportional-basis to any shareholder), such exclusion must be justified by its serving the interest of the company (article 2441); (iii) that, where an extraordinary corporate action gives rise to one of the situations specified by law, shareholders who did not contribute to the approval of the relevant resolution must have the right of withdrawal as described above.

Moreover, for some proposed resolutions, the Civil Code provides for the directors, the members of the board of auditors or the external auditor to prepare disclosure documents, adequately in advance of the date set for the decision, and file them at the registered office of the issuer.

For example:

In the case of mergers Article 2501-septies of the Civil Code provides for the following documents to be made available:

- the merger plan with the reports of the boards of directors of the companies involved in the merger describing and justifying, from the legal and economic standpoints, the merger plan and the share exchange ratio and the reports of the experts on the fairness of such exchange ratio;
- annual accounts for the last three years of the companies involved in the merger, with the reports of the persons responsible for running the companies and controlling the accounts; and
- the balance sheets of the companies involved in the merger;
- for increases in capital that exclude or limit the right of pre-emption, Article 2441 of the Civil Code provides for the following documents to be made available:
- the report of the directors explaining the reasons for the exclusion or limitation; and
- the opinion of the board of auditors, if it exists, and the external auditor on the fairness of the issue price.

For issuers admitted to trading in a RM the provisions of the Civil Code are supplemented by further disclosure requirements laid down in Consob Regulation 11971/1999. Among other things, this regulation requires:

- disclosure requirements for extraordinary corporate actions (mergers, spin-offs, increases in capital by way of contributions in kind; major acquisitions and disposals; transactions with related parties, other changes to the constituent instrument and

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| | <p>issues of bonds, purchases and sales of treasury shares, reduction of the capital to cover losses);</p> <ul style="list-style-type: none"> • periodic disclosure obligations in conjunction with the approval of the annual accounts and the release of the half-yearly and quarterly reports; and • other disclosure obligations (for example, Article 84 of Consob Regulation 11971/1999 requires listed issuers and widely distributed issuers to provide the public with the information the holders of their financial instruments need to exercise their rights by publishing a notice in at least one national daily newspaper; Article 83 of Consob Regulation 11971/1999 requires listed issuer to disclose information on any changes to the rights attached to their financial instruments). <p>If a merger involves the issue of new shares, Consob reviews and approves the prospectus-like disclosure. For mergers not involving the issue of shares, Consob reviews public disclosures. It does not approve these but may intervene to require corrective action, such as additional disclosure to the market.</p> <p>Holding the company and its directors responsible in case of violations of law</p> <p>The Civil Code provides on a general basis for the directors and members of the board of auditors of limited companies (<i>società per azioni</i>), and general managers appointed by the shareholders' meeting or in accordance with the bylaws, to fulfill the duties they are charged with by law or the bylaws with the diligence required by the nature of the office and their specific powers. They are liable to the company for losses arising from failure to fulfill their duties (Article 2392 of the Italian Civil Code).</p> <p>The company by a resolution adopted in a meeting of shareholders may bring derivative actions against the persons referred to above (Article 2393 of the Italian Civil Code). Such actions may also be brought by qualified shareholders representing, for companies whose securities are listed on a RM, one fortieth of the share capital, or a smaller percentage provided for in the bylaws (Article 2393-<i>bis</i> of the Italian Civil Code).</p> <p>These derivative actions do not preclude individual shareholders who have been directly injured by fraud or gross negligence from claiming damages (Article 2395 of the Italian Civil Code).</p> <p>Under Article 2409 of the Italian Civil Code, shareholders representing one-tenth of the share capital (5 percent in listed companies), the board of auditors or the supervisory board are empowered to activate a judicial investigation of the company management, reporting to the court a well-founded suspicion of a serious breaches of duties of the directors or internal auditors. By Article 152 of the CL, also Consob is empowered to activate the same judicial investigation of the board of auditors of listed companies.</p> <p>Bankruptcy or insolvency of the company</p> <p>Pursuant to article 2348 of the Civil Code all company's shares of the same class must be treated equal in the event of insolvency.</p> <p>Substantial holdings of voting securities</p> <p>Article 120 of the CL requires persons who directly or indirectly hold more than 2 percent of the capital of a company whose shares are admitted to listing in a RM must inform the investee company and Consob. Notifications must also be given when</p> |
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| | <p>holdings reach other prescribed thresholds, namely 5 percent, 10 percent, 15 percent, 20 percent, 25 percent, 30 percent, 50 percent, 66.6 percent, 90 percent and 95 percent. Holders must also notify reductions below previously notified thresholds.</p> <p>Article 121 of the Consob Regulation 11971/1999 requires these declarations be made without delay and in any event within five trading days of the day of the transaction that triggered the obligation, regardless of the date on which it is to take effect. Consob makes the information it receives public within three trading days of receiving it. This information is available in Consob's website. These rules apply to persons acting in concert (Article 120 of Consob Regulation 11971/1999).</p> <p>Article 122 of the CL defines a number of types of shareholder agreements that are subject to special obligations, including agreements relating to voting rights, the joint exercise of a dominant influence over a company, and the purchase of shares. These agreements must be made public and notified to Consob and the relevant company within five days of their stipulation.</p> <p>In addition, according to Regulation 809/2004/EC offering and listing prospectus must indicate the name of any person who directly or indirectly has an interest in the issuer's capital or voting rights which is notifiable under the issuer's national law, together with the amount of each persons' interest, or if there are no such persons, and appropriate negative statement.</p> <p>Under Consob Regulation 11971/1999 on an annual basis information must be given on the list of persons that have a holding directly or indirectly of more than two percent of the subscribed share capital represented by voting shares, as recorder in the shareholders register along with any notification received in accordance with article 120 of the CL. This list must show the number of shares held by each party, differentiating where possible between ordinary and preferential shares.</p> <p>In the case of issuers whose securities (shares) are widely held, the obligation to notify substantial holdings apply, but only in connection with a change of control, which must be notified immediately.</p> <p>Holdings of voting securities by directors and senior management</p> <p>Article 114(7) of the CL and Articles 152-<i>sexies</i> and following of Consob Regulation 11971/1999 require directors and senior management having access to inside information, controlling shareholders, and shareholders owning at least 10 percent of the share capital, and any person who control an equity issuer admitted to trading in a RM to inform the public and Consob of transactions involving the issuer's shares or other financial instruments linked to them that they have carried out directly or through nominees, when such transactions exceed EUR 5,000 over a year. Notification must be made to Consob and the issuer within five trading days of the execution of the transaction. The listed issuer must make public the information not later than the end of the trading day following its receipt.</p> <p>Issuers widely held are not subject to notification of insiders' holdings. However on an annual basis the full list of shareholders must be made available to the public.</p> <p>Article 84 bis of Consob Regulation 11971/1999 requires equity issuers admitted to trading in a RM to make available in the Remuneration Report—to be submitted to the annual shareholders meeting—holdings in the issuer and controlled companies held, directly or indirectly, by their directors, members of the board of auditors and general</p> |
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| | <p>managers.</p> <p>Annex 3 of the Consob regulation also requires the disclosure of detailed information where stock-option plans exist for directors and general managers.</p> <p>Information on the holdings of the directors and managers and the existence of stock-option plans must also be included in offering and listing prospectuses.</p> <p>Consob supervision</p> <p>Consob's Corporate Governance Division, formed in 2011, is responsible for monitoring compliance by issuers with obligations relating to shareholder rights. It includes an office of takeovers and major shareholdings (16 staff) and a shareholders' rights office (12 staff).</p> <p>In 2012, the office of takeovers and major shareholdings reviewed 13 mandatory bids, and provided exemptions from the mandatory bid rule in 7 other cases. It also reviewed 850 major shareholding notices and 155 shareholder agreements.</p> <p>It issued 55 information requests in relation to major shareholdings and 26 in relation to takeover bids. It also required market disclosure in relation to 4 major shareholdings and 14 takeover bids.</p> <p>One on-site inspection of an issuer was carried out to verify whether a number of shareholders were acting in concert.</p> <p>Sanctions were imposed in 18 cases relating to reporting of major shareholdings, and in 3 cases relating to the mandatory bid provisions.</p> <p>Review of disclosure material relating to mergers is the responsibility of the Issuers Information Division. Four mergers were subject to review in 2012.</p> <p>Issuers admitted to trading in AIM</p> <p>Special provisions included in the CL in connection with shareholders rights are not applicable to issuers admitted to trading in AIM. However, the listing rules require that companies:</p> <ul style="list-style-type: none"> • submit an admission document, which is more abbreviated than a prospectus, but must which overall must be prepared following Annex I,II and III of the Prospectus Regulation; • voluntarily submit to the obligations concerning mandatory tender offers, at a threshold of 30 percent; • seek shareholder approval for fundamental changes of business; • report substantial corporate transactions, which is defined as one which exceeds 25 percent of the asset class; • comply with the obligations on related party transactions established by Consob Regulation; • report transactions by directors, without delay if they exceed EUR 50,000 within one year; • report substantial holdings, without delay, at a threshold of five percent. <p><i>Borsa Italiana</i> is responsible for ensuring compliance with these obligations. Consob may nonetheless exercise the powers provided for by Article 77bis of the CL, including</p> |
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| | <p>the power to exclude or suspend financial instruments from trading and the power to require all necessary information to the market operator. Consob is also responsible for investigating and prosecuting market abuse and may exercise all powers set forth by Article 187octies of the CL.</p> <p>Cross border</p> <p>The offering and/or listing prospectuses for financial instruments issued by a foreign issuer must be drawn up in accordance with Annex 1B of Consob Regulation 11971/1999. Annex 1I of that regulation also requires foreign issuers to submit a declaration to the effect, <i>inter alia</i>, that the issuer guarantees the equal treatment of all the holders of its financial instruments whose conditions are identical. The declaration must be accompanied by a legal opinion issued by a lawyer licensed to practice in the country in which the issuer has its headquarters. Prospectuses must include information on the system of corporate governance and the legal framework within which the issuer operates likely to have a significant impact on the equal treatment of investors.</p> |
| Assessment | Fully implemented |
| Comments | <p>The IOSCO methodology explicitly states that this Principle should apply to issuers of public offering, listed or publicly traded. As indicated in Principle 16, this contrasts with the current European regime whereby certain requirements are only applicable to issuers admitted to trading in a RM. The assessors acknowledge that in some areas the Italian legal framework has extended obligations to issuers widely held, in particular in connection with related party transactions. But several other obligations have not been extended to them, including the notifications of substantial and insider holdings—although change of control must be notified and a full list of shareholders given on an annual basis. But more generally not all set of stricter obligations applicable to issuers admitted to trading in a RM are applicable to them, although many of them do (including in matters of disclosure of inside information, provisions on related party transactions and prospectus in connection with tender offers). As in connection with Principle 16, the warning in the prospectus is a mitigating factor. However, given the limited significance of this category, as explained under Principle 16, these limitations have not been taken into consideration for the grade. Nevertheless the assessors encourage the authorities to align the requirements for this category with the IOSCO Principles, in particular if this category were to expand.</p> <p>Finally, at the time of this assessment the AIM market was not considered significant due to its size, and thus was not taken into consideration for the grade. In any case it is important to mention that Borsa Italiana listing rules do subject companies listed in AIM to at least the set of obligations required by the Methodology, including tender offer and notification of insider and substantial holdings, although in a more flexible manner than for issuers admitted to trading in a RM. If this market were to grow, then the differences in the framework for these issuers vis-à-vis issuers listed in a RM should be revisited. In this regard, in the context of the EU proposals in connection with markets for SMEs, the assessors encourage the authorities to review what should be the appropriate balance between investor protection and easing of access to capital for SMEs.</p> <p>Finally, the assessors note that cooperative companies which are admitted to trading in a RM are exempted from certain requirements that apply to listed companies under national law. They were explained that this situation stems from historical reasons and by the need to adapt the legal framework to the peculiarities of these companies.</p> |

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| | <p>Moreover, legislative decree no. 91/2012 has recently amended the Consolidated Law to align the requirements applicable to cooperative companies to the provisions of the EU Shareholders Rights Directive. Given that there are only eight listed cooperatives this issue has not been considered for the grade. However, if such cooperatives are to remain listed, then mechanisms should be found to ensure fair and equitable treatment.</p> |
| Principle 18. | Accounting standards used by issuers to prepare financial statements should be of a high and internationally acceptable quality. |
| Description | <p>Audited financial statements</p> <p><i>Public offers of securities</i></p> <p>The latest approved annual and (if applicable) consolidated accounts to be included in the prospectus must be audited and accompanied by an opinion given by an auditing firm in accordance with the CL and Legislative Decree 39/2010. Public offerings of financial products other than EU securities may not be made if the auditing firm rendered an adverse opinion or a disclaimer as to the latest approved financial statements (Article 96 of the CL).</p> <p><i>Annual report and financial reports</i></p> <p>According to article 154 ter of the CL the issuer of shares or debt securities admitted to trading in an RM and that have Italy as their home state, must present their annual financial report and auditing report to the annual meeting within 120 days of the end of each financial year and make it public at least 21 day before the meeting at the company's headquarters, on the company website and in the other ways envisaged by Consob by regulation.</p> <p>Use of unaudited financial statements</p> <p>Half yearly and quarterly reports do not have to be audited. The accounting principles applicable to the interim reports are the same as those applying to the annual financial statements.</p> <p>Accounting standards</p> <p>As required by the Italian and the European Union's legislation, the financial statements must conform with the requirements of the relevant European directives and with the IFRS issued by the International Accounting Standards Board (IASB) as endorsed in the European Union.</p> <p>Where financial statements are prepared in accordance with the IFRS, the official interpretive body is International Financial Reporting Interpretations Committee, the committee established by the IASB for issuing interpretations.</p> <p>All entities subject to Consob's jurisdiction, including issuers admitted to trading in an RM, ISPs and AMCs, are required to prepare financial statements in accordance with IFRS. Issuers admitted to trading in MTFs (such as AIM) are not required to submit their financial statements according to IFRS. Issuers whose securities are widely held must apply IAS/IFRS. As far AIM is concerned, issuers can submit their financial statements according to (i) local GAAP, (ii) IFRS or (iii) US GAAP.</p> <p>For the purposes of offerings or listings by foreign issuers, under the relevant European Regulation (809/2004/EC), third country issuers must present historical financial information in accordance with IFRS, Japanese GAAP, or US GAAP.</p> |

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| | <p>Review of compliance with accounting standards</p> <p>Review of financial statements by issuers admitted to trading in a RM and issuers of widely held securities is carried out by the Office for Accounting in the Consob's Issuers Information Division.</p> <p>The financial reports of filing companies are reviewed using a mixed approach, with 80 percent chosen on a risk basis and the other 20 percent on a sample basis. In 2012, 58 issuers' financial statements were reviewed, or around 20 percent of all listed companies.</p> <p>The Office maintains a watchlist of 47 companies whose compliance with financial reporting requirements is most at risk. Of these, 34 are subject to monthly reporting requirements, and 13 to quarterly reporting.</p> <p>In the process of its review activities, the Office made 529 requests for information pursuant to article 115 of the CL on Finance in 2012. In 119 cases, Consob required public disclosures of additional information and documents in accordance with Article 114 of the CL.</p> <p>Under Article 157 of the CL, the resolution of the shareholders' meeting or meeting of the supervisory board approving the annual accounts may be challenged by Consob within six months of the entry of the annual accounts or the consolidated accounts in the Company Register. The article does not apply to companies with shares listed only on RMs in other EU countries.</p> |
| Assessment | Fully implemented |
| Comments | As noted in the description under Principle 16, issuers listed on the AIM Italia market have the choice of preparing their financial reports under IFRS, Italian GAAP or US GAAP. The assessors have not reviewed the standards in Italian GAAP. But, as noted under Principle 16, the AIM Italia market is small. It is not material for the assessment of Principle 18. |
| Principles for Auditors, Credit Ratings Agencies, and Other Information Service Providers | |
| Principle 19. | Auditors should be subject to adequate levels of oversight. |
| Description | <p>Qualifications</p> <p>Pursuant to the Decree Law no. 39 of 2010 (DL) (implementing the Audit Directive), auditors must be registered in a registry kept by the MEF. This register was established in September 2012 (though it is not yet fully operational). Prior to 2012 there were two different registers, one kept by Consob and the other kept by the professional body on behalf of the MoJ. Pursuant to such DL all auditors previously registered in one of such registers have been automatically included in the registry of the MEF.</p> <p>To be included in the register an auditor must (i) have the appropriate academic degree, (ii) have three years of training and (iii) pass an exam. In addition an auditor must complete 120 hours of continuing education on a three year basis, with a minimum level of 20 hours each year. The DL confers on the MEF the authority to further develop such requirements, after consulting Consob.</p> <p>The DL establishes two sections in the registry:</p> |

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| | <p>One for “active” auditors which are those auditors with statutory engagements;</p> <p>The other for inactive auditors, which are those auditors who have not worked on statutory auditing activities for three consecutive years.</p> <p>Auditors in the inactive section are not required to comply with the ongoing training obligations, nor are they subject to the quality control reviews established in the DL.</p> <p>Oversight framework</p> <p>Pursuant to article 22 of the DL auditors that conduct audits on public interest entities (PIEs) are under the oversight of Consob. Statutory auditors, on the other hand, are under the oversight of the MEF.</p> <p>The definition of PIEs in Italy is broader than the one included in the Auditing Directive. Overall it includes listed companies, issuers whose financial instruments are widely distributed, and financial companies, including banks, investment firms, asset management companies and insurance companies.</p> <p>Consob’s power to oversee auditors pre-dates the Auditing Directive. Prior to such Directive Consob exercised its oversight through the imposition of requirements to be kept in its registry, and the supervision of the organization and activities of audit firms, including through quality control reviews. Moreover, through its monitoring program to review issuers’ compliance with financial disclosure obligations, Consob requests the working papers from the auditors.</p> <p>With the implementation of the Directive, Consob can no longer exercise its oversight power ex-ante; rather it continues to be exercised ex-post through the quality control reviews conducted by Consob under the DL of 2010. According to article 20 of the DL, auditors of PIEs must be subject to such review on a three year cycle. In addition, such oversight continues to be complemented with the indirect oversight exercised via the supervisory program for issuers.</p> <p>Enforcement Powers</p> <p>According to article 22 of the DL of 2010, Consob has extensive powers over PIE auditors including authority to (i) request information; (ii) and conduct inspections. Article 26 provides it with enforcement powers including: (a) pecuniary sanctions that can range from EUR 10,000 to EUR 500,000; (b) revoke one or more engagements, and (c) ban from accepting new engagements for a period not exceeding three years. Breaches of the independence rules are punishable with pecuniary sanctions ranging from EUR 100,000 to EUR 500,000. In addition, Consob can request that the MEF (i) suspend the auditor for a period not exceeding five years, or (ii) remove the auditor from the registry.</p> <p>Practice</p> <p>As of the time of this assessment there were roughly 150,000 auditors in the registry. However, only 19 auditing firms had PIE engagements and were therefore subject to Consob oversight. The number of PIE engagements amounted to roughly 3,000. While in theory with the implementation of the new registry all the auditors in the registry could potentially take PIE engagements, this is not expected, mainly due to the concentration of PIE engagements and organization structure requirements. Currently the big four firms carry out roughly 90 percent of PIE engagements—each one with roughly market share of about 15 to 24 percent. There are also two medium size firms</p> |
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| | <p>(Mazars and BDO) with a material number of PIE engagements.</p> <p>Consob has conducted a first cycle of reviews for auditors of PIEs covering all PIE auditors. In the case of the big four, such initial reviews were done via inspections that included a review of the quality control systems of the firm (covering leadership responsibilities for quality within the firm, ethical requirements, acceptance and continuance of clients' engagements, human resources, engagement performance and monitoring). In all other PIE audit firms the review also included a sample of engagements. Consob has developed criteria to determine the engagements to review, which includes factors such as the relevance of the issuer; the significance of non audit fees; cases where the fee charged by the audit firm is lower than the fee charged by the previous firms; and where the remuneration of the audit firm is lower than the average for the industry. For the second cycle with the big four Consob will include also a sample of engagements.</p> <p>Reviews for large firms usually involved about five staff, lasted for about a year, and involved three to four months in the field. For other firms, the teams included about three staff. The inspection lasted 6–7 months, and involved 8–10 days a month for 5–6 months.</p> <p>In all cases, the inspection concluded with a presentation and a discussion with management of the auditing firm of the main findings, then a formal report was issued along with recommendations, the firms were given 30 days to respond and a final report was issued. The follow up has included meetings and calls, and Consob expects also to use the second cycle of reviews to check on the correct implementation of remedial actions undertaken by the firm.</p> <p>For the large firms, the main deficiencies found relate to independence issues (i.e. compliance with the independence rules in the provision of non audit services), adequate direction and supervision, proper formalization of the engagement quality control review and the correct and complete performing of the acceptance process for new clients; while in small and medium firms more significant deficiencies were found; including deficiencies in: planning and risk assessment; obtaining sufficient evidence and appropriate audit evidence; and the documentation of audit judgements.</p> <p>Besides the quality control reviews that lead to remedial actions, in 2012 Consob performed enforcement activities on specific audit engagements, which ended in five sanctions: three administrative pecuniary sanctions, two temporary prohibitions for an audit partner to carry out statutory audits of PIEs. In addition, Consob sent communications to BI in relation to banks' irregularities detected in the course of the review of engagements.</p> |
| Assessment | Fully implemented |
| Comments | |
| Principle 20. | Auditors should be independent of the issuing entity that they audit |

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| Description | <p>Requirements concerning independence</p> <p>Article 10 of the Decree Law of 2010 establishes a general principle of independence for statutory auditors and a prohibition on them being involved in any way in the decision-making process of the audited company.</p> <p>Auditors must establish procedures to prevent and promptly detect situations that may compromise their independence. Such procedures must be documented, and be subject to quality control reviews. Article 10 requires auditors to document in their working papers all significant threats to independence.</p> <p>In addition, article 10 establishes certain outright prohibitions:</p> <p>An auditor cannot conduct an audit if, between the company and the auditors or its network, there is a financial, business, employment or other direct or indirect relations, including those arising from the provision of non audit services from which an informed, objective and reasonable third party would conclude that the independence is compromised. If independence is likely to be compromised as in cases of self-review, personal interest, advocacy, familiarity or intimidation, the auditor must take measure to reduce such risks. If the risks are of such importance as to compromise independence, then the audit should not be conducted.</p> <p>Fees shall not be subject to any condition, or be fixed on the basis of the result of the audit, and must not depend either on the provision of non audit services to the firm that will conduct the audit, its parent companies, or subsidiaries.</p> <p>In addition, special provisions established in the Decree Law 2010 apply to auditors of PIE firms, in particular:</p> <p>Audit firms are subject to rotation on a nine year basis; and individual auditors are subject to a seven year rotation. The assignment cannot be renewed until at least three years have elapsed. In addition, the responsible auditor is subject to a seven year rotation, with a two year cool-off.</p> <p>There is a list of prohibited non-audit services for auditors, their subsidiaries and their parent companies: which includes bookkeeping and other services related to the accounting records; design and implementation of accounting information systems; evaluation and assessment services and issuing independent opinions; actuarial services; external management of internal audit services; consulting and services related to business organization aimed at staff selection, training and management; securities brokerage, investing consulting or investment banking services; legal defense services and other services identified by Consob.</p> <p>The auditor, partner and those who have taken part in the management and supervision of the audit cannot hold corporate positions in the direction and supervisory bodies of the audited company, nor can they take independent or subordinate relationships until at least two years have elapsed from the conclusion of the engagement. Directors, members of supervisory bodies or managers responsible for preparing the corporate account cannot carry statutory audits until at least two years have elapsed.</p> <p>Pursuant to article 18 of the DL of 2010, auditors of PIEs must publish in their websites within three months of the end of the fiscal year a transparency report, which must provide a description of (i) their legal form and ownership structure; (ii) any network; (iii) their internal quality control review system and a statement of their management body on its effectiveness; (iv) the date of the last quality control review; (v) measures to ensure independence and a statement to the effect that the internal compliance has</p> |
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| | <p>been carried out; (vi) measure to ensure ongoing training; (vii) financial information, including total turnover subdivided into fees for statutory audit services; other audit services; tax advisory services and other non audit services; and (viii) information on the basis used to calculate the remuneration of partners.</p> <p>Before the audit firm publishes its transparency report, Consob checks the information provided in the draft report, comparing it with evidence gathered during the quality control reviews. If some information does not seem to be correct, Consob asks the audit firm to change it prior to its publication. Moreover, after the publication of the transparency report, Consob has the power to ask the audit firm to make some changes to it when the information is not correct.</p> <p>Issuers Governance</p> <p>Pursuant to article 19 of the DL of 2010, PIEs must establish an internal audit committee in charge of monitoring (i) the financial reporting process; (ii) effectiveness of the internal quality control reviews, internal audit, and risk management systems; (iii) the statutory audit of annual accounts and (iv) the independence of the statutory auditor.</p> <p>In practice the specific mechanism to comply with this requirement depends on the governance structure adopted by the company. The majority of Italian companies still adhere to the "Italian" framework, which includes the existence of a <i>collegio sindacale</i>. In such companies, the monitoring function is given to such body. The members of the <i>collegio sindacale</i> must be accountants registered in the MEF registry, and pursuant to Consob Regulations must be independent.</p> <p>Resignation of auditors</p> <p>Pursuant to article 13 of the DL the audited firm and the auditor or audit firm must promptly inform Consob of the revocation, resignation or consensual termination of an audit contract, providing the reasons for it. The above mentioned communication must be submitted to Consob within 15 days.</p> <p>Enforcement of compliance with auditors' independence</p> <p>Monitoring compliance of auditors with independence requirements is done under a three tiered approach:</p> <p><i>Internal controls:</i> In large audit firms, in addition to the local risk managers, there are global ethics committees in charge of reviewing that engagements respect the independence principle.</p> <p><i>"Monitoring" by issuers:</i> as indicated above the DL requires the existence of an internal body to monitor selection and independence.</p> <p><i>Review by Consob:</i> Review of the procedures and practices to ensure the independence of auditors is one of the items reviewed by Consob during its quality control reviews.</p> |
| Assessment | Fully Implemented |
| Comments | The assessor notes that the deadline for communication of revocation, resignation or termination of an audit contract appears long when compared to practices in other jurisdictions. |
| Principle 21. | Audit standards should be of a high and internationally acceptable quality |
| Description | According to article 11 of the Legislative Decree 39/2010, which transposes the EU |

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| | <p>Directive 2006/43/EC, the statutory audits must be carried out in accordance with the auditing standards adopted by the EC. Pursuant to articles 11 and 12 of such Decree, pending the adoption of standards by the EC, the auditing standards should be set by professional associations together with Consob, taking into account the international standards. The Decree indicates that specific arrangements must be entered between the MEF and the relevant professional associations to define the procedures for the preparation of the auditing standards. Consob staff indicated that such procedures have not been established, as the Italian authorities intend to wait for the completion of a framework at the EU level.</p> <p>As a consequence the auditing standards set by Consob pursuant to article 162 of the Legislative Decree 58/1998 continue to apply. Such standards were adopted by Consob having consulted the <i>Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili</i>.</p> <p>Such standards are derived from the International Standards of Auditing (ISAs) issued by the International Auditing and Assurance Standards Board. According to Consob and auditing firms consulted, the domestic standards are consistent with ISAs. Furthermore they are considered to be stricter than ISAs, as the main difference between the two is that the domestic standards are more prescriptive in particular issues in regard to the way to comply with particular obligations. For example, the domestic standards are stricter in regard to the procedures to obtain confirmations from banks and third parties.</p> <p>Italy is currently in the process of adoption of the new IAASB set of "clarified" standards. Implementation is expected for the financial accounts closed at December 31, 2013. Consob and auditing firms explained that there will be very few differences between the standards adopted in Italy and the clarified ISAs. Such differences would relate to the inclusion of references to the Italian Law. For example, in the ISA 260-262 the relationship with the audit committee is described in a broad manner; in such case, the domestic ISAs would include a reference to the Italian law that establishes more specific obligations.</p> <p>Compliance with ISAs</p> <p>Auditors are required to have in place quality control systems. In addition, Consob exercises oversight through the quality control reviews and enforcement.</p> |
| Assessment | Fully implemented |
| Comments | |
| Principle 22. | Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision. |
| Description | <p>Credit ratings are used in Italy for the purposes of determining risk weights under the standardized approach for calculating the capital requirement for credit risk for financial intermediaries. In this regard BI recognized credit quality assessments issued by CRAs as external credit assessment institutions (ECAIs).</p> <p>Pursuant to the CRA Regulation, ESMA is responsible for the supervision of CRAs whose ratings are used for regulatory purposes in the EU.</p> <p>To this end CRAs are subject to registration by ESMA based on a series of requirements established in the CRA Regulation. ESMA also has ongoing supervisory powers,</p> |

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| | <p>including the power to inspect CRAs.</p> <p>Registration Requirements</p> <p>The CRA Regulation provides ESMA with the authority to obtain all information it deems necessary from a CRA seeking registration in order to determine whether the requirements for registration have been fulfilled. As part of any application for registration, the applicant is expected to provide detailed information and evidence as to how it demonstrates compliance with the applicable requirements of the EU CRA Regulation. The content and format is provided for in the annexes of EU CRA Regulation. CESR (now ESMA) published Guidance in connection with the registration process, which distinguishes seven areas of requirements: (i) General Organization and Governance; (ii) Internal Controls; (iii) Business Activities and Resources; (iv) Conflicts of Interest; (v) Rating Process and Methodology; (vi) Disclosures and (vii) Endorsement. All documents related to these seven areas have to be provided in the form of policies and procedures.</p> <p><i>Quality and integrity of ratings</i></p> <p>The EU Regulation requires that CRAs put in place written procedures and methodologies providing for a fair and thorough analysis of all information relevant to credit analyses. In particular, CRAs are required to use rating methodologies that are “rigorous, systematic, continuous and subject to validation based on historical experience, including back-testing”. CRAs are also required to put in place procedures for permanent monitoring as well as regular updates of credit ratings as new information becomes available.</p> <p>The EU Regulation also requires that a credit rating agency establish a review function responsible for periodically reviewing its methodologies, models and key rating assumptions, such as mathematical or correlation assumptions, and any significant changes or modifications thereto as well as the appropriateness of those methodologies, models and key rating assumptions where they are used or intended to be used for the assessment of new financial instruments.</p> <p><i>Record keeping</i></p> <p>The EU CRA Regulation introduces several requirements concerning internal record keeping. There is a general requirement to maintain internal records of credit rating activities and to retain them for six years or the duration of the rated instrument.</p> <p><i>Sufficiency of resources</i></p> <p>The EU CRA Regulation introduces a requirement for CRAs to have sufficient resources in order to carry out high-quality credit assessment. Annex 2 of the Regulation describes the information to be provided in the application for registration. The list of covered areas includes “financial resources to perform credit rating activities”, “staffing of credit rating agency and its expertise” as well as “documents and detailed information related to the expected outsourcing arrangements including information on entities assuming outsourcing functions”.</p> <p><i>Addressing Conflicts of Interest</i></p> <p>EU Regulation requires CRAs to take all necessary steps to ensure that the issuing of a credit rating is not affected by any existing or potential conflict of interest or business relationship involving the credit rating agency issuing the credit rating, its managers, rating analysts, employees, any other natural person whose services are placed at the</p> |
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| | <p>disposal or under the control of the credit rating agency, or any person directly or indirectly linked to it by control. To ensure compliance with such principle CRA must comply with the requirements set out in Sections A and B of Annex I.</p> <p><i>Organizational requirements (Annex I Section A)</i></p> <p>CRA must have an administrative or supervisory board. Its senior management must ensure that conflicts of interest are properly identified, managed and disclosed. In addition to their overall responsibilities as members of the board, independent members of the administrative or supervisory board have the specific task of monitoring the effectiveness of measures and procedures instituted to ensure that any conflicts of interest are identified, eliminated or managed and disclosed. The compliance officer must ensure that any conflicts of interest relating to the persons placed at the disposal of the compliance function are properly identified and eliminated. The compliance officer must report regularly on the carrying out of his or her duties to senior management and the independent members of the administrative or supervisory board.</p> <p><i>Operational requirements (Annex I Section B)</i></p> <p>CRA are subject to a general obligation to identify, eliminate or manage and disclose, clearly and prominently, any actual or potential conflicts of interest that may influence the analyses and judgments of its rating analysts, employees, or any other natural person whose services are placed at the disposal or under the control of the credit rating agency and who are directly involved in issuing a credit rating or approving a credit rating.</p> <p><i>Prohibitions</i></p> <p>The EU regulation prohibits CRA (i) from issuing ratings when the CRA directly or indirectly owns financial instruments of the rated entity or related parties or has any direct or indirect ownership interest; or a control relationship or certain other specific types of relationships that may cause conflicts of interest, as well as (ii) from providing consultancy or advisory services to the rated entity or a related third party regarding the corporate or legal structure, assets, liabilities or activities of that rated entity or related third party. A credit rating agency may provide ancillary services.</p> <p><i>Specific rules concerning analysts</i></p> <p>Certain rules on analysts, include the prohibition to participate in fee negotiations, prohibition on trading securities, analysts rotations, or non “business contingent” remuneration. In relation to article 7, annex 1 Section C introduces several rules for rating analysts and other persons directly involved in credit rating activities (including securities and derivatives trading by such analysts and persons and their compensation arrangements). These rules address among others: Specific disclosures;</p> <p>Disclosure of rated entities and related parties from which a CRA receives more than five percent of annual revenues;</p> <p>Disclosure of (i) the largest 20 clients of the credit rating agency by revenue generated from them; (ii) a list of those clients of the credit rating agency whose contribution to the growth rate in the generation of revenues in the previous financial year exceeded the growth rate in the total revenues of the credit rating agency in that year by a factor of more than 1.5 times. Any such client shall be included on the list only where, in that year, it accounted for more than 0.25 percent of the worldwide total revenues of the credit rating agency at global level, and (iii) list of all ratings including the proportion of</p> |
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| | <p>unsolicited ratings.</p> <p><i>Transparency and timeliness</i></p> <p>The CRA Regulation introduces a general requirement to ensure timeliness on the release and distribution of credit ratings (where newly issued or for subsequent changes). A credit rating agency shall disclose any credit rating, as well as any decision to discontinue a credit rating, on a non-selective basis and in a timely manner. In the event of a decision to discontinue a credit rating, the information disclosed shall include full reasons for the decision.</p> <p><i>Information on ratings</i></p> <p>The CRA Regulation introduces several requirements related to the publication of CRAs' procedures, methodologies, models and key rating assumptions. When methodologies, models or key rating assumptions used in credit rating activities are changed, the CRA must immediately disclose the likely scope of credit ratings to be affected. When announcing a credit rating, a credit rating agency shall explain in its press releases or reports the key elements underlying the credit rating.</p> <p><i>Historical defaults</i></p> <p>The CRA Regulation introduces several requirements related to the publication of information about historical default rates of the CRAs credit rating. These requirements comprise a general obligation to disclose information on its historical performance to a central repository for CRAs (CEREP) managed by ESMA and an obligation of periodic disclosure (every six months) data about the historical default rates of its rating categories, distinguishing between the main geographical areas of the issuers and whether the default rates of these categories have changed over time.</p> <p><i>Confidentiality</i></p> <p>The CRA Regulation contains requirements designed to ensure CRAs protect non-public information. There is a general obligation not to use or share confidential information for any other purpose except the conduct of credit rating activities, and as a result the obligation to take measures to achieve such objective.</p> <p>Enforcement Powers</p> <p>The EU CRA Regulation provides ESMA with a set of enforcement powers in cases where a regulated CRA fails to meet registration requirements after its initial registration including the power to withdraw a firm's license, if licensing requirements are no longer met. In addition, in the case of infringements to certain provisions of the Regulation, ESMA can (i) temporarily prohibit the CRA from issuing ratings with effect in the EU, (ii) suspend the use for regulatory purposes of ratings with effect in the EU, (iii) require a CRA to bring the infringement to an end, (iv) issue notices, and (v) impose fines. Recently, through secondary legislation, the European Commission (EC) established the amount of the fines that can be imposed. Infractions are grouped and in each case the Regulation establishes a minimum and a maximum fine that can be imposed for each type of infringement. In the lowest case the fine can range from EUR 10,000 to EUR 50,000, while in the highest from 300,000 to 750,000. Aggravating and mitigating factors trigger automatic increases or decreases of the fine. Sanctions are made public after their imposition by the Board of Supervisors (BoS). Sanctions can be appealed to an Appeal Board. There is one Appeal Board for the three European Supervisory Authorities (ESAs), composed of two experts from each sector (and their alternates). Finally, decisions of the Appeal Board can be appealed to the European</p> |
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| | <p>Court of Justice.</p> <p>Practice</p> <p>Before July 2011, the registration of CRAs was in charge to colleges of European regulators, in which Consob participated. The bulk of CRAs including those active in Italy were registered based on a thorough process conducted by such colleges.</p> <p>Since July 2011 all registration and supervisory responsibilities concerning CRAs were transferred from the National Competent Authorities (NCAs) to ESMA. ESMA has a dedicated unit for the supervision of CRAs. Currently this unit has 16 staff (15 officers and the head of unit), with a mix of policy, market and supervisory experience. The unit is expected to grow to 26 people by 2013. With the approval of CRA3 ESMA will receive funding to hire 15 more staff. Not all of them would be assigned to this unit, as other divisions provide supporting services and therefore also require an increase in resources. There is a Technical Committee chaired by the Executive Director of ESMA, composed of NCAs and observers of the EC, the European Banking Authority and the European Insurance and Occupational Pensions Authority, which provides advice to the unit on its policy work and international cooperation.</p> <p>Since its operation, the CRA Unit has conducted significant supervisory work. This work included:</p> <p><i>Registration and certification.</i> It provided advice and assistance to NCAs with the application process. Since July 2011 it has taken charge of the assessment of new applications, with one new CRA being registered upon application received directly by ESMA. There are currently 18 registered CRAs and one certified CRA. There are five applications pending.</p> <p><i>Perimeter.</i> ESMA contacted around 30 companies the activities of which prima facie could be considered to fall under the CRA Regulation and requested explanations. It is currently preparing guidance on the scope of the CRA Regulation to be published in 2013.</p> <p><i>On-going supervision.</i> ESMA is taking a multidimensional approach, which includes desk reviews—based on notifications of changes, complaints and other periodic data—and on-site inspections, both horizontal (thematic across several entities) and vertical (on individual entities). Last year, ESMA conducted on-site inspections of three global CRAs with a view to better understanding their business models and operations and gaining expertise. As a result of such inspections, ESMA sent individual reports to each CRA with a request for changes and a plan for implementation, which ESMA is monitoring. In addition, it published a report summarizing main findings, which is available on ESMA's website. Based on the findings from these inspections it is currently conducting a review of banking rating methodologies. In addition, based on its risk analysis it decided to conduct a vertical individual on-site inspection on the internal controls of another CRA. As per the CRA Regulation, the CRA Unit must conduct inspections on all CRAs by 2014. Conducting these inspections is in the work plan of the Unit.</p> <p><i>Development of a central repository (CEREP).</i> Pursuant to the obligations established in the CRA Regulation, ESMA developed CEREP, which is a data repository that makes available information on past performance of ratings (six months lag) via the ESMA webpage. CRA3 will require such data to be available in real time. Another information technology tool, SOCRAT will facilitate the processing of ratings data in a standard and automatic manner to support ESMA's supervisory activities and would provide the Unit</p> |
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| | <p>more input for its risk assessment framework.</p> <p>In addition, the Unit has made progress in the development of a CRA Risk Assessment Framework, as the basis to support its supervisory program, and the intensity of supervision of different CRAs. Overall the work program will be risk-based. The risk factors included in the framework are: environmental risk, operational risk, business model risk and governance risk. The Unit developed criteria/alerts for each type of risk, in order to foster a consistent view of risk by the officers. It is estimated that roughly 70 percent of the supervisory resources would be spent on the large CRAs; however, the approach of the Unit is that there should be at least some engagement with all CRAs, even the small ones. In this regard, each CRA has been assigned a relationship manager in charge of continuous monitoring of such CRA. Feedback from the relationship managers would be one of the inputs for the risk assessment framework. Such minimum engagement would include also periodic (annual) meetings with the compliance officers of the CRAs. Once the inspections on all CRAs are concluded, it is estimated that on an on-going basis the Unit will conduct two thematic reviews and two vertical reviews per year, in addition to other supervisory work (registrations, handling of complaints, etc).</p> <p>A system of internal oversight has been developed by ESMA. Medium term objectives are prepared by the staff of the CRA Unit (and discussed with the MB), and discussed and approved at BoS level. This process also applies to the annual work plan and the risk based supervisory approach. There is monitoring of implementation of the work plan via reporting to the management board and major changes to the objectives are to be reported to the BoS during the course of the year where necessary.</p> <p>ESMA has been active ensuring coordination with non-EU regulators. ESMA has finalized MoUs with a number of jurisdictions including the United States, Canada, Australia, Hong Kong, Japan, Brazil, Singapore, Mexico and Argentina. In addition, ESMA has been actively involved in IOSCO's consultation on the establishment of a global "college" for CRAs. The expectation is that regulators would not only share information, but also that they would be able to conduct joint inspections.</p> <p>Mechanisms for public accountability are also in place. In particular, ESMA will make available to the public a public version of the work program, an annual report, and reports following thematic reviews, such as the one published in March 2012.</p> |
| Assessment | Broadly implemented |
| Comments | <p>As stated in the description of this Principle, ESMA is the authority responsible for the supervision of CRAs used for regulatory purposes in the EU. Thus, this grade corresponds to ESMA. It has been assigned based on a review conducted on ESMA as part of the EU FSAP conducted in November 2012. The comments included below apply to ESMA, and not to the Italian supervisory authorities.</p> <p>Over the next couple years, ESMA needs to finalize the implementation of its risk-based supervisory approach for CRAs. Overall, the approach developed by the Unit is comparable to approaches taken by other regulators. In this regard, a risk-based supervisory approach is a sound way to go, provided that at least a minimum engagement is kept with the small CRAs, since they can be important in a domestic context. This is already envisioned by ESMA. Furthermore, the mission believes it is important that after the initial on-site inspections required by regulation for all CRAs, small CRAs are at least included from time to time in the samples for thematic on-site inspections. This would be in addition to the basic level of engagement via the</p> |

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| | <p>relationship managers and the meetings with compliance officers. In addition, meetings with senior management of the CRAs should also be considered. Finally, it is important that the Unit keeps close coordination with the NCAs, as through their monitoring of issuers and market surveillance functions they can acquire information useful for the supervision of CRAs.</p> <p>The enforcement framework for CRAs should be reviewed. The mission considers positive the fact that the framework requires disclosure of the sanctions after their imposition by the BoS. However, the pecuniary sanctions that ESMA can actually impose appeared rigid and in practice could be too low to have any deterrent effect—although it is early to predict whether the publication of the sanction would suffice to alter behavior. The mission acknowledges that pecuniary sanctions are only one tool to influence behavior.</p> |
| <p>Principle 23.</p> | <p>Other entities that offer investors analytical or evaluative services should be subject to oversight and regulation appropriate to the impact their activities have on the market or the degree to which the regulatory system relies on them.</p> |
| <p>Description</p> | <p>Pursuant to the general obligations explained in Principle 7, Consob is required to conduct periodic assessments of its regulations to ensure that the system remains appropriate. This includes, assessing whether there are other analytical or evaluative services that require regulation, beyond what is already under the perimeter of regulation. Currently the framework focuses on entities that provide recommendations. Consob staff indicated that at this time there are no other information services providers whose activities could require additional regulation by Consob. In this regard, for example, valuation services are already subject to regulation, as these services can only be provided by auditing firms or judicial experts.</p> <p>The Italian framework contains two types of provisions that apply to persons that provide recommendations:</p> <p>Disclosure obligations: there is general framework that applies to any person who produces recommendations, whether regulated or not, which applies stricter obligations for regulated entities (Consob Regulation 11971/1999)</p> <p>Obligations related to the organizational structure: these obligations apply only to regulated entities.</p> <p>Provisions on fair disclosure</p> <p>Pursuant to article 69 of Regulation 11971, recommendations must disclose clearly and prominently the identity of the person responsible for their production, in particular the name and job title of the individual who prepared the recommendation and the name of the legal person responsible for its production.</p> <p>Where the relevant person is an authorized person, the recommendation must disclose the identity of the authority that issued the authorization to provide investment services. Where the relevant person is not an authorized person, but is subject to self-regulatory standards or codes of conduct, such person must include in the recommendation a clear and prominent reference to a website where such standards or codes can be accessed.</p> <p>Pursuant to article 69 bis relevant persons must ensure that the recommendations meet the following:</p> <ul style="list-style-type: none"> • facts are clearly distinguished from interpretations, estimates, opinions and other |

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| | <p>types of non-factual information;</p> <ul style="list-style-type: none"> • all sources are reliable or, where there is any doubt as to whether a source is reliable, this is clearly indicated; • all projections, forecasts and price targets are clearly labeled as such and that the material assumptions made in producing or using them are indicated. <p>Pursuant to article 69 ter, where the relevant person is an independent analyst, an authorized person, a related legal person, any other relevant person whose main business is to produce recommendations, or one of their employees or collaborators, such relevant person shall ensure that the recommendations meet the following requirements:</p> <ul style="list-style-type: none"> • all material sources are indicated, • any basis of valuation or methodology used to evaluate a financial instrument or an issuer of a financial instrument, or to set a price target for a financial instrument, is adequately summarized; • the meaning of any recommendation made is adequately explained and any appropriate risk warning is included; • reference is made to the planned frequency, if any, of updates of the recommendation and to any major changes in the planned coverage policy previously announced; • the date at which the recommendation was first released for distribution is indicated, as well as the relevant date and time for any financial instrument price mentioned; • where a recommendation differs from a recommendation concerning the same financial instrument or issuer, issued during the 12-month period immediately preceding its release, this change and the date of the earlier recommendation are indicated clearly and prominently. <p>Disclosure of interests and conflicts of interest</p> <p>Relevant persons must disclose in each recommendation all relationships and circumstances that may reasonably be expected to impair its objectivity, in particular where relevant persons have a significant financial interest in one or more of the financial instruments which are the subject of the recommendation, or a significant conflict of interest as a consequence of dealings with the issuer. Where the relevant person is a legal person, the circumstances and relationships also apply to any legal or natural person working for it, under a contract of employment or otherwise, when such persons were involved in preparing the recommendation.</p> <p>Where the relevant person is a legal person, the information to be included in recommendations must at least include:</p> <ul style="list-style-type: none"> • any interests or conflicts of interest of the relevant person or of related legal persons that are accessible or reasonably expected to be accessible to the persons involved in the preparation of the recommendation; • any interests or conflicts of interest of the relevant person or of related legal persons known to persons who, although not involved in the preparation of the |
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| | <p>recommendation, had or could reasonably be expected to have access to the recommendation prior to its dissemination to customers or the public.</p> <p>In addition to such obligations, recommendations produced by an independent analyst, an authorized person, a related legal person or any other person whose main business is to produce recommendations, must disclose the following information:</p> <ul style="list-style-type: none"> • major shareholdings that exist between the relevant person or any related legal person on the one hand and the issuer on the other hand. • other significant financial interests held by the relevant person or any related legal person in relation to the issuer; • where applicable, a statement that the relevant person or any related legal person is a market maker or liquidity provider in the financial instruments of the issuer; • where applicable, a statement that the relevant person or any related legal person has been lead manager or co-lead manager over the previous twelve months of any publicly disclosed offer of financial instruments of the issuer; • where applicable, a statement that the relevant person or any related legal person is party to any other agreement with the issuer relating to the provision of investment banking services, provided that this would not entail the disclosure of any confidential commercial information and that the agreement has been in effect over the previous 12 months or has given rise during the same period to the payment of a compensation or to the promise to get a compensation paid; • where applicable, a statement that the relevant person or any related legal person is party to an agreement with the issuer relating to the production of the recommendation. <p>If the relevant person is an authorized person, recommendations must specify, for natural or legal persons who work for such relevant person, under a contract of employment or otherwise, and who were involved in preparing the recommendation, the following information:</p> <ul style="list-style-type: none"> • whether the remuneration of such persons is tied to investment banking transactions performed by the relevant person or any related legal person; • the price at which the shares were acquired and the date of acquisition where such persons received or purchased the shares of the issuer prior to a public offering of such shares. <p>Authorized persons who produce recommendations must disclose to the public:</p> <ul style="list-style-type: none"> • in general terms, the organizational and administrative arrangements, including information barriers, set up within the authorized person for the prevention and avoidance of conflicts of interest with respect to recommendations; • on a quarterly basis, the proportion of all recommendations that are "buy", "hold", "sell" or equivalent terms, as well as the proportion of issuers corresponding to each of these categories to which the authorized person has supplied material investment banking services over the previous twelve months. |
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| | <p>Organizational requirements for authorized entities</p> <p>As further explained under Principle 31, intermediaries are required to have resources and procedures, including internal control mechanisms, to ensure an efficient provision of services. To minimize the risk of conflict of interest, authorized persons are required to develop (provide in writing), apply and maintain an effective conflicts of interest management policy in line with the principle of proportionality. This policy must consider the circumstances of which the intermediaries are or should be aware, connected with the structure and business of the parties belonging to its group. Finally, they must establish internal procedures to ensure that exchanges of information do not occur between the sectors of an investment firm that must be kept separate in accordance to BI regulations.</p> <p>Submission of recommendations to Consob</p> <p>Issuers of financial instruments, licensed parties and legal entities in a controlling relationship with them, which publish written recommendations, are required to submit them to Consob.</p> <p>Practice</p> <p>As of the time of the assessment there were not a significant number of independent analysts. However journalists in Italy do play an important role on disseminating research and in this role they are subject to the disclosure regime outlined above. They also have a code of ethics developed by their professional association.</p> <p>Consob monitors compliance with obligations concerning analysts via its monitoring of the market and market trends.</p> <p>In addition, Consob has a database with all research produced in Italy (as there is the obligation to send the research to Consob). From time to time Consob undertakes analysis of it, for example if there were important changes from one recommendation to another. This information is available and used also by the market surveillance department. In the past it has undertaken a few investigations, and a few on-site inspections that triggered remedial actions, such as for example, a request to an intermediary to change its procedures. There have not been disciplinary actions associated with research.</p> <p>Currently Consob is conducting analysis related to the distribution of research at different times to different types of intermediaries, as this could have critical effects on market abuse.</p> |
| Assessment | Fully implemented |
| Comments | |
| Principles for Collective Investment Schemes | |
| Principle 24. | The regulatory system should set standards for the eligibility, governance, organization and operational conduct of those who wish to market or operate a collective investment scheme. |
| Description | <p>Legislative framework</p> <p>CIS activity is regulated by Title III of Part II of the CL and related regulations.</p> <p>Investment funds can be open-end or closed-end, depending on the kind of assets they can invest in. Participants in open-end funds have the right to request at any time to</p> |

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| | <p>redeem units; in closed-end funds the right to redeem units can be exercised only at predetermined maturity dates.</p> <p>In Italy, two different kinds of legal form are envisaged for CIS:</p> <p>(i) contractual—investment funds managed by an AMC; and (ii) statutory—operated by a <i>Società d'investimento a capitale variabile</i> (SICAV).</p> <p>Under the current law, a SICAV can only operate an open-end CIS. At end 2012, there were no SICAVs in activity.</p> <p>The management of investment funds must be carried out by AMCs, whereas the assets of a SICAV can be managed by the SICAV itself or by an appointed AMC. When self-managed additional capital requirements apply to them.</p> <p>The BI is responsible for authorization of AMCs and SICAVs (after consulting with Consob) and both the BI and Consob, in their respective areas of competence, have responsibility for supervision.</p> <p>Regulatory framework—Authorization</p> <p><i>Marketing a CIS</i></p> <p>CIS's units or shares can be marketed and distributed only by CIS operators (AMCs and SICAVs), investment firms (IFs) and banks. All marketing entities are subject to authorization by the competent supervisory authorities (Consob and the BI). For personal selling, CIS operators must use the services of registered financial salespeople who satisfy specific requirements and are supervised by Consob (Article 31 of the CL). Hedge Funds (HFs) as defined in Principle 28 cannot be offered to the public.</p> <p><i>Operating a CIS</i></p> <p>CIS management can only be undertaken by authorized AMCs, SICAVs and AMCs using the European passport arrangements (Article 33(1) of the CL).</p> <p>Eligibility criteria</p> <p>The CL sets out the criteria for authorizing AMCs (Article 34) and SICAVs (Article 43). More detailed requirements are set out in BI's Regulation of 8 May 2012 and, for competence and integrity requirements, MEF rules (Ministerial Decrees 468/1998 and 469/1998). Detailed provisions on the organization of AMCs and SICAVs are contained in the joint BI and Consob Regulation of October 29, 2007.</p> <p><i>Fit and proper test</i></p> <p>Persons who perform administrative, managerial or control functions must fulfill experience, integrity and independence requirements (Article 34(1)(d) of the CL for AMCs; Article 43(1)(d) for SICAVs). These requirements are set out in MEF regulations. Overall integrity requirements are limited to not having had criminal sanctions. Compliance with fit and proper requirements is assessed by the CIS operators' board, which must submit a certification as part of the licensing file.</p> <p>A subsequent failure to fulfill the requirements established in MEF regulation results in disqualification from office. If the board does not act, BI, or Consob can declare the disqualification. As such requirements are narrowly defined, the disqualification does not cover all the cases where a removal of a director might be necessary or advisable in the interest of investors. In this regard, BI staff explained that especially in smaller AMCs there are more problems with fit and proper requirements of directors. The mechanism that they have used is convening the board with a request to change a particular</p> |
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| | <p>member (or the whole board). BI staff stated this mechanism has proven effective in many, but not in all cases.</p> <p>Shareholders who hold more than 10 percent of the voting capital of an AMC or a SICAV must satisfy the same integrity requirements (Articles 34(1)(e) and 43(1)(e) of the CL).</p> <p><i>Financial capacity and resources</i></p> <p>AMCs and SICAVs are required to have adequate resources to ensure an efficient provision of the collective portfolio management activities (Articles 40.1(c) and 50 of the CL, and BI and Consob Regulation of October 29, 2007).</p> <p>Article 6 of the CL gives the BI authority to issue regulations on capital adequacy for AMCs and Article 34(1) (c) to set a minimum paid up capital requirement.</p> <p>BI Regulations require a minimum initial paid up capital of EUR 1 million. They also establish minimum own funds requirements. Own funds cannot be less than:</p> <p>the higher of:</p> <ul style="list-style-type: none"> • 0.02 percent of the amount by which the value of the portfolios of all CIS (except closed-end CIS not reserved to “qualified investors”) and pension funds managed by the management company exceeds EUR 250 million, up to a maximum of EUR 10 million; and • one quarter of their preceding year’s fixed overhead costs. <p>in the case of management of guaranteed pension funds, the amount necessary to meet the obligation to repay the capital.</p> <p>In case of management of closed-end CIS not reserved to qualified investors, the CIS operator has to acquire a stake of at least 2 percent of the CIS’s initial NAV (1 percent if the amount exceeds EUR 150 million) and deduct it from own funds.</p> <p>The amount of own funds cannot be less than the minimum initial paid-up capital.</p> <p>BI Regulation of May 8, 2012 also establishes the rules for the calculation of own funds.</p> <p><i>Adequate corporate governance, organizational structure and procedures</i></p> <p>BI and Consob Regulation of October 29,2007 sets out principles, as well as detailed requirements in connection with the corporate governance and the internal organization of IFs, AMCs and SICAVs. Such principles and requirements are further explained in Principle 31.</p> <p><i>Depositaries</i></p> <p>Assets of CIS whether operated by AMCs or SICAVs must be held by a depositary bank (Article 36(2) of the CL). Since 2011, banks that wish to perform custodial services must obtain a separate/specialized license from BI, which is also the competent authority for their supervision. A depositary bank must meet specified requirements for own funds, adequate organization and experience, etc. Article 38 of the CL assigns specific control functions to the depositary bank including:</p> <ul style="list-style-type: none"> • verifying the legitimacy of the operations for issuing and redeeming units and the application of fund income; • verifying that the calculation of unit value is correct, or (if appointed to do so by the asset management company) carrying out the calculation; |
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| | <ul style="list-style-type: none"> • verifying that for transactions involving a fund's assets any consideration is remitted to it within the customary time limits; and • carrying out the instructions of the asset management company unless they conflict with the law, the fund rules or the prescriptions of the supervisory authorities. <p>Record keeping</p> <p>Under BI and Consob Regulation of October 29, 2007 (Articles 5(2) (g) and 30(1)), AMCs and SICAVs must have systems and procedures to preserve adequate, ordered records of management events of the intermediary and its internal organization. By Article 66(2) of Consob Regulation 16190/2007, AMCs and SICAVs must keep, for each CIS they manage, all documentation relating to every phase of the investment decision making process. They must also keep detailed records of transactions with investors such as subscriptions and redemptions (BI and Consob Regulation of October 29, 2007 Article 44), and records of the transmission and execution of orders on a fund's account (Articles 42 and 43).</p> <p>On-going obligations in connection with the authorization requirements</p> <p>AMCs and SICAVs must report to Consob and the BI changes to the conditions of their authorization, as further explained under Principle 29.</p> <p>Periodic reports</p> <p>AMCs and SICAVs are required to provide BI information for supervisory purposes.</p> <p>There is a set of quantitative information pertaining (i) to the AMC, in particular data on assets and liabilities (quarterly); profits and losses (twice a year); their regulatory capital (on a quarterly basis) and other statistical information (also on a quarterly basis); (ii) to the CIS they manage, including monthly information for each open-end funds on the analytical composition of the funds' portfolio and positions in the different financial instruments, the funds' assets, the number and value of the units and the fees and commissions. These data are transmitted using standardized procedures and they are entered into BI's database.</p> <p>This information is forwarded by BI to Consob on a monthly basis. Aggregate information on the composition of the fund portfolio must be sent by the AMCs and SICAVs to Consob directly on a quarterly basis.</p> <p>In addition, on an annual basis they are required to submit to Consob and BI:</p> <p>Annual and semiannual fund reports, within 90 and 60 days from the end of the period, respectively. Both reports must be accompanied by the report of the management board and by the external audit report. For closed end funds, the AMC must submit an interim management report within 45 days from the end of the first and third quarter.</p> <p>Annual report by the compliance function, the internal audit function, and the risk management function.</p> <p>They must also provide Consob and the BI with an annual report on organizational structure and the accounting system, and provide a quarterly report on AUM subject to a delegated investment process.</p> <p>Conflicts of interest</p> <p>Article 40 of the CL states that AMCs and SICAVs must organize themselves so as to minimize the risk of conflicts of interest, including conflicts between the pools of assets under management. Where a conflict of interests exists, they must ensure fair</p> |
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| | <p>treatment of unit-holders.</p> <p>Detailed provisions relating to conflicts are set out in related regulations. Article 73 of Consob Regulation 16190/2007 prohibits AMCs and SICAVs from paying or receiving from third parties, in relation to the management of CIS, fees, commissions and non-monetary benefits that could have an impact on their compliance with the general requirements to act honestly, fairly and professionally in accordance with the best interests of the CIS. The Regulation specifies permissible payments and requires that adequate information be given to investors, prior to the provision of the service, about the existence, nature and amount (or calculation criteria) of these fees, commissions or non-monetary benefits.</p> <p>Articles 37–40 of BI and Consob Regulation of October 29, 2007 require conflicts of interest between the AMC and the CIS, between clients and the CIS, or between different CIS to be identified and managed through adequate organizational measures. They provide criteria for identifying conflicts and require AMCs to adopt a conflicts of interest policy and specify its content.</p> <p>AMCs and SICAVs must keep a record of the types of activities in which a conflict of interest entailing a material risk of damage to the interests of one or more CIS or other clients has arisen or, in the case of an ongoing collective portfolio management activity, may arise.</p> <p>These regulatory rules are supplemented by an Industry Protocol on independence and the management of conflicts of interest developed by <i>Assogestioni</i> (the association of Italian AMCs). Among other things, the Protocol recommends that persons appointed to perform management functions should not be members of the board of directors of companies:</p> <ul style="list-style-type: none"> • whose securities are among fund assets under management nor of companies belonging to the group that are involved in the distribution of the fund units; • that act as depositary; • that provide investment services of dealing on own account, executing orders on behalf of clients, placement, reception and transmission of orders, investment advice, management of multilateral trading facilities or non-core services regulated by the CL or other services in the interest of the portfolio managed. <p>This Protocol has been approved by Consob under its safe harbor approach.</p> <p><i>Related party transactions</i></p> <p>As a general principle, AMCs and SICAVs can carry out transactions where they have directly or indirectly a conflicting interest, including an interest arising from intra-group dealings, provided they ensure fair treatment of the CIS they manage, taking into account the costs connected with the transactions to be carried out.</p> <p>Under the BI Regulation of May 8, 2012, a CIS must not invest in securities issued by its AMC or in assets sold by a shareholder or an officer of the AMC (other than listed financial instruments or derivatives), and it must not buy from or sell securities to such related parties (specific rules are provided for real-estate funds).</p> <p>Conduct of business rules</p> <p>Article 65(1) of Consob Regulation 16190/2007 requires that, in providing a collective asset management service, AMCs and SICAVs must:</p> |
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| | <ul style="list-style-type: none"> • operate diligently, correctly and transparently in the interests of investors in CIS and market integrity; • ensure that management takes place independently in compliance with objectives, investment policy and specific risks of the CIS, as indicated in the offer documentation or in the management regulation or CIS statute; • acquire a suitable awareness and understanding of the financial instruments and assets in which fund assets can be invested and their liquidity condition, and must have correct, transparent and suitable evaluation systems; • assure equal treatment of all investors of a single CIS managed and abstain from any conduct that may prejudice the interests of a CIS to the benefit of another CIS or a customer; • act to prevent unjustified costs being debited to a CIS and its investors. <p>Article 36(4) of the CL provides that the promoter, the manager and the depositary bank of a CIS must act independently and in the interests of the unit-holders.</p> <p>These general obligations are supplemented by specific rules for particular types of conduct.</p> <p><i>Best execution</i></p> <p>Articles 68, 69 and 70 of Consob Regulation 16190/2007 require AMCs and SICAVs to adopt all reasonable measures and implement effective mechanisms to achieve the best possible result with regard to the price, cost, speed and probability of execution and settlement, to the size and nature of the order, or to any other consideration relevant to its execution.</p> <p>AMCs and SICAVs must monitor the efficacy of their order execution measures on financial instruments and their execution strategy in order to identify and, if necessary, correct any failings.</p> <p>AMCs and SICAV must make appropriate information available to investors on their order execution and transmission strategies.</p> <p><i>Investment due diligence and allocation of trades</i></p> <p>Article 66 of Consob Regulation 16190/2007 requires AMCs and SICAVs to:</p> <ul style="list-style-type: none"> • acquire reliable, up-to-date information to prepare forecasts and carry out analyses; • define the consequent general investment strategies; • carry out a qualitative and quantitative analysis of a potential investment's contribution to risk-return profiles and the liquidity of the fund; • ensure that investment decisions are implemented in compliance with objectives, investment strategies and risk limits. <p>Article 72 of the Regulation limits the circumstances in which CIS orders may be aggregated with other orders or the investment manager's own order and provides rules for the location of trades when aggregation of orders is permitted.</p> <p><i>Churning</i></p> <p>The rules on investor due diligence, together with the general obligations of AMCs and SICAVs, are designed to ensure that trades are not entered into inappropriately to further the interests of the CIS operator at the expense of CIS investors.</p> |
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| | <p><i>Underwriting</i></p> <p>There are no direct prohibitions on a CIS purchasing securities during an underwriting where a principal underwriter has an affiliated relationship with the CIS operator. Where the underwriter is a company belonging to the same group of the CIS operator, the purchase of financial instruments during the underwriting is subject to the quantitative limits laid down in the BI Regulation of May 8, 2012 (no more than 25 percent of the amount of the underwriting commitment taken by the group company).</p> <p>More generally, a CIS's investment may be carried out only if it is consistent with the CIS general investment objectives, investment strategies and specific risks of the CIS previously defined by the board of directors; and the specific conflict of interests is evaluated by the board.</p> <p><i>Fees and expenses</i></p> <p>AMCs and SICAVs have a specific obligation to prevent unjustified costs being charged to the CIS and the relevant investors (Article 65.1(e) of Consob Regulation 16190/2007).</p> <p>For potential conflicts arising from the payment or receipt of fees, see above under conflicts of interest.</p> <p><i>Delegation</i></p> <p>Under the CL, AMCs (Article 33(4)) and SICAVs (by virtue of Article 50(1)) may delegate specific functions to third parties provided that it does not turn the company into an empty shell. AMCs remain responsible to participants in the CIS for the actions of delegates.</p> <p>Detailed provisions governing delegation are set out in BI and Consob Regulation of October 29, 2007. Among other things, they include:</p> <ul style="list-style-type: none"> • if internal control functions or other essential or important operative functions are outsourced, the CIS operator remains liable for compliance with all obligations established by laws and regulations; • the delegation must not jeopardize the relationship and obligations of the CIS operator with regards to its clients. • the CIS operator must oversee outsourced functions and manage the risks connected with outsourcing; • the CIS operator must retain the competence to deliver outsourced functions; • the service provider must collaborate with supervisory authorities with respect to outsourced activities; • the CIS operator, external auditors and supervisory authorities must have effective access to data and information about outsourced activities and to premises in which the service provider operates. <p>Additional safeguards are provided where investment decisions are outsourced to a service provider (Article 33 of BI and Consob Regulation of October 29, 2007). In particular, the AMC must be in a position to assess that the activity of the delegate complies with the instructions received and with the objectives, investment policy and risk profile of the CIS and that it does not infringe any applicable rules or regulations. If investment choices are delegated to an intermediary established in a non-EU country, the delegation is subject to the existence of a memorandum of understanding between the Italian authorities and the relevant third country authority.</p> |
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| | <p>By Consob Regulation 11971/1999, the prospectus of the CIS must include information on the delegation and its scope.</p> <p>The CIS operator must provide the supervisory authorities, upon request, with all the information required to enable them to check that outsourced services are implemented in compliance with the conditions set forth in BI and Consob Regulation. Through the powers conferred to them in the CL, BI and Consob can take measures if the delegation gives rise to conflicts of interest that are not adequately managed, including asking the AMC to terminate the delegation contract. To this end delegation contracts must be conferred for a specified period of time and must be revocable with immediate effect by the delegating AMC.</p> <p>International cooperation</p> <p>The CL contains specific provisions (Articles 41-42) for CIS which are marketed or managed across jurisdictions or where key services are provided by entities located in different countries. The cooperation arrangements that apply are described under Principles 13–15.</p> <p>The marketing in Italy of non-harmonized CIS (including CIS from outside Europe) must be authorized by the BI after consulting Consob, provided that the operating arrangements are compatible with those provided for Italian CIS.</p> <p>Supervision and ongoing monitoring</p> <p><i>Responsibilities and powers of regulators</i></p> <p>The responsibilities and powers of the regulators, the BI and Consob, are set out in the CL and related regulations.</p> <p>In general terms, the BI is responsible for matters regarding authorization of CIS, limitation of risks, sound and prudent management and financial stability of CIS and CIS operators (Article 5(2) of the CL). Consob has authority for matters regarding transparent and proper business conduct of CIS operators and CIS public offerings (Articles 5(3) and 94 of the CL).</p> <p>In particular, the BI has supervisory responsibility for:</p> <ul style="list-style-type: none"> • the capital adequacy of CIS operators, risk mitigation and permissible shareholdings; • duties concerning the deposit and sub-deposit of financial instruments and money pertaining to clients; • criteria and prohibitions relating to investment activity having regard, inter alia, to group relationships; • prudential rules for limiting and spreading risk; • the standard formats and procedures to be used for accounting statements; • the methods of calculating the value of units or shares of CIS; • the methods and procedures to be adopted to value securities and assets in which resources are invested and the frequency of valuation; • corporate governance, general requirements of organization, remuneration and incentive systems; • business continuity; |
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| | <ul style="list-style-type: none"> • administrative and accounting organization, including establishment of the compliance function; • risk management; internal audit; and • senior management responsibilities. <p>Consob has authority for matters regarding transparent and proper conduct of CIS operators and CIS public offerings. In particular, Consob has supervisory responsibilities for:</p> <ul style="list-style-type: none"> • reporting obligations in the provision of collective portfolio management activities; • methods and criteria to be adopted in advertising and promotion communications and in investment research; • disclosure obligations to participants in the CIS; • best execution of CIS orders; • churning; • the obligation to ensure that collective portfolio management is performed in accordance with the CIS investment objectives; • the conditions under which inducements may be paid or received. <p>Consob also has supervisory responsibilities for:</p> <ul style="list-style-type: none"> • procedures, including internal audit; • the correct and transparent provision of the collective portfolio management activities; • rules of conduct, including decision making process and due diligence requirements, monitoring of compliance with regulations; • complaint handling; • personal transactions; • management of conflicts of interest that are potentially prejudicial to customers; • handling of orders; • record keeping. <p>Supervisory powers</p> <p>The powers of supervision, investigation and enforcement described under Principle 10 and 11 apply in relation to CIS vehicles.</p> <p>Both Consob and the BI have the power to require documents and information (Article 8 of the CL); summon directors, senior managers and members of the board of auditors (Article 7(1)(a)); and to require meetings of the board of directors (Article 7(1)(b)).</p> <p>Consob has the power to conduct investigations of possible violations under its general investigative powers (Articles 8(5bis) and 187 octies of the CL).</p> <p>Sanctions</p> <p>The CL provides for the imposition of administrative sanctions on individuals, not on legal entities (although the latter are jointly and severally liable for the payment of sanctions). Therefore, directors and persons performing managerial functions and non-executive personnel of AMCs or SICAVs are liable to pecuniary administrative sanctions</p> |
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| | <p>of between EUR 2,500 and EUR 250,000 for violation of the CL or the general or specific rules issued by the BI or Consob pursuant to the CL.</p> <p>The same sanctions are enforceable against members of the board of auditors (Article 190 of the CL).</p> <p>These administrative sanctions are applied by the BI or Consob, within their respective sphere of competence (Article 195 of the CL).</p> <p>Criminal sanctions are also available. Any person who violates the provisions governing conflicts of interest or the separation of assets, undertaking transactions or committing actions that cause injury to investors or customers with the aim of obtaining an undue profit for himself or others, is punished by imprisonment for a term of between six months and three years and by a fine of between EUR 5,165 and EUR 103,291 (Articles 167 and 168 of the CL).</p> <p>The unauthorized provision of collective asset management services and/or the marketing in Italy of units or shares of CIS in violation of the applicable rules is a criminal offence. It is punishable by imprisonment for term of up to four years and a fine of up to EUR 10,329 (Article 166 of the CL).</p> <p>Practice</p> <p><i>Authorization</i></p> <p>The BI's External Relations and General Affairs Department is responsible for the authorization process. It verifies that the applicant meets all the preconditions for authorization, except that verification of fit and proper requirements relies mainly on the self-certification. BI does consult however the database that it has of persons who have held positions as board members in financial companies. The assessment of all other aspects is based on a detailed and thorough analysis of the ownership structure, the proposed program of operation and its organization, internal controls and procedures for managing conflicts of interest. The process usually involves requests for additional information, as well as a meeting with the management of the applicant.</p> <p>The authorization is given only for such specific activities foreseen in the program of operations. BI has requested changes to the incorporation documents of some applicants, to narrow the objects of the companies to specific activities, rather than allowing more open-end language.</p> <p>The number of requests for new authorizations of AMCs is small (one application for authorization in 2012). In the past the BI has denied very few applications (roughly one to two denials in the last four years). It is more the practice that an applicant withdraws the application in cases where substantial changes are required.</p> <p><i>Ongoing monitoring</i></p> <p><i>BI</i></p> <p>The BI's ongoing supervision of AMCs is undertaken by the BI's AMCs Division, which consists of 18 staff, and by staff of BI's branches in Rome, Milan, and Turin.</p> <p>In its supervision of AMCs, the BI uses the standards methodology used by all supervision areas of the BI such as the bank supervision areas, the Supervisory Review and Evaluation Process (SREP). This consists of two phases, an evaluation phase and a correction/follow up phase. In the evaluation phase, conducted annually with a half yearly update, scores are attributed to risk areas (strategic; market, credit/counterparty and liquidity: operational and reputational) and cross-cutting profiles (governance and</p> |
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control system; profitability; and capital adequacy). The evaluation is a combination of quantitative and qualitative factors, and draws on the extensive data sets held in the BI's systems, derived from the periodic reports from regulated entities listed above, other information supplied by a firm, information from supervisory activities, complaints and notifications by the internal board of auditors (*collegio sindacale*) and external auditors. Risk scores are assigned on a scale of 1 (low risk) to 6 (high risk). Higher risk scores lead to more intensive supervision.

Concerning CIS, BI receives very granular data as detailed above that allows it to rely on off-site monitoring for topics such as compliance of funds with investment rules and valuation.

In 2012, in its off-site supervision work the BI examined 157 AMCs (84 percent of all AMCs), and found problems requiring rectification in 65 of those firms. Interventions took the form of formal letters (222 such letters were issued) and meetings with the firms (159 meetings were held).

On-site inspections are carried out by the BI's Supervision Inspectorate. On-site inspections are planned for as part of the annual planning cycle, with the firms to be inspected determined by the line supervisors. Selection on targets for on-site inspections is based on the size of AMCs (so that large firms are more likely to be inspected) and on industry sectors (to ensure coverage of both open-end and closed-end funds). On-site inspections also include a rating of the AMC which can then be contrasted against the rating given by the AMC unit.

As a matter of course results of the inspections are delivered by BI in a meeting with the board of the AMC specifically convened by BI for such purpose. As per the files examined, different types of actions might follow an on-site inspection, including requesting remedial actions and pecuniary sanctions on the individuals involved. Furthermore, depending on the case, certain precautionary measures, such as limiting new activities (for example, opening of new funds) can follow an inspection.

Up until 2012 BI's on-site inspections of AMCs usually include also inspections of the depositary bank's activities in relation to the AMC, as a way to validate the information. The information below does not include the number of such associated inspections. Since 2012, depositary banks are required to hold a separate/specialized license and thus now, they are subject to on-site inspections specifically on their custodial services. At the time of this assessment, two of the three custodian banks had already been inspected.

On-site inspections conducted by BI and Consob on AMCs

| <i>Year</i> | <i>Consob on-site inspections Commenced</i> | <i>BI on-site inspections [non-bank entities]</i> | <i>Total</i> |
|-------------|---|---|--------------|
| 2012 | 3 | 10 | 13 |
| 2011 | 1 | 12 | 13 |
| 2010 | 4 | 12 | 16 |
| 2009 | 1 | 12 | 13 |

Source: BI and Consob

In addition to requiring AMCs to take remedial action for defects identified through the BI's supervisory activities, the BI has used its powers to impose pecuniary sanctions for

identified breaches. Following on-site inspections, sanctions were imposed on managers and on members of the board of auditors:

| Sanctions imposed by BI | | | |
|-------------------------|----------------|--|-------------------------|
| Year | Number of AMCs | Number of managers and auditors sanctioned | Total Amount (EUR 000s) |
| 2012 | 7 | 59 | 1,299 |
| 2011 | 6 | 42 | 638 |
| 2010 | 7 | 59 | 1,082 |
| 2009 | 5 | 59 | 764 |
| Source: BI | | | |

The most common reasons for sanctions being imposed are shortcomings in internal controls, including defects in the functions played by the internal board of auditors.

In 2011 and 2012, four AMCs were placed in crisis procedure, two in special administration and two in compulsory liquidation.

Consob

Ongoing supervision of AMCs is carried out by the Consob's Investment Management Department, which consists of 13 staff. On-site inspections are carried out by the office for inspections on intermediaries and markets in the Consob's Inspectorate Division.

Consob uses a risk-based approach to its supervision of asset management activity.

In regard to AMCs, to enable it to focus on areas of greatest risk, it conducts detailed background analysis (macroeconomic factors and their impact on specific sectors, such as the real estate sector) and then links this to the business model and likely behaviors of individual CIS operators. For each AMC, an analysis is conducted of their strategic behavior (business model), functional behavior (processes and procedures) and operating behavior (portfolio investment decisions). Using both quantitative and qualitative data, each AMC is assigned a risk score on a scale on 1 to 10. Higher risk firms are subject to more intensive supervision.

In the case of CIS, analysts are assigned a specific type of funds to monitor (for example, real state, open ended, etc). Through their extensive off-site monitoring analysts can identify (i) trends for a specific type of funds that need further analysis, or (ii) potential concerns in a specific fund (because it deviates significantly from the rest of the funds in such category). An example of the former are (i) the analysis conducted by Consob on total return funds, in light of the fact that the trend of these funds (net subscriptions) was very different from that of other open-end funds (net redemptions), as well as of (ii) real estate funds.

Inspections can be performed in the implementation of an annual plan decided by the regulators; however, they can be performed whenever the competent regulator gather information on possible violations of laws and regulations, including on the basis of complaints lodged by investors. In practice, Consob makes more limited use of on-site inspections in its supervision of CIS operators than BI. Over a four year period, nine on-site inspections of CIS managers have been commenced: four in 2009; one in 2009; four

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| | <p>in 2010; one in 2011; and three in 2012. Consob staff highlighted that the granularity of the data provided by the AMC, which include information at the individual portfolio level, allows it to conduct very strong off-site supervision in connection with its functions. Inspections by BI, on the other hand, can be focused on general issue of governance, internal control, and risk management.</p> <p>From 2006 to 2011 Consob directly applied administrative sanctions, amounting to EUR 3.3 million, against 12 AMCs and 147 natural persons responsible for management or control functions. In 2012, Consob applied 67 sanctions against natural persons responsible for management or control functions of 6 AMCs.</p> |
| Assessment | Broadly Implemented |
| Comments | <p>The grade of this principle stems from the limitations in the current licensing framework, and by the limited use of on-site inspections, and its potential effect on supervision and enforcement, as described below.</p> <p>File reviews of the processes used by BI in authorizing AMCs showed that the process is very robust and that BI with input from Consob, carry out thorough analysis of applications. However, the current definition of fit and proper is a source of concern as described in Principle 3. It would be highly desirable for the BI to have more discretion when vetting the integrity of directors or managers of asset management firms. This limitation is compounded by the limited powers that BI has to order the removal of individual directors. The assessors acknowledge however that the supervisory authorities have used other tools at their disposal, such as the convening of the board, to request changes when they were deemed necessary, and that in the majority of the cases such request have been met by the regulated entities.</p> <p>The limited number of on-site inspections is another issue for consideration, as explained under Principle 12; however mitigated by (i) the granularity of the information received, (ii) the active and robust off-site supervision carried out by both BI and Consob, and (iii) the very high coverage (measured by assets and clients) of inspections conducted by BI and Consob.</p> <p>For AMCs, the BI staff recognizes that operational risk—for example in relation to the segregation of assets—may be better examined through on-site inspections which test whether firm processes apply effectively in practice.</p> <p>Selling and distribution practices are monitored through supervision of the intermediaries which carry them out. Those supervision of distribution practices are taken into consideration in Principle 31.</p> |
| Principle 25. | The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets. |
| Description | <p>Legal form and investors' rights</p> <p>CIS can be investment funds or SICAVs. Participation in a fund is regulated by the rules of the fund which must be approved by the BI—except for funds reserved for sale to sophisticated investors (reserved funds) and hedge funds that are not sold to retail investors. BI Regulation of May 8, 2012 sets out criteria and minimum content for fund rules. Through its approval process the BI reviews that the fund rules are (i) complete, (ii) concise (avoids overlap with the prospectus); (iii) consistent (the structure including fees is consistent with the investment objectives), and (iv) clear. The BI has developed standard fund rules that a CIS can use. In such case, there is no need for pre-approval. For SICAVs, the BI has corresponding powers with respect to the instrument of</p> |

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| | <p>incorporation and articles of association (Article 43(2) of the CL).</p> <p>The CL, the BI Regulation of May 8, 2012 and Consob Regulation 11971/1999 require the legal form and the structure of the CIS to be disclosed in the CIS's rules and in the CIS' prospectus.</p> <p>The BI Regulation of May 8, 2012 contains prudential requirements placing limits on risk and requiring investment diversification. CIS operators must observe these requirements on an on-going basis.</p> <p><i>Responsibility for monitoring compliance with form and structure requirements</i></p> <p>A CIS's rules and any amendments to them are subject to approval by the BI except for non-retail funds such as hedge funds and reserved CIS. The BI's regulations on the minimum content of the fund rules requires the operator to give full information about the characteristics of the fund, including the fund's duration, its objectives, the kind of assets it may invest in, its liquidity, the kind of risks involved, the financial benchmark if any, the conditions for subscribing and redeeming units, and so on.</p> <p>The BI is responsible for ensuring that restrictions and limitations on investments are complied with and it does so via the supervisory activities described under Principle 24 above.</p> <p><i>Changes to investors' rights</i></p> <p>Changes to investor rights require changes to fund rules which must be approved by the BI. The content of any amendment to fund rules must be published by using at least the same methods set out in the prospectus for publication of NAV.</p> <p>Changes to essential characteristics of the fund, the substitution of the manager or changes affecting the non-economic rights of unit-holders, must be promptly notified to individual participants. Amendments to the rules do not take effect for a period of at least 40 days following the date of publication of the notice to allow investors to evaluate the changes and decide whether to redeem their units before the changes take effect (BI Regulation of May 8, 2012).</p> <p><i>Separation of assets/safekeeping</i></p> <p>Article 36(6) of the CL provides that each investment fund and each sub-fund constitutes an independent pool of assets, separate for all purposes from the assets of the asset management company and from those of each unit-holder, as well as from any other assets managed by the same company. Fund assets are immune from claims by the asset management company's creditors.</p> <p>Article 36(2) requires that fund assets must be deposited with an authorized depository bank. The depository bank can be either an Italian bank or a branch of an EU bank. Since 2011 banks that wish to provide custodial services must obtain a separate/specialized license from the BI.</p> <p>The BI's Circular 263 of 2006 establishes the conditions for appointment as depository bank. They include:</p> <ul style="list-style-type: none"> • minimum amount of own funds (not less than EUR 100 million); • adequate experience; • adequate organizational structure. <p>The BI and Consob Regulation of October 29, 2007 prohibit delegation of investment</p> |
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| | <p>functions to the depositary bank.</p> <p>Pursuant to the CL the custodian must act independently from the AMC and in the interests of the unit-holders (Article 36(4)). The current framework does not prohibit that the custodian bank be of the same group of the AMC; however it does prohibit the appointment of a custodian with interlocking directors.</p> <p>In practice depositary services are concentrated on three banks that belong to foreign owned groups (State Street, Société Générale and BNP Paribas).</p> <p>The BI Regulation of May 8, 2012 sets out conditions for the sub-deposit of the CIS assets to a third party, which must be either a bank or investment firm or another entity subject to prudential regulation. In any case, the depositary banks remains liable vis-à-vis the CIS operators and unit-holders.</p> <p>Compliance with segregation and custody requirements is monitored through different mechanisms including (i) on site inspections performed by BI on the AMCs, (ii) inspections conducted by BI on the depositary banks, and (iii) a special report that external auditors must provide on an annual basis.</p> <p>Winding up</p> <p>The procedures for winding up of a fund must be detailed in the fund rules (Article 39(2)b of the CL). Article 48 of the CL regulates the dissolution and voluntary liquidation of SICAVs.</p> <p>BI regulations establish that:</p> <ul style="list-style-type: none"> • fund rules must indicate the possible causes of the winding-up and the corporate body competent to take the relevant resolution; • the decision has to be notified in advance to the BI and published by the same means used to publish the NAV; • liquidation must follow proceed according to a specified given sequence of stages; • the procedure's completion must be notified to the BI. <p>Under provisions of Article 57 (6bis) of the CL—as amended by art. 1 of Italian Legislative Decree no. 47 of 16.04.12—should a CIS not be able to meet its financial obligations and should there be no reasonable prospects that this situation will be overcome, one or more creditors or the asset management company may request the liquidation of the CIS before the court of the place in which the asset management company has its registered office. The court, having consulted with the Bank of Italy and the legal representatives of the asset management company, where the risk of damages is considered grounded, orders the liquidation of the fund with a decision resolved in the council chamber. In this event, the Bank of Italy will appoint one or more liquidators. Asset management companies or entities may also be appointed liquidators. The provision of the Bank of Italy is published in extract form in the Official Journal of the Italian Republic.</p> <p>The legislation and related regulations provide special procedures for the winding-up of AMCs and SICAVs in cases of crisis or where other problems arise in managing the assets. In this regard both the special administrative procedure and the compulsory liquidations applicable to IFs have been extended to AMCs.</p> <p>In 2011 and 2012, four AMCs were placed in crisis procedure, two in special</p> |
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| | administration, and two in compulsory liquidation. |
| Assessment | Fully implemented |
| Comments | The IOSCO Principles do not prohibit that the custody of assets of a CIS be entrusted to a custodian from the same group of the AMC; however it requires that in such case appropriate safeguards be in place. In the assessors' opinion such safeguards are in place in Italy as (i) custodians can only be banks that meet certain requirements and are authorized by the BI, (ii) custodians are subject to inspections by the BI; (iii) and special reports are requested to the external auditors on the compliance of the AMC with the segregation requirements. |
| Principle 26. | Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme. |
| Description | <p>Disclosure to investors</p> <p><i>Prospectus and Key Investor Information Disclosure - KIID)</i></p> <p>Under Articles 94 and 98-ter of the CL and Consob Regulation 11971/1999, CIS operators must prepare a comprehensive prospectus. Chapter III of Title I of Part II of the Consob issuers Regulation (11971/1999) deals specifically with provisions concerning interests in CIS.</p> <p>For CIS other than closed-end funds, a separate document, the KIID, must be prepared in accordance with EU Regulation 583/2010. The prospectus for a closed-end fund must include a summary that, in a concise manner and in non-technical language, provides key information in the language in which the prospectus was originally drawn up. The summary (for closed-end CIS) and the KIID (for other CIS) must ensure, together with the prospectus, that all material information is conveyed to permit prospective investors to evaluate the proposed investment and, in particular, the risks associated with it.</p> <p>The prospectus and, for CIS other than closed-end CIS, the KIID must be published and made available free of charge to investors upon request. The CIS offeror must also provide the KIID to intermediaries responsible for placement or marketing. Offerors of CIS must post (and constantly update) on their website the prospectus, periodic financial reports and, if not included in the prospectus, the fund rules. Offerors of real-estate CIS must publish on their website and make available to investors valuation reports prepared by the independent experts, the deeds of contribution, purchase and sale of real estate assets and other information.</p> <p>Prospectuses must include all relevant information about the CIS, as required by the IOSCO Principles, including information about: the legal constitution of the CIS; the rights of investors; the operator; asset valuation methodology; procedures for subscription, redemption and pricing of units; custodial arrangements; investment policy; risks; fees and charges.</p> <p>Prospectuses must be drafted in compliance with the models provided in Consob Regulation 11971/1999, depending on the type of CIS. The model prospectus for closed-end CIS complies with the provisions of European prospectus directive and related regulation. The model prospectus for other CIS complies with the provisions of Directive 2009/65/EC.</p> <p>The summary to be included in the prospectus for closed-end funds must be drawn up in a common format set out in European Regulation EU 486/2012 to facilitate</p> |

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| | <p>comparability.</p> <p>The KIID prepared for CIS other than closed-end CIS must be drawn up in a common format set out in EU Regulation 583/2010 to facilitate comparison. In particular, it must provide information about: identity of the CIS; investment objectives and investment policy; past-performance presentation or, where relevant, performance scenarios; costs and associated charges; risk/reward profile of the investment, including appropriate guidance and warnings in relation to the risks associated with investments in the relevant CIS.</p> <p>The KIID prepared for CIS other than closed-end CIS must contain the risk and reward profile of the investment by using a synthetic indicator calculated according to the methodology developed by CESR (now ESMA).</p> <p><i>Periodic and ongoing reports</i></p> <p>AMCs (and SICAVs) must prepare an annual and a semi-annual report for each CIS they manage. Standard formats and procedures to be used for preparing accounting statements have been established by the BI (BI Regulation of May 8, 2012). BI Regulation of May 8, 2012 provides specific instructions on accounting and financial reporting by CIS. For closed-end funds admitted to trading on a regulated market, an interim management statement must also be prepared. Accounts must be prepared in accordance with IFRS.</p> <p>CIS operators are required to calculate NAV and to disclose information on the value of CIS units at least every week (for harmonized open-end funds), at least monthly (for non-harmonized open-end funds) or at least half-yearly (for closed-end funds), on the day established in the fund rules.</p> <p>Updated data on the risk-reward profile and costs of a CIS must be disclosed to investors by the end of February of each year (Article 19(1) of Consob Regulation 11971/1999).</p> <p><i>Regulator's powers</i></p> <p>Consob pre-vets prospectuses for closed-ended funds before their publication (see Article 23(2) of Consob Regulation 11971/1999). Prospectuses for open-end funds are not subject to a pre-approval process, but must be notified to Consob. Consob may, within 20 working days or 10 working days of the notification by the offeror, require CIS operators to include supplementary information in the prospectus and adopt specific procedures for its publication.</p> <p>In practice, Consob reviews a risk-based sample of disclosure documents, including both the prospectus and the KIIDs. This review is part of the off-site supervision process. In 2012, more than 500 documents were filed with Consob. Consob reviewed disclosure documents issued by the largest AMCs by AUMs for funds that were offered to the public, this resulted in a review of over 100 KIIDs and related prospectuses. Consob also reviewed three more prospectuses because of concerns identified through the off-site supervision process. One of these reviews resulted in an on-site inspection of an AMC.</p> <p>Reviews are carried out immediately after notification in case of particularly innovative financial structures, such as complex total return swap funds, and coupon funds, as well as in cases of aggressive advertising. For example, recently all documents concerning coupon funds were reviewed in order to ensure that no misleading information was being conveyed to investors.</p> |
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| | <p>For all CIS, Consob may suspend the public offering as a precautionary measure for a maximum of ten days (in the case of closed-end CIS) or ninety days (for other CIS) in the event of a well-founded suspicion of violation of the requirements or prohibit the offer in the event of an ascertained violation of the applicable rules and regulations or if there are grounds to suspect a violation of the rules. In 2012, Consob temporarily prohibited advertisement in 2 cases and prohibited public offers in three cases. Consob may also make public the fact of non-compliance with the applicable laws and regulations; and require trading to be suspended (for suspected violations) or prohibited (for proven violations) on regulated markets.</p> <p>Advertising</p> <p>Article 101 of the CL provides that:</p> <ul style="list-style-type: none"> • documentation relating to any form of advertisement concerning a public offering shall be provided to Consob at the time of advertising; • prior to the publication of the prospectus, public offerings of CIS other than closed-end CIS may not be advertised in any way; • advertisements must comply with the guidelines laid down by Consob in Regulation 11971/1999 with regard to the accuracy of the information and its conformity with the contents of the prospectus. <p>The Article gives Consob power to:</p> <ul style="list-style-type: none"> • suspend the further dissemination of an advertisement as a precautionary measure for a maximum of ten days (in the case of closed-end CIS) or ninety days (for other CIS) in the event of a well-founded suspicion of violation of the legislative provisions or the related regulations; • prohibit the further dissemination of an advertisement in the event of an ascertained violation of provisions or rules prohibit the making of the public offering in the event of failure to comply with the measures referred to under the previous points. <p>Consob's supervision of advertisements is carried out ex post.</p> |
| Assessment | Fully implemented |
| Comments | <p>The IOSCO methodology does not explicitly require a system of ex-ante review of prospectus; rather it requires that effective mechanisms are in place that allows the regulator to exercise the powers detailed in the corresponding question of the methodology. The key question here is whether the ex-post regime developed by Consob would allow for such result. The examples provided by Consob lead to conclude that the risk based supervisory approach developed by Consob is sufficiently robust, as it allows it to intervene immediately in the cases where the potential of problems with transparency are greater (new or complex products), while relying more on ex-post supervision in cases where the main concern is one of fairness of behavior. In addition, the assessors note that the rules of the CIS must be approved.</p> |
| Principle 27. | Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme. |
| Description | <p>Asset valuation</p> <p><i>Principles for asset valuation</i></p> <p>BI's Regulation of May 8, 2012 governs methods for valuing CIS assets and calculating</p> |

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| | <p>net asset value (NAV). Under the Regulation the board of the CIS operator is responsible for ensuring the implementation of adequate procedures (including the use of independent experts). The auditor is required to verify that the rules established by the BI for asset valuation are complied with. The criteria used must be consistently applied during the life of the scheme.</p> <p>The CIS operator—or the depositary bank if the CIS operator gives it responsibility for calculating the NAV—must have IT systems, professional and technical resources and procedures, including internal control procedures that ensure on a constant basis a fair and correct representation of the fund assets.</p> <p>The BI Regulation sets out detailed criteria for the valuation of listed financial instruments, unlisted financial instruments, derivative instruments including OTC derivatives, structured bonds, units or shares issued by other CIS, shares in start-ups, real estate, credits, repos and securities lending transactions, and other asset classes.</p> <p>Listed securities and listed derivatives are valued at market value (criterion consistent with fair value definition of IAS 39).</p> <p>If market prices are not available, CIS operators must value fund assets by a fair price procedure (BI Regulation of May 8, 2012). In particular, for listed securities temporarily suspended from trading or for which the volume and frequency of trading do not allow for the formation of reliable prices, operators must adopt the criteria established for unlisted securities.</p> <p>Unlisted securities are valued at cost adjusted to reflect the securities' estimated realizable value. This is consistent with paragraph 46 of IAS 39, which establishes similar rules for cases where fair value is not reliable.</p> <p>Unlisted derivatives are valued at current value, which is consistent with level 2/level 3 of IFRS.</p> <p>The BI Regulation requires real property to be valued using the current value and sets out detailed criteria, consistent with IAS 40, for valuation. Investment property must be revalued every year. For real-estate funds, independent experts must value properties.</p> <p>Valuation criteria must be consistently applied, unless changes are necessary as a consequence of exceptional and objective circumstances.</p> <p><i>Calculation of NAV and publication</i></p> <p>For harmonized open-end CIS the NAV must be calculated and published at least weekly; for non-harmonized open-end funds and closed-end funds the minimum frequency for the NAV valuation and publication is, respectively, monthly and half-yearly. In practice, the NAV for harmonized open-end funds is calculated daily.</p> <p><i>Independent audit</i></p> <p>The external auditor responsible for audit of a CIS's financial statements must also render an opinion on the CIS's statement of operations, including compliance with the criteria established by the BI for the valuation of fund assets.</p> <p>Pricing and redemption of interests</p> <p><i>Disclosure</i></p> <p>Fund rules must set out the procedure for redeeming units or shares. There must be no obstacles to the exercise of the redemption right by participants or to reimbursement within the prescribed time limits. Fund rules must set out the exceptional cases where</p> |
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| | <p>redemption may be suspended in the interest of participants to the CIS.</p> <p>The value of CIS units, calculated with the frequency required by the CIS rules or bylaws, must be published in a newspaper having adequate circulation in the areas where the CIS is marketed, with an indication of the CIS NAV reference date.</p> <p>For CIS reserved to qualified investors and HFs, the operator may choose different means of disclosure, to be indicated in the fund rules.</p> <p><i>Pricing errors</i></p> <p>The BI Regulation of May 8, 2012 specifies the actions AMCs must take in the case of pricing errors. AMCs must provide adequate information about the errors that occurred in the valuation of CIS assets by a press release published in the same way as the NAV (except for minor errors occurring in a limited period of time, where information can be provided in the CIS report). Clients adversely affected by pricing errors must be individually notified. AMCs must indemnify investors and the fund damaged by the mispricing, unless the error is less than 0.1 percent of the fund's NAV.</p> <p>AMCs may specify in fund rules a threshold (proportional to the cost of issuing and sending the means of payment) below which they are not required to indemnify redeeming investors.</p> <p>The AMC and the depositary bank must notify promptly BI about pricing errors. Additionally they must communicate the remedial actions taken. These notifications are the basis for off-site monitoring by BI. In addition, when onsite inspections are conducted BI generally checks that cases of pricing errors verified have been settled by the AMC according to its rules.</p> <p>The authorities pointed out that in the past the number of pricing errors was more significant, but it has decreased overtime, mainly as a result of the implementation of better systems by the AMCs.</p> <p><i>Suspension/deferral of valuations and redemptions</i></p> <p>Circumstances in which there may be suspension or deferral of routine valuation and pricing and regular redemption must be described in CIS rules. If a suspension is a result of technical problems (such as the unavailability of prices on a relevant market or a strike), it must be notified immediately to BI and the AMC has to calculate ex post the units' value to settle subscriptions and redemptions received during the period of suspension.</p> <p>Fund rules can also indicate that the operator may suspend or defer redemption of units where, owing to their unusually large volume, they cannot be handled by an orderly selling of the assets of the fund in a short period.</p> <p><i>Reporting to regulator and regulator's powers of intervention</i></p> <p>All decisions to suspend redemptions must be reported to the BI.</p> <p>BI can delay or suspend redemption of CIS units. In addition, Consob and the BI can, where it is in the public interest or the interest of participants suspend or place a temporary limitation on the issue or redemption of interests (Article 7(3) of the CL).</p> |
| Assessment | Fully implemented. |
| Comments | The assessors note that the current regulatory framework does not require application of IFRS for valuation of CIS assets. However, the valuation methodology required by BI |

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| | regulations is consistent with the approaches taken in IFRS, especially in regard to the applications of IAS 39 and IAS 40, and in the use of fair value methodologies for the valuation of instruments where current market prices are not available. |
| Principle 28. | Regulation should ensure that hedge funds and/or hedge funds managers/advisers are subject to appropriate oversight. |
| Description | <p>HF managers</p> <p>AMCs operating hedge funds (HFs) are subject to authorization and registration by BI, after consulting Consob (article 34 of the Consolidated Law).</p> <p>Currently the regime applicable to AMC that operate HFs is the same that for other AMCs, as described in Principle 24. However, such regime will be subject to review with the transposition of the Alternative Investment Fund Managers (AIFM) Directive, to be implemented by July 22, 2013.</p> <p>In this regard HFs managers are required to have adequate resources to ensure the efficient provision of management of collective portfolios (article 40.1(c) of the CL and Consob Regulation Implementing article 6.2 bis of the CL). Specifically they are subject to the same prudential requirements as any other AMC.</p> <p>Detailed provisions on risk management requirements are laid out in BI Regulation of May 8 2012. HFs are required to employ a risk management process that enables them to identify, monitor, measure and mitigate risks to which the portfolio of assets are exposed. The risk management process must be appropriate in view of the frequency of redemptions, and the nature, scale and complexity of the investment strategy. As other AMCs, HF managers are required to set up a permanent risk management function hierarchally and functionally independent from the operating units. They must also establish and maintain a compliance function, with the necessary authority, expertise and access to all relevant information. It must also be functionally independent from the operating units. They must also set up a permanent internal audit unit. HF managers are also subject to the same obligations on delegation that other AMCs. Requirements concerning conflict of interest are also applicable to HF managers (article 40 of the CL).</p> <p>Powers over HF managers</p> <p>Both BI and Consob, in the respective areas of their competences may carry on-site inspections of HF managers to ascertain compliance with their obligations (article 10 of the CL). They may:</p> <ul style="list-style-type: none"> • Require information and data (CL article 8) • Summon directors, senior managers and members of the board of auditors (7.1a of the CL) • Order the meeting of the board of auditors and set the agenda of its meeting; in case of inaction of the AMC, proceed directly to convene the board of directors (article 7.1b and c of the CL). <p>The BI and Consob can collect information from HF managers at the request of foreign regulators, in the same terms described in Principles 13–15.</p> <p>The BI and Consob may carry enforcement actions, in similar terms as for other AMCs (see principle 24).</p> <p>Hedge Funds</p> <p>HFs cannot be publicly offered and the minimum amount of each subscription is</p> |

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| | <p>EUR 500,000.</p> <p>By way of derogation of article 39 of the Consolidated Law, the rules of HFs and reserved funds are not subject to BI approval (article 37.2 of the Consolidated Law).</p> <p>The marketing in Italy of foreign HFs must be authorized by BI after consulting Consob, provided that the operating arrangements are compatible with those required for Italian CIS. The conditions and procedures for such authorization are established by Regulation issue by BI on May 8, 2012. In the case of HFs from non-EU countries, these conditions include the existence of cooperation arrangements.</p> <p>Assets of HFs must be entrusted to a depositary bank which must satisfy the requirements set forth in Principle 24 (level of own funds, adequate organization and experience), and specific control functions are assigned to the depositary bank.</p> <p>Disclosure to investors</p> <p>BI Regulation of May 8, 2012 requires the production of annual and semi-annual reports that must be made available to investors as well as the standard format for disclosing the value of the funds units.</p> <p>Reporting to the regulatory authorities</p> <p>HFs are currently subject to periodic reporting requirements, which allow the regulators to conduct robust off-site monitoring. Such reports include detailed information on the funds, including data concerning counterparties in derivatives transactions and credit amount. Furthermore, the information foreseen by the AIFM Directive includes data concerning borrowing and exposure risks.</p> <p>Practice</p> <p>As of December 2011, there were 120 HFs authorized in Italy with net assets of roughly EUR 11.7 billion. Out of this number 98 are funds of hedge funds, with net assets of EUR 11.3 billion.</p> <p>Both Consob and BI have monitored closely the HF industry during the current crisis, as there were concerns regarding the possibility that investors could redeem their units in the timeframe and conditions established in the fund rules. A general communication on liquidity was issued on 2008, which was followed by emergency legislation that allowed BI to change the regulations for HFs, to introduce gates and side pockets.</p> <p>Supervision of HFs managers triggered specific actions on HFs managers, including: (i) the convening of relevant persons of six AMCs, (ii) a 60 day suspension of the administrative bodies of one AMC; further examination led Consob to ask the MEF to dissolve the administrative and control bodies for serious violations; (iii) another AMC was sent to compulsory administrative liquidation; and later on Consob requested the MEF to withdraw its authorization.</p> |
| Assessment | Fully implemented |
| Comments | Overall BI and Consob have exercised a more intense supervision over HFs than what has been customary in many industrialized jurisdictions. |
| Principles for Market Intermediaries | |
| Principle 29. | Regulation should provide for minimum entry standards for market intermediaries. |

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| Description | <p>Regulatory background</p> <p>Investment services in relation to financial instruments can only be carried out authorized investment firms (IFs) and banks (Article 18(1) of the CL).</p> <p>Investment services and activities (core services) are defined in Article 1(5) of the CL:</p> <ol style="list-style-type: none"> a. dealing for own account; b. execution of orders for clients; c. subscription and/or placement with firm commitment underwriting or standby commitments to issuers; c-bis. placement without firm or standby commitment to issuers; d. portfolio management; e. reception and transmission of orders; f. investment consultancy, and g. management of multilateral trading systems. <p>Financial instruments are broadly defined by Article 1(2) of the CL and include shares, debt securities, money market instruments, units in collective investment undertakings and a variety of options, futures, swaps and other derivative contracts.</p> <p>By Article 18(4) of the CL, authorized entities can also provide a variety of non-core services, defined in Article 1(6) of the CL. These include safekeeping and administration of financial instruments and related services, safe custody services and investment research and financial analysis or other forms of general recommendation regarding transactions in financial instruments. However, proposals are being developed under the MiFID review to make custody a core service.</p> <p>Banks and IFs that have their registered offices and head offices in any Member State of the European Economic Area (EEA), other than Italy, have the benefit of the European passport. They do not require authorization by the Italian authorities.</p> <p>Banks and IFs located outside the EEA must be authorized under the Consolidated Law if they wish to provide services in Italy.</p> <p>Financial salespeople (tied agents) are required to be registered in a special register (Article 1 of the Consolidated Law). Only natural persons can be registered salespeople and a registered person can only act for one firm, which is responsible for their conduct.</p> <p>At the end of 2012, 97 IFs and almost 700 banks were authorized to provide investment services. Of the IFs only a small number (14) are authorized to conduct proprietary trading. Almost all IFs and banks authorized to provide investment services provide financial advice. There were 52,268 financial salespeople on the register, of whom 33,480 active.</p> <p>Bank and banking groups dominate all facets of the investment services industry. Consob data indicates that at June 30, 2012:</p> <ul style="list-style-type: none"> • the top nine banks have almost 8.5 million clients (61 percent of all investment services clients), and other banks have 19 percent of clients; and • the top nine banks hold EUR 701 billion of financial instruments owned by retail clients (61 percent of the total), while other banks hold 23 percent. |
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| | <p>More than 80 percent of all tied agents act for the top 20 intermediaries, most of which are banks.</p> <p><i>Authorization</i></p> <p>Consob, after consulting the BI, authorizes the provision of investment services in Italy by investment firms whose registered offices and head offices are located in Italy. The BI authorizes the provision of investment services and activities by banks licensed in Italy and by special financial intermediaries registered under Article 107 of the Consolidated Law on Banking (dealers dealing on own account and for clients in derivatives; some underwriters). The BI is not obliged to consult with Consob in relation to requests by banks for an authorization to conduct investment services, other than where a bank seeks authorization to operate an MTF (Article 19 of the Consolidated Law).</p> <p><i>Basic requirement</i></p> <p>An authorization to carry out investment services can only be granted if the applicant complies with the conditions set out in the CL and related regulations (Consob Regulation 16190/2007 and the BI's Supervisory Instructions for banks). Neither the BI nor Consob has power to exempt from the requirement to be authorized or from the conditions of authorization.</p> <p>Authorization may be refused if an applicant does not comply with the authorization requirements and in particular if the applicant cannot demonstrate that sound and prudent management is ensured and the company is able to exercise investment services or activities correctly (Article 19(2) of the Consolidated Law).</p> <p><i>Capital requirement</i></p> <p>Licensees must meet minimum and ongoing capital requirements. These are described under Principle 30.</p> <p><i>Competence and integrity</i></p> <p>Competence and integrity standards are set out in MEF Decree 468/1998. They require directors and members of the board of auditors to have a minimum of three years appropriate experience, and senior managers to have at least five years relevant experience. A person is not permitted to be a director, member of the board of auditors or senior manager if they have previous criminal convictions for bankruptcy or other criminal convictions resulting in imprisonment, are ineligible to act as a company director, or are subject to precautionary measures issued by a judicial authority. Automatic disqualification applies if the director has committed a market abuse or a public offering violation.</p> <p>Compliance with these standards must be certified by the board of an applicant for authorization, including in relation to the experience of board members. Consob also conducts checks with judicial authorities in relation to convictions or court orders.</p> <p>Integrity requirements also apply to controlling shareholders and holders of an investment that could have a significant influence on a regulated firm (Article 14 of the Consolidated Law and related MEF regulations). This includes but is not limited to any shareholder over 10 percent.</p> <p><i>Governance and internal controls</i></p> <p>By Article 5(2)(a) of the BI and Consob Regulation of October 29, 2007, investment firms must have sound corporate governance mechanisms, including decision-making processes and an organizational structure that clearly specify and document the</p> |
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| | <p>hierarchical relations and the breakdown of functions and responsibilities.</p> <p>In the authorization process, the composition, functions and responsibilities of corporate bodies are examined to ensure that there are no areas of uncertainty or overlap of tasks that might damage the company's functional efficiency. The adequacy of the organizational structure and internal controls is assessed to ensure they are consistent with sound and prudent management. In particular, BI examines:</p> <ul style="list-style-type: none"> • the reliability of internal systems for risk measurement, monitoring and management and of accounting systems; • the adequacy of technical and human resources devoted to the area of business; • in case of dealing activity, the organization and management of the technical structure for trading financial instruments on official markets; • in case of management of investment portfolios on a client-by-client basis, the consistency of the internal organization with the administrative and accounting separation. <p>Practice</p> <p>Applications are reviewed by the Office on Authorization and Supervision of Investment Firms at Consob which has a total staff of 24.</p> <p>Applicants must submit a detailed application, including information about the proposed program of operations, business plan and strategy, organization structure, governance, internal controls and risk management, compliance arrangements, the identity of persons performing administrative, managerial and control functions, shareholders, and (where relevant) group structure. Consob asks the BI for an opinion on the application and conducts a detailed analysis of the application. As indicated under Principle 24, fit and proper requirements are subject to self-certification by the board. However, Consob does an additional check on criminal records, and if the person has provided investment services in other jurisdictions, it asks for information on fit and proper requirements from the competent foreign regulator. Consob staff regularly ask for additional information to assist their analysis or that of the BI. BI provides a formal opinion on the application. A meeting with the applicant's board is a regular part of the review process.</p> <p>As for BI's review of an application of a bank that wants to provide investment services, the BI's assessment of applications is based on the same criteria as are used in its assessment of applications for authorization of banking activities.</p> <p>In addition, in their MoU the BI and Consob agreed on the set of information that an applicant for a bank license must submit to the BI, in connection with its transparency and business conduct obligations. This set of information was included in a Regulation of BI of 2009. In addition BI staff informed that in deciding applications their staff also follows guidelines/instructions that Consob staff uses. For example, Consob's practice is not to provide a license for execution of orders unless the applicant can demonstrate that it also has the capacity to provide investment advice.</p> <p>Authorizations are given specifically for the activities included in the program of operations and for which the applicant has demonstrated that it has the capacity to conduct according to the laws and regulations. BI staff explained that in practice they have requested companies amend their incorporation documents to narrow the objects</p> |
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| | <p>of the company to the activities authorized.</p> <p>Ongoing requirements</p> <p>Authorized IFs are required to give notice to Consob and the BI of any material change in the licensing conditions and on the occurrence of specified events. Among others, the following notification requirements apply (Article 19(3 bis) of the CL):</p> <p>Any person who intends to acquire or dispose of a qualifying shareholding (10 percent or more) must give prior notice to the BI. Prior notice has to be given also where the increase or decrease in shareholding exceeds one of the established thresholds (20, 30, and 50 percent of voting capital) or determines the acquisition or loss of company's control. BI verifies that integrity requirements are met and that the acquisition or the disposal of the shareholding does not jeopardize the sound and prudent management of the intermediary or holding company. BI staff indicated that there is more room to assess integrity in the context of a change in ownership, as other aspects can be taken into consideration beyond the integrity requirements established in the MEF Decree. Furthermore, the authorities provided examples of cases where a change of ownership was denied.</p> <p>Any agreement governing the exercise of votes attached to shares that exceeds the thresholds mentioned above must be notified within five days from the date of conclusion.</p> <p>A change in the board of directors, board of auditors, general managers, persons who perform functions equivalent to those of general manager or internal auditors, within 30 days.</p> <p>The dates of commencement, interruption and resumption of the performance of each authorized investment service, within 30 days.</p> <p>Any change in the constituent document, by-laws or organizational structure (in the latter case every year) and in general every other significant change, within 30 days.</p> <p>In addition, the board of auditors and the external audit firm must inform the BI and Consob without delay of any acts or facts they come across in the performance of their duties that may constitute a management irregularity or a violation of the provisions governing the activity of Italian investment firms (Article 8(3) and (4) of the Consolidated Law).</p> <p>Corporate officers (directors, members of the board of auditors and senior management) who cease to meet integrity requirements set forth in MEF Decree 468/1998 must be suspended. Revocation of their appointment is then decided:</p> <ul style="list-style-type: none"> • by a general meeting of shareholders for directors and members of the board of auditors; • by the board for senior managers (Article 4 of MEF Decree 468/1998). <p>If the board does not act, Consob or the BI can disqualify a person. Other than when a board member ceases to meet such requirements, or when an automatic disqualification applies because of administrative sanctions for maker abuse or public offering, neither the BI nor Consob can remove an individual director. In practice, the BI in particular has recommended removal of directors (or appointment of an independent director) in small firms, for example, where the shareholders are also the members of the board. When an on-site inspection detects weaknesses in the operation of the firm, BI convenes the board and requests the changes. BI staff informed that very often such</p> |
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| | <p>requests are met, although not in all cases.</p> <p>Where qualifying shareholders (holding 10 percent or more of a firm’s capital) do not fulfill the requirements established by the MEF Decree 469/1998, the voting rights attached to the shares exceeding the threshold cannot be exercised, and purported exercise of them is void.</p> <p>Powers of the regulatory authorities</p> <p>The BI and Consob have extensive powers of intervention where an authorized entity fails to comply with its obligations, including licensing requirements. These include:</p> <ul style="list-style-type: none"> • the power to convene meetings of an entity’s directors, board of auditors or managers (Article 7(1) of the CL); • the BI can exercise powers for stability purposes under Article 7(2) of the CL. These include the power to restrict operations; to prohibit the distribution of dividends and the payment of interest on interests forming regulatory capital; and limit the variable component of remuneration; • the power to take injunctive measures and order persons subject to their supervision to put an end to irregular conduct, including by prohibiting the firm from engaging in further transactions or placing other limitation with regard to each type of transaction involving single services or activities, where the violations are likely to prejudice interests of a general nature or there is an urgent need to protect the interests of investors or the market (Articles 51–52 of the CL); • in situations that endanger investors or the market, the BI and the Chairman of Consob may suspend the administrative bodies of, respectively, a bank and an investment firm as a matter of urgency and appoint a provisional administrator to take over its management where there is evidence of serious administrative irregularities or serious violations of laws, regulations or by-laws (Article 76 of CL on Banking and Article 53 of the CL); • the BI, acting on its own initiative or on a proposal from Consob, can suspend the voting rights attached to a qualifying shareholding in an investment firm where the influence exercised by the shareholder is likely to be prejudicial to the sound and prudent management of the intermediary or obstruct its effective supervision (Article 16 of the CL). <p>The MEF, acting on a proposal from the BI or Consob, may also (i) dissolve the administrative and control bodies of the firm, where certain circumstances occur (serious violations, serious capital losses, etc.) (Article 70 of the Consolidated Law on Banking and Article 56 of the CL); and (ii) withdraw authorization to carry on business and order the compulsory administrative liquidation of a firm where administrative irregularities or the violations of laws, regulations or bylaws are exceptionally serious (Article 80 of the CL on Banking and Article 57 of the CL).</p> <p>Public disclosure of licensed intermediaries</p> <p>Consob is required to enter investment firms (Italian, EEA and non-EEA) authorized to provide services in Italy in a register (Article 20 of the Consolidated Law). This register can be accessed by the public on Consob’s website. The register contains details about the firm and the services it is authorized to provide, and whether it is subject to any major intervention procedure such as administration or compulsory liquidation. Additional information—such as financial statements and the names of the intermediary’s senior management and of other individuals authorized to act in its</p> |
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| | <p>name—is included in documents filed with the public Register of Companies.</p> <p>A register of financial salespersons is held by the Authority for the Single Register of Financial Salesmen operating under Consob's supervision (Article 31 of the CL). It is publicly available and indicates, for each financial salesperson: name; date and place of birth; place of residence; date of entry in the register; name of the authorized intermediary on whose behalf the financial salesperson works; any suspension in force in the form of a precautionary measure or a sanction.</p> <p>Investment Advisers</p> <p>In line with the requirements of the MiFID directive (2004/39/EC), investment advice about financial instruments is an activity requiring the provider to hold an authorization as an investment service provider.</p> <p>Advisers are subject to the same obligations as other investment services providers, including: capital and operational control requirements; rules about the segregation of client assets; record keeping requirements; and rules about conflicts of interest.</p> <p>Advisers not dealing on behalf of clients (financial advisors and financial consulting companies under Articles 18<i>bis</i> and 18<i>ter</i> of the Consolidated law) are not allowed to hold client funds or financial instruments.</p> |
| Assessment | Broadly Implemented |
| Comments | <p>File reviews of the processes used by Consob in authorizing IFs showed that the process is very robust and that Consob staff, with input from the BI, carry out thorough analysis of applications. BI also does a thorough analysis of banks wishing to provide investment services.</p> <p>However, the assessors have the same concern about the definition of fit and proper and the application of the integrity test for directors and senior managers as is discussed in the comments of Principles 3 and Principle 24. This limitation is compounded by the lack of power of BI and Consob to remove individual directors. The assessors acknowledge however that the supervisory authorities have used other tools at their disposal, such as the convening of the board, to request changes in board members when they were deemed necessary, and that in the majority of the cases such request have been met by the regulated entities. Therefore the broadly implemented grade.</p> <p>As noted in the comments under Principle 1, it seems desirable for the BI to consult formally with Consob in relation to applications by banks for authorization to provide investment services. That would ensure that Consob's perspective, informed by its experience as the conduct and transparency regulator, was made available to the BI during the authorization assessment process.</p> <p>Finally, the deadline for notification of certain events appears long, in particular those under a 30-day deadline.</p> |
| Principle 30. | There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake. |
| Description | <p>Capital requirement</p> <p>Authorized firms are subject to minimum and ongoing capital requirements. IFs that provide only advisory services and do not hold client funds or assets are subject only to the minimum initial capital.</p> |

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| | <p>Capital standards are set by the BI after consultation with Consob. The BI's Regulation of October 27, 2007 implements the European capital adequacy directive (Directive 2006/49/EC), as amended.</p> <p>As described in the BCP, in the case of banks the regulatory framework applies the same definition of capital, risk coverage, calculation and thresholds for internationally and non-internationally active banks. These are derived from the transposition of Basel II and II.5 into the European framework, as transposed into Italian legislation. Further details on the capital regime applicable to banks can be found in the BCP assessment.</p> <p>Thus the comments below will focus mainly on capital for IFs.</p> <p><i>Minimum capital</i></p> <p>Minimum capital required under BI Regulation is as follows:</p> <p>(a) EUR 120,000 for IFs that offer only investment advice on a risk-free basis, provided they are not authorized to hold, even temporarily, clients assets;</p> <p>(b) EUR 385,000 for IFs that offer the following investment services on a risk free basis, provided they are not authorized to hold, even temporarily, client assets: placement, without firm commitment underwriting or standby commitments to issuers; portfolio management; receipt and transmission of orders. The same amount is required for firms that, in addition to one or more of these services, also provide investment advice;</p> <p>(c) EUR 1 million for IFs that provide the following investment services:</p> <ul style="list-style-type: none"> • any of the services mentioned under a. or b. where the services are not provided on a risk-free basis or where the firms are authorized to hold their clients' assets; underwriting of financial instruments and/or placement, with firm commitment underwriting or standby commitments to issuers; dealing on own account; execution of orders on behalf of clients; • operation of MTFs. IFs are required on an ongoing basis to comply with minimum capital requirements. <p>As discussed in the BCP the loss absorption portion of capital seems higher than in the general European framework, but still allowing that a large part of capital be composed of instruments other than common shares. In practice however, no tier 1 hybrids have been issued by IFs and the total amount of tier 2 and tier 3 included in the regulatory capital is negligible at aggregate level.</p> <p><i>Ongoing capital requirements</i></p> <p>Banks and IFs are subject to risk-based supervisory capital requirements fixed by the BI (after having consulted Consob) that address the risks of the investment services the firm is authorized to provide. These capital requirements are designed to address the following categories of risk: position risk on debt and equity securities; settlement risk; counterparty risk; credit risk; foreign exchange risk; concentration risk; risk on positions in commodities; operational risk, and other risks.</p> <p>For banks' supervisory capital requirements, the BI rules follow Basel Committee standards and the Guidelines issued by European Banking Authority. BI's supervisory instructions require continuing compliance on both a solo and consolidated basis. The BI has power to impose additional capital charges that must be included in calculating</p> |
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| | <p>the overall capital requirement.</p> <p>The BI's Regulation on prudential supervision for IFS establishes the capital adequacy supervisory framework based also on the Basel three "pillars" approach (BI Regulation of October 24, 2007).</p> <p>Capital requirements for IFS vary according to the nature and amount of risk assumed by the firm on an ongoing basis. For each class of firm, the capital rules specify the risks that are used to determine the amount of supervisory capital they must hold. IFS must have adjusted tier 2 capital at least equal to the capital requirement provided for with respect to credit risk and operational risk as well as supplementary tier 3 capital.</p> <p>The supervisory capital of an IFS must at all times be at least the required minimum initial capital.</p> <p><i>Liquidity requirements</i></p> <p>As described in the BCP assessment, banks are subject to liquidity requirements. In general, banks are required to formalize their policies for the governance of liquidity risk and implement an effective process for its management, in accordance with the characteristics, scale and complexity of the activities performed and taking into consideration the relevance of the bank in the market of each EU country in which it operates. Banks are required to identify and measure liquidity risk on a forward looking basis according to a methodology similar to the Basel 3 coverage ratio, even though the use of internal models to measure inflows and outflows is permitted to a limited extent. Banks must keep a liquidity buffer consistent with the chosen risk appetite. Compliance with the regulatory framework is reviewed through off-site and on-site examination within the SREP, which also includes an overall evaluation of the liquidity risk profile of the bank. A similar requirement is in place for IFS.</p> <p>The authorities informed that with the implementation of CRDIV liquidity ratios will also be imposed in banks. The discussion of whether such ratios would also apply also to IFS is on-going. BI informed that it included the two largest IFS in the sample of ISPs which information has been given to EBA, to analyze the impact of the application of the liquidity ratios.</p> <p><i>Information and Accounting systems data</i></p> <p>As further described in Principle 31, BI and Consob Regulation of October 29, 2007 sets standards for a regulated entity's information systems and accounting and management information systems. Accounting and management information systems must be reliable, permit the correct and prompt recording of transactions and provide a true view of risks to which the intermediary is exposed and of its profits and losses, assets and liabilities and financial position.</p> <p><i>Reporting</i></p> <p>Banks and banking groups are required to send the BI periodic reports regarding capital adequacy (quarterly at the solo level, and half-yearly at the consolidated level). Banks and banking groups also transmit detailed monthly data on their financial activity. The rules on disclosure in financial statements require that specific data should be provided on banks' securities and foreign exchange trading and on supervisory capital cover.</p> <p>IFS are required to report regularly to the BI on:</p> <ul style="list-style-type: none"> • assets and liabilities |
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| | <ul style="list-style-type: none"> • profit and loss account; • aggregate portfolio composition and position on financial instruments held at the reference date; • supervisory capital; • capital requirements; • data on the flow of transactions and on assets under management; • balance sheet statements. <p>The frequency is the same for all IFs providing the same investment services. Different reporting intervals are set for different types of information.</p> <p>Reports on the aggregate portfolio composition, supervisory capital and capital requirements listed above are reported monthly by IFs authorized to deal for own account and placement with firm commitment underwriting or guarantees to issuers. Reports on supervisory capital and capital requirements are reported quarterly by other IFs. Reports on assets and liabilities, and data on the transaction flows and assets under management are submitted quarterly; profit and loss account semi-annually and balance sheets statements must be submitted annually.</p> <p>Independent audit</p> <p>As PIEs, banks and IFs are required to have their financial statements audited by independent external auditors. As well as auditing the financial statements, the external auditor is required to assess the overall reliability of the internal control system, including the organizational structure and internal control function.</p> <p>Monitoring by regulator</p> <p>The BI monitors exposure to risks on a continuous basis using the periodic reports on capital adequacy and the statistical data on banks' balance-sheet and income items. The BI has formulated guidelines for the analysis of financial risks and developed instruments for calculating the VaR of the trading book.</p> <p>Information on the financial condition of intermediaries and their supervisory capital position is used to inform the BI's risk management system.</p> <p>Regulator's powers of intervention</p> <p>The BI has powers to deal with a IF's failure to comply with capital requirements, including powers to: impose more stringent capital requirements on intermediaries (Article 7(2) of the Consolidated Law); order them to put an end to the irregularities (Article 51(1) of the Consolidated Law); prohibit the intermediary from engaging in new transactions including with respect to single services or activities, as well as to single branches or establishments (Article 51(2) of the Consolidated Law).</p> <p>If an intermediary fails to restore its supervisory capital after it has fallen below the required minimum, BI or Consob may adopt specific precautionary measures provided for by the law, such as special administration or compulsory administrative liquidation (Articles 56 and 57 of the Consolidated Law).</p> <p>At April 30, 2012, 17 IFs and 1 branch of a European investment firm were subject to compulsory administrative liquidation procedures.</p> <p>BI staff informed that when they see profitability deteriorating, they make projections of when the losses would result in a breach of capital requirements, and based on such</p> |
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| | <p>analysis they send formal warning letters to the firm asking it to take measures to top up the capital. Assessors were presented with examples of cases where such actions were taken. In one case, a warning letter was followed up by request to Consob to extend a planned inspection to check on capital requirements. Eventually such case triggered additional actions, including a pecuniary sanction to the board and members of the auditing board.</p> <p>Risks from outside the regulated entity</p> <p>Ongoing capital requirements take into account both on- and off-balance-sheet items. IFs belonging to banking groups or to groups of investment firms are subject to consolidated supervision provided for this kind of group (in Italy or in an EU country). For IFs that are not part of a banking group, Italian regulation conforms with the European capital adequacy directive.</p> |
| Assessment | Fully implemented |
| Comments | |
| Principle 31. | Market intermediaries should be required to establish an internal function that delivers compliance with standards for internal organization and operational conduct, with the aim of protecting the interests of clients and their assets and ensuring proper management of risk, through which management of the intermediary accepts primary responsibility for these matters. |
| Description | <p>Background</p> <p>Requirements for banks and IFs to have adequate internal functions are set out in Consob and BI Regulation of October 29, 2007; provisions in Consob Regulation 16190/2007; and in the BI supervisory instructions on bank’s organization and corporate governance of March 4, 2008.</p> <p>Corporate Governance</p> <p>Part 2 Title 1 of BI and Consob Regulation of October 29, 2007 sets out detailed requirements for corporate governance, organization requirements, remuneration and incentives systems, continuity of business, and accounting and administrative organization.</p> <p>Article 6 of the Regulation contains principles to guide corporate governance, in particular it requires intermediaries (i) to define the duties of different corporate bodies with a view to ensuring balancing of powers and effective and constructive dialogue; (ii) to take precautions to prevent prejudicial effects on management from the joint presence in the same body of two or more functions (strategic, managerial, control); and (iii) to ensure membership in corporate bodies, in terms of number and professionalism, that enables them to perform their tasks adequately.</p> <p>Articles 8–10 of the Regulation define the responsibilities of the key internal governance organs:</p> <ul style="list-style-type: none"> • the strategic supervisory body: identifies the objectives, strategies, profile and risk levels, defining company policies and those of the risk management system; checks the correct implementation and coherent evolution of the business activity ; approves processes related to the services and regularly verifies their suitability; • the management body: implements the corporate policies and those of the business risk management system; constantly verifies suitability of the business risk management; defines flows of information; duties and responsibilities of the |

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| | <p>corporate structure and ensure that policies and procedures are communicated to staff;</p> <ul style="list-style-type: none"> • and the control body (<i>collegio sindacale</i>) which is responsible for compliance with the obligation to report irregularities in management and breaches of rules governing the provision of services. <p>Internal Organization</p> <p>As a general principle article 5 of this Regulation requires intermediaries to have an organizational structure that aims to ensure healthy, prudent management, limitation of risk and stability of equity. To this end intermediaries must have (i) robust corporate governance arrangements, including decision making and an organizational structure that clearly specific the hierarchical relations, and breakdown in functions and responsibilities, (ii) effective business risk management systems; (iii) measure to ensure that all relevant parties know the procedures; (iv) suitable internal control mechanisms; (v) policies and procedures to ensure that staff has the qualifications, skills and knowledge necessary; (vi) effective communication of information; (vii) systems and procedures to ensure appropriate recording of management events; (viii) criteria and procedures aimed at guaranteeing that the assignment of multiple functions to relevant parties does not prevent them from adequately carry out their functions; (ix) procedures and system able to protect security, integrity and confidentiality of information, (x) policies, systems, resources and procedures to ensure continuity of services, (xi) accounting procedures and policies that enable the timely supply of documents to the supervisory authorities.</p> <p>Intermediaries are required to regularly control and evaluate the suitability and effectiveness of such requirements and to take measure to address any deficiency.</p> <p>Pursuant to this Regulation, IFs must have in place the following control functions:</p> <ul style="list-style-type: none"> • a compliance function: assesses the suitability and effectiveness of the procedures adopted to ensure the intermediary's compliance with laws and regulation(Article 16) • a risk management function: collaborates in the definition of the business risk management system; oversees its functioning and verifies compliance with it (Article 13); and • an internal audit function: assesses the suitability and effectiveness of the intermediary's control processes, procedures and mechanisms (Article 14). <p>To ensure their independence the Regulation requires that (i) the functions have the authority, resources and competencies necessary to carry out their functions; (ii) the managers are not hierarchically subordinate to the managers of the departments they control and are appointed by the management body by agreement with the strategic supervisory body, and with consultation with the control body; they report directly to the corporate bodies; (iii) they must not participate in the provision of the services they control; (iv) they are separate in organizational terms, (v) and the methods to determining the salaries of the relevant parties do not compromise their objectivity. Exceptions can be made in connection with (iii), (iv) and (v) based on proportionality, and provided that the function remains effective.</p> <p>Information systems</p> <p>BI and Consob Regulation of October 29, 2007 also sets standards for a regulated entity's information systems and accounting and management information systems.</p> |
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| | <p>Accounting and management information systems must be reliable, permit the correct and prompt recording of transactions and provide a true view of risks to which the intermediary is exposed and of its profits and losses, assets and liabilities and financial position.</p> <p>Accounting and information systems must be structured taking into consideration the need to:</p> <p>Ensure that the framework for segregation of assets is complied with by adopting measure that at all times allow the financial instruments and cash of customers to be distinguished from those of the intermediary;</p> <ul style="list-style-type: none"> • Allow to reconstruct all transactions carried out for each customer and the overall position; • Know the volume of business for each investment service provided and the related costs and revenues; • Enable the timely supply to the regulatory authorities of documents providing a faithful picture of the financial and economic position, and which comply with all principle and all rules, including of accounting, that apply. <p>Finally the information systems must ensure a high level of security. Procedures and systems must be able to protect the security, integrity and confidentiality of information considering the nature of the information and guarantee of the continuity and regularity of services.</p> <p>Outsourcing</p> <p>By Article 21 of Consob and the BI Regulation of October 29, 2007, intermediaries outsourcing essential or important operative functions or any investment business or service remain liable for compliance with all obligations relating to investment services or their business and specifically must ensure that: outsourcing does not involve the delegation of responsibility by corporate bodies; no changes are made to the relationship and obligations of the intermediary with regard to its customers; there is no risk to compliance by the firm with the preconditions of its authorization or its ongoing obligations; no other conditions to which the intermediary's authorization is subject are suppressed or changed.</p> <p>Outsourcing cannot reduce the effectiveness of the control system nor prevent the supervisory authorities from checking that intermediaries fulfill all their obligations (Article 19(2) of Consob and the BI Regulation of October 29, 2007).</p> <p>Evaluation of compliance, internal controls and risk management</p> <p>As indicated above, IFs are required to have in place internal functions for compliance, internal controls and risk management. These units serve as a first line in connection with the monitoring of compliance, as they are required to provide annual reports to the board in their respective areas. Such reports must also be sent to Consob and BI.</p> <p>In addition, as well as auditing the financial statements, the external auditor of an IF is required to assess the overall reliability of the internal control system, including the organizational structure and internal control function.</p> <p>Finally, the BI evaluates the adequacy of internal controls, risk management and compliance as part of the analysis it performs of the intermediary's overall organization. This assessment is performed through off-site review of documentation concerning controls (including by-laws, organization charts and internal rules) and periodic</p> |
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| | <p>meetings with the bank's officers to review problems brought to light by off-site analysis and on-site inspections.</p> <p><i>Protection of clients</i></p> <p>Authorized intermediaries are under a general obligation to act diligently, fairly and transparently in the interests of customers and the integrity of the market. They also must have resources and procedures, including internal control mechanisms, suitable for ensuring the efficient provision of services and activities (Article 21(1) of the Consolidated Law). Specific aspects of this obligation are elaborated in the BI and Consob Regulation of October 29, 2007.</p> <p><i>Investor complaints</i></p> <p>Article 17 of the BI and Consob Regulation of October 29, 2007 requires intermediaries to adopt procedures that are able to assure a timely processing of any complaints made by retail customers or potential retail customers. The terms and conditions for the processing of complaints must be communicated to customers in advance. Records of the essential elements of each complaint received must be recorded together with steps taken to solve the problem raised.</p> <p>In its annual report, the compliance control function must report, among other things, on the overall situation of complaints received (Article 16(3) of the BI and Consob Regulation of October 29, 2007).</p> <p>In addition, all investment service providers, including banks, are part of the alternative dispute resolution mechanisms managed by Consob.</p> <p><i>Client funds and assets</i></p> <p>The segregation of client assets is required by the legislation and related regulations (Articles 6 (1.b), and 22 of the Consolidated Law and BI Regulation of October 29, 2007, adopted with the agreement of Consob). Article 22 of the CL stipulates that the financial instruments and funds of individual customers held in whatever capacity by an IF, and the financial instruments of individual customers held in whatever capacity by a bank must be separate for all intents and purposes from those of the intermediary and from those of other customers.</p> <p>Actions with respect to such assets may not be brought by creditors of the intermediary or on behalf of such creditors, nor by creditors of the custodian or sub-custodian, if any, or on behalf of such creditors. Creditors of individual customers may bring actions up to the amount of the assets owned by such customers.</p> <p>Unless customers have agreed otherwise in writing, IFs and banks cannot use on other own behalf or on behalf of third parties financial instruments belonging to their customers. Nor may investment firms use on their own behalf or on behalf of third parties liquid balances belonging to customers.</p> <p>IFs must deposit money received by clients in a bank before the end of the business day following their receipt. The deposit account is opened in the name of the depositing IF with a note that the deposit is made on behalf of its clients. These deposit accounts are kept separate from those of the intermediary.</p> <p>Market intermediaries may—with the written consent of clients—sub-deposit financial instruments in central depositories or other authorized sub-depository entities. Specific accounting rules apply regarding the depository where clients' assets are deposited</p> |
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| | <p><i>DEA</i></p> <p>In April 2012, the BI and Consob published a joint communication in the form of Guidelines to "Systems and controls in an automated trading environment for platforms, investment companies and competent authorities". These guidelines implement ESMA "Guidelines on systems and controls in a highly automated trading environment for trading platforms, investment firms and competent authorities" (ESMA 2011/456). The Italian version of the official ESMA document was published in April 2012 in the form of Guidelines to "Systems and controls in an automated trading environment for platforms, investment companies and competent authorities."</p> <p>Among other things, the Guidelines deal with DEA or sponsored access to the market.</p> <p>In particular Guideline 8 requires intermediaries that provide sponsored access or direct market access to establish policies and procedures to ensure the trading of those clients complies with the rules and procedures of the relevant trading platforms to which the orders are submitted. Intermediaries offering DEA can use pre and post trade controls, which can be proprietary, bought from a vendor, provided by an outsourcer or offered by the platform itself (i.e., they should not be the controls of the direct market access/sponsored access client). Intermediaries remain responsible for the effectiveness of controls and have to be solely responsible for setting up the key parameter, and modify the parameters of the pre-trade controls.</p> <p>Currently 25 banks/ investment firms provide direct market access (DMA) services to clients (non sponsored). Consob has recently sent letters to such firms to highlight the importance of complying with the Guidelines.</p> <p>Know your client and suitability rules</p> <p><i>Customer due diligence</i></p> <p>Legislative Decree 231/2007 transposes the European money laundering Directive and its related legislation. It requires intermediaries to comply with the customer due diligence requirements in connection with relationships and transactions relating to the performance of their institutional or professional activity. Any person who opens, changes or closes a business relationship, or carries out a single transaction, or several transactions which appear to be linked, amounting to EUR 15,000 or more must be identified as well as the person, if any, on whose behalf the transaction is carried out. Identifying details of the customer and where relevant the beneficial owner must be verified and recorded.</p> <p>Records relating to the opening of an account must be kept for 10 years.</p> <p><i>Suitability requirements</i></p> <p>In providing investment and non-core services, intermediaries must acquire the necessary information from customers (Articles 39 ff of Consob Regulation 16190/2007).</p> <p>In particular, before entering into contracts for portfolio management or investment advice services and starting to supply investment services or related non-core services, authorized intermediaries must ask investors for information about their awareness and experience in investing in financial instruments, financial position and investment objectives before recommending investment services or products to the customer or potential customer.</p> <p>Based on such information the intermediaries must assess whether the transaction</p> |
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| | <p>recommended or executed as part of the provision of portfolio management services is suitable for the client, using as criteria: (i) correspondence with the customers' investment objectives, (ii) nature of the transactions, and (iii) whether the customer has the necessary experience and awareness of the nature of the transaction to understand the risk involved (the suitability test).</p> <p>When providing investments services other than portfolio management and investment advice, the intermediaries must request information from the customer or potential customer regarding his/her awareness and experience in the investment sector relevant to the type of instrument or service proposed or requested. Based on such information the intermediary must verify that the customer has the necessary level of experience and awareness to understand the risks deriving from the instrument or investment service offered or requested (the appropriateness test).</p> <p>Under MiFID, these provisions do not apply to intermediaries providing execution-only services, provided that specified conditions are satisfied; including clearly informing the client that the intermediary is not obliged to assess appropriateness and therefore that the customer will not benefit from the protections derived from such obligation.</p> <p>If intermediaries providing investment consultancy or portfolio management services are unable to obtain the necessary information from clients, they must abstain from providing those services.</p> <p>For investment services other than consultancy or portfolio management, if the customer or potential customer decides not to provide the necessary information, or where such information is insufficient, the intermediaries must advise the customer or potential customer that such a decision inhibits any intermediary verification that the service or instrument is appropriate to the customer. To this end intermediaries will have to consider any information available (i.e., age, professional qualifications, propensity to incur risks assessed also on the basis of historical data pertaining past activities). The intermediaries may rely on the information provided by the customer or potential customer unless it is clearly exaggerated, incorrect or incomplete.</p> <p>The acquisition of relevant information is a dynamic process, which implies the obligation to periodically update such information.</p> <p>In March 2009, Consob issued guidance on the distribution of illiquid products (Communication 9019104). It provides recommendations to intermediaries on how to comply with the legislation implementing MiFID in relation to the distribution of illiquid products (such as structured products and OTC derivatives) to retail clients, and is designed to prevent mis-selling of these products. It sets out in detail the analysis and assessment an intermediary should undertake before deciding on the suitability or appropriateness of these products for a retail client.</p> <p>Disclosure to clients</p> <p><i>Customer access to terms and conditions of services</i></p> <p>Pursuant to MiFID provisions, article 23 of the CL requires IFs to enter into written contracts with retail clients for the provision of investment services or non-core services, except for the provision of advisory services. A copy of this contract is given to the customer. Details of what is required in these contracts are set out in Article 37 of Consob Regulation 16190/2007 and additional requirements for portfolio management services in Article 38. Among other things, the contract must contain details of the services to be provided and fees.</p> |
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| | <p><i>Information to clients</i></p> <p>Articles 27–32 of Consob Regulation 16190/2007 require intermediaries to provide information to retail clients and set out the details of the information required. This includes details about: the intermediary and the services it provides; the safeguarding of client assets; financial instruments; and costs and charges.</p> <p><i>Reporting to clients</i></p> <p>Intermediaries must provide detailed information to clients about:</p> <ul style="list-style-type: none"> • the receipt, transmission and execution of orders and fees applying—for retail clients information must be provided no later than the first business day after the execution of the order (Article 53 of Consob Regulation 116190/2007); • portfolio management services—for retail clients, this must contain details about the client’s portfolio, including fees. These reports must be sent every six months, or quarterly if requested by the client, or annually if the client receives information each time a transaction is executed. Where the client portfolio is leveraged, the report must be given each month (Article 54). <p>An intermediary that holds financial instruments, cash or cash equivalents belonging to clients must provide each client, at least once a year, with a statement about the client’s assets holdings (Article 56).</p> <p><i>Books and records</i></p> <p>Article 29 of the BI and Consob Regulation of October 29, 2007 requires that, for all services provided and all operations carried out, intermediaries must keep suitable, orderly records of activities that enable the supervisory authorities to verify compliance with rules on investment services and business and accessory services and, in particular, the fulfillment of obligations with regards to customers or potential customers. These records must be kept for at least five years. Records must be kept on storage devices that enable the information to be saved and easily recovered so as to enable regulatory authorities to have prompt access and reconstruct each essential stage of each operation.</p> <p><i>Conflicts of interest</i></p> <p>Article 23 of the BI and Consob Regulation establishes general principles to guide the management of conflicts of interest, in particular (i) intermediaries must take all reasonable steps to identify conflicts of interest that may arise with the customer or between customers, (ii) intermediaries must also manage conflicts of interest by taking suitable organizational steps and by ensuring that the assignment of more than one function to relevant parties involved in activities involving conflict of interest not prevent them from acting independently, (iii) when the steps taken in accordance to (ii) do not suffice to ensure that the risk of harming the interest of customers is avoided, then the intermediaries must inform customers clearly, before acting on their behalf of the nature and/or sources of conflict, so that they can make an informed decision, and (iv) the information pursuant to (iii) must be kept in a permanent record device and must be of sufficient detail.</p> <p>Intermediaries are required by Article 25 of the Regulation to have a written and effective conflicts of interest management policy in line with the principle of proportionality.</p> <p>The conflicts of interest management policy must: enable the identification, in relation</p> |
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| | <p>to investment services and business and accessory services provided, of the circumstances that generate or may generate conflicts of interest able to seriously damage the interests of one or more customers; define the procedures to be followed and steps to be taken to manage such conflicts. In connection with this obligation, the Regulation requires intermediaries to adopt measures and procedures aimed at (i) preventing or controlling exchange of information between relevant parties involved in activities entailing a risk of conflict of interest when the exchange may damage the interest of one or more customers; (ii) guaranteeing separate supervision of relevant parties whose main functions involve interest that are potentially in conflict with those of the customer ; (iii) eliminate any direct connection in the remuneration of relevant parties with the activities that generate the conflict of interest; (iv) prevent or limit the exercise of influence by a relevant party; (v) prevent or control the simultaneous participation of a relevant party in different services or business, when this may harm the correct management of conflicts of interest.</p> <p>Intermediaries are required to establish and regularly update a registry in which they must record (i) the type of investment services or accessory services concerned, (ii) the situation that has given rise to the conflict of interest, or in case of services underway, the situation that might give rise to such conflict that can significantly harm the interest of one or more clients.</p> <p>Supervision</p> <p><i>Consob</i></p> <p>Ongoing supervision of IFs is carried out by Consob's Office of Authorization and Supervision of Investment Firms within the Intermediaries Division. The office consists of 24 staff.</p> <p>Consob's IT systems are sophisticated and contain comprehensive data on each intermediary. This data includes both quantitative data, such as holdings of each client of an intermediary, and qualitative such as the intermediary's business plan and budget. This information, which stems from the periodic reporting obligations of the IFs is complemented with information coming from other sources, including investors' complaints. All this information is used as the basis for the monitoring of IFs. A risk based approach is taken to supervision. Two systems are used:</p> <ul style="list-style-type: none"> • an early warning system: The early warning system applies to all IFs. Inputs into the system are quarterly statistical data and data from prospectuses issued by Ifs (mainly banks). The Consob system analyses this data and produces risk indicators relating to the conduct implications of this data. For example, the data analyzed includes execution services, placement or distribution activity, portfolio management and the stock of client assets. It highlights potential areas of conflicts of interest, risky and complex products, and innovative products, as well as rapid changes in business activity. This is used for identifying risks particularly in smaller firms. If the early warning system shows high risk, this triggers immediate supervisory action, including potentially an on-site inspection. Consob provided specific examples where the early warning did trigger the on-site inspection of smaller firms. • an annual rating system: This system is applied to a subset of regulated firms (about 150). Selection criteria used are size (number of clients, market share etc), and the nature and degree of inherent risk in the activity carried on by the firm. Firms are clustered into subgroups with like characteristics. Detailed analysis is undertaken of each firm's business model, client base, services, distribution channel and market share; and other factors such as information from firm reports and financial |
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| | <p>statements, client complaints and information received from supervision activities. Risk ratings are assigned on the basis of quantitative and qualitative factors, on a scale of 1 (high risk) to 5 (low risk), using a standardized methodology and weighting system. Firms rated in the higher risk categories are subject to more intensive off-site supervision and are usually also subject to an on-site inspection.</p> <p>A mixture of off-site supervision and on-site supervision is used.</p> <p>A variety of interventions are used in off-site supervision, including requests for data and information, formal convening of meetings with an intermediary's management or its board, and in egregious cases injunctive action or the commencement of sanctioning procedures. For example, 130 requests for information were made in 2012.</p> <p>On-site inspections are carried out by Consob's Inspectorate Division, sometimes with staff from line supervision area as part of the inspection team (see Principle 12 for more detailed description of the on-site inspection process). The number of on-site inspections is established as part of the annual planning process, with the line supervision area deciding on which firms are to be subject to on-site inspections. On-site inspections may also be undertaken on an ad hoc basis if required. Typically, on-site inspections are wide scope (but not full scope), for example covering the adequacy of internal controls and governance, but—varying according to the particular circumstances of the firm involved—also focusing on key risk areas. Since the introduction of MiFID, compliance with client suitability obligations is almost always part of the scope of inspections. Inspections include detailed reviews of individual transaction files (for example, individual client files).</p> <p>During 2009–2010, Consob conducted thematic inspections on the nine largest banks to verify their compliance with MiFID. Follow up inspections were carried out in two cases (and two more are planned for this year).</p> <p>Consob can also use resources from the Finance Police (the <i>Guardia di Finanza</i>) to carry out inspections on its behalf in cases where there is a need to use their specialist expertise, such as in forensic examination of computer systems.</p> <p>Consob indicated that when the weaknesses detected via on-site inspections are significant, they convene the board of the intermediary and request that the board develops a specific plan for remedial actions. In 2012, Consob required 10 such meetings, 7 for banks and 3 for investment services providers.</p> <p><i>The BI</i></p> <p>The BI's Ongoing Supervision of banks is conducted by the Banking Supervision Department. Details on the supervision of banks are contained in the BCP assessment.</p> <p>The BI's ongoing supervision of IFs is carried out by the Investment Firms Division of the BI's Specialized Intermediaries Supervision Department. The division consists of 10 staff. IFs that are part of banking groups and banks authorized to carry on investment services are supervised by the banking supervision department. A number of IFs is supervised by three local branches (smaller firms acting mainly in local markets).</p> <p>In its supervision of IFs, the BI uses the standards methodology used by all supervision areas of the BI such as the bank supervision areas: the Supervisory Review and Evaluation Process (SREP). This consists of two phases, an evaluation phase and a correction/follow up phase. In the evaluation phase, conducted annually with a half yearly update, scores are attributed to risk areas (strategic; market, credit/counterparty and liquidity: operational and reputational) and cross-cutting profiles (governance and</p> |
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control system; profitability; and capital adequacy). The evaluation is a combination of quantitative and qualitative factors, and draws on extensive data sets held in the BI's systems, deriving from periodic reports from regulated entities, other information supplied by a firm, information from supervisory activities, complaints and notifications by the internal broad of auditors and external auditors. Risk scores are assigned on a scale of 1 (low risk) to 6 (high risk). Higher risk scores leads to more intensive supervision.

The focus of BI's ongoing supervision activities—both off-site and on-site—is typically capital adequacy (especially where a firm's poor earnings pose a risk), governance, organization and control systems.

BI staff highlighted that in their off-site activities they pay attention to small firms mainly because of the reputational risk for BI, as the BI has a low level of risk tolerance.

On-site inspections are carried out by the BI's inspection division. BI staff highlighted that on-site inspections are usually carried out on firms graded as a 4, as firms under 5 or 6 would already be subject to more intense scrutiny. The list can be complemented by size (i.e., inspections planned because of the size of the IFs).

As in the case of AMCs, the results of inspections are delivered to the firms in a meeting with the board convened for such specific purpose. An inspection can be followed up by different types of actions from remedial actions, to pecuniary sanctions on the board and members of the auditing board.

Consob and the BI share plans for carrying out on-site inspections, and the results of inspections. Each may request the other to cover issues relevant to their area of responsibility in an on-site inspection. For example, the BI has on a number of occasions requested a Consob on-site inspection to include BI issues in its scope. Some joint inspections have taken place.

On-site inspections of authorized investment firms

| Year | Consob on-site inspections Commenced | BI extensions of on-site inspections at the request of Consob | BI on-site inspections commenced [non-bank entities] | Consob extensions of on-site inspections at the request of BI | Total |
|------|--------------------------------------|---|--|---|-------|
| 2012 | 11 | 3 | 16 | 2 | 32 |
| 2011 | 8 | 5 | 10 | - | 23 |
| 2010 | 8 | 7 | 12 | 2 | 29 |
| 2009 | 12 | 6 | 15 | - | 33 |

Sources: Consob and the BI

Consob also supervises tied agents through its off-site supervision processes. On-site inspections are not used because Consob's focus is on the supervision obligations of the authorized intermediary for whom tied agents act. Supervision is based on reports Consob receives from intermediaries and investors, and from the Criminal Judicial Authority or the Criminal Judicial Police. In practice, around 70 percent of warnings come from the intermediary for whom the tied agent acts. Consob uses a specific rating

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| | <p>system to identify cases for intervention, based on the number of clients involved, the size of losses caused by the violating behavior, the likely sanction and the agent's compliance history.</p> <p>Enforcement measures as a result of supervision activities</p> <p>In both BI's and Consob's case weaknesses detected through both off-site and on-site supervisory work trigger requests for remedial actions.</p> <p>In the case of Consob the emphasis has been on the remedial actions. Consob explained that in practice the costs of remedial actions can be even more expensive than any pecuniary sanction that Consob can impose. In egregious cases, however, a sanction can follow the on-site inspection and a couple of cases were provided to that effect. In addition, in such type of cases, Consob may also impose some type of injunctive relief, and once case was provided to that effect. More often a pecuniary sanction or other type of disciplinary sanctions, such as suspension of a person, followed a second on-site inspection.</p> <p>In 2012, Consob imposed pecuniary sanctions on two employees of two IFs and employees of two banks, for a total of EUR 920,000.</p> <p>In 2012 the BI imposed pecuniary sanctions on employees of four IFs for a total of EUR 165,500.</p> <p>In 2012, Consob issued 457 warnings to tied agents, and commenced 71 sanction processes. It disqualified 59 agents, suspended 12 others and imposed 1 pecuniary sanction.</p> |
| Assessment | Broadly implemented |
| Comments | <p>Consob's and BI's off-site supervision of intermediaries is very robust. They have highly developed systems and use the data in these systems to support a sophisticated approach to regulation of intermediaries. They have detailed information about the intermediaries they regulate. In both cases their supervision focused on critical topics. In this regard the assessors note the emphasis by Consob on the intermediaries' business models and their implications for intermediary conduct. This has translated also in an emphasis of on-site work in connection with distribution practices.</p> <p>The assessors looked in particular at the case of potential miss-selling by banks of their debt instruments, including complex instruments, in the period following the financial crisis in 2008. Consob acted in 2009 and 2010 on the policy front by producing detailed guidance on illiquid products and how they were distributed to retail investors, and on steps needed to comply with suitability requirements for these products. It also carried out on-site inspections of nine banks to test compliance with MiFID requirements. It responded to problems detected by convening meetings with senior managements and boards of directors and requiring them to submit detailed remediation plans. It has followed up on the implementation of these plans, and is currently carrying out a second round of inspections.</p> <p>Nonetheless, the comments made under Principle 12 (and Principle 24) about the limited use of on-site inspections as a supervisory tool apply also to supervision of intermediaries by Consob and the BI. Consob's own experience illustrates that on-site inspections are essential to enable it to identify cases where a firm's processes are not working effectively in practice, or other factors such as incentive structures are influencing conduct in an undesirable way. The assessors acknowledge, however, that in</p> |

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| | terms of market share (both assets and number of clients) on-site inspections have covered a high percentage of the population. |
| Principle 32. | There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk. |
| Description | <p>Early warning systems</p> <p>Formal early warning systems such as capital trigger points are not used, but BI monitors compliance with capital requirements on a regular basis and the reports provided by intermediaries (described under Principle 30) give it information about all firms' profitability and compliance with supervisory capital requirements. In this regard, as stated above firms whose activities bear market risk are required to submit information on their supervisory capital and capital requirements on a monthly basis. For others, whose capital is more stable, such submission is done on a quarterly basis.</p> <p>BI staff informed that breaches are not frequent. Furthermore as indicated under Principle 30 their policy is that when they see problems in profitability, they immediately send official letters of warning to the firms requesting remedial action, and examples were given to that effect.</p> <p>Regulator's powers to intervene</p> <p>The regulators have powers to intervene in the event of crisis of an intermediary. They include:</p> <ul style="list-style-type: none"> • BI's powers to restrict operations; prohibit dividends distribution; prohibit payment of interest on financial instruments with form the regulatory capital; limit the variable part of remuneration (Article 7(2) of the Consolidated Law); • the powers of the BI and Consob to take injunctive measures, including by prohibiting an intermediary from engaging in new transactions (Articles 51 and 52 of the Consolidated Law); • the powers of the BI or the Chairman of Consob to suspend administrative bodies (Article 76 of the Consolidated Law on Banking and Article 53 of the Consolidated Law) and place the firm under special administration; • the power of MEF, on a proposal from the BI or Consob to dissolve the administrative and control bodies (Article 70 of the Consolidated Law on Banking and Article 56 of the Consolidated Law); • the power of MEF, on a proposal from the BI or Consob to withdraw authorization and require compulsory administrative liquidation (Article 80 of the Consolidated Law on Banking and Article 57 of the Consolidated Law). <p>Plans for dealing with failure of regulated firm</p> <p>Similar to banks, IFs and AMCs in Italy are subject to two special regimes designed to deal with crisis management and resolution of failed firms: special administration and compulsory liquidations. Both procedures are established with considerable detail in the CL. In addition, a regulation from BI further details such procedures.</p> <p>The special administration regime is designed to address crisis problems in "solvent" firms, and thus the objective of the administration is to address such problems and bring the firm back to normality. The administration is declared by the MEF, based on a request and consultation with both BI and Consob. On-site inspections usually precede applications to MEF for special administrations.</p> |

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| | <p>Special administrators have the same powers as the managers of the company had. The special administrators are third parties (individuals) not BI staff. BI is in charge of their appointment. BI selects them based on the type of firm involved and the problems detected in such firm, so that their profile matches the needs of the administration. An oversight committee composed of three external parties (not BI staff) must also be appointed by BI for each special administration. BI seeks to include individuals with a mix of expertise in such committees</p> <p>The special administrators are required to submit quarterly reports to the BI Unit; in practice more regular reporting (and consultation of difficult issues) occurs.</p> <p>BI staff informed that there is a success rate of roughly 50 percent of the cases; that is, in 50 percent of the cases the firms were back to normal.</p> <p>The compulsory liquidation is a process designed to deal with insolvent firms, and in essence is a bankruptcy procedure that takes place administratively (not in the judiciary). Liquidators are third parties (not BI staff), also appointed by BI. BI must also appoint an oversight committee. The liquidator's role is to take all actions necessary to liquidate the company, including the determination of creditors and their claims, sale of assets and the distribution of the firms' liquidated assets among the creditors. According to the legal framework, certain significant acts (such as a merger) required pre-approval by BI.</p> <p>In practice compulsory liquidations usually follow a "failed" special administration.</p> <p>In the last four years, three AMC were placed in special administration—and two went into compulsory liquidation; while five IFs were put into compulsory liquidation (including the two from special administration). Compulsory liquidations can be long, especially in cases of fraud. Currently there are 18 compulsory liquidations in process. BI staff indicated that a special task force (with seven specialized staff) has been appointed to address this problem. In the last six months this task force was able to close five of such cases.</p> <p>BI keeps a special register of experts that can be appointed administrators or liquidators. They are subject to a specific Code of Conduct and Guidelines issued by BI.</p> <p>Transfer of clients accounts</p> <p>Transfer of clients accounts usually takes place during the special administration, as in such case the administrator has the general powers of a manager. BI staff indicated that this is the procedure used in 99 percent of bank cases and 70 percent of IFs. In this case the procedure is quick (a simple transfer from one intermediary to another).</p> <p>In the case of compulsory liquidation, customers entitled to restitution of financial instruments and funds in connection with investment services are entered into a special section of the statement of liabilities. The liquidators are required to return such assets. Where the segregation of the firms' assets from those of the customers entered in the special section of the statement conforms with the law (article 22 of the CL) but the separation by customer of the assets of such customer is not respected or the financial instruments are not sufficient to effect all the restitutions, the liquidators where possible, effect restitutions pro rata according to the rights on the basis of which each customer was admitted in the special section of the statement or liquidate the financial instruments belonging to the customer and allot the proceeds on the same pro-rata basis. Customers entered into the special section participate with the unsecured creditors in full when the separation of the firm's assets from those of customers was</p> |
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| | <p>not respected or when such a separation was respected but the claims are not fully satisfied.</p> <p>BI staff informed that transfer of clients' accounts under a compulsory liquidation in practice can take between three to four months, because the Italian regime requires the liquidator to ascertain the existence of assets, and claims of investors and creditors. But these are usually cases that involve fraud.</p> <p>In connection with positions on derivatives markets, the rules of the CC&G allow the transfer of client positions but this must be done within three hours of the time at which default was confirmed or positions must be closed out. Given that currently intermediaries work with omnibus accounts, in practice transfer of positions usually cannot be achieved in the three hours stipulated by CC&G Regulations. Those positions are usually closed. BI staff informed that with the implementation of EMIR, clients will have the right to choose to have individual accounts which will facilitate transfer of positions rather than closing them out.</p> <p><i>Compensation schemes</i></p> <p>Authorized intermediaries must be members of an investor compensation scheme recognized by MEF after consulting Consob and the BI (Article 59 of the CL).</p> <p>Branches of EU IFs and banks established in Italy may supplement the protection provided by the compensation system in force in their home country by joining a recognized compensation system in respect of activity carried on in Italy. Unless they are members of an equivalent foreign compensation system, branches of non-EU investment firms and banks established in Italy must join a recognized compensation system in respect of activity carried on in Italy.</p> <p>Currently there is only one investor compensation scheme recognized by the MEF, <i>Fondo Nazionale di Garanzia</i> (FNG), which covers the activities of IFs and banks with respect to their investment services. The operation of the Fund is provided for under relevant by-laws and regulation, which are approved by the MEF, after having heard the BI and Consob.</p> <p>The FNG protects all types of investors against a defaulted firm, including corporate investors, for claims arising from the provision of investment services, except the following investors who are not covered: institutional investors, public entities, companies belonging to the same group of the defaulted firm, shareholders directly or indirectly holding at least five percent of the capital of the firm, directors, managers, statutory auditors and external auditors of the firm or of other group company, investors sanctioned for AML, investors contributing to the defaulted firm as determined in the insolvency proceedings and spouse or family members of the persons mentioned above.</p> <p>The cover is provided for claims arising as a result of the inability of the firm to (i) repay money owed to or belonging to investors and held on their behalf in connection with investment services, and (ii) return to investors any securities belonging to them and held, administered or managed on their behalf in connection with investment services.</p> <p>The maximum amount of compensations is equal to EUR 20,000 for each investor.</p> <p>The funding of the FNG is based exclusively on contributions from participating firms. Contributions are levied on an annual basis, and if it is necessary then additional contributions can be called.</p> |
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| | <p>Communication and cooperation with other authorities</p> <p>The BI and Consob are required to act in a coordinated manner in the supervision of intermediaries, and to share information. For foreign intermediaries, where the authorization of an EU investment firm to carry on business has been revoked by the competent authority, its Italian branches may be subjected to compulsory administrative or liquidation.</p> <p>The provisions governing special administration and compulsory administrative liquidation apply, where compatible, to branches of non-EU investment undertakings.</p> <p>In the case of a crisis of an intermediary that could have cross-sector or cross-border implications the BI and the Consob may cooperate also by way of exchange of information with domestic and foreign authorities within the general framework described under Principles 13–15.</p> |
| Assessment | Fully implemented |
| Comments | The implementation of EMIR will facilitate transfer of clients' positions in the event of default of an intermediary, as clients will have the right to require individual accounts. |
| Principles for the Secondary Markets | |
| Principle 33. | The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight. |
| Description | <p>Authorization of secondary markets</p> <p>Regulation of secondary markets (RMs) is governed by Title I of Part III of the CL, and related regulations, notably Consob Regulation 16191/2007 on markets.</p> <p>The establishment of all RMs requires authorization by Consob (Article 63 of the CL), which is also in charge of their supervision. Before authorizing markets on which there is wholesale trading in private and public debt securities other than government securities, or trading in money market instruments and financial derivatives based on public securities, or trading in interests rates or currencies), Consob must consult the BI. Consob supervises RMs.</p> <p>Wholesale markets in government securities are authorized by MEF, after consulting Consob and the BI (Article 66). These markets are under the supervision of the BI (Article 76), although Consob retains responsibility for the market abuse provisions. The CL and MEF Decree 216/2009 set out the regulatory framework for these markets. In practice, the BI is responsible for supervising the MTS market and the Bondvision market, the latter jointly with Consob since it also trades non-government bonds.</p> <p>MTFs are treated as "unregulated markets" and can be operated by exchange market operators, banks and IFs, subject to registration by Consob. Conditions applying to MTFs are set out in Article 77 bis of the CL, in Consob Regulation 16191/2007 and in MEF Decree 216/2009 for wholesale MTFs in government securities.</p> <p>Consob supervises MTFs that trade financial instruments. MTFs operating wholesale markets in government securities are supervised by the BI after consulting with Consob (Article 77 bis (6) of the CL).</p> <p>Consob has powers to elaborate through regulations the framework for RMs and MTFs.</p> <p><i>Clearing and settlement systems</i></p> <p>Market operators in Italy are not permitted to assume principal, settlement, guarantee</p> |

or performance risk. These activities can only be performed through separate entities (clearing houses), which are subject to prudential requirements including mandatory margin assessment and collection, capital and financial resources, member contributions, guaranty funds and position limits (Articles 68, 69 and 70 of the CL and Rules adopted by the BI and Consob on February 22, 2008).

Central depositories are regulated by Title II of Part III of the CL.

Authorization criteria

RMs

Detailed criteria that must be satisfied before a market can be authorized are set out in the CL and in Regulation 16191/2007 (and, for wholesale markets in government securities, MEF Decree 216/2009). Criteria that must be satisfied include:

- market rules must conform to EU law and be sufficient to ensure the transparency of the market, the orderly conduct of trading and the protection of investors (Article 63(1)(b) of the CL). Market rules and procedures must be transparent and non-discretionary and must guarantee correct and orderly trading; market operators must set objective criteria to allow the efficient execution of orders. Market rules must set out:
- the conditions and procedures for the admission, exclusion and suspension of intermediaries and financial instruments to and from trading;
- the conditions and procedures for the conduct of trading and any obligations of intermediaries and issuers;
- the procedures for ascertaining, publishing and distributing prices;
- the types of contract admissible and the methods for determining the minimum amounts which may be traded.
- the terms and conditions for the clearance, settlement and guarantee of transactions concluded on the markets. (Article 62(2) of the CL);
- financial resources must be sufficient for the proposed operation of the market (Article 3 of Consob Regulation 16191/2007);
- significant shareholders and persons performing administrative, managerial or control functions must meet the integrity requirements set out in MEF Decree 471/1998;
- persons performing administrative, managerial or control functions must meet experience requirements set out in MEF Decree 471/1998;
- the market operator must have adequate organizational and risk management arrangements;
- the operator must have adequate technological and human resources for monitoring and supervising trading;
- the operator must have appropriate measures to identify and manage any conflicts of interest (Consob Regulation 16191/2007 Articles 8 and following).

For wholesale markets in government securities, analogous provisions apply. In particular, the market rules are approved by the MEF (after consulting the BI and Consob) and must conform with European law and be sufficient to ensure the market efficiency, adequate and correct information and the orderly conduct of trading (Article 66 of the CL and MEF Decree 216/2009).

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| | <p>Applicants for authorization must submit a plan of activities illustrating the type of activities planned and the organizational structure of the market operator. This includes details of the systems, including IT systems, to be used in operating the market.</p> <p><i>MTFs</i></p> <p>To be authorized to operate an MTF, an applicant must meet the standards that apply to their authorization as market operators, banks or IFs. Under Article 77 bis of the CL, Consob must identify the minimum operating requirements for MTFs, including obligations of their operators with regard to: the trading and finalization processes of transactions; the admission of financial instruments; information provided to the public and to users; access to the system; monitoring of the observance of system rules by users.</p> <p>For wholesale MTFs in government securities such minimum requirements are identified by the MEF after consulting BI and Consob.</p> <p>Article 19(1) of Consob Regulation 16191/2007 on Markets and art. 21 of MEF decree n.216/2009 (for wholesale MTFs in government securities) require that operators of MTFs must establish and maintain:</p> <ul style="list-style-type: none"> • Transparent, non-discretionary rules and procedures to guarantee fair and orderly trading process, together with objective criteria for the effective execution of orders; • Transparent rules concerning the selection of financial instruments that may be traded; • Transparent rules based on objective criteria governing access to the system; • Effective devices and procedures to continuously monitor compliance with rules by users • Measures necessary to promote the efficient regulation of transactions concluded through MTFs. <p><i>Systematic internalizers</i></p> <p>Systematic internalizers must give notice to Consob at least 15 days before commencing operation of the details of their proposed services (Article 21 of Consob Regulation 16191/2007).</p> <p><i>Practice</i></p> <p>There have not been applications for new RMs. As for MTFs, the meetings conducted led to the conclusion that Consob's review of applications is thorough, and particular attention is given to IT robustness.</p> <p>Securities and market participants</p> <p><i>Market products</i></p> <p>Conditions and procedures for admission, exclusion and suspension of financial instruments to and from trading, including the types of product, contract trading instruments terms and conditions are established in the rules of the RM. Pursuant to article 63 of the CL, in order to authorize the operation of a RM, Consob is required to be satisfied that market rules are conform with EU law and are sufficient to ensure transparency of the market, orderly conduct of trading and protection of investors. Changes to such rules require approval by Consob. In addition, Consob is responsible</p> |
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| | <p>for pre-vetting the prospectus for admission to listing.</p> <p>Pursuant to article 64 of the CL the market operator is responsible for the admission, exclusion and suspension of financial instruments and market participants. Such decisions must be informed immediately to Consob. Consob can forbid the implementation of admission decisions and the exclusion or order to revoke a suspension decision for financial instruments and trading operators within five days from receiving the communication. Consob can also request the market operator to suspend financial instruments from trading.</p> <p>For MTFs, MTF operators must submit their rules to Consob (or, for wholesale markets in government securities, to the BI and MEF) which indicate the financial instruments admitted to trading on these markets at the moment of registration. As in the case of RMs MTFs operators are responsible for decisions on admissions. Changes to the rules and procedures are not subject to approval by Consob; however in practice market operators do inform Consob in advance and when necessary hold meetings with Consob staff.</p> <p>Pursuant to article 77bis of the CL Consob (or BI for wholesale MTFs in government securities) may request MTFs operators to exclude or suspend financial instruments from trading.</p> <p><i>Members</i></p> <p>Market rules for both RMs and MTFs must set out, in a non-discriminatory way, the conditions under which access to markets is granted. Consob (and the MEF for wholesale markets in government securities) must review such rules as part of the authorization process in the case of RMs, or the registration process in the case of MTFs. The review of such rules takes into account the fairness and objectivity of access criteria. Changes to such rules require pre-approval in the case of RMs, and notification in the case of MTFs. In practice, however, MTFs operators inform Consob (and BI for wholesale MTFs in government securities) in advance of the changes and seek its opinion prior to implementation.</p> <p>Fairness of order execution procedures and market resilience</p> <p>Trade matching and execution algorithms are required to be part of the market and trading systems rules that must be submitted to Consob for authorization of the RM or registration of the MTF (and the MEF for wholesale markets in government securities).</p> <p>Market microstructure and trade matching/execution systems are monitored through supervision activity carried out by Consob and by the BI for wholesale markets in government securities. Ad hoc reviews are also carried out when changes in market microstructure are implemented by market operators.</p> <p>Procedures for trading halts must be set out in the rules of RMs. For example, Borsa Italiana Rules (Article 4.3.9) provide for automatic suspension of trading in instruments when price variation limits are exceeded.</p> <p>In April 2012, Consob issued a Resolution (DME/120270714) requiring operators of RMs and MTFs to comply with the ESMA Guidelines on systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities. The Guidelines provide a set of measures that operators must implement in terms of systems and controls aimed at ensuring fair and orderly trading, and preventing market abuses. Main areas covered are adequate pre-trade controls; conformance tests to ensure that members/participants or users' IT systems are</p> |
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| | <p>compatible with the trading platforms' electronic trading systems; automatic and discretionary mechanisms to constrain trading or to halt trading in response to significant variations in price to prevent trading becoming disorderly; undertake adequate due diligence of the member/participants or user before accepting their market access and the ability to check their respective controls and arrangements afterwards; and rules and procedures designed to prevent, identify and report instances of possible market abuse. In addition, RMs and MTFs must keep adequate record of their systems and controls covered by the Guidelines to enable Consob to assess compliance with MiFID and other relevant regulatory obligations. Consob required RMs and MTF operators and market participants to provide a self-assessment signed by the board explaining their processes for implementation. Consob received 5 self assessments produced by the trading venues and 75 by investment firms. Consob staff informed that this topic was on the scope of one on-site inspection recently finalized on a trading venue. In addition, Consob staff informed that this area is going to be checked through on-site inspections on investment firms planned in 2013. The BI issued similar requirements to operators of wholesale markets and MTFs in government securities. Verification of the information provided was conducted also in an inspection that was taken place at the time of the self-assessment.</p> <p>Finally both RMs and MTFs are required to notify Consob immediately of any malfunction of the systems via an incident report. The same applies to the wholesale market, in this case the reports are sent to BI. The reports must clearly indicate the type of malfunction that took place and the measures taken by the market operator to address it. In many cases there are follow-up questions by Consob and BI on such reports.</p> <p>Assessment of systems</p> <p>According to article 11 of Consob Regulation 16191/2007 on Markets, the company's board of directors must submit to Consob on an annual basis at the time of submission of the financial statements, a report on the organizational structure adopted covering a) the separation of operation departments from audit departments, and the management of possible situations of conflict of interest in the assignment of duties; b) internal audit activities; c) reporting procedures. The reports must all contain information on: (i) organizational chart and responsibilities chart, (ii) delegation procedures; (iii) internal audit systems organization; (iv) methodologies introduced to ensure observance of market rules and regular operations with particular reference to technology support services; (v) direct controls to guarantee reliability and integrity of accounting and management data; (vi) assessment of the risk containment measure adopted, indicating any functional failing discovered; (vii) main results of actual controls implemented within the company at various organizational level; (viii) organizational controls adopted for antimony laundering. Such report may make reference to the previous year's report to Consob on aspects of no significant change.</p> <p>Pursuant to article 12 of the Regulation, at least once a year market operators must submit the audit plan relating to the auditing of the main IT structures for the provision of institutional services, with particular reference to IT security measures and planned business continuity procedures. Such audit must be performed by third parties or by the market operator internal audit unit, provided that such department is different from and independent of the production departments. Market operators must inform Consob without delay of the results of the audit, together with the measures adopted or to be adopted to remedy any deficiency.</p> |
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| | <p>A similar obligation exists for MTFs in connection with the submission of the audit plan relating to auditing of main IT structures, pursuant to article 20 of the same Regulation. As MTFs operators must already hold a license (of bank, IF, or market operator), they are subject to the reporting obligations of each of these categories of participants.</p> <p>Similar rules are provided by MEF Decree 216/2009 for wholesale RMs and MTFs in government securities. In this case reports are sent to BI.</p> <p>Finally as indicated above, last year Consob and BI required both RMs and MTFs operators to provide self-assessment of their compliance with ESMA Guidelines on systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities.</p> <p>Operational information</p> <p>Rules and related implementing provisions of RMs and MTFs must be publicly available, including on the websites of market operators and MTFs.</p> <p>Article 15 of Consob Regulation 16191/2007 requires market operators to establish electronic procedures to record the transactions carried out each of their markets. The records to be preserved for a period of not less than eight years should make possible to establish: the identity of the intermediaries; for markets that use electronic trading systems, the individual orders entered into the systems, including those modified deleted unfilled and the date and time in which they were entered, modified or deleted; the type of transactions; the object of transactions; the quantity; the unit price; the day and time of execution of the transaction.</p> <p>Pre-trade and post-trade transparency rules are in line with MiFID rules (see under Principle 35). Information about the identity of parties to trades is not made available to system users or the public and is accessible only by market operators, Consob and, where relevant, the BI.</p> |
| Assessment | Fully implemented |
| Comments | |
| Principle 34. | There should be ongoing regulatory supervision of exchanges and trading systems which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants. |
| Description | <p>Surveillance by the RMs and MTFs</p> <p>RMs and MTF operators are required to monitor transactions executed by market participants through their facilities to identify any infringement of the rules, abnormal trading or potential market abuse (Article 64(1)(b-bis) of the CL and Articles 19(2)(d) and 45(3) of Consob Regulation 16191/2007).</p> <p>Article 187 nonies of the CL requires RMs and authorized intermediaries (which includes MTF operators and systematic internalizers) to notify Consob without delay of transactions that on reasonable grounds appear to involve a violation of the market abuse provisions.</p> <p><i>Borsa Italiana</i></p> <p>As indicated under Principle 9, <i>Borsa Italiana</i> has some supervision responsibilities. In particular, it has responsibility for: admissions to listing on the main equities market and monitoring issuers' compliance with their listing obligations. Decisions of the Borsa</p> |

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| | <p>Italiana on listing are subject to review by Consob within five days and Consob can override Borsa Italiana's decision. Consob has not yet exercised this power; sole authority over listing of issuers admitted to MTFs, as well as compliance with their listing obligations, market surveillance and supervision and enforcement of trading rules. In market surveillance its role is complementary to that of Consob.</p> <p>Borsa Italiana has an active program to supervise listing disclosure obligations of listed issuers, including their material event disclosure obligations. Six staff are in the admissions to listing department, and close to 20 staff in the issuer supervision department.</p> <p>Borsa Italiana's market supervision department consists of 12–15 staff. It focuses on orderly trading and the detection of problematic trading. Two main activities are carried out: real time surveillance of all cash and derivatives markets to ensure that trading is orderly, and where necessary to impose trading halts or suspensions; and end of day alerts produced through analysis of current and previous trading (using its trading database) to detect possible fraudulent trading, or other forms of market abuse. It uses its proprietary surveillance system for market monitoring.</p> <p>In this market supervision activity, <i>Borsa Italiana</i> has frequent contact with Consob, especially in relation to the disclosure obligations of issuers. If it detects serious or potentially criminal conduct, this is reported immediately to Consob.</p> <p><i>Borsa Italiana</i> has the power to sanction issuers and market participants for breaches of its rules, and is in the process of raising the maximum sanction from EUR 100,000 to EUR 500,000. <i>Borsa Italiana</i> has applied sanctions to market participants.</p> <p><i>MTFs</i></p> <p>As indicated above MTFs must also have in place systems for purpose of ensuring orderly trading and detecting market abuse. For example, in the case of EUROLTX, it uses a "modified" SMARS. EUROLTX has four staff dedicated to market surveillance. It refers to Consob roughly 8–10 cases a year.</p> <p>Market surveillance by Consob and BI</p> <p>Consob supervises RMs in real time. As further explained in Principle 36, Consob uses its IT systems to identify unusual transactions on the markets for which it has regulatory responsibility. Consob also uses a purpose-built system to detect anomalous trading trends in securities markets. If these trends indicate the possibility of market abuse the Market Supervision area refers the matter to the Market Abuse Office (which has a staff of 21) which is responsible for the investigations.</p> <p>For purposes of market surveillance, Consob has access to a significant number of data. As described in Principle 36 Consob has access to: data about trades which took place on RMs (sent to Consob daily by the relevant market operator and stored in Consob databases); complete data concerning orders characteristics, directly and completely accessible by Consob in real time (held on Borsa Italiana's system), and reports by market intermediaries of trades executed outside a RM or MTF for shares admitted to trading in an EU RM, real time data via a dedicated system (BrokerInfo) allowing the analysis of market participants' conduct (orders, deals, trading book, etc.) suspicious transaction reports (STRs) from market operators and market participants.</p> <p>The BI performs real time monitoring of trading on RMs and MTFs in government securities. This enables it to assess the liquidity condition of the markets and the trading</p> |
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| | <p>behaviors of market participants. Continuous analysis is conducted to assess the liquidity of different type of securities as well as the contribution of each market maker to the overall efficiency of the market. Consob has the same level of access as BI to data on MTS.</p> <p>Ongoing supervision</p> <p><i>Off site</i></p> <p>RMs must satisfy Consob and the BI (for wholesale markets in government securities) that regulatory standards are met on an ongoing basis.</p> <p>Consob's Regulation on Markets (Regulation 16191/2007) requires market operators to provide, on an on-going basis, detailed information, including information about:</p> <ul style="list-style-type: none"> • arrangements to ensure compliance with the rules and the proper functioning of the market (with particular reference to IT systems); an external audit of the IT must take place on an annual basis, and the corresponding report must be sent to Consob; • internal organization, procedures and IT systems; • outsourcing arrangements; • the evaluation of the risk-limitation measures adopted, highlighting any operational shortcomings found. <p>An equivalent set of rules is in force for wholesale markets in government securities, pursuant to MEF Decree no. 216/2009 and the Supervisory Instructions issued by the BI on August 28, 2012.</p> <p>Consob receives regular reports from market operators, including reports about the deliberations of internal bodies (shareholder meetings and meetings of the internal control board); financial statements; an annual report on organizational structure and steps taken to ensure appropriate separation of functions, and internal audit activities (Articles 9 and 10 of Consob Regulation 16191/2007).</p> <p>Similar provisions apply for reporting to BI by operators of wholesale markets in government securities (MEF Decree 216/2009 Articles 8 and following and BI Supervisory Instructions of August 28, 2012).</p> <p>MTFs are also subject to reporting requirements under Consob Regulation 16191/2007 and MEF Decree 216/2009, including submitting at least annually audit plans and reporting on the outcomes of internal audits.</p> <p>Both RMs and MTFs are subject to record keeping requirements and Consob and the BI have access to the books and records of market and MTF operators (see Articles 74(2) and 77 of the CL; Articles 4 and 15 of Consob Regulation 16191/2007).</p> <p>Failure by a RM or an MTF to comply with regulatory requirements makes persons performing administrative or managerial functions liable to pecuniary administrative sanctions (Article 190 of the CL).</p> <p>Consob holds regular meetings with operators of RMs and with MTFs. In the case of Borsa Italiana, there are meetings on a monthly basis with staff from different divisions and a quarterly meeting with the CEO. In the case of EUROLTX, meetings take place roughly every two months.</p> <p>BI holds also meetings with MTS management quarterly or more frequently if circumstances make this appropriate.</p> |
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| | <p><i>On site work</i></p> <p>Consob also conducts on-site work in connection with RMs and MTFs, which is risk based. In practice this means that more resources are spent on the supervision of Borsa Italiana.</p> <p>Since 2009, Consob has carried out on-site inspections of all RMs and MTFs, and some systematic internalizers. These inspections have focused on particular areas of concern specific to each market operator. In the case of Borsa Italiana there have been three inspections in the last 10 years. In the case of EUROLTX there was an inspection conducted in 2009, when EUROLTX decided to transform from a RM to a MTF.</p> <p>BI has also conducted on-site inspections of MTS.</p> <p><i>Approval of market rules</i></p> <p>For RMs, amendments to market rules or by-laws must be approved in advance by Consob. Consob has used its powers to require changes to market rules, for example by requiring rules to have a specific order-to-trade ratio to preserve market quality and ensure market system robustness.</p> <p>RMs are required to submit new rules to consultation with market participants. In practice Consob receives the draft rules at the same time that stakeholders receive them; then it receives the version as revised on the basis of the consultation, which version has been approved by the RM's board but not by its shareholder meetings. Consob then submits this version to its board, presenting views and concerns and provides informal feedback to the RM; then formal approval by the RM's shareholder meeting takes place. In this way Consob's concerns are taken into consideration prior to formal approval by the RM shareholders' meeting.</p> <p>The rules of MTFs do not require pre-approval by the relevant regulator but must be provided to it. However, as stated above the practice is for the market operator to inform Consob in advance of the change of rules and seek an informal exchange of views.</p> <p>In 2012 Consob verified/approved:</p> <ul style="list-style-type: none"> • 7 amendments to the rules adopted by RMs; • 13 amendments to the rules adopted by MTFs; • 2 amendments to the rules adopted by systematic internalizers. <p>Rules of wholesale markets in government securities are subject to MEF's approval after consulting BI and Consob. BI staff informed that in practice the market operators have informal discussions with BI so that when the proposed rules are sent, they already incorporate comments by BI.</p> <p><i>Powers of intervention</i></p> <p>Consob can adopt measures for the purpose of ensuring transparency of the market, the orderly conduct of trading and the protection of investors, and to this end it may act in the place of the market operator (Article 74 of the CL). The BI, with respect to the markets it supervises may adopt measures for ensuring the overall efficiency of the market and the orderly conduct of trading, and to this end it may act in the place of the market operator (Article 76 of the CL).</p> <p>Consob can require stock exchange companies to amend market rules (Article 73(4) of the CL). MEF has analogous powers under Article 66 of the CL and MEF Decree</p> |
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| | <p>216/2009. It may require changes to rules on the proposal of BI after consulting with Consob.</p> <p>Under the CL, Consob also has powers of direct intervention in the operation of the market. These include the power to: override a market operator's decision to admit a financial instrument for trading, or to admit a market participant (Article 64 (1bis) (a)); and require the market operator to suspend trading in financial instruments, or to suspend a market participant (Article 64 (1bis) (c)).</p> <p>Article 74(3) of the CL gives Consob the power, in cases of necessity and as a matter of urgency, to adopt the measures required for the purposes of ensuring the transparency of the market, the orderly conduct of trading and the protection of investors, including by acting in the place of the market operator. The BI has an analogous power under Article 76(2-ter) for the purposes of ensuring the overall efficiency of the market and the orderly conduct of trading in wholesale government securities.</p> <p>For MTFs, Article 77 bis(2) of the CL gives Consob the power request an MTF operator to exclude or suspend financial instruments from the trading platform. Article 77 bis(6) gives the BI the same powers with respect to wholesale MTFs in government securities.</p> <p>Under Article 75(1) of the CL, in the event of serious irregularities in the management of markets or in the administration of market operators and wherever it is necessary for the protection of investors, MEF, acting on a proposal from Consob, has the power to dissolve the administrative and control bodies of the market operator. The powers of the dissolved administrative bodies are then conferred on a special administrator who exercises them in accordance with directives issued by Consob and under its control, until the administrative bodies are reconstituted.</p> <p>Where irregularities are exceptionally serious, MEF, acting on a proposal from Consob, can issue a decree revoking the authorization referred to in Article 63 CL.</p> <p>By Article 75(2) of the CL, Consob may cancel the authorization of a RM when, among other things, the market operator or RM no longer satisfies the conditions required for the authorization; or the market operator has seriously and systematically violated the relevant provisions.</p> <p>By Article 76 of the CL, the powers assigned to Consob are given to the BI for wholesale markets in government securities.</p> <p>Failure by a RM or an MTF to comply with regulatory requirements makes persons performing administrative or managerial functions liable to pecuniary administrative sanctions (Article 190 of the CL).</p> |
| Assessment | Fully implemented. |
| Comments | <p>There are a few differences in the regulatory treatment of RM vis-à-vis MTFs, for example RMs are subject to preapproval of their rules, while in the case of MTFs rules are notified and supervision is exercised ex-post. Overall these differences do not seem to pose any major concerns.</p> <p>As indicated under Principle 3, the assessors note that the recognition of wholesale government markets is in the hands of the MEF, as well as the imposition of certain extraordinary measures. For the reasons stated under such Principle this issue does not raise major concerns. However the assessors recommend that these powers be vested in the regulatory authorities.</p> |

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| Principle 35. | Regulation should promote transparency of trading. |
| Description | <p>General background</p> <p>Pre- and post-trade transparency rules in relation to shares admitted to trading on an EU RM are in line with EU laws and in particular MiFID and its implementing EC Regulation 1287/2006 (directly applicable in EU Members States).</p> <p>Although not required under EU law, Italian legislation also set standards for pre- and post-trade transparency obligations for RMs and MTFs where financial instruments other than shares are traded.</p> <p>In addition, intermediaries are subject to post-trade transparency obligations on transactions concluded outside RMs, MTFs and Sis on financial instruments admitted to trading in a RM.</p> <p>Consob staff explained that the approach has focused on market led solutions so that RMs, MTFs and systematic internalizers may design their transparency rules take into account the market microstructure, the nature of the instruments traded, volumes traded and the participants involved.</p> <p>Shares admitted to trading on a RM</p> <p>For shares admitted to trading on a RM, pre-trade transparency requirements are set in Article 25 of Consob Regulation 16191/2007. Market operators and MTFs must publish at least the pre- and post-trade information required by EU Regulation 1287/2006/EC. For example, for order driven continuous markets, the EU Regulation requires real time pre-trade disclosure of the aggregate number of orders and the shares they represent at each price level, for at least the five best bid and offer price levels vis-à-vis market participants. Post-trade transparency includes a comprehensive set of information on the transaction executed, including date and time, identification of the securities transacted, quantity and price.</p> <p>In addition, for transactions on shares admitted to trading in a RM concluded outside a RM or MTF intermediaries must provide the post-trade information required by Article 27 of Regulation 1287/2006/EC.</p> <p>Pre- and post-trade information must be made public at reasonable commercial terms and in a manner that is easily accessible. RMs and MTFs operators are required to publish the information during normal trading hours. Pre- and post-trade information must be made available to the public as far as possible in real time through one of the following channels: the RM or MTFs; third party structures; own arrangements.</p> <p>Operators and authorized intermediaries must inform Consob of the channel they use to disclose pre- and post-trade information. Consob has approved 12 reporting channels provided by third parties.</p> <p>SIS are also subject to pre-and post trade transparency requirements.</p> <p><i>Waivers</i></p> <p>Waivers to pre-trade transparency obligations for shares are as provided for in EU legislation:</p> <ul style="list-style-type: none"> • the system uses a trading method by which prices are established by reference to prices generated by another system, provided that reference price has a widespread publication and is generally considered reliable by market users; |

- pre-arranged transactions formalized through the trading system in accordance with the rules of the RM or MTF;
- block trades meeting the minimum size requirements of the European Regulation.

Waivers for post-trade transparency requirements are those envisaged in the EU Regulation—deferred publication of information for transactions large in scale (block trades), with thresholds and deferred timings indicated in the EU Regulation 1287/2006.

Waivers must be verified and authorized by Consob and must be set out in market rules.

Financial instruments other than shares admitted to trading in a RM or MTF

For financial instruments other than shares, Article 32 of Consob Regulation 16191/2007 (and MEF Decree 216/2009 for wholesale markets and MTFs in government securities) require RMs and MTFs operators to have an adequate pre- and post-trade transparency regime, taking into account the market microstructure, the type of financial instruments traded, the size of the transactions and type of investors, with particular regard to the market share of retail investors. Pre- and post-trade information must be made public under reasonable commercial terms and in a manner that is easily accessible.

Article 33 of the same Regulation extends such pre- and post-trade transparency requirements to Sis.

In addition, for transactions on financial instruments other than shares admitted to trading in a RM concluded outside a RM, MTF or SI, intermediaries must provide the post-trade information required by Article 34 of Consob Regulation 16191/2007. This includes information about: the date and time of the transaction; the identification details of the financial instrument; and the price and quantity of the transaction concluded.

These obligations apply to off market transactions with a value of EUR 500,000 or less. For transactions over this threshold, intermediaries must make public at least information relating to the date and time of the transaction, the identity of the financial instrument and the price, and a statement that the value of the transaction exceeds the threshold.

This information must be published with reference to each transaction by the end of the working day following conclusion of the transaction.

Pursuant to the regulations, intermediaries can comply with this requirement by using (i) RM facilities, (ii) other investment facilities, (iii) third party facilities, or (iv) their own websites.

Dark trading and dark orders

In case of dark trading (dark pools, or markets where there is no pre-trade transparency) waivers to pre-trade transparency requirements are governed by the EU rules. As required by these rules, each use of a waiver by RMs and MTF operators must be previously authorized in by Consob.

Market microstructure, including the way orders interact, must be set out in the rules of RMs and MTF operators, and be approved by Consob (or, where relevant, MEF).

Priority rules in the trading systems are established in the rules adopted by RMs and MTFs operators, approved by Consob (or, where relevant by the MEF).

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| Assessment | Fully implemented |
| Comments | <p>The assessors note that the IOSCO Principles and Methodology focus on organized markets; and that the OTC markets fall outside of the Principles.</p> <p>As explained above pre-and post trade transparency obligations for shares stem from the European framework. In practice, different from other markets in Europe, there is little fragmentation of Italian equities markets in different trading venues, as the <i>Borsa Italiana</i> continues to dominate trading.</p> <p>As for corporate bonds, the assessors highlight that overall these markets are subject to a higher level of transparency in Italy due to the extension of the pre and post-trade transparency obligations to instruments different from shares. Furthermore as explained above, post-trade transparency obligations for shares and debt instruments have been extended also to off market transactions.</p> <p>According to a survey carried out by Consob in 2011, the degree of fragmentation in trading in the domestic bond markets is more significant. However, as per information provided by Consob, in practice services such as Bloomberg and Reuters provide consolidated information for bonds, since the bulk of bond issuers are large banks. New rules on the consolidation of information are expected to be adopted at EU level in the context of the MiFID review.</p> |
| Principle 36. | Regulation should be designed to detect and deter manipulation and other unfair trading practices. |
| Description | <p>Prohibition of market abuse</p> <p><i>Market or price manipulation and misleading information</i></p> <p>Market and price manipulation and the dissemination of false or misleading information are prohibited in relation to both listed (Articles 185 and 187 ter of the CL) and unlisted financial instruments (Article 2637 of the Italian Civil Code). The offence is defined in broad terms in Articles 185 (criminal offences) and Article 187 ter (administrative violations). For listed financial instruments, breach of the prohibition makes the offender liable to both criminal and administrative sanctions.</p> <p>Criminal and administrative proceedings are run separately and autonomously under a “dual track regime” and can be taken for the same violating conduct.</p> <p><i>Insider trading</i></p> <p>Insider trading is both a criminal offence (Article 184 of the CL) and an administrative violation (Article 187 bis). An insider for these purposes is anyone possessing inside information by virtue of his membership of the administrative, management or supervisory bodies of an issuer, his holding in the capital of an issuer or the exercise of his employment, profession, duties, including public duties, or position. Tipping and recommending or inducing others to deal on the basis of such information is also prohibited. Secondary insider trading (that is, by a tippee) is an administrative but not a criminal offence.</p> <p><i>Front running</i></p> <p>Front running of client orders amounts to a violation of intermediaries’ obligations and is subject to administrative pecuniary sanctions. In some circumstances, it may also amount to a market abuse practice.</p> |

Regulatory approach

Consob is the regulatory authority responsible for investigating market abuse, including insider trading. The Market Abuse Office in Consob's Market Division is responsible for detection and investigation market abuse offences. It consists of 21 staff.

Consob has direct access to all information concerning trading on financial instruments admitted to trading on RMs, whether or not the transactions are carried out on a RM. Continuous monitoring of trading to identify unusual or improper trading is performed by: monitoring the day-to-day trading activity and the conduct of market intermediaries through the examination of their business operations; and monitoring day-to-day the obligation of issuers to immediately disclose any price sensitive information.

Market monitoring activities are carried out by using:

- data about trades which took place on RMs (sent to Consob daily by the relevant market operator and stored in Consob databases). These data can be used for analysis at later stages via appropriate queries.
- complete data concerning orders characteristics, directly and completely accessible by Consob in real time (held on Borsa Italiana's system).
- reports by market intermediaries of trades executed outside a RM or MTF for shares admitted to trading in an EU RM, real time data via a dedicated system (BrokerInfo) allowing the analysis of market participants' conduct (orders, deals, trading book, etc.).
- suspicious transaction reports (STRs) from market operators and market participants. The following table summarizes the number of STRs received by Consob.

| Suspicious trading reports | | |
|----------------------------|------------------|-----------------|
| Year | Trading platform | Number of cases |
| 2009 | Borsa Italiana | 187 |
| | EuroTLX | 4 |
| 2010 | Borsa Italiana | 220 |
| | EuroTLX | 8 |
| 2011 | Borsa Italiana | 231 |
| | EuroTLX | 10 |
| | Hi-MTF | 2 |
| 2012 | Borsa Italiana | 174 |
| | Euro LTX | 6 |
| | Hi-MTF | 5 |

Source: Consob

Based on these information sets, Consob has developed systems to carry out inquiry programs which detect major market anomalies and related participant behavior.

When anomalies are detected, the head of the trading supervision office identifies an officer responsible for examining the case. If the anomaly seems to be serious, a detailed report is prepared requesting Head of the Market Division to open a formal investigation. These investigations are carried out by the Market Abuse Office. The Head of the Market Division takes decisions of this kind after discussing the case within a market abuse committee. Decisions on the imposition of sanctions correspond to the

Commissioners (Board).

Administrative sanctions for market abuse offences

| Year | Abuse type | Number of cases |
|------|---------------------|-----------------|
| 2009 | Insider trading | 11 |
| | Market manipulation | 6 |
| | Total | 17 |
| 2010 | Insider trading | 11 |
| | Market manipulation | 4 |
| | Total | 15 |
| 2011 | Insider trading | 2 |
| | Market manipulation | 5 |
| | Total | 7 |
| 2012 | Insider trading | 5 |
| | Market manipulation | 6 |
| | Total | 11 |

In 2012, Consob imposed pecuniary sanctions totaling EUR 2.57 million. Assets to the value of EUR 5.89 million were confiscated.

Cross market supervision and foreign linkages

Consob has extensive powers of cooperation and has signed several bilateral and multilateral MoUs with foreign authorities, including the IOSCO MMoU. See responses under Principles 13 to 15.

Details on the cooperation arrangements in place and the number of requests for information to and from foreign authorities for the purpose of investigating market abuses have been provided under Principle 14.

Consob has access to information about all trading activity taking place on Italian RMs and trading venues. This enables it to monitor cross market activity on both securities markets and related derivatives markets.

Consob's staff highlighted the importance of international cooperation for the successful investigation of market abuse cases. Furthermore, staff highlighted that in the majority of the cases there has been the need to request cooperation from a foreign regulator, as they involve remote participants, or ultimate actors/beneficiaries that are not located in Italy.

Commodity markets

A segment of the derivatives RM operated by Borsa Italiana (IDEM) is dedicated to trading commodity futures on energy (IDEX). Consob has also approved a proposal by Borsa Italiana to launch a commodity futures market on agricultural products (AGREX).

Consob is the competent authority for the supervision of those financial commodity derivatives markets. Consob has direct access to the information that permits to identify concentrations of positions in energy derivatives. The *Autorità per l'energia elettrica e il gas* (AEEG) is the competent authority for the supervision of the underlying energy market, where the reference price for the financial futures contracts is determined. Consob and AEEG signed an MoU in 2008 for the exchange of the relevant information between the two authorities. The MoU provides for the establishment of a Technical

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| | <p>Committee and a Contact Body intended to manage the exchange of information between the two authorities.</p> <p>Criminal prosecution</p> <p>Prosecution of market abuse is not centralized in one single office; rather all prosecutors are competent to hear market abuse cases, if the facts happened in their "region". In practice, most cases are heard by the Office of Milan, due to the fact that the Borsa Italiana is located in Milan. Officials estimate that roughly 95 percent of market abuse cases are prosecuted by the Milan Office.</p> <p>The Office has more than 100 prosecutors to cover all types of cases. There is a section specialized in economic crime, which includes market abuse cases. Twelve prosecutors are dedicated to market abuse cases.</p> <p>The bulk of the complaints received by this office are tax related and a significant number are also AML related. The number of "complaints" related to market abuse is more limited. For example in 2011 they had 128 cases. Referrals by Consob are a very important source to start an investigation. In 2012, nine reports were made to prosecutorial authorities as part of investigations into insider trading (two reports) and market manipulation (seven reports). Twenty-seven arraignments followed from these referrals.</p> <p>Below is a list of criminal cases related to insider trading and market manipulation. It includes cases where Consob has been party to the procedure; thus it might not constitute a full list of cases. As can be seen in the information below, the criminal authorities indicated that settlement is used frequently, as officials focused on getting the money back. The settlement is on the penalty not the evidence. In the case of convictions, the years of imprisonment are kept at a level that allow for conditional execution (i.e., the person does not suffer jail).</p> |
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| Criminal cases in connection to insider trading and market manipulation | | | |
|---|-----------|------------------------------|---|
| Year | No. cases | Crime | Outcome as of 31 December 2012 |
| 2004 | 2 | Market man. | 2 settlements 1 judgment of conviction 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) |
| 2005 | 6 | Insider Trad. Market man. | 4 judgments of conviction 3 settlements 3 judgments of non-suit |
| 2006 | 9 | Insider Trad. Market man. | 4 judgments of conviction 6 settlements 3 judgments of acquittal 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) |
| 2007 | 12 | Insider Trad. Market man. | 4 judgments of conviction 5 settlements 2 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) 1 judgment of non-suit 2 judgments of acquittal |
| 2008 | 5 | Insider Trad. Market man. | 1 judgment of conviction 1 settlement 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) 3 judgments of acquittal |
| 2009 | 1 | Market man. | 1 judgment of conviction |
| 2010 | 3 | Insider Trad. Market man. | 1 judgment of conviction 1 judgment of acquittal |
| 2011 | 6 | Market man. | 1 settlement 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) |

| Criminal cases in connection to insider trading and market manipulation | | | |
|---|-----------|------------------------------|---|
| Year | No. cases | Crime | Outcome as of 31 December 2012 |
| 2004 | 2 | Market man. | 2 settlements 1 judgment of conviction 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) |
| 2005 | 6 | Insider Trad. Market man. | 4 judgments of conviction 3 settlements 3 judgments of non-suit |
| 2006 | 9 | Insider Trad. Market man. | 4 judgments of conviction 6 settlements 3 judgments of acquittal 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) |
| 2007 | 12 | Insider Trad. Market man. | 4 judgments of conviction 5 settlements 2 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) 1 judgment of non-suit 2 judgments of acquittal |
| 2008 | 5 | Insider Trad. Market man. | 1 judgment of conviction 1 settlement 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) 3 judgments of acquittal |
| 2009 | 1 | Market man. | 1 judgment of conviction |
| 2010 | 3 | Insider Trad. Market man. | 1 judgment of conviction 1 judgment of acquittal |
| 2011 | 6 | Market man. | 1 settlement 1 acquittal for “ <i>prescrizione</i> ” (statute of limitation/lapse of time) |

Officials mentioned the need to preserve the independence of the prosecution function

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| | from the government, for example in regard to its self-organization, as a key issue to ensure effective enforcement. Resources are also mentioned as a challenge, in particular support staff. |
| Assessment | Fully implemented |
| Comments | <p>Consob is active in monitoring market activity to detect and investigate potential cases of market abuse. It uses sophisticated systems for detection and investigations are thorough. Files examined reveal a systematic approach to the collection of information and appropriate use of Consob's investigative powers. When cases are established, Consob has shown it is prepared to use its sanctioning powers, and its power to confiscate the proceeds of offences. The level of sanctions is high. In sum, there is a good track record that supports the fully implemented grade.</p> <p>On the other hand, criminal cases appear limited, and in particular there seems to be a preference for money penalties rather than imprisonment. It is not clear to the assessors whether in such context criminal enforcement is achieving its objective of being a powerful deterrence tool. Challenges to criminal enforcement have been taken into consideration in the grade of Principle 12. The assessors acknowledge that such challenges exist in many jurisdictions.</p> |
| Principle 37. | Regulation should aim to ensure the proper management of large exposures, default risk and market disruption. |
| Description | <p>Article 70 of the CL gives the BI the power, in agreement with Consob, to regulate systems for clearing and guarantee of transactions involving financial instruments. By Article 52 of the BI and Consob Regulation of 22 February 2008, the BI, in agreement with Consob, approves the regulation that operators of central counterparties must adopt to establish the organizational and operating rules of those systems and any amendments to that regulation. Under the BI and Consob Regulation of 22 February 2008, central counterparties must adopt measures to manage and control risk.</p> <p>Article 77 of the CL provides that the supervision of central counterparties is carried out by the BI as regards systemic risk containment and stability, and by Consob as regards transparency and investor protection. The BI and Consob have power to require central counterparties and market participants to provide information and records concerning the clearing and settlement transactions and may carry out inspections. In cases of necessity and as a matter of urgency, the BI can act in the place of the central counterparties.</p> <p>Monitoring of large positions</p> <p>Large exposures are monitored, on a real time basis, by the Italian central counterparty, authorized intermediaries and market participants, under the supervision of the BI and Consob.</p> <p>In particular, positions are monitored as follows:</p> <p>the Italian central counterparty, <i>Cassa di Compensazione e Garanzia SpA (CC&G)</i>, monitors positions of its clearing members on real time, considering separately the members' own positions versus positions of clients (in omnibus accounts). CC&G limits its exposure to potential losses from defaults by clearing members via margin requirements. CC&G routinely calculates intraday margins.</p> <p>The BI monitors large exposures taken by the Italian central counterparty's members on their proprietary and customer accounts (omnibus accounts) through a connection to</p> |

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| | <p>CC&G's internal system. BI has access to information almost on real time. BI has a view on a specific moment of the day, essentially when margin calls are collected; this allows BI to see whether all clearing members have been able to meet their margin calls. Information on contracts and open positions held by CCP members is stored in a BI database on a daily basis and the BI uses a range of tools to analyze this information. In particular one of the reports produced by BI refers to the positions of each member, long and short, per market, for the last seven days, and on the ranking of the largest contributors to exposures; another one to the guarantees collected (margins and default fund).</p> <p>Consob receives from the CC&G, at the end of each trading day, trade level and aggregate data on open positions held by each member in proprietary and customers' accounts. A real time view on positions taken by any market participant is also possible using tools enabling remote access to the CC&G systems.</p> <p>In addition as per its Operational Rules, CC&G can request clearing members to provide information. Further, the rules give CC&G the power to suspend a clearing member that does not provide the requested information.</p> <p>Using their information gathering powers (described under Principle 10), the BI and Consob can ask market participants to provide them with information and records about their activity on regulated and OTC markets, and on their dealings on behalf of clients and on their own account. This includes information about the beneficial ownership of client positions.</p> <p>Market rules do not set position limits, but the CCP has the power to impose them on clearing members through a differentiation in the request of margins, and individual participants can impose them on clients to prevent them from carrying large exposures. Under Article 7(2) of the CL, the BI has the power to compel intermediaries to reduce their large exposures for financial stability purposes. CC&G can require in exceptional circumstances some of the market platforms to suspend trading activity for the time needed to collect intraday margins.</p> <p>Since there is only one CCP that clears trades on all relevant markets, information is centralized and the position of intermediaries trading on more than one market can be monitored.</p> <p>Default procedures</p> <p>CC&G has a formalized internal procedure for managing defaults. The procedure explicitly focuses on limiting market impact in liquidating the defaulter's positions and foresees a sufficient level of flexibility and coordination with other entities involved.</p> <p>In the event of the default of a clearing member participating in a market served by CC&G and LCH Clearnet SA (the interoperability model), the CCP of the defaulting member informs the other CCP. The procedure is reviewed at least once a year and whenever changes occur in laws, regulations or the internal operational system that might affect the default procedure. The authorities are immediately informed of a default and of any relevant information pertinent to its management. Default procedures can be triggered also in case of non fulfillment or partial fulfillment of the obligations of payments or margins. In this case the CC&G must inform the BI and Consob to allow a decision to be made on whether to declare a market insolvency.</p> <p>All the key aspects of the default procedure are described in detail in the CC&G Rules, which are available on the CC&G website. The CC&G's Operational Rules are approved</p> |
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| | <p>by the BI in agreement with Consob.</p> <p>To provide a degree of protection to clients, the rules establish that in the event of a default, CC&G will make its best efforts to transfer open positions of clients to another member. Open positions must be transferred within three hours from the time at which default was confirmed. Positions that were not transferred as well as the open positions entered in the defaulting member's own account must be closed. BI staff informed that in practice such transfer could be not feasible, given the current deadline vis-à-vis the fact that current rules require segregation on an omnibus account only rather than through individualized customer accounts (so far such a situation never occurred). BI staff informed that with the implementation of EMIR, clients will have the right to opt for individual accounts.</p> <p>Once all positions are closed, CC&G will close the accounts of the defaulting clearing member. The losses are covered according to the following procedures: (i) margins from the defaulting clearing member, (ii) the default funds from the defaulting clearing member, (iii) own funds of CC&G up to five million EUR; (iv) the default fund from other market participants and (v) other assets of CC&G. CC&G manages three separate default funds, one for the cash and derivatives equity markets, one for bonds and repos, and one for derivatives on energy. CC&G conducts periodic stress tests on the default funds.</p> <p>Under the CL, the collateral posted with a CCP may not be subject to enforcement proceedings or preventive measures initiated by the creditors of individual participants or by the body that administers the CCP itself, even in the event of bankruptcy proceedings; therefore a stay or a reversal is hardly conceivable.</p> <p>The Italian legal framework and CC&G rules permit the identification and separate treatment of client and proprietary resources; as a further guarantee for customers, client account assets may not be used to cover house account losses, whereas house account assets may be used to cover client account losses.</p> <p>BI and Consob organize simulation exercises on an annual basis with all participants involved.</p> <p>Short selling on equities markets</p> <p>Consob has used its broad powers of market intervention on a number of occasions in recent years to adopt measures to require disclosure of short selling transactions and to impose temporary restrictions banning a number of short selling transactions.</p> <p>Use of powers of this kind is now governed by EU Regulation 236/2012 (the Short Selling Regulation). The Regulation introduced a harmonized and detailed regime that applies throughout the EU for: disclosure of material net short positions in shares to competent authorities and to the public (Articles 5 and 6); and restrictions on uncovered short sales in shares (Article 12).</p> <p>The Short Selling Regulation (Chapter V) grants extensive powers of intervention to national authorities and to ESMA to require additional disclosure and to undertake temporary additional restrictions on short selling of financial instruments in exceptional circumstances. Competent authorities have been assigned strong supervisory and investigatory powers to ensure compliance with the Regulation. Under Article 4-ter(2) of the CL, Consob is the competent authority to receive the notification and exercise the powers provided for under the Short Selling Regulation as regards equity instruments. By Article 4-ter(5) of the CL, Consob is the authority responsible to coordinate the</p> |
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| | <p>exchange of information and cooperation with the EU Commission, ESMA and the EU national competent authorities for the purposes of the Short Selling Regulation.</p> <p>The Short Selling Regulation also provides a supervisory regime for short selling in sovereign debt and sovereign CDS, including restrictions on uncovered short sales and uncovered CDS (Articles 4, 13 and 14) and reporting to competent authorities of individual net short positions (Articles 8 and 10).</p> <p>Failure to comply with obligations in the Short Selling Regulations makes the violator liable to administrative sanctions under Article 193 ter of the CL.</p> <p><i>Reporting</i></p> <p>The Short Selling Regulation contains a reporting regime for short sales:</p> <p>Article 5 requires a natural or legal person who has a net short position in shares admitted to trading on a trading venue to notify the relevant competent authority where the position reaches or falls below 0.2 percent of the issued share capital of the issuer and each 0.1 percent above that;</p> <p>Article 6 requires a natural or legal person who has a net short position in shares admitted to trading on a trading venue must disclose details of that position to the public where the position reaches or falls below 0.5 percent of the issued share capital of the issuer and each 0.1 percent above that.</p> <p>Article 9 sets out the details that must be in any notification or disclosure.</p> <p>The European Commission is empowered to adjust reporting thresholds on a proposal of ESMA.</p> <p>Records of the gross positions which make a significant net short position must be kept for five years. Public disclosure of information must be made in a manner ensuring fast access to information on a non-discriminatory basis. The information must be posted on a central website operated or supervised by the relevant competent authority.</p> <p>Consob has been active in the monitoring of compliance with short selling measures adopted by it. In this regard, on-site inspections followed a measure adopted in 2011 and monetary sanctions were imposed on the participants found to have breach the ban.</p> <p><i>Settlement failures</i></p> <p>By Article 46 of the BI and Consob Regulation of February 22, 2008, the operator of settlement services must issue a regulation governing the organization and functioning of settlement services. The regulation must include, among others: the operating procedures that persons admitted to settlement services must comply with, including those that must be followed in the event of the provision of settlement services for third parties; and settlement risk limitation measures.</p> <p>Such Regulation and its subsequent modifications are subject to approval by BI, in agreement with Consob.</p> <p>By Article 47 of Consob and the BI Regulation of 22 February 2008, clearing and settlement system operators must adopt all the measures needed to ensure the intraday finality of settlements and minimize the time between the moment of acquiring and processing the data on the individual transactions to be settled and that of their settlement. As a matter of practice, Consob receives a daily feed from settlement and depositary systems.</p> |
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| | Consob staff informed that there is a low level of settlement fails in the market. Thus, in their supervision they have focused on “pathological” issues. |
| Assessment | Fully implemented |
| Comments | <p>Principle 37 has a more limited scope than the Principles for PFMI; therefore the grade given to this Principle does not imply a full assessment of the jurisdiction against the PFMI.</p> <p>As indicated above the implementation of EMIR will facilitate transfer of clients’ positions in the event of default of an intermediary, as clients will have the right to require individual accounts.</p> |