european corporate governance institute

Directors' Remuneration in Listed Companies

Spain*

Name and contact details of respondent

Name	Dr. Ignacio Farrando
Affiliation	Law School, University Pompeu Fabra
Email	ignacio.farrando@upf.edu
Telephone	+34 93 542 22 27
Fax	+34 93 542 17 19

*The information and opinions included in this document are not intended to provide legal advice, and should not be relied on or treated as a substitute for specific advice concerning individual situations.
Spanish law, regulation and best practices are stated as they stood at June 2008.

Questionnaire

1. General

1.1 Please indicate, as a general reference, the laws, case law, regulations, exchange rules and best practices concerning directors' remuneration in your country with respect to listed companies. Please indicate where these provisions (such as, for example, exchange rules) apply only to domestically-incorporated companies.

1. Please indicate, as a general reference, the laws, case law, regulations, exchange rules and best practices concerning directors' remuneration in your country with respect to listed companies.

A) Mandatory rules concerning directors' remuneration (laws and regulations).

 Real Decreto Legislativo 1564/1989, de 22 de diciembre, por el que se aprueba el Texto Refundido de la Ley de Sociedades Anónimas [=*Spanish Public Limited Companies Act 1989*] (hereafter: LSA). This Act applies to every "*Sociedad Anónima*" (*Public Limited Company*) incorporated in Spain and whether it is listed or not. The LSA includes several rules regarding the directors' remuneration, as follows:

▪ Article 9.h LSA: "*The by-laws which shall govern the operation of the company, must state:* (…) (h) *the structure of the body to which the management of the company is entrusted, specifying the directors to whom power of representation is granted* (…). *The number of Directors shall also be specified being, where there exists a board of directors, no less than three, or, at least the maximum and minimum number, as well as the term of office and the system of remuneration, if they receive any*".

▪ Article 130 LSA: "*The directors' remuneration shall be established in the by-laws. Where it consists of a share in the profits, it may only be paid out of profits after tax, after setting aside the required amounts for the statutory reserve and the reserve provided for by the articles and after declaring a dividend to the shareholders of 4 % or higher, as established in the by-laws.*

The remuneration consisting in the award of shares, or share options, or any performance-related remuneration, shall be specifically established in the by-laws, and its application will require an agreement of the shareholders' meeting. This agreement will express, in its case, the number of shares to give him, the exercise price of the option rights, the value of the shares that are the reference and the duration of this remuneration system".

▪ Article 75.1 LSA: "*The company will be only able to acquire its own shares, or the issued by its dominant company, within the limits and with the requirements that follows: 1. That the acquisition has been authorized by the shareholders general meeting, by means of agreement that will have to establish the modalities of the acquisition, the maximum number of shares to acquire, the minimum and maximum price of acquisition and the duration of the authorization, that in no case will be able to exceed eighteen months.*

When the acquisition intends shares of the dominant company, the authorization will have to also come from the shareholders general meeting of this company.

When the acquisition has by object shares that there are directly to be given to the workers or directors of the company, or as a result of the exercise of option rights of which those are the owners, the agreement of the general meeting will have to express that the authorization is granted with this purpose".

▪ Article 200.9 LSA: "*The notes on the annual accounts shall contain, in addition to the matters specifically provided for in the Commercial Code, in this Act, and in the regulatory developments, the following:* (…) *Ninth. The amount of salaries, allowances and emoluments of all kinds earned in the financial year by the senior officers and the members of the Board of Directors, on whatever basis, as well as the obligations entered into in relation to pensions or payment of life insurance premiums for former and present members of the Board of Directors and senior officers. When the member of the Board is a legal entity, the previous requirements will apply to the physical people who represent them*".

This information shall be given as an aggregate amount for each type of payment."

▪ 4ª Additional Provision LSA: "*The implementation of remuneration systems consisting on share or stock option grants, and any other remuneration system linked to the share quotation, addressed to general directors or other persons that perform senior management functions reporting directly to the board of directors, executive commissions or managing directors of the listed company, needs be passed by the shareholders meeting*".

 Real Decreto 1784/1996, de 19 de julio, por el que se aprueba el Reglamento del Registro Mercantil [=*Companies Registry Regulations 1996*] (hereinafter: RRM). This Act applies to every "*Sociedad Anónima*" (*Public Limited Company*), and other legal entities, incorporated in Spain, whether it is listed or not. The main rules regarding the directors' remuneration are:

▪ Article 124.2.d RRM: "(…) a*dditionally* [to attribute powers to executive directors], *the by-laws will be able to create a consultative committee. It will have to be determined in the by-laws if the authority for the appointment and revocation of the consultative committee is of the advice of board of directors or the general meeting; its composition and requirements to be a member; its operation, remuneration and number of members; the form to adopt agreements; the concrete consultative or informative power as well as the their specific denomination in which it will be possible to be added, among other adjectives, the term* «family». *Also it will be possible to include in the by-laws any other organ whose function is merely honorary and establish the corresponding system of remuneration of their members*".

▪ Article 124.3 RRM: "(…) *in any case, it will be indicated (in the by-laws) the number of directors or at least, the maximum and minimum number, as well as the term for which they are appointed, and the remuneration system, if they are remunerated. The remuneration correspondent to the directors will be equal for all of them unless the opposite is expressly stated in the by-laws*".

 Ley 24/1988, de 28 de julio, del Mercado de Valores [=*Spanish Securities and Exchange Act 1988*] (hereafter: LMV).

▪ Article 116 LMV: "*1. The public limited companies listed in a stock exchange shall make public annually a report on corporate governance* (…) *4.* (…) *In any case the minimum content of the report on corporate governance is the following one:* (…) *b)* (…) *The identity and remuneration of the members of the board of directors and its committees* (…)".

▪ 15ª Additional Provision LMV: "*The company senior management, whose shares are admitted to negotiation in a Stock market, will have to communicate to the CNMV the deliveries of actions and the rights of option on actions that receive in execution of a company system of remuneration. Also they will have to communicate the systems of remuneration, and their modifications, referenced to the value of the shares that respect such settle down. This communication will be made public under the regime of relevant facts (...)*

(...)

In the case of companies whose shares are listed in a Stock market, this obligation will be also applicable in relation with the deliveries of shares and rights of option on actions that receives in execution of systems of remuneration to their directors, as well as with the systems of remuneration, and their modifications, referenced to the value of the actions that settle down for the mentioned directors".

 Real Decreto 1362/2007, de 19 de octubre, por el que se desarrolla la Ley 24/1988, de 28 de julio, del Mercado de Valores, en relación con los requisitos de transparencia relativos a la información sobre los emisores cuyos valores estén admitidos a negociación en un mercado secundario oficial o en otro mercado regulado de la Unión Europea [=*Royal Decree 1362/2007 developing the LMV regarding the transparency requirements about the issuers whom securities are listed in the European Union*] (hereinafter: RD 1362/2007).

▪ Article 47 RD 1362/2007. *"1 To the effects of application of the regime of disclosure, the directors of companies whose shares are listed in a Spanish official secondary market, or another regulated market domiciled in the European Union, will communicate to the CNMV, directly or through the company, the granting of any system of remuneration that entails the delivery of shares of the company in which they exert its position, or of option rights on these, or whose liquidation is tied to the evolution of the price of those shares, as well as the later modifications of these systems of remuneration* (…).

2. This obligation (…) *will be also applicable to those directors of companies whose shares are listed in a Spanish secondary official market or in another regulated market domiciled in the European Union that are beneficiaries of analogous systems of remuneration to which they have been described* (…)*".*

 Orden ECO 3722/2003, de 26 de diciembre, sobre el informe anual de gobierno corporativo y otros instrumentos de información de las sociedades anónimas cotizadas y otras entidades [*Regulation of the Spanish Chancellor of Exchequer 3722/2003, about the corporate governance annual report and other information systems of the listed companies and other entities*] (hereafter: Regulation 3722/2003).

▪ Article 1º Regulation 3722/2003: "*1. The annual report on corporate governance shall have this minimum content:* (…) (b) *Structure of the administration of the company.- Within this epigraph, will be contained the following information, at least: (...) Remuneration of the members of the board of directors. The global remuneration of the board will be to include in any case. To this end, it will be understood in any case included within the remuneration the amount of salaries, allowances and emoluments of all kinds earned in the financial year by the members of the board of directors, on whatever basis, as well as the engagements entered into in relation to pensions or payment of life insurance premiums for former and present members of the board of directors"*

B) Spanish best practices (soft law) concerning directors' remuneration in listed companies

The current official best practices in Spanish corporate governance is represented by the *Código Unificado de Buen Gobierno of the CNMV 2006* [*Unified Good Governance Code*: CNMV 2006], made by a special working group on the good governance of listed companies (19 May 2006) [hereinafter: CUBG].

This CUBG replace the other two Spanish former soft-law reports (*Código Olivencia* [February 26, 1998] and *Informe Aldama* [January 8, 2003]).

In the directors' remuneration subject, the current CUBG recommends:

"Remuneration.

The Code starts from the conviction that complete transparency regarding directors' remuneration, including total payments to executive directors, is a way to mitigate the risk of immoderate compensation.

This transparency should extend to all remuneration components and concepts, including director severance packages. Given the complexity of deferred payment schemes (insurance or pensions), these will be best understood if they are translated for comparative purposes into an estimated amount or annual equivalent cost.

The Code recommends that boards approve a detailed remuneration policy, as envisages in Recommendation 40, to be written up and submitted to the General Shareholders' Meeting. This is on top of the proposal made in Recommendation 41, whereby individual directors' remuneration should be listed in the notes to the annual accounts.

It is recommended as follows:

> *35. The company's remuneration policy, as approved by its Board of Directors, should specify at least the following points:*
>
> *(a) The amount of the fixed components, itemised where necessary, of board and board committee attendance fees, with an estimate of the fixed annual payment they give rise to;*
>
> *(b) Variable components, in particular:*
>
> > *(i) The types of directors they apply to, with an explanation of the relative weight of variable to fixed remuneration items.*
> >
> > *(ii) Performance evaluation criteria used to calculate entitlement to the award of shares or share options or any performance-related remuneration;*
> >
> > *(iii) The main parameters and grounds for any system of annual bonuses or other, non cash benefits; and*
> >
> > *(iv) An estimate of the sum total of variable payments arising from the remuneration policy proposed, as a function of degree of compliance with pre-set targets or benchmarks.*
>
> *(c) The main characteristics of pension systems (for example, supplementary pensions, life insurance and similar arrangements), with an estimate of their amount or annual equivalent cost.*
>
> *(d) The conditions to apply to the contracts of executive directors exercising senior management functions. Among them:*
>
> > *(i) Duration;*
> >
> > *(ii) Notice periods, and*
> >
> > *(iii) Any other clauses covering hiring bonuses, as well as indemnities or "golden parachutes" in the event of early termination of the contractual relation between company and executive director.*

Guidelines

Although this Code upholds companies' right to privately decide on remuneration matters and its primary insistence is on their transparency and approval by the competent bodies, it also makes recommendations regarding the content of remuneration policy.

In particular, it urges the exclusion of external directors from remuneration schemes with a variable component linked to the company's net profit or other financial management indicators (for example, operating profit or ebitda), or the value of its share at a given point in time. The idea is to forestall any conflict of interest for external directors when called on to evaluate accounting practices or take other decisions with a possible bearing on the company's reported earnings, given that such earnings or evaluations could have an impact on their income. At the same time, the Code acknowledges that an earnings-related remuneration scheme positively correlated with changes in shareholder value should, if correctly applied, align directors' interests with those of shareholders. Seeking a balance between the two preceding objectives, it urges that variable remuneration be confined to executive directors, but does not suggest that receiving variable payments should disqualify an independent director from maintaining such status.

The Code also advises companies not to use the average remuneration of peer companies as a benchmark for their own remuneration policies: because the desire to converge with the average among those receiving less will not meet with any symmetrical effort from those receiving more, activating what is known as the "ratchet effect".

As regards share-based incentives, variable payments should prize not the absolute change in the price of the share but its improvement relative to the cost of capital for shareholders or that of peer organisations. This is so directors do not pocket disproportionate sums due merely to the general progress of the market or moments of stock euphoria.

Except where individual remuneration is variable or linked to the company's performance, directors' compensation shall not be deemed variable simply because the company's bylaws state that the sum of variable payments may not exceed a given percentage of its profits.

In sum, the Code recommend that director remuneration should suffice to attract and retain the right kind of person but not be so high as to compromise their independence.

It is recommended as follows:

> *36. Remuneration comprising the delivery of shares in the company or other companies in the group, share options or other share-based instruments, payments linked to the company's performance or membership of pension schemes should be confined to executive directors.*
>
> *The delivery of shares is excluded from this limitation when directors are obliged to retain them until the end of their tenure.*
>
> *37. External directors' remuneration should sufficiently compensate them for the dedication, abilities and responsibilities that the post entails, but should not be so high as to compromise their independence.*
>
> *38. In the case of remuneration linked to company earnings, deductions should be computed for any qualifications stated in the external auditor's report.*
>
> *39. In the case of variable awards, remuneration policies should include technical safeguards to ensure they reflect the professional performance of the beneficiaries*

and not simply the general progress of the markets or the company's sector, atypical or exceptional transactions or circumstances of this kind.

The advisory vote of the General Shareholders' Meeting

The moderating influence of a stringent transparency regime can be enhanced by submitting the remuneration policy approved by the board to the advisory vote of the Annual General Shareholders' Meeting, as proposed by the European Commission in its Recommendation of 14 December 2004. Because of this advisory nature, there seems no need for any limiting condition to the effect that the vote should be requested a minimum percentage of shareholders. The advisory vote is an innovative Spanish corporate practice, allowing the Shareholders' Meeting to take a stance which, without affecting the validity of the company's remuneration commitments, may equate to a vote of confidence or no confidence in the directors' stewardship.

One acceptable limit to the transparency principle concerns specific bonuses or parameters whose disclosure to competitors could harm the corporate interest by revealing more than is necessary of the listed company's commercial strategy.

It should be noted that compensation in the form of shares or options has been governed since 1999 by the terms of article 130 of the Public Limited Companies Law.

It is recommended as follows:

40. The board should submit a report on the directors' remuneration policy to the advisory vote of the General Shareholders' Meeting, as a separate point on the agenda. This report can be supplied to shareholders separately or in the manner each company sees fit.

The report will focus on the remuneration policy the board has approved for the current year with reference, as the case may be, to the policy planned for future years. It will address all the points referred to in Recommendation 34, except those potentially entailing the disclosure of commercially sensitive information. It will also identify and explain the most significant changes in remuneration policy with respect to the previous year, with a global summary of how the policy was applied over the period in question.

The role of the Remuneration Committee in designing the policy should be reported to the Meeting, along with the identity of any external advisors engaged.

Disclosure of individual remuneration

The Code makes the supplementary but separate recommendation that remuneration transparency should extend beyond the board as a whole to individual directors. It also urges the disclosure of individual non cash payments, and the performance of the shares and options delivered to directors in that year or previous years. Individual directors' emoluments should be listed in companies' notes to the annual accounts. The Code recommends that as well as disclosing all remuneration items, these notes should include a section on the relation between payments to executives and the company's performance in the year.

It is recommended as follows:

41. The notes to the annual accounts should list individual directors' remuneration in the year, including:

(a) A breakdown of the compensation obtained by each company director, to include where appropriate:

(i) Participation and attendance fees and other fixed director payments;

(ii) Additional compensation for acting as chairman or member of a board committee;

(iii) Any payments made under profit-sharing or bonus schemes and the reason for their accrual;

(iv) Contributions on the director's behalf to defined-contribution pension plans, or any increase in the director's vested rights in the case of contributions to defined-benefit schemes;

(v) Any severance packages agreed or paid;

(vi) Any compensation they receive as directors of other companies in the group;

(vii) The remuneration executive directors receive in respect of their senior management posts;

(viii) Any kind of compensation other than those listed above, of whatever nature and provenance within the group, especially when it may be accounted a related-party transaction or when its omission would detract from a true and fair view of the total remuneration received by the director.

(b) An individual breakdown of deliveries to directors of shares, share options or other share-based instruments, itemised by:

(i) Number of shares or options awarded in the year, and the terms set for their execution;

(ii) Number of options exercised in the year, specifying the number of shares involved and the exercise price;

(iii) Number of options outstanding at the annual close, specifying their price, date and other exercise conditions;

(iv) Any change in the year in the exercise term of previously awarded options.

(c) Information on the relation in the year between the remuneration obtained by executive directors and the company's profits, or some other measure of enterprise results".

The CUBG also recommends, concerning the *Nomination and Remuneration Committees*, the follow:

"*Getting the right directors appointed is of capital importance for an efficiently performing board. The Nomination Committee, whose role is an advisory one, assists the board in achieving this objective and can help forestall conflicts of interest among board members in connection with directorship appointments. Hence the Code advocates that the Nomination Committee should propose the candidates for independent directorships, as well as assessing and reporting on other prospective appointees.*

The Remuneration Committee, meantime, must have the right expertise and judgement for the complex technical and political task of designing a remuneration system for directors and senior officers that manages to be both fair and efficient. The board should bear these requirements in mind when appointing Committee members, and providing them with any advisory resources they need.

Although the Code defends the principle that both committees should be composed entirely of external directors, it also proposes regular consultations with company chairmen and chief executives, especially when the business at hand affects executive directors.

In view of the key role this Code assigns the Nomination Committee (section III.5) in the appointment of independent directors, it is proposed that as well as being formed exclusively of external directors, independents should be a majority.

It is recommended as follows:

> *54. The majority of Nomination Committee members –or Nomination and Remuneration Committee members as the case may be– should be independent directors.*
>
> (…)
>
> *Remuneration Committee*
>
> *57. The Remuneration Committee should have the following functions in addition to those stated in earlier recommendations:*
>
> *(a) Make proposals to the Board of Directors regarding:*
>
> *(i) The remuneration policy for directors and senior officers;*
>
> *(ii) The individual remuneration and other contractual conditions of executive directors;*
>
> *(iii) The standard conditions for senior officer employment contracts.*
>
> *(b) Oversee compliance with the remuneration policy set by the company.*
>
> *58. The Remuneration Committee should consult with the Chairman and chief executive, especially on matters relating to executive directors and senior officers*".

2. Please indicate where these provisions (such as, for example, exchange rules) apply only to domestically-incorporated companies.

About this subject, we can identify three main rules.

First: the article 47.2 RD 1362/2007 [see *supra* 1.1.A] saying that the communication of remuneration systems of directors and management to the CNMV is also applicable "*to those directors of companies whose shares are listed admitted in a Spanish official secondary market or in another regulated market domiciled in the European Union that are beneficiaries of analogous systems of remuneration*".

Second: the article 1.4 *Royal Decree* 3722/2003, where is established that "*the foreign companies whose securities are listed in the Spanish secondary markets, besides doing it in other foreign secondary markets, will have the obligation to put the annual report on*

corporate governance to disposition of the shareholders in the official language of the Spanish State".

And third: the artículo 5.a of *Circular 1/2004, de 17 de marzo, de la CNMV, sobre el informe anual de gobierno corporativo de las sociedades anónimas cotizadas y otras entidades emisoras de valores admitidos a negociación en mercados secundarios oficiales de valores, y otros instrumentos de información de las sociedades anónimas cotizadas* [*Regulation 1/2004 of the CNMV, March 17th 2004, regarding the listed companies's anual corporate governance report, and other issuers of listed securities and other public companies information instruments*] where is established with respect to the annual report on corporate governance of foreign entities that "*the foreign entities whose securities are listed in a Spanish official market, besides to doing it in other foreign secondary markets, will have the obligation to put the report to disposition of the shareholders, at least, in Spanish, as well as to send annually a copy to the CNMV. These (foreign) entities will be only forced to elaborate and to spread an annual report on corporate governance according to this Regulation when they did not make any equivalent report in accordance with the rules of their countries of origin, or the countries in which are the markets in which they are listed. Foreign entities, which they have issued securities that are listed in Spanish official secondary markets, and that are controlled in their totality, directly or indirectly, by another organization, will be able to send the annual report on corporate governance of the dominant entity, when this report is equivalent to which would correspond to elaborate and to spread to the foreign subsidiaries.*

In such case, the controlled foreign subsidiary will send annually to the CNMV a copy of the report written in Spanish by its dominant entity in addition to another paper indicating that it is in the situation mentioned in the previous paragraph, identifying the dominant entity, and justifying the omission of its annual report on corporate governance".

1.2 As to best practices, please specify whether they are described in either a private (voluntary or non-statutory) code or other official report, and whether a "comply or explain" principle is applicable to compliance with the relevant provisions by listed companies. Where the "comply or explain" principle applies, please indicate, where such evidence is available, whether companies generally comply with best practices.

1. <u>As to best practices, please specify whether they are described in either a private (voluntary or non-statutory) code or other official report.</u>

See *supra* 1.1.B. The current official best practices in Spanish corporate governance is represented by the *Código Unificado de Buen Gobierno of the CNMV 2006* [*Unified Good Governance Code*: CNMV 2006], made by a special working group on the good governance of listed companies (19 May 2006).

As the CUBG says, the Government agreed on 29 July 2005 to set up a Special Working Group to advise the *Spanish Securities Markets Commission* (=*Comisión Nacional del Mercado de Valores* [herein after: CNMV]) with regard to the harmonisation and update of the two former reports for the good governance of listed companies (Olivencia and Aldama reports), and to make any supplementary recommendations that it considered to be warranted. The membership of the Special Working Group was approved by the State Secretary for the Economy at the proposal of the Chairman of the CNMV. The Special Working Group unanimously approved the proposal for a CUBG and also some other supplementary recommendations to the Government, CNMV and Spanish financial institutions.

2. <u>As to best practices, please specify whether a "comply or explain" principle is applicable to compliance with the relevant provisions by listed companies.</u>

Article 116.4.f LMV includes the principle "*comply or explain*" in requiring listed Spanish firms to specify their "*degree of compliance with corporate governance recommendations, justifying any failure to comply*" in their annual corporate governance reports.

Article 116.5 LMV permits the CNMV to spread the relevant information, as it thinks, about the listed companies' effective observance of the annual corporate governance reports recommendations.

As the CUBG says as an explanation for this core principle: "*Spanish legislation leaves it up to companies to decide whether or not to follow corporate governance recommendations, but requires them to give a reasoned explanation for any deviation, so that shareholders, investors and the markets in general can arrive at an informed judgment*". And, even more, due to this principle of "voluntariness", the CUBG does not replicate legally binding precepts among its recommendations, omitting "*certain recommendations that are necessary in other countries or advocated by the European Commission, on the grounds that they are already written into Spanish law*".

2. Where the "comply or explain" principle applies, please indicate, where such evidence is available, whether companies generally comply with best practices.

Individually, as we say before, all the listed companies must publish on their web pages the annual corporate governance report (article 116.1 LMV).

And in global terms, the "*Observatorio de gobierno corporativo y transparencia informativa de las sociedades cotizadas en el mercado continuo español*" [*Fundación de Estudios Financieros*] publish every year a report concerning the degree of compliance of the Spanish listed companies with the corporate governance recommendations [see for year 2007: http://www.ieaf.es/_img_admin/1206704727PAPELES_N_22.pdf].

1.3 Please describe in summary: the institutional structure for adopting executive remuneration rules or best practice codes; and any major proposals for reform concerning directors' remuneration.

1. Please describe in summary: the institutional structure for adopting executive remuneration rules or best practice codes

The institutional structure in Spain to adopt executive remuneration rules is the same one that is applicable for passing any other Spanish law.

For official best practices codes a resolution by the Board appointing the relevant Special Committee is needed. When the best practices codes are not official (that is: any other different of the CUBG), there are not special requirements needed.

2. Please describe in summary: any major proposals for reform concerning directors' remuneration.

There are no proposals for law reform concerning directors' remuneration (June 2008), neither to reform the CUBG.

2. Disclosure

2.1 Are listed companies required to publish a remuneration report, indicating the details of the compensation paid to the members of the Board of Directors? How often must it be published and where is it retrievable?

1. Are listed companies required to publish a remuneration report, indicating the details of the compensation paid to the members of the Board of Directors?

There is no a legal duty to published separately a specific "*remuneration report*" but the information about the compensation paid to the members of the Board of Directors must be included in the annual corporate governance report (art. 116 LMV and, implementing this rule, the Regulation 3722/2003 (see *supra* 1.1.A).

From another point of view, the CUBG recommended, only for listed companies, that the board should submit a *report on the directors' remuneration policy* to the General Shareholders' Meeting as a separate point in the agenda. This report can be supplied to shareholders separately or in the manner each company sees fit. The report will focus on the remuneration policy the board has approved for the current year with reference, as the case may be, to the policy planned for future years. It will address all the points referred to in Recommendation 34, except those potentially entailing the disclosure of commercially sensitive information. It will also identify and explain the most significant changes in remuneration policy with respect to the previous year, with a global summary of how the policy was applied over the period in question.

2. How often must it be published and where is it retrievable?

The listed companies' corporate governance report is annual and can be consulted on the web page of the company (articles 117 LMV and 4 Regulation 3722/2003), as well as in the web page of the CNMV (because this report is a significant fact [article 116.3 LMV]).

2.2 Must these reports be submitted, or are recommended to be, to a Securities Market Regulator or to a public authority responsible for collecting these documents?

The article 116.2 LMV establishes that the corporate governance annual report must be submitted to the CNMV. A copy of this report must be submitted to other authorities, such as the *Banco de España* (*Spanish Central Bank*) or the *Dirección General de Seguros y Planes de Pensiones* (*General Authority of Insurances and Pension Schemes*), when applicable (i.e.: the listed company is a bank or a insurance company) [article 116.2 LMV].

From this point of view, when the directors' remuneration consists of shares or stock options of the company, they must inform the CNMV of this situation (or the changes on that) [artículo 47 RD 1362/2007 (see *supra* 1.1.A)].

2.3 What information on directors' remuneration, individually and collectively, and on the remuneration committee, must be included, or is recommended to be included as best practice, in the financial reports? Please include in your answer any specific requirements which apply to particular elements of remuneration, such as stock options, bonuses, and termination payments.

1. What information on directors' remuneration, individually and collectively, and on the remuneration committee, must be included, or is recommended to be included as best practice, in the financial reports?

The article 200.9 LSA provides that the following content relative to Directors' remuneration must be included in the annual reports of all Spanish *Sociedades Anónimas*, listed or not on the securities markets: "*the amount of salaries, allowances and emoluments of all kinds earned in the financial year by the senior management staff and the members of the Board of Directors, on whatever basis, as well as the engagements entered into in relation to pensions or payment of life insurance premiums for former and present members of the Board of Directors and the senior management staff*".

The article 200.9 LSA also provides that "*this information about the directors' remuneration shall be given as an aggregate amount for each type of payment*".

The CUBG establish on recommendation n. 41 the follow: "*the Code makes the supplementary but separate recommendation that remuneration transparency should extend beyond the board as a whole to individual directors. It also urges the disclosure of individual non cash payments, and the performance of the shares and options delivered to directors in that year or previous years. Individual directors' emoluments should be listed in companies' notes to the annual accounts. The Code recommends that as well as disclosing all remuneration items, these notes should include a section on the relation between payments to executives and the company's performance in the year*".

2. Specific requirements which apply to particular elements of remuneration, such as stock options, bonuses, and termination payments.

The CUBG establishes in recommendation n. 41 the following:

> *"The notes to the annual accounts should list individual directors' remuneration in the year, including:*
>
> *(a) A breakdown of the compensation obtained by each company director, to include where appropriate:*
>
> *(i) Participation and attendance fees and other fixed director payments;*
>
> *(ii) Additional compensation for acting as chairman or member of a board committee;*
>
> *(iii) Any payments made under profit-sharing or bonus schemes and the reason for their accrual;*
>
> *(iv) Contributions on the director's behalf to defined-contribution pension plans, or any increase in the director's vested rights in the case of contributions to defined-benefit schemes;*
>
> *(v) Any severance packages agreed or paid;*
>
> *(vi) Any compensation they receive as directors of other companies in the group;*
>
> *(vii) The remuneration executive directors receive in respect of their senior management posts;*
>
> *(viii) Any kind of compensation other than those listed above, of whatever nature and provenance within the group, especially when it may be accounted a related-party transaction or when its omission would detract from a true and fair view of the total remuneration received by the director.*
>
> *(b) An individual breakdown of deliveries to directors of shares, share options or other share-based instruments, itemised by:*
>
> *(i) Number of shares or options awarded in the year, and the terms set for their execution;*
>
> *(ii) Number of options exercised in the year, specifying the number of shares involved and the exercise price;*

(iii) Number of options outstanding at the annual close, specifying their price, date and other exercise conditions;

(iv) Any change in the year in the exercise term of previously awarded options.

(c) Information on the relation in the year between the remuneration obtained by executive directors and the company's profits, or some other measure of enterprise results".

2.4 Is timely disclosure required with respect to stock options, their vesting, exercise, and the sale of the relevant shares to third parties?

The informative requirements concerning the stock options are at the vesting moment (see articles 130 and 75 LSA: *supra* 1.1.A; and article 47 RD 1362/2007: *supra* 1.1.A) and, annually, in the notes to the annual accounts (article 200.9 LSA: see *supra* n. 1.1.A).

2.5 What are the rules on disclosure of share transactions executed by the company's insiders (such as directors, officers, auditors, etc)?

Artículo 9 of the *Real Decreto 1333/2005, de 11 de noviembre, por el que se desarrolla la Ley 24/1988, de 28 de julio, del Mercado de Valores, en materia de abuso de mercado* [=*Royal Decree 1333/2005, developing the LMV concerning market abuse*] establishes that the directors, senior management and people with narrow ties with these, of a Spanish society, "*they will have to communicate to the CNMV all the operations conducted on shares of the issuer listed in a regulated market or on derivatives or other financial instruments related to these shares*".

When the issuer does not have its address in the European Union, they will have to communicate to the CNMV those transactions when the shares of the issuer have been admitted to quotation in first place within the European Union in a Spanish official secondary market.

And the article 31 RD 1362/2007 *establishes that the directors of a Spanish company whose shares are listed in a country member of the European Union "they will have to inform, independently of the percentage that represents, of the proportion of rights of vote that are left in its hands after the operations of acquisition or transmission of shares or rights of vote, as well as of financial instruments that they give right to acquire or to transmit shares that have attributed right of vote".*

This obligation of notification also is demanded: (1) at the moment of the acceptance of its appointment -and it cessation- like directors; and (2) when the listing takes place for the first time, in an official secondary market or another market regulated domiciled in the European Union, of the shares of an issuer for which Spain is the country of origin.

There is also a regulation of the CNMV approving model forms of notification of major holdings of directors, and executives, transactions by issuers in own shares, and other model forms [*Circular 2/2007, de 19 de diciembre, de la CNMV, por la que se aprueban los modelos de notificación de participaciones significativas, de los consejeros y directivos, de operaciones del emisor sobre acciones propias, y otros modelos*].

2.6 What information on directors' remuneration must be included in public offer prospectuses and listing particulars?

The *Real Decreto 1310/2005, de 4 de noviembre, por el que se desarrolla parcialmente la Ley 24/1988, de 28 de julio, del Mercado de Valores, en materia de admisión a negociación de valores en mercados secundarios oficiales, de ofertas públicas de venta o suscripción y del folleto exigible a tales efectos* [*Royal Decree 1310/2005, partially developing the LMV concerning the IPOs and the*

admissión to the listing] and the *Regulation 3537/2005 of the Ministry of Economy, developing article 27.4 LMV* [*=Orden EHA 3537/2005, de 10 de noviembre, por la que se desarrolla el artículo 27.4 de la Ley 24/1988, de 28 de julio, del Mercado de Valores*] established "*til the day that the CNMV does not produce the models of prospectus for IPOS* (…)*, the prospectus must have the information required by the diagrams and models included in the Regulation 809/2004 CE that, taking into account the nature of the issuer and the securities, the CNMV decides in each specific case".*

3. Remuneration of the Board of Directors

3.1 Who fixes the board of directors' remuneration? What are the relevant procedures? (In two-tier systems, please refer to the supervisory board.)

1. Who fixes the board of directors' remuneration?

Pursuant to article 130 LSA, the corporate body in charge of fixing the directors remuneration in Spain is the Shareholders Meeting (see *supra* n. 1.1.A).

2. What are the relevant procedures?

Pursuant to article 130 LSA, director remuneration shall be established in the company by-laws (see *supra* n. 1.1.A).

3.2 Are there provisions and/or practices as to the amount of the remuneration and its distribution (for example, as to whether distribution should be proportionate) among board members? What types of remuneration are allowed?

1. Are there provisions and/or practices as to the amount of the remuneration and its distribution (for example, as to whether distribution should be proportionate) among board members?

Article 130 LSA establishes that when the remuneration consists of a share in profits, it may only be paid out of profits after tax, after setting aside the required amounts to the statutory reserve and the reserve provided for by the articles and after declaring a dividend to the shareholders of four percent or of such higher rate as is established in the by-laws (see *supra* n. 1.1.A).

Article 124.3 RRM provides that the remuneration correspondent to the directors will be equal for all of them, unless the opposite is expressly stated in the by-laws (see *supra* n. 1.1.A).

2. What types of remuneration are allowed?

There are not legal provisions about what types of director's remuneration are allowed. All of them (but with different requirements) are allowed.

3.3 Are personal loans to the company's directors and officers allowed?

There is not a specific prohibition in Spain about this subject. The general one is related with the loans directed to acquire the shares of the company (article 81 LSA).

There are only some information rules about personal loans to the company's directors and officers (*ad exemplum*: article 200.10 LSA establishing the duty to show this information in the notes of the accounts).

4. Executive Directors' Remuneration

4.1 Who fixes the executive directors' remuneration? What are the relevant procedures? Are shareholders required to approve directors' remuneration, the remuneration policy, or the remuneration report (see question 2) on an annual or other basis?
(In two-tier systems, please refer to the management board.)

1. Who fixes the executive directors' remuneration?

The article 130 LSA established that the corporate body in charge of fixing the Executive Directors' remuneration in Spain is the Shareholders' Meeting (see *supra* n. 1.1.A). However there is a controversy when the executive directors are tied with the company with a contract (*ad exemplum*: by a labor relation), concerning the power of the board of directors to fix this kind of remuneration.

2. What are the relevant procedures?

There is not a specific rule about procedure and, for that, general rule (Shareholders' Meeting approval) must apply.

However, the recommendation n. 57 CUBG established for the listed companies this recommendation:

"*The Remuneration Committee should have the following functions in addition to those stated in earlier recommendations:*

(a) Make proposals to the Board of Directors regarding:

(i) The remuneration policy for directors and senior officers;

(ii) The individual remuneration and other contractual conditions of executive directors.

(iii) The standard conditions for senior officer employment contracts.

(b) Oversee compliance with the remuneration policy set by the company".

3. Are shareholders required to approve directors' remuneration, the remuneration policy, or the remuneration report (see question 2) on an annual or other basis?

Shareholders are not required to approve Directors remuneration periodically, but only by means of establishing this remuneration in the company's articles (article 130 LSA). However the articles contain only the system of remuneration (i.e.: bonus, salary, stock options, etc) and the maximum amount (i.e.: 5 % net profit, etc.), and, therefore, the board of directors usually sets the concrete remuneration of each director.

The recommendation n. 40 CUBG established for the listed companies the follow:

"*The board should submit a report on the directors' remuneration policy to the advisory vote of the General Shareholders' Meeting, as a separate point on the agenda. This report can be provided to shareholders separately or in the manner each company sees fit.*

The report will focus on the remuneration policy the board has approved for the current year with reference, as the case may be, to the policy planned for future years. It will address all the points referred to in Recommendation 34, except those potentially entailing the disclosure of commercially sensitive information.

It will also identify and explain the most significant changes in remuneration policy with

respect to the previous year, with a global summary of how the policy was applied over the period in question.

The role of the Remuneration Committee in designing the policy should be reported to the Meeting, along with the identity of any external advisors engaged".

4.2 Is the board required, or recommended as best practice, to create a remuneration committee? If yes, please specify: (i) the committee's composition (if independent directors should be appointed to this committee, please give the relevant definition and indicate whether any special procedures apply to the appointment of independent non-executive directors); (ii) the committee's competences and which company body it reports to; and (iii) how the committee operates.

1. Is the board required, or recommended as best practice, to create a remuneration committee?

Yes. It is considered best practice under the CUBG that the board of directors of listed companies creates a remuneration committee.

The article 124.2.d RRM authorize the by-laws to create a consultative committee (see *supra* n. 1.1.A).

2. If yes, please specify: (i) the committee's composition (if independent directors should be appointed to this committee, please give the relevant definition and indicate whether any special procedures apply to the appointment of independent non-executive directors); (ii) the committee's competences and which company body it reports to; and (iii) how the committee operates.

The recommendation n. 44 CUBG establish for the listed companies: "*in addition to the Audit Committee mandatory under the Securities Market Law the Board of Directors should form a committee, or two separate committees, of Nomination and Remuneration. The rules governing the make-up and operation of the Audit Committee and the committee or committees of Nomination and Remuneration should be set forth in the board regulations, and include the following:*

(a) The Board of Directors should appoint the members of such committees with regard to the knowledge, aptitudes and experience of its directors and the terms of reference of each committee; discuss their proposals and reports; and be responsible for overseeing and evaluating their work, which should be reported to the first board plenary following each meeting.

(b) These committees should be formed exclusively of external directors and have a minimum of three members. Executive directors or senior officers may also attend meetings, for information purposes, at the Committees' invitation.

(c) Committees should be chaired by an independent director.

(d) They may engage external advisors, when they feel this is necessary for the discharge of their duties.

(e) Meeting proceedings should be minuted and a copy sent to all board members".

The CUBG defines the independent director as follow: "*Directors appointed for their personal or professional qualities who are in a position to perform their duties without being influenced by any connection with the company, its shareholders or its management*".

As such, the following shall in no circumstances qualify as independent directors:

(a) Past employees or executive directors of group companies, unless 3 or 5 years have elapsed, respectively, from the end of the relation.

(b) Those who have received some payment or other form of compensation from the company or its group on top of their directors' fees, unless the amount involved is not significant. Dividends or pension supplements received by a director for prior employment or professional services shall not count for the purposes of this section, provided such supplements are non contingent, i.e. the paying company has no discretionary power to suspend, modify or revoke their payment, and by doing so would be in breach of its obligations.

(c) Partners, now or on the past 3 years, in the external auditor or the firm responsible for the audit report, over that period, of the listed company or any other within its group.

(d) Executive directors or senior officers of another company where an executive director or senior officer of the company is an external director.

(e) Those having material business dealings with the company or some other in its group or who have had such dealings in the preceding year, either on their own account or as the significant shareholder, director or senior officer of a company that has or has had such dealings.

Business dealings will include the provision of goods or services, including financial services, as well as advisory or consultancy relationships.

(f) Significant shareholders, executive directors or senior officers of an entity that receives significant donations from the company or its group, or has done so in the past 3 years.

This provision will not apply to those who are merely trustees of a Foundation receiving donations.

(g) Spouses, partners maintaining an analogous affective relationship or close relatives of one of the company's executive directors or senior officers.

(h) Any person not proposed for appointment or renewal by the Nomination Committee.

(i) Those standing in some of the situations listed in a), e), f) or g) above in relation to a significant shareholder or a shareholder with board representation.

In the case of the family relations set out in letter g), the limitation shall apply not only in connection with the shareholder but also with his or her proprietary directors in the investee company.

Proprietary directors disqualified as such and obliged to resign due to the disposal of shares by the shareholder they represent may only be re-elected as independents once the said shareholder has sold all remaining shares in the company.

A director with shares in the company may qualify as independent, provided he or she meets all the conditions stated in this Recommendation and the holding in question is not significant.

4.3 Which types of remuneration are permitted? In answering, please consider each of the following: (a) bonuses; (b) stock options, including discounted stock options; (c) stock grants; (d) profit sharing; (e) benefits in kind.

All kinds of remuneration for the executive directors are possible.

4.4 Are there specific rules, including shareholder approval requirements, as to these different types of remuneration?

1. Are there specific rules, including shareholder approval requirements, as to these different types of remuneration?

Yes. The article 130 LSA establishes two special rules.

(a) If the directors' remuneration consists in a profit sharing scheme, this can only be possible where there are liquid profits and the reserves (by law or in the by-laws) are fully covered, and the shareholders are given a dividend of 4%, or a higher dividend fixed than the by-laws have established.

(b) The director's remuneration consisting in the delivery of shares, or options over the same ones, or referenced to the value of the shares, must be specifically provided in the by-laws, and its application will require an agreement adopted in the Shareholder Meeting. This agreement must express, in this case, the number of shares to give him, the price of exercise of the option rights, the value of the shares used as reference and the duration of this remuneration system.

In addition to that, the Additional Provision number 4 LSA provides that the implementation of remuneration systems consisting on share or stock option grants, and any other remuneration system linked to the share quotation, addressed to general Directors or other persons that perform senior management reporting directly to the board of directors, executive commissions or managing directors of the listed company, needs be passed by the shareholders meeting.

4.5 Are there any restrictions on how payments are made?

There is no specific legal provision in Spain on how payments should be made.

4.6 Are there any specific requirements for termination payments made on loss of office, whether through dismissal, retirement, on a takeover, or otherwise?

Aside from the informative obligations (*ad exemplum*: see CBGC recommendations n. 35 and 41), there is not a legal rule on this subject. See *supra* n. 2.3.

4.7 Are there any specific requirements concerning directors' service contracts with respect to, for example, their duration and disclosure?

The directors for all kinds of *Sociedades Anónimas*, listed or not, have a maximum term of 6 years (article 126.2 LSA), but they can be reelected without limit.

The CUBG establishes that "*independent directors should not stay on as such for a continuous period of more than 12 years*" (recommendation n. 29).

5. Non-executive Directors' Remuneration

5.1 Are non-executive directors separately paid for their participation in committees of the board of directors? Do any restrictions apply to the payment of non-executive directors' *via* stock options?

1. Are non-executive directors separately paid for their participation in committees of the board of directors?

Spain has not any specific legal provision about that. Although it is usual to pay to all kinds of directors an extra remuneration for the job performed in the committees.

2. Do any restrictions apply to the payment of non-executive directors' *via* stock options?

There is no specific legal provision in the LSA or the LMV that restricts the use of stock options to remunerate non-executive directors. However the CUBG urges the exclusion of external directors from remuneration schemes with a variable component linked to the company's net profit or other financial management indicators (for example, operating profit or ebitda), or the value of its share at a given point in time.

The idea is to forestall any conflict of interest for external directors when called on to evaluate accounting practices or take other decisions with a possible bearing on the company's reported earnings, given that such earnings or evaluations could have an impact on their income.

At the same time, the Code acknowledges that an earnings-related remuneration scheme positively correlated with changes in shareholder value should, if correctly applied, align directors' interests with those of shareholders. Seeking a balance between the two preceding objectives, it urges that variable remuneration be confined to executive directors, but does not suggest that receiving variable payments should disqualify an independent director from maintaining such status.

For this reason the recommendation n. 36 CUBG establishes that "*remuneration comprising the delivery of shares in the company or other companies in the group, share options or other share-based instruments, payments linked to the company's performance or membership of pension schemes should be confined to executive directors*" (point n. 36 I CUBG). But, finally, there is an exception: "*The delivery of shares is excluded from this limitation when directors are obliged to retain them until the end of their tenure*".

5.2 May a company make payments to non-executive directors, additional to their directors' fees, for services, such as legal or brokerage services, outside the usual scope of directors' duties?

1. May a company make payments to non-executive directors, additional to their directors' fees, for services, such as legal or brokerage services, outside the usual scope of directors' duties?

There is no specific legal provision in Spain about that and, for this reason, the possibility of payments to any directors (executive or not), additional to their remuneration, for services, outside the usual scope of directors' duties (i.e.: legal or brokerage services, consultancy, etc.) is highly controversial when this is not written in the company articles or passed by the Shareholders' General Meeting.