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Conference on European Company Law: The way forward

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Panel discussion:

**"Groups of companies and the current European Company Law
framework"**

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Foreword

Before addressing a number of legal issues, I would like to explain what the Pirelli Group is, how it is set up and how it actually works.

The Pirelli Group includes 98 different legal entities (all companies equivalent to s.p.a./s.r.l. companies under Italian law) on the world's five inhabited continents, in 34 different countries, 16 of which are EU members.

The Group's Headquarter is in Italy.

To provide a simplified overview of the Pirelli Group, from an industrial and commercial organisation point of view, we might say that Pirelli's

“World” is divided not only into “Countries” but into “Regions” (Europe, Emea, Latam, North America, Asia Pacific) with at the top specific “Business Units” competent for the single product lines (cars, motorbikes, truck & buses, agro).

In organizational terms this means that each individual country has a “Country Manager” (in smaller countries this is the same person as the C.E.O. of the legal entity operating there) who reports to a “Region Manager” who, in turn, reports to a “Business Unit Manager” reporting to the Parent Company’s C.E.O..

In practice, a C.E.O. of a legal entity operating in a specific country will follow the instructions given by the Country Manager (if the latter is not the same person as the C.E.O.) who will in turn, on the basis of the hierarchy illustrated above, follow the instructions of the Region Manager and the Business Unit Manager.

Some examples can help us better understand the functioning of the Pirelli Group’s organisational structure.

For example, the planning of investments and their amount for each year is decided centrally at the Headquarter on the basis of the strategies defined for individual “Business Units”.

Each “Business Unit” (on the basis of the budget available to them) determines the amount of “investment” admitted in individual Regions, which then divide up their budget taking into account the requirements of individual countries, which in turn divide up it between the various legal entities. So far individual legal entities operating in a certain country must implement the investment plan on the basis of this framework.

Level of productivity and allocation of products to the market are also affected by the above group's organization. Specifically, allocation of a product made in a specific country to that country, rather than another is decided by each Business Unit manager, so it does not depend on the Country or Region.

The Group activity has two collective organizational moment. At managerial level, a number of Committees which coordinate activities and support the Board of Directors which is in charge for defining and approving Group strategies and material transactions.

In particular, the Management Committee (composed of the Parent Company's CEO, the COO, the General Counsel, the CFO and Business Unit and Regional Managers) examines the monthly management reports on the entire Group's results and establishes any corrective manoeuvres and specific actions required in production and sales strategies.

The Board of Directors of the Parent Company decides the more significant transactions (such as entering a new geographical market). For example, last year, it has been decided to launch an industrial presence in Mexico (with a new factory) and in Russia (with new factories and commercial companies). The relevant decisions were adopted by the Board of Directors of Pirelli & C. (that is the Parent Company) and following these decisions the subsidiaries put in place the consequent activities (also assuming formal resolution).

LEGAL ISSUES

1. Everyone knows that groups have been and are still considered a “risk factor”, to govern -“negatively”- in terms of protection of minorities and of the creditors of each subsidiary. In this sense, the German model of 1965 is paradigmatic, as it is the different (and much more recent) Italian model of 2003, which start with a provision dedicated (not to “governance”, but) to “the parent company’s liabilities” (article 2497 of the Civil Code).

The Pirelli Group’s experience – as an example of a cross-border group - suggests to the EU legislator a different and very important need on the part of enterprise: the need to be able to depend on a number of basic principles which are the same everywhere in EU addressing the most significant aspects of “group governance”. In substance, enterprises need to know in advance -“positively”- a number of basic rules, in compliance with which a company may either exercise or be subject to a directing and coordinating activity.

2. At this point an initial question arises: why should this be done at EU level? In other words, do we really need “European law” governing groups?

There has been much debate around this, and the conclusions reached are not uniform.

My opinion – supported by the experience of the Pirelli Group – is that it is necessary to take action at the community-wide level.

We must consider that the activity of a cross border group is by definition transnational, meaning it comes into contact with (and is regulated by) the

lex societatis of different States. “Group governance” is generally not very well defined, not in a uniform way, in any case, at national level, with the result that there is much uncertainty as to how a transnational group can be managed.

What we need is to create uniform legislation at the community level – a “framework directive” – establishing a number of basic principles of “group governance” and thereby overcoming the diversities and uncertainties found at national level.

The basic purpose of these principles must be improvement *of the flexibility of the management of groups in its international business activities*. In this sense I absolutely agree with the Reflection Group’s Report. Perhaps, I believe we have to go forward.

3. Action at EU level must, at least:

- i) establish that the parent company (and its board of directors) has legitimate powers of directing and coordinating the subsidiaries activity;
- ii) define the general principles of “correct management” which the parent company must comply with in directing and coordinating its controlled companies or *subsidiaries* (and therefore identifying ranges and limits within which the parent company may pursue its unitary entrepreneurial policy through different companies);
- iii) outline the powers and duties of the board of directors of subsidiaries, defining the meaning of “legal autonomy” of controlled companies and subsidiaries. The solution to this problem is even more important if we consider that there is no clear, univocal

- solution in European Union countries regarding which interests the directors of a subsidiary or a controlled company are to pursue;
- iv) provide uniform rules regarding possible “liability for (illegitimate) exercise of unitary direction”;
 - v) specify the duties of the parent company in the event of a “crisis” in one or more controlled company or subsidiary.

And, let me repeat, this does not mean tightening business activities at group level, but rather facilitating them.

4. Everyone realises that no national legislation clearly addresses the “group governance” issues mentioned above.

For historic reasons, the only partial key exception is German law governing business groups (*Konzernrecht*). But this model of legislation, while it undeniably has its merits, dates back to 1965 and is, above all, oriented toward “protection” of the shareholders and creditors of controlled companies (referred to as *Schutzrecht*) rather than “organisation” of group governance (*Organisationsrecht*).

“Forum Europaeum Corporate Group Law” (which certainly influenced the work of the Winter Commission and the 2003 Action Plan) proposed – as a key rule for group management – the solution put forward by the French Court of Cassation, known as the “Rozenblum” principle. But this proposal addressed only one specific aspect of “group governance”.

Alternatively, it could be considered the Italian model contained in article 2497 et seq. of the Civil Code. Italian corporate law is particularly concerned with regulating the “liability” of the parent company (article 2497 of the civil code), group “publicity” (article 2497 bis) and infragroup

loans (article 2497 quinquies), but does not organically address the issue of group “governance”.

5. The group of companies is definitely the most common “form of organisation” in the European community for exercising economic activities of a certain scale and complexity. It therefore appears utmost important that this “form of business organisation” is regulated, as it has historically been the case of other forms and models of organisation of economic activities, starting with the “joint-stock company”.

This is what the experience of a large group, which is, to a great extent, European, suggests.

It is up to the community institutions (and the best legal practice) to identify the full course of this new path.

Tradition and the “imagination” of European lawmakers, meant as a “supreme virtue” (Franz Wieacker comes to mind, among others) may be of great help here.

At the end, I would like to thank the European Commission for giving me, and the Pirelli Group I represent, the possibility to express an opinion as such sensitive matters in the knowledge –quoting Alfred North Whitehead– that “a clash of doctrines is not a disaster- but an opportunity.” Thanks again to the European Commission for this opportunity.