

## **Carraro S.p.A.**

### **REPORT ON CORPORATE GOVERNANCE 2007**

#### **Introduction**

Carraro S.p.A. adheres to the new Corporate Governance Code drafted by the Corporate Governance Committee of Borsa Italiana S.p.A. in March 2006 (hereinafter the "Corporate Governance Code") by the methods and under the terms set out in this report. During the year the company updated its corporate governance system to adopt the principles and application criteria of the Corporate Governance Code. This document will set out those recommendations that were not applied, those partially applied, or those for which adaptation processes are yet to be completed.

This report has been compiled according to the indications of the Corporate Governance Code itself. The report is issued to shareholders together with documentation for the Shareholders' Meeting legally convened to approve the financial statements.

The Board of Directors of the Company is also planning to submit some amendments to the Company Articles of Association that affect the governance system and bring it into line with recent amendments to the Consolidated Law on Finance (Legislative Decree 58/1998) by Law No. 262/2005 and Legislative Decree No. 303/2006.

#### **1. Role of the Board of Directors**

Corporate organization is based on the "traditional model" and is founded on the following corporate bodies: Shareholders' Meeting, Board of Directors and Board of Statutory Auditors. The Board of Directors is the collegiate body for administration of the Company, defining strategic planning for both the Company and the Group that it heads, with responsibility for governance. For this purpose it is vested with the widest powers of ordinary and extraordinary administration of the Company, and has the power to undertake any action it considers necessary for the implementation and achievement of corporate objectives, excluding only those that law or the Articles of Association, in compliance with the Corporate Governance Code, exclusively reserves to the Shareholders' Meeting.

In particular, pursuant to provisions of the Articles of Association, by mandates granted to it and by corporate practice, the Board is responsible for the most significant matters, including:

- Examination and approval of strategic, industrial, commercial, organizational and financial plans for the Company and the Group;
- Examination and approval of the budget and transactions of significant economic, asset and financial importance to the Company and the Group;
- Examination and approval of the corporate governance system of the issuer and the Group;
- Assessment of the adequacy of the general organizational and administrative structure of the Company and the Group;
- Award and revocation of mandates to the Chairman, the Managing Director, and the award or revocation of special mandates to directors of the Company;
- The establishment, following recommendations from the relevant Committee and the Board of Statutory Auditors, of the remuneration of the Chairman, the Managing Director and the individual members of the Board and of Committees;
- Monitoring of the general performance of Company and Group management, regularly comparing plans with results, with particular attention to the most significant economic, financial and asset transactions;
- Carrying out an annual assessment of the size, composition and performance of the Board and its Committees;
- Definition of the rules of Corporate Governance, and supervision of adoption and compliance with the rules, with reference to the adopted Corporate Governance Code;
- Examination and approval of the guiding principles, operating limits and preliminary and final financial risk management operations of the Company and the Group and monitoring compliance with corporate policies;
- Examination of all regular quarterly, half-yearly and annual economic and financial reporting documentation;
- Examination and approval of transactions with related parties, including situations concerning directors' interests.

The Articles of Association provide that the Board of Directors has the power to adopt resolutions regarding:

- The establishment or closing of secondary places of business;
- The transfer of the registered offices within national territory;
- Mergers or demergers of companies in the cases provided by Articles 2505, 2505-bis and 2506-ter of the Italian Civil Code;

- A reduction in registered capital in the event of withdrawal of a shareholder;
- Adaptations of the Articles of Association to conform to regulatory provisions, except where the Board considers it appropriate for such resolutions to be submitted to an extraordinary shareholders' meeting.

At its meeting of 22 February 2007, the Board completed its annual assessment of the size, composition and performance of the Board and its Committees.

The positions held by each Board member in other financial, banking, insurance, or large companies listed on regulated markets, including foreign markets, are listed below:

Professor Giorgio Brunetti holds the post of Director in the following listed companies:

1. Autogrill S.p.A.;
2. Benetton Group S.p.A.:

He is a Director of the following unlisted companies:

1. Messaggerie Libri S.p.A.;
2. Messaggerie Italiane S.p.A.;

He is also a Statutory Auditor in:

1. Autorità per l'energia e il gas (*Italian Energy and Gas Authority*).

Mr. Sergio Erede holds the posts indicated in the following listed companies:

1. Manifatture Lane Gaetano Marzotto & Figli S.p.A. – Director;
2. Interpump Group S.p.A. – Director;
3. Autogrill S.p.A. – Director;
4. Luxottica Group S.p.A. – Director;
5. Valentino Fashion Group S.p.A. – Director;
6. Gruppo Editoriale l'Espresso S.p.A. – Director;
7. Banca Nazionale del Lavoro S.p.A. – Vice Chairman.

He also holds the posts indicated in the following unlisted companies:

1. Società Italo Britannica L. Manetti – H. Roberts S.p.A. – Director;
2. BNL Progetto S.p.A. – Director;

3. Manuli Rubber Industries S.p.A. – Director.

Dr. Antonio Cortellazzo holds the posts indicated in the following listed companies:

1. Benetton Group S.p.A. – Statutory Auditor.

He also holds the posts indicated in the following unlisted companies:

1. Benind S.p.A. – Auditor.
2. Nem Due SGR S.p.A. – Chairman of the Board of Statutory Auditors.
3. Olimpias S.p.A. - Chairman of the Board of Statutory Auditors.
4. Pagnan Finanziaria S.p.A. – Director.
5. Schematrentaquattro S.r.l. - Chairman of the Board of Statutory Auditors.

With respect to determination of the maximum number of posts compatible with efficient performance as a director of the Company, and in relation to the current composition of the Board, it is considered that such an assessment has already been made by shareholders when appointing directors at the ordinary shareholders' meeting of 11 May 2006 and subsequently by the individual directors concerned upon acceptance of their posts.

The Board therefore preferred not to express its position on this matter, as it believes further study is necessary, also pending a Consob order establishing the limit on the cumulative number of posts that may be accepted by each member of the controlling bodies pursuant to Article 148 bis of the Consolidated Law on Finance.

## **2. Composition of the Board of Directors**

The current members of the Board of Directors will remain in office until the approval of the financial statement at 31.12.2008. The Board consists of the Chairman Mr. Mario Carraro, the Managing Director Mr. Carlo Borsari, Directors Francesco Carraro, Enrico Carraro, Tomaso Carraro, Onofrio Tonin, Prof. Giorgio Brunetti, Mr. Sergio Erede and Dr. Antonio Cortellazzo.

The Board of Directors is composed of executive and non-executive directors; Messrs. Mario Carraro, Carlo Borsari, Tomaso Carraro and Enrico Carraro are executive directors. The other members of the Board of Directors are non-executive.

Among the non-executive directors, pursuant to the Corporate Governance Code, and taking account of the information provided by each director, Prof. Giorgio Brunetti, Mr. Sergio Erede

and Dr. Antonio Cortellazzo were independent directors in the year 2006. See paragraph 3 below for further details.

By resolution of the Board of Directors of 22 February 2007, Dr. Antonio Cortellazzo was also appointed as “Lead Independent Director”.

By Corporate practice, the Board of Directors meets at least quarterly in the presence of the Board of Statutory Auditors.

During 2006, the following meetings of corporate bodies have been held:

|                          |                                                                                                                                                               |
|--------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 23.02.2006               | Analysis of provisional data for 2005                                                                                                                         |
| 29.03.2006               | Board of Directors to examine and approve the Carraro Group consolidated financial statement and Carraro S.p.A. draft financial statement at 31 December 2005 |
| 11.05.2006               | Board of Directors to examine and approve the quarterly report at 31 March 2006                                                                               |
| 10.05.2006<br>11.05.2006 | Shareholders' meeting to approve the 2005 financial statement and renewal of company appointments (first and second convocation)                              |
| 11.05.2006               | Board of Directors to appoint the Chairman and Managing Director and grant powers                                                                             |
| 12.09.2006               | Board of Directors to examine and approve the half-year report at 30 June 2006                                                                                |
| 26.09.2006               | Analysis of three-year plan                                                                                                                                   |
| 09.11.2006               | Board of Directors to examine and approve the quarterly report at 30 September 2006                                                                           |
| 20.12.2006               | Approval of 2007 Budget                                                                                                                                       |

Table 1 sets out the percentage attendance of members of the Board of Directors.

The Chairman Mr. Mario Carraro was granted all powers of ordinary and extraordinary administration provided by law and/or the Articles of Association, with the sole limitation of powers listed below, which are reserved to the Board of Directors:

- Acquisition or cession of shareholdings, including minority shareholdings;
- The grant of surety bonds, liens or mortgages on company assets;

- Acquisitions or cessions of immovable property;
- Approval of the economic-financial budget.

The maintenance of the Chairman's mandate is justified by the preservation of continuity, guaranteed by the principal shareholder, in management policies and the strategic vision of the Company and the Group, in view of his experience in the fields of business, clients and the markets in which the Company has operated over time. In fact, the Chairman performs a coordinating and strategic policy role, while executive management of the Company and the Group is the responsibility of the Managing Director. It is therefore considered that the comment in the Corporate Governance Code, which at point 2.P.4 advises against concentrating corporate posts in a single person, has been respected.

The Managing Director Mr. Carlo Borsari is vested, as from 11 May 2006, with all powers of ordinary administration, with the exclusion of any power of extraordinary administration pursuant to law and the Articles of Association, and the following powers, which are reserved to the Board of Directors or the Chairman of the Board of Directors:

- The stipulation, amendment and/or cancellation of franchising contracts or licencing of industrial property rights.
- The recruitment and dismissal of Company managers and the establishment of their remuneration.
- The issue or revocation of general mandates or authorizations.
- The grant of surety bonds, the establishment of liens or mortgages on company assets
- The purchase, sale, exchange, or granting of guarantee rights on:
  1. Immovable property
  2. Businesses or business divisions
  3. Company shareholdings.
- Approval of the Company economic-financial budget and any business plans.
- The stipulation, amendment and cancellation of bank and finance contracts in any form (in particular obtaining credit, loans, advances on stocks, invoices and goods, or discounts).
- The issue, acceptance or guarantee of Company bonds.
- The opening and closing of local units, premises, subsidiaries and branches.

For the purposes of clarity but without limitation on the award of powers of ordinary administration thus delegated, it should be noted that the Managing Director may (in all cases within the limits set out in the following paragraph):

- Keep and sign the Company's correspondence.
- Sell and purchase goods, products, and any other unregistered moveable property, and in general stipulate, amend and cancel service provision contracts and any other contract – asset or liability – necessary or useful for the management of the Company.
- Purchase and sell motor vehicles.
- Collect any sum due to the Company from any party (state, public and private bodies, firms and natural and/or legal persons), and issue corresponding receipts.
- Recruit and dismiss managers, staff and workers, and stipulate, amend and cancel the relevant employment contracts.
- Stipulate, amend and cancel coordinated and continuous collaboration contracts and consultancy contracts.
- Represent the Company in all dealings and relations with tax, finance, administrative and legal offices of the state and its subordinate local administrations, social security, insurance or health insurance bodies, with the power to agree on revenues, issue declarations and certificates, bring legal proceedings before all the administrative and judicial authorities of the Italian Republic, present declarations, lodge petitions against any order of the authorities and offices indicated above, and sign the relevant documents and/or consequent deeds.
- Represent the Company in legal proceedings before all the authorities of the Italian Republic and of foreign states, including supranational authorities, appoint lawyers and counsel for lawsuits, including for appeal, revocation, and annulment proceedings and proceedings before the Constitutional Court.
- Settle and reconcile any pending proceedings or dispute between the Company and third parties, therein including employment disputes with managers, staff and workers, appoint arbitrators, including arbitrators as *amiable compositeurs*, and sign the relevant deeds of settlement.
- Represent the Company in any bankruptcy proceedings with all the necessary powers, initiate and/or request bankruptcy declarations, attend creditors' meetings, accept and exercise the office of member of creditors' committees if the Company is entitled to such an appointment, declare credits, affirming their existence, accept and reject proposals

for composition with creditors, and take any other action necessary and/or useful for such procedures.

- Receive letters and packages, both ordinary post and registered and/or insured, from the posts and telegraphs offices, shipping companies, and any other transport company, collect postal and telegraphic money orders and cheques of any kind and for any sum, request and receive sums, securities, goods and documents, signing the relevant receipts, releases and exonerations from liability with any public and/or private administration, including any public or private savings institution, the State Treasury, the Deposits and Loans Fund, the public debt, customs and state railway offices, whether the headquarters or regional and/or peripheral offices, including regional headquarters of the Revenue and their local sections and undertake any action or transaction with the aforementioned administrations.
- Sign bills of exchange as drawer with clients of the Company, issue receipts for bills of exchange and securities to order, endorse cheques, bills of exchange and credit instruments, but only to collect them and pay them into the current accounts of the Company or protest them, present for discounting bills of exchange issued by Company clients in favour of the Company and drafts issued by the Company in favour of its clients.
- Receive, establish, and release deposits, including security deposits, and establish restrictions of any kind.
- Undertake all financial transactions for the ordinary administration of the Company, open bank current accounts and a current account in the name of the Company at the post office current account department, sign cheques payable from such current accounts, including when overdrawn, within granted limits, verify such current accounts and approve their statements of account.
- Undertake each and every activity concerning the observance of safety, environmental protection and privacy regulations, and represent the Company before each and every public and private office and body established for this purpose.
- Delegate part of the powers indicated above to executives, managers or employees of the Company or to third parties, provided that such delegated powers do not give rise to a supervisory role as provided by Articles 2203 et seq. of the Civil Code.

The following value limits are applicable to powers of ordinary administration granted to the Managing Director:

- The Managing Director may settle, conclude and reconcile lawsuits or disputes (therein including arbitration) of an amount not exceeding €1,000,000 (one million Euro) per individual dispute.
- The Managing Director may negotiate, stipulate, amend and/or cancel:
- Contracts for the purchase of machinery, plant, equipment and/or motor vehicles for an amount not exceeding €1,000,000 (one million Euro) per individual contract.
- Consultancy contracts for an amount not exceeding €500,000 (five hundred thousand Euro) per contract.
- Any other contract which involves obligations on the Company for amounts not exceeding €1,000,000 (one million Euro) per individual contract, with the exception of supply contracts for goods to clients of the company, to which the said limit does not apply.

By resolution of 22 February 2007, the Board resolved to grant the following powers to Mr. O. Tonin, to be exercised only in cases of urgency:

- Sign correspondence and deeds of ordinary administration.
- Generally proceed to execute, operate and maintain technical installations, entering into obligations on behalf of the Company vis-à-vis third parties with respect to purchases and supplies.
- Represent the Company in all matters relating to taxes, contributory and revenue duties of any nature, with the power to lodge and sign appeals to the competent authorities and commissions, including central commissions.
- Endorse and collect postal and telegraph orders, bank drafts and current account cheques, bills of exchange issued or endorsed by third parties in favour of the Company, demand sums from both private individuals and any public body or administration for capital, interest and accessory costs issuing the relevant receipts and discharges.
- Make security deposits, collect and issue receipts continuously for the redemption of deposits and the consequent withdrawal of securities and sums or interest accrued with state and regional authorities, state railways, provinces and municipalities, undertaking to notify the custodian institutions of variations that occur subsequent to the present resolutions in the powers of representation hereby granted and to hold the aforementioned institutions immune from any damage that may arise for them from any failure to notify; demand and issue receipts for warrants from the state treasury or any public savings institution.

- Withdraw letters, parcels and packages, including registered or insured post, from post offices and any other public or private office; withdraw material addressed to the Company from state railways or any other carrier, issuing the relevant discharges and discharges.
- Sign documentation, invoices and declarations and undertake all customs and foreign exchange formalities relating to final or temporary imports, including in relation to international services.
- Sign declarations of conformity of tractors and other machinery manufactured by the Company, taking all action necessary to expedite such operations.
- Enter into or reduce medium or long term loans and debts with any Italian or foreign credit institution, including in the form of current accounts, and open lines of credit for the discount and assignment of bills of exchange etc. for any value, establishing the conditions thereof.
- Stipulate, amend or cancel consultancy contracts for an amount not exceeding €50,000 for each contract by sole signature, for amounts exceeding €50,000 by joint signature with a Managing Director.
- Make any payment to or withdrawal from current accounts and lines of credit with Italian and foreign credit institutions, including by the issue of cheques in the name of the Company or third parties drawn on balances of current accounts with banks, including overdrawn accounts, endorse and discount bills of exchange issued or endorsed by third parties in favour of the Company, sign extended payment contracts with the issue of the relevant bills of exchange, and generally undertake any bank transaction with any Italian or foreign credit institution.

On 22 February 2007, the Board of Directors of Carraro Spa also granted some of the aforementioned powers to Mr. Enrico Gomiero, Director of Administration, Finance and Control, and Dr. Tiziana Votta, General Manager Systems, with mandates to take action separately from other delegated representatives.

The General Managers, the Director of Human Resources and Systems and the Works Managers were granted, by means of the relevant mandates, limited powers related to the performance of their relevant roles.

### **3. Independent Directors**

The Board makes an annual assessment the independent status of each director and circumstances that could prejudice their independence of judgement.

Among the non-executive directors, pursuant to the Corporate Governance Code, and taking account of the information provided by each director, Prof. Giorgio Brunetti, Mr. Sergio Erede and Dr. Antonio Cortellazzo were independent directors in the year 2006.

During its meeting of 22 February 2007, the Board assessed the independence requirements of the said directors, after obtaining all appropriate information on the existence or otherwise of the respective requirements indicated above, including on the basis of information supplied by each director. The assessment was carried out by the Board on the basis of the requirements of applicable legislation (Article 147 ter of the Consolidated Law on Finance) and, with more regard to the substance than the form, those listed in the Corporate Governance Code (3.C.1).

The Board of Statutory Auditors, as part of the tasks awarded to it by law, verified the application of the verification criteria and procedures adopted by the Board to assess the independence of its members and has announced that it will indicate its conclusions in its report to the shareholders' meeting.

Specifically, it should be pointed out that Prof. Giorgio Brunetti and Mr. Sergio Erede were appointed Directors of the Company for the first time during the shareholders' meeting held on 12 June 1997 and subsequently confirmed thereafter, the last occasion being the shareholders' meeting held on 11 May 2006.

The fact that they had held the post of Director of the Company for more than nine of the last twelve years was not considered by the Board as an obstacle to the maintenance of independence requirements. In fact, it is considered that their personal and professional characteristics in any case guarantee the maintenance of their independence of judgement, which constitutes a fundamental element of independence, and that their considerable time as directors has enabled them to acquire profound knowledge of the company and its mechanisms, which as such is a value to be preserved.

### **4. Processing of corporate information**

The circulation of information, in particular 'price sensitive' information relating to the Company is treated with the necessary confidentiality.

All directors, heads of business units, managers, department heads and other employees are required to maintain the confidentiality of documents and information acquired in the

performance of their duties and to comply with established procedures for external communication of such documents and information.

The Chairman and the Managing Director ensure the proper management of confidential information. To this end Carraro S.p.A has adopted formal procedures for internal management and external communication of documents and information regarding the company, with particular reference to 'price sensitive' information.

Additionally, following the adoption into the Italian legal system of European Directive 2003/6/EC by Law 62/2005 on 'market abuse' and in particular by the Consolidated Law on Finance (Article 114, paragraph 1), and the relevant regulations issued by Consob, Carraro S.p.A. adopted, by resolution of the Board of Directors dated 11 May 2006, "Procedures for the processing of privileged information", establishing a "Register of persons who have access to privileged information" and issuing a "Procedure for maintenance and update" of the said Register. These procedures and the Register were compiled according to the provisions of Articles 114, 115 bis and 181 of the Consolidated Law on Finance and Article 152 bis to 152 quinquies of the Regulation on Issuers (Consob Resolution 11971/1999 and subsequent amendments).

The Board of Directors has approved the "Code of Conduct on Internal Dealing" dated 20 December 2002 and updated it on 29 March 2006 following the implementation in Italy of Directive 2003/6/EC by Law 62/2005 on 'market abuse', which amended the legislative framework on Internal Dealing (Article 114, paragraph 7, of Legislative Decree No. 58/98, the Consolidated Law on Finance, and Articles 152 sexies et seq. of the Regulation on Issuers, Regulation No. 11971/1999, amended by Consob Resolution No. 15232 dated 29 November 2005).

The Code of Conduct sets itself the objective of regulating information flows relating to transactions made by Significant Persons and persons closely linked to them in financial instruments issued by Carraro S.p.A.

The person responsible for the receipt, management and disclosure to the market of information relating to transactions undertaken by Significant Persons has been identified as the Director of Administration, Finance and Control. The person responsible is obliged to perform their assigned functions as indicated in the Code.

Significant Persons must notify the person responsible of the transactions undertaken in financial instruments issued by the Company by them or persons closely linked to them which cumulatively exceed €5,000 (five thousand Euro) over the course of the year, complying with the notification deadlines established by the Code.

Account is therefore taken of transactions made by each Significant Person, by spouses who are not legally separated, by dependent children, including spouse's children, and, if cohabiting for at least a year, the parents, relatives and relatives-in-law of Significant Persons.

"Blocking periods" are also defined, during which no transactions can be made.

The Board of Directors may, for contingent and exceptional reasons, prohibit or limit the undertaking of transactions by some or all Significant Persons during certain other periods of the year.

The Company is assessing whether to prepare a single procedure that provides common and systematic treatment for obligations and precautions relating to the processing of company information, especially privileged information.

## **5. Establishment and functioning of internal committees of the Board of Directors**

On 11 May 2006 the Board resolved to re-establish the following Committees:

- The Internal Control Committee;
- The Remuneration Committee.

All committees have a merely advisory and consultative function and assist the Board in its investigations of matters within their respective remits.

Each committee is assisted from time to time in the organization of its meetings by corporate departments. Minutes are kept of each committee meeting.

Committee members have the right to access information and company departments necessary for the performance of their tasks and – when considered necessary – may avail themselves of external consultants.

Although the Board has not approved a specific budget for each committee, the committees may periodically avail themselves of the financial resources necessary for the performance of their respective tasks. Each committee reports periodically to the Board on its activities.

A process is underway to adapt the functions of such Committees in the light of recent legislative developments.

## **6. Appointment of directors**

Directors are appointed at three-year intervals by approval of the shareholders' meeting. The curriculum vitae of each candidate for directorships, indicating any suitability to be classified as an independent director, is made available to shareholders at the company headquarters

at least fifteen days before the scheduled date of the shareholders' meeting convened to appoint directors.

It should also be noted that with respect to the appointment of directors, the Board of Directors is planning to submit some amendments to the Articles of Association to an extraordinary shareholders' meeting. Such amendments are necessary to adapt the Articles of Association to the recent amendments to the Consolidated Law on Finance (Legislative Decree 58/1998) by Law No. 262/2005 and by Legislative Decree 303/2006, which provide for a list voting mechanism for the election of directors, in order to ensure that at least one director can be elected by the minority.

The Board of Directors does not consider it necessary to establish an internal committee for proposed appointments. This function is carried out by the Board of Directors itself.

## **7. Remuneration of Directors**

In accordance with the Corporate Governance Code adopted by the Company, a Remuneration Committee has been established to improve alignment between the remuneration system and the creation of value. The Remuneration Committee, composed of two independent directors, Dr. Antonio Cortellazzo and Mr. Sergio Erede, and non-executive director Mr. Onofrio Tonin, provides advice and consultancy to the Board.

In general, the remuneration of directors is commensurate with responsibilities and mandates granted to them, taking account of the characteristics of the sector of activity, the complexity of the Company and the Group and the professional qualities of each person, without prejudice to the objective of creating value for shareholders in the medium-long term.

The remuneration of the Managing Director is linked to the economic results of the Company in relation to objectives established by the Board of Directors.

During 2006, the Remuneration Committee met twice to deliberate and make proposals for the Board of Administration, on the advice of the Board of Statutory Auditors, on the total amount of emoluments to be granted to directors. Such proposals were consequently approved by the shareholders' meeting. The Board, again on the proposal of the Remuneration Committee, defines the distribution of the total remuneration among individual members.

The details of remuneration are set out in the specific annex to the supplementary note to the financial statement at 31.12.2006.

## **8. Internal Control System**

The Board of Directors is responsible for the internal control system, for which it establishes the remit and periodically assesses its suitability and functional effectiveness, ensuring the main corporate risks to the Company and the Group are identified and managed in a satisfactory manner.

The internal control system, using an adequate process of control and management of the main risks, has the objective of:

- a) verifying the adequacy of Company processes in terms of effectiveness and efficiency;
- b) guaranteeing the reliability and accuracy of financial information;
- c) guaranteeing that Company assets are safeguarded;
- d) ensuring conformity of operations to internal and external regulations.

The Board of Administration ensures that its assessments and decisions relating to the internal control system, the approval of financial statements and half-yearly reports and relations with audit companies are supported by adequate preliminary investigative activities. Such activities are normally awarded to the Internal Control Committee, which at its meetings systematically deliberates on matters directly or indirectly concerning internal control, including verification of the correct application of established accounting principles which may involve meetings and exchanges of information with the audit company. A report on the results of this activity is provided to the Board of Directors.

On 11 May 2006, the Board of Directors resolved to re-establish an Internal Control Committee from among its members. The Committee is composed of three directors, of which two are independent (Prof. Giorgio Brunetti and Dr. Antonio Cortellazzo) and one is a non-executive director, Mr. Onofrio Tonin. Prof. Brunetti serves as chairman of the Internal Control Committee.

The current composition of the Committee is in line with the recommendation of the Corporate Governance Code, which advises that at least one member should possess experience in the field of accounting and finance.

The Chairman of the Board of Statutory Auditors or another Statutory Auditor designated from time to time by the former, together with the head of internal control, and Company employees participate whenever necessary in the work of the Committee, which meets at least quarterly, to deliberate on matters on the agenda. The proceedings of each meeting are recorded in the minutes.

During 2006, the Internal Control Committee met nine times, mainly to examine the following questions, in accordance with the tasks assigned to it by the Corporate Governance Code:

- assessment and approval of transactions with related parties according to the relevant procedure;
- verification of the constant application of IAS/IFRS international accounting standards in the annual financial statement and the half-yearly report, examination of the statutory and consolidated financial statement at 31.12.2006, with particular reference to assessment criteria;
- analysis of the impact of the new 2006 legislation on corporate governance of the Company, with an assessment of the adequacy of internal procedures particularly in respect of Internal Dealing and the processing of privileged information.;
- analysis of the new Corporate Governance Code with its related effects, and the need to adapt the previously applicable code;
- examination of the advancement of the planned adoption of the Organizational Model pursuant to Legislative Directive 231/2001;
- periodic information prepared by the Internal Audit department during 2006;
- assessment of the effectiveness of the account audit process by direct discussions with the audit company.

Since 22 February 2007, the Managing Director, Mr. Carlo Borsari, has been designated by the Board as the executive director responsible for supervising the functionality of the internal control system. As such he is required to carry out the following tasks:

- a) Supervision of the identification of the main corporate risks, taking account of the characteristics of the activities of the issuer and its subsidiaries, and subjecting them to periodic examination by the Board of Directors.
- b) Implementation of policy defined by the Board of Directors, providing for the planning, implementation and management of the internal control system, constantly assessing its overall adequacy, efficiency and effectiveness; he is also responsible for the adaptation of the system to the dynamics of operating conditions and the legislative and regulatory situation.
- c) Formulating proposals to the Board of Directors for the appointment, revocation and remuneration of one or more heads of internal control.

The Company has established an internal audit department which is headed by the head of internal control.

This department is independent of all other corporate departments and reports to the Board of Directors, normally through the Internal Control Committee, and to the executive director responsible for supervising the functionality of the internal control system.

Its activities during 2006 were mainly those relating to topics discussed at meetings of the Internal Control Committee.

On 29 March 2007 the Board of Directors resolved to adopt the Organizational Model pursuant to Legislative Decree 231/2001, formalizing and implementing an organizational structure which already exists within the Company and is constantly updated. It should also be noted that the adoption took place following the conclusion of an assessment of the risks connected with the matters covered by the decree and an analysis of the state of corporate procedures that highlighted failures and areas for improvement, resulting in an adjustment plan. In accordance with the provisions of the decree, a Supervisory Body has been established to monitor the application of the legislative provisions and the proper functioning of the Model. This body is composed of an independent director who is a member of the Internal Control Committee and who acts as Chairman, together with the head of the internal audit department and the head of the legal office.

#### **9. Directors' interests and transactions with related parties**

On 11 May 2006 the Board resolved to adopt a new text of the Procedure for Approval of Transactions with Related Parties, amended following the adoption of the new IFRS accounting standards. Specifically, guidelines and criteria have been established to identify the main transactions with related parties and, on the advice of the Internal Control Committee, an advance information and approval procedure for transactions with related parties has been approved by the Board of Directors.

In this manner the Board ascertains that the transactions in which a director possesses an interest, on his own behalf or on behalf of third parties, and those entered into with related parties are undertaken in a transparent manner in accordance with criteria of substantive and procedural propriety.

## **10. Auditors**

The Board of Statutory Auditors supervises compliance with law and the Articles of Association and has a management monitoring function. In their current formulation, the Company's Articles of Association provide at Article 30 that the Board of Statutory Auditors is composed of three auditors and two replacements, who are appointed from lists presented by shareholders that, individually or together with others, represent at least 3% of voting shares at shareholders' meetings.

The current Board was appointed by the shareholders' meeting of 11 May 2006 and will conclude its term at the shareholders' meeting held to approve the 2008 financial statement. No members were elected by minorities as a single list was presented for election.

The current auditors possess the independence requirements established by law for auditors and those established by the Corporate Governance Code for directors.

The Board of Statutory Auditors has ascertained that its own members continue to meet the independence requirements. The procedural methods of assessment, compiled by the Board, are set out at the bottom of this paragraph.

During 2006, no situations have occurred in which members of the Board of Statutory Auditors have been obliged to declare their own interests or those of third parties in a certain transaction by the issuer.

Information is exchanged between the Board of Statutory Auditors and the Internal Control Committee through the systematic participation at Committee meetings of the Chairman of the Board of Statutory Auditors or an Auditor designated by the Board.

With respect to the appointment of members of the Board of Statutory Auditors, it should be noted that the Board of Directors is planning to submit to an extraordinary shareholders' meeting some amendments to the Articles of Association which are necessary to adapt them to the recent updates of the Consolidated Law on Finance (Legislative Decree 58/1998) introduced by Laws No. 262/2005 and No. 303/2006.

On that occasion the Articles of Association must also adopt the legislative provision that requires election of the Chairman of the Board from auditors appointed by the minority, and the recommendation of the Corporate Governance Code that provides for the lists of candidates for the post of Auditor to be deposited at least 15 days before the shareholders' meeting.

Outcome of the assessment of the independence of members of the Board of Statutory Auditors:

“The Board of Statutory Auditors, as provided at point 10.C.2. of the Corporate Governance Code, acknowledges that it has adopted the same criteria for assessment of the continued validity of the independence requirements as those provided by the Corporate Governance Code for directors, and that it has assessed each of its members according to procedures that ensure an impartial and true assessment.

On completion of the assessment, the Board attests that the independence requirements established by the Corporate Governance Code remain valid for each of its members.”

### **11. Relations with shareholders**

The Company’s interest in establishing and maintaining a continuous dialogue with shareholders in general as well as institutional investors and analysts has taken the form of Investor Relations, which carries out its role in conjunction with top management through prompt and thorough communication of significant events, and through periodic meetings with analysts and investors.

The Company recently commenced a study for a renewal of its website, the general structure of which will be changed, dedicating an appropriate section to Corporate Governance.

The public distribution of quarterly reports, the half-year report, the financial statement for the year and consolidated financial statement, together with shareholders’ meetings at which participation is encouraged and facilitated, represents the Company’s fundamental means of communication between shareholders and the Board of Directors.

The Company has not currently adopted regulations for shareholders meetings, as it is considered that the powers granted to the Chairman of the meeting by the Articles of Association - which include, *inter alia*, the task of supervising the proceedings of the meeting – enable it to guarantee the orderly progress of the meeting and avoid the risks and problems that could arise for shareholders’ meetings from any failure to observe regulations. Each shareholder is always guaranteed the right to contribute to matters under discussion.

The following meetings of the company bodies are scheduled for 2007:

|                          |                                                                                                                                                                |
|--------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 22.02.2007               | Analysis of provisional financial statement for 2006                                                                                                           |
| 29.03.2007               | Board of Directors to examine and approve the Carraro Group consolidated financial statement and Carraro S.p.A. draft financial statement at 31 December 2006. |
| 14.05.2007<br>15.05.2007 | Shareholders' meeting to approve the 2006 financial statement (first and second convocation).                                                                  |
| 15.05.2007               | Board of Directors to examine and approve the quarterly report at 31 March 2007.                                                                               |
| 12.09.2007               | Board of Directors to examine and approve the half-year report at 30 June 2007.                                                                                |
| 14.11.2007               | Board of Directors to examine and approve the quarterly report at 30 September 2007.                                                                           |

**TABLE 1: STRUCTURE OF THE BOARD OF DIRECTORS AND COMMITTEES**

| Board of Directors                                          |                     |           |                       |             |              |                               | Internal Control Committee |              | Remuneration Committee    |              |
|-------------------------------------------------------------|---------------------|-----------|-----------------------|-------------|--------------|-------------------------------|----------------------------|--------------|---------------------------|--------------|
| Position                                                    | Members             | Executive | Non-executive         | Independent | % attendance | No. of other posts            | Member                     | % attendance | Member                    | % attendance |
| Chairman                                                    | Carraro Mario       | X         |                       |             | 100%         |                               |                            | %            |                           | %            |
| Managing Director                                           | Borsari Carlo       | X         |                       |             | 100%         |                               |                            |              |                           |              |
| Director                                                    | Carraro Francesco   |           | X                     |             | 25%          |                               |                            |              |                           |              |
| Director                                                    | Carraro Enrico      | X         |                       |             | 100%         |                               |                            |              |                           |              |
| Director                                                    | Carraro Tomaso      | X         |                       |             | 100%         |                               |                            |              |                           |              |
| Director                                                    | Brunetti Giorgio    |           | X                     | X           | 100%         | 5                             | X                          | 100%         |                           |              |
| Director                                                    | Cortellazzo Antonio |           | X                     | X           | 100%         | 6                             | X                          | 100%         | X                         | 100%         |
| Director                                                    | Erede Sergio        |           | X                     | X           | 75%          | 10                            |                            |              | X                         | 100%         |
| Director                                                    | Tonin Onofrio       |           | X                     |             | 100%         |                               | X                          | 100%         | X                         | 100%         |
| Number of meetings held during the year of reference (2006) |                     |           | Board of Directors: 8 |             |              | Internal Control Committee: 8 |                            |              | Remuneration Committee: 2 |              |

**TABLE 2: BOARD OF STATUTORY AUDITORS**

| Position                                                        | Members             | Percentage attendance at Board meetings | Number of positions held (listed companies) |
|-----------------------------------------------------------------|---------------------|-----------------------------------------|---------------------------------------------|
| Chairman                                                        | Roberto Saccomani   | 100%                                    | -                                           |
| Statutory Auditor                                               | Francesco Secchieri | 100%                                    | -                                           |
| Statutory Auditor*                                              | Federico Meo        | 50%                                     | -                                           |
| Replacement Auditor**                                           | Renzo Lotto         | 50%                                     | -                                           |
| Replacement Auditor                                             | Marina Manna        | -                                       | -                                           |
| Number of meetings held during the year of reference (2006): 10 |                     |                                         |                                             |

\* Statutory Auditor from 11 May 2006

\*\* Statutory Auditor up to 11 May 2006

**TABLE 3: OTHER PROVISIONS OF THE CORPORATE GOVERNANCE CODE**

| <b>System of mandates and transactions with related parties</b>                                                                                                                                  | <b>YES</b> | <b>NO</b> | <b>Summary of reasons for any deviation from the recommendations of the Code</b>                                                                                                               |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------|-----------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Has the Board of Directors awarded mandates, defining:                                                                                                                                           |            |           |                                                                                                                                                                                                |
| a) limits                                                                                                                                                                                        | X          |           |                                                                                                                                                                                                |
| b) method of execution                                                                                                                                                                           | X          |           |                                                                                                                                                                                                |
| c) and frequency of reporting?                                                                                                                                                                   |            | X         | Directors with mandates follow current practice at meetings of the Board of Directors with respect to the most significant transactions of those undertaken as part of the mandates they hold. |
| Does the Board of Directors reserve to itself the examination and approval of transactions of particular economic, asset and financial importance (including transactions with related parties)? | X          |           |                                                                                                                                                                                                |
| Has the Board of Directors established guidelines and identification criteria for "significant" transactions?                                                                                    | X          |           |                                                                                                                                                                                                |
| Are the aforementioned guidelines and criteria described in the report?                                                                                                                          | X          |           |                                                                                                                                                                                                |
| Are the procedures for approval of transactions with related parties described in the report?                                                                                                    | X          |           |                                                                                                                                                                                                |
| <b>Procedure for the most recent appointment of directors and auditors</b>                                                                                                                       |            |           |                                                                                                                                                                                                |
| Was the deposit of candidatures for directorship made with at least ten days notice?                                                                                                             | X          |           |                                                                                                                                                                                                |
| Were candidatures for directorships accompanied by an indication of eligibility for designation as independent?                                                                                  | X          |           |                                                                                                                                                                                                |
| Was the deposit of candidatures for the post of auditor made with at least ten days notice?                                                                                                      | X          |           |                                                                                                                                                                                                |

|                                                                                                  |   |   |                                                                                                                                                                                                                                                                                                                                         |
|--------------------------------------------------------------------------------------------------|---|---|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                                  |   |   |                                                                                                                                                                                                                                                                                                                                         |
| Were candidatures for auditor accompanied by an extensive report?                                | X |   |                                                                                                                                                                                                                                                                                                                                         |
| <b>Shareholders' meetings</b>                                                                    |   |   |                                                                                                                                                                                                                                                                                                                                         |
| Has the Company approved regulations for Shareholder's meetings?                                 |   | X | The Company has not currently adopted regulations for shareholders meetings, as it is considered that the powers granted to the Chairman of the meeting by the Articles of Association - which include, inter alia, the task of supervising the proceedings of the meeting – enable it to guarantee the orderly progress of the meeting |
| Are the regulations attached to the report (or does it indicate where they are obtainable)?      |   | X | See previous point                                                                                                                                                                                                                                                                                                                      |
| <b>Internal Control</b>                                                                          |   |   |                                                                                                                                                                                                                                                                                                                                         |
| Has the Company appointed heads of internal control?                                             | X |   |                                                                                                                                                                                                                                                                                                                                         |
| Are the heads of internal control hierarchically independent of heads of operating departments?  | X |   |                                                                                                                                                                                                                                                                                                                                         |
| Organizational unit in charge of internal control (pursuant to Article 9.3 of the Code)          |   |   | Internal Auditing                                                                                                                                                                                                                                                                                                                       |
| <b>Investor Relations</b>                                                                        |   |   |                                                                                                                                                                                                                                                                                                                                         |
| Has the Company appointed a head of investor relations?                                          | X |   |                                                                                                                                                                                                                                                                                                                                         |
| Organizational units and details (address/telephone/fax/email) of the head of Investor Relations |   |   | Administration, Finance and Control Headquarters<br>Via Olmo, 37 – 35011 – Campodarsego (PD)<br>Tel. 049.92.19.253<br>Fax 049.92.19.166<br>Email: webfinance@carraro.com                                                                                                                                                                |