



# THE ROLE OF THE BOARD IN THE NEW NORMAL: THE BOARD 2.0

**Governance Committee**  
Position Paper

**AmCham Italy**



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**American Chamber of Commerce in Italy**



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## INTRODUCTION

This paper, prepared by the Governance Committee, comes at a time of historical change, accelerated by the pandemic and the evolution of the global business environment.

Both multinationals and smaller companies are facing new challenges not only from a business but also – if not especially – from an organizational point of view.

One of the main elements that emerged is the review of governance processes and structures, an aspect that is becoming increasingly important in providing companies' strategic direction and decision-making, supporting the actions of top management.

At this stage, the main business players are manifesting a clear need to renew the idea of governance and update the profile of their boards, making them more 'capable' of dealing with current complexities by introducing new cross-cutting skills capable of creating value within the company, and adapting them to the new paradigms (ESG, diversity, etc.) that are increasingly important in the eyes of institutional investors. The new forms of governance must ensure process efficiency and effective decision-making so as to shorten the time between planning and implementation of actions resulting from decisions taken by the board.

Time, composition, competences and organization emerge as the pillars around which to design the profile of the Board 2.0, capable of increasing corporate competitiveness and adding skills.

In this paper, drawn up by some of Italy's leading governance experts, the aim was to start from a description of the Board's operation in order to understand the process and decision-making, and then to review the main models used, comparing the Board 'Made in the USA' and the Board 'Made in Italy' in order to identify differences and idiosyncrasies.

Finally, an attempt was made to introduce the concept of Board 2.0 starting from an understanding of the current business environment and the risks and opportunities that companies have to deal with on a daily basis.

The final part is dedicated to presenting some 'disruptive' ideas on the topic of the Board with the aim of initiating an open and taboo-free debate on this topic.

We are convinced that this document can be a starting point to begin a process of dialog with stakeholders, companies and even institutions, in light of the recent legislative bill presented on this topic, which confirms both the goodness of our choice to set up a Committee dedicated to governance and the topicality of this document.

The hope is that this paper can be a source of inspiration for all those who deal with governance on a daily basis and a starting point for the institutions to find cutting-edge regulatory solutions capable of fostering the competitiveness of the national economy and greater attractiveness for American investments.

Enjoy the read.

  
Simone Crolla

*Managing Director - American Chamber of Commerce in Italy*

# 1. THE ROLE OF THE BOARD: OBJECTIVES, RESPONSIBILITIES AND COMPETENCES

A profound socioeconomic transformation is under way, significantly accelerated by the pandemic. Never before has it seemed essential to identify an effective and efficient system of governance, one that is compliant with industry regulations but also able to manage the change that has already taken place with the right skills and methods.

And while issues related to sustainability impose new reflections on the need to first and foremost involve shareholders and then all stakeholders in the management of the enterprise<sup>1</sup>, more than ever it seems necessary to reflect on the role (current and prospective) of the board, to which civil law exclusively entrusts the Company's management.

As is well known, aside from the traditional (or tripartite) Italian system of having a Constitutive Body (the Shareholders' Meeting), a governing body (the board of directors, or board) and a Control Body (the board of Statutory Auditors), civil law has long allowed the choice to opt for:

- The German-style two-tier system (which provides for an intermediate body, the Supervisory board, between the Shareholders' Meeting and the management board, with the function of senior management, strategy setting, control, and approval of the financial statements).
- The Anglo-Saxon one-tier system (where the management and control functions are entrusted to a single body, within which independent directors perform control and risk mitigation).

In this regard, it seems appropriate that a prior examination introducing these reflections should take place by processes in order to focus attention on the board of directors' substantive scope of operation.

Today very significant attributions and responsibilities are concentrated in the governing body, the sound exercise of which should be carried out through this logic, that is, acquiring the reference data through a cross-functional view.

While 'directional' processes aimed primarily at outlining the organization's strategy and medium- to long-term planning are typically characterized by unstructured decisions, it may seem difficult to organize them through overly rigid schemes.

Nevertheless, it is possible to delineate four stages through which the work of the governing body is carried out: with respect to these stages, the input is represented by information resources, the process output by the adoption of the resolution.

The examination in four stages, specifically:

1. Initiative
2. Investigation
3. Deliberation
4. Implementation

also allows us to examine who is responsible (who), the activities to be performed (what), the main rules of the game (how), and the timing of the workflow (when).

Insofar as applicable, it is worth considering international best practices, which in Italy are enumerated in the Corporate Governance Code approved by the Corporate Governance committee of Borsa Italiana S.p.A. in January 2020 (the 'Corporate Governance Code'). This code currently constitutes the best example of good governance practices from which the universe of large listed and unlisted companies in our country draws inspiration.

## INITIATIVE STAGE

The first stage (Initiative) allows us to reflect on the roles and assignments of the board and its specific responsibilities and committees.

In fact, it is necessary to first identify the actors who, as participants in the governance process, play a driving role with respect to the initiation of the process preparatory to taking a board resolution.

The **Chair**, who holds the formal role of convening the board, is aided and supported by the corporate secretariat – a function dedicated to coordinating the board (and possibly the committees) – and is the true process owner of board activities.

Normally, the Chair has authorizing duties, namely to convene the board of directors, set the agenda, coordinate the work, and ensure that all board members are assured adequate information on the matters under discussion. The Chair is usually the legal representative of the company and ensures the promotion of transparency of the company's business, making sure to represent all shareholders.

In general, the Chair ensures a continuity of relations between the board and the directors holding special offices and has access to all information within the corporate structure, making available to the Chief Executive Officer (or director) any information that is not acquired by them directly, for the purpose of the orderly conduct of that structure.

In order to avoid concentrations of power and to foster proper internal dialectics, the tasks and powers of administration are clearly and evenly distributed among and within the different bodies.

Likewise, the number of members of the corporate bodies is appropriate to the complexity of the

1. The term engagement is intended to refer to the process used by an organization to engage stakeholders with a well-defined purpose and to achieve a common outcome. The identification and definition of a stakeholder engagement process allows the involvement of key ('relevant') stakeholders internal and external to the organization in order to identify and understand their needs (mostly heterogeneous with regard to predominantly non-financial matters, i.e., sustainable matters) with the ultimate goal of planning actions aimed at the creation of shared value by the organization

organizational structure, and their composition reflects adequate professional and honorability requirements as well as an appropriate degree of diversification in terms of skills, experience, age, gender, and international perspective.

With regard to technical expertise, the initiative is allocated to different **committees** according to the subjects involved, identifying in order the Internal Audit and Risk committee, the remuneration committee, the appointments committee, and finally the strategy committee.

Among other duties the internal audit and risk committee is responsible for actions related to risk management policies and the assessment of the functionality, efficiency, and effectiveness of the internal control system, as well as for the adequacy of the organizational, administrative, and accounting structure (preparatory to an effective parallel control over management).

In addition to having a proposal-making function in the area of personnel incentives (especially personnel with strategic responsibilities within the organization), the remuneration committee is responsible for the implementation of remuneration and incentive systems and for assessing the consistency of these systems with long-term strategies.

The appointments committee has the power to confer particular assignments or proxies on one or more directors, as well as the appointment and dismissal of the General Manager (and other members of the executive board).

The initiative is the responsibility of the CEO - General Manager and/or the executive committee whenever the resolutions being adopted are related to the delegated management functions.

The proper identification of the delegation – in which the CEO operates with ‘supervised’ autonomy with a requirement for periodic disclosure to the board – is one of the key elements in establishing efficient and effective governance<sup>2</sup>.

The work of the Chair and the CEO - General Manager enjoys valuable support and counterbalance in the activities of the board committees: the participation of these committees in the initiative stage allows for facilitation and improvements in the effectiveness of the work, fostering the distribution of tasks and monitoring of each area of intervention.

The board committees communicate the order of the internal work to be done, preparing the schedule for the following months, the documentation necessary to carry out these activities specifying the functions and business areas involved, the type of resolution to be submitted to the board of directors, and the timeframe in which the matter is expected to be dealt with.

This way the corporate secretariat is in a better position to fulfill its role by facilitating the collection of the documentation necessary for the conduct of the work and preparing the calendar of ordinary corporate events in good time, taking into account the needs of each committee.

2. Overly broad delegation actually depletes the board of directors in its function of ‘high administration’ and strategy setting, and reduces it to a place of ratification of the CEO’s decisions. Conversely, too little delegation is intuitively dysfunctional with respect to the need for decisions to be made with the timeliness and speed that today necessarily affect the conduct of business.

## INVESTIGATION STAGE

The second stage (Investigation) allows for a brief mention of the importance of adequate information flows, their organization and timeliness, and verification of the quality and sufficiency of the information.

Many companies have been working on setting up a mechanism to ensure that directors carry out the task entrusted to them in an informed and knowledgeable manner, adequate in terms of time available, and coordinated with the work of other corporate bodies in order to avoid unnecessary duplication or dystonia.

Generally, internal rules are adopted to regulate the timing, format and contents of the documentation to be sent to the individual members of the bodies for the informed adoption of resolutions on the matters on the agenda, the identification of the persons required to send information flows to the corporate bodies, the determination of the minimum content of the information flows, including indications concerning the company’s exposure to all types of relevant risks and the types of transactions. Indication of the respective risks and the confidentiality obligations that the members are bound to and the mechanisms to ensure compliance are provided.

The circulation of information takes several trajectories: a first pertains to the circulation of information from the organizational structure to the corporate bodies, and a second pertains to the organization of infra-board information circulation.

The goal is to give the necessary emphasis to one of the pillars of good corporate governance: the ‘transparency of management activities.’

Regarding the importance of information flows, two best practices in this area are noted in order to expand opportunities for monitoring business risks:

- a. The increase in the flows of non-executive directors (and the simultaneous increase in the number of independent directors).
- b. The involvement of directors without proxies.

Such implementations, especially in complex areas of business, make it possible to better manage potential conflicts of interest.

## INFORMATION FLOWS AND DIGITIZATION

Finally, with regard to the issue of the quality and sufficiency of the information flows and documentary supports made available to the directors, it is good to remember that excessive information and/or information not provided in a timely manner is tantamount to omitted information, or at any rate insufficient information.

To address the shortcomings that plague the timeliness of information circulation, where possible and in accordance with their structure and size, Italian boards are increasingly equipping

themselves with specially designed IT platforms to support the board's work.

In fact, a true digitization of information flows is underway, providing for near-real-time ways of transmitting information that can guarantee both the completeness and degree of detail of the flows and the full protection of confidentiality requirements.

From convening the meeting and sharing the agenda (and documents supporting the discussion) to distributing the minutes and resolution, the directors thus have the ability to concentrate information relevant to their resolutions in shared, digital platforms that can ensure the circulation of data, observations and reflections.

The opportunity for further development and digitization is very high: while today digitization primarily consists of sharing and managing information flows (the input is provided directly by the functions or divisions involved from time to time under the close supervision of the corporate secretariat, as the function dedicated to receiving information and taking care of its transmission), an expansion of the use of these tools to all the stages covered by this analysis is desirable, not to mention broadly foreseeable.

### **DELIBERATION STAGE**

The third stage (Deliberation) allows for further examination of the different distribution of roles within the board and its committees in the decision-making phase and to emphasize the importance of healthy and transparent dialog among members.

At this stage, the importance of a proper qualitative and quantitative composition of board members and the requirements of professionalism and honorability required of them, gender balance, and sound management of conflicts of interest are well grasped.

The time devoted to the analysis and discussion of the items placed on the agenda is crucial in the context of the board's work. Moreover, proper attention must always be paid to a number of elements, the consistency of which is definitely significant so that the adoption of appropriate board decisions is ensured.

The first relevant element concerns the process of selection and appointment of directors to the governing body. The rules of the board of directors and the by-laws help outline the appointment system, together with the specialized input of the appointments committee.

The second element to be considered, on the other hand, concerns the identification of the professional requirements that each board member must possess. Indeed, there is an increasingly topical issue regarding the verification and existence of the criteria of honorability, professionalism and independence of the directors<sup>3</sup>.

In fact, the board is required to preliminarily identify "its own qualitative and quantitative composition that is considered optimal," to ensure that the top bodies effectively carry out the role assigned to them.

The board of directors must also reflect an adequate degree of diversification in terms of, among other requirements, skills, experience, age, gender, and international projection. To this end, the directors must have a professionalism appropriate to the role to be filled, calibrated with respect to the company's operational and dimensional characteristics, as well as widespread and diversified skills so that each member can contribute to identifying and pursuing appropriate strategies and ensuring effective risk governance in the company's areas of operation.

Directors must also devote time and resources commensurate with the complexity of their assigned duties and direct their actions to the pursuit of the company's overall interest.

When the board is renewed, the 'optimal qualitative and quantitative composition' must then be brought to the attention of the shareholders so that the choice of candidates to be presented can take into account the professional skills required.

The board of directors is called upon to carry out its tasks through open discussion, an organizational structure that involves the establishment of committees with advisory and propositional functions with the clear value of increasing the efficiency and effectiveness of the board's work.

This evidence initially stems from an observation of international best practices and has been adopted by the Corporate Governance Code, which recommends its establishment.

The board committees undoubtedly favor the adoption of decisions taken "with full knowledge of the facts," playing an important investigative role to be expressed through recommendations, proposals and opinions to be submitted to the attention of the meeting, and they can fulfill a 'calming' function of potential conflicts of interest since they are made up of independent and non-executive directors.

Having verified the profile of those involved in the decision-making process, let us now look at the method of opinion formation, which is preparatory to voting on the resolution to be adopted.

As anticipated in the previous stage, it is good operating practice to ensure access to the information documentation and sufficient and appropriate time to discuss the topics placed on the agenda. Fundamental to either aspect is the role of the Chair, who coordinates and guides the work with authority.

In concrete terms, the adoption of an ideal number of topics has the clear advantage of allowing for better preparation by each director on the topic, resulting in a more appropriate and informed consideration, as well as sufficient time to devote to discussion for each topic on the agenda so that each meeting can reasonably conclude with the adoption of the scheduled resolutions.

3. In this regard, for the banking sector note the contents of Ministry of Economy and Finance Decree no. 169 of November 23, 2020, which represents the latest piece of the complex system of national and European supervisory regulations and guidelines on the requirements and eligibility criteria for corporate officers of banks and financial intermediaries. In order to ensure the sound and prudent management of the intermediary, it is stipulated that individuals performing administration, management and control functions must be fit for the performance of the task and thus meet the requirements of professionalism, honorability and independence; satisfy criteria of expertise and propriety; and devote the necessary time to the effective performance of the task.

In the same vein and with the same objectives, it is stressed that – while the Chair and the board always prefer decisions to be made unanimously – decisions need not be made by unanimous vote, the criterion of majority rule certainly being more functional for streamlined, effective management.

### IMPLEMENTATION STAGE

The fourth phase (Implementation) outlines the responsibilities for reporting and implementing resolutions, as well as the role of the board of directors in identifying an organizational structure of proper quality and quantity.

At this stage the Chair/Secretary dynamic and the role of the CEO and/or General Manager again come into play.

In the analysis of corporate governance processes, the stage pertaining to the execution of adopted resolutions is often overlooked.

And in fact, one of the most valuable safeguards to be implemented at this stage – in order to be able to give the resolution full value and effectiveness – certainly concerns carrying out the fulfillments necessary for the execution of the decisions made by the board of directors over time. This translates into assigning this responsibility to a designated person who will assist the governing body and inform it of the status of implementation and deployment.

For this reason, it is correct to recall how the identification of a monitoring and control system with respect to the actual implementation of the adopted resolutions is increasingly an indispensable element of good corporate governance, in order to ensure compliance with all the specific requirements necessary for the implementation of the resolution, as well as its full compliance with what the board previously resolved (rules, procedures, policies).

### CONCLUSIONS

However, the examination, albeit brief, allows us to identify some critical issues that emerge from the exercise of the administration entrusted to the Italian board in the prevailing traditional system.

First, the centrality of correctly identifying the **qualitative and quantitative composition** of the board of directors of each company, which inevitably has specific complexities and characteristics, appears to be imperative today. The independent selection of directors with the right qualifications for the role they are going to play on the boards is essential to ensure the best management of the company.

In this regard, self-assessment, which should be an ideal time to identify the substantive characteristics of the board of the future, is still an underutilized tool for extensive and prospective analysis on the composition of the enterprise's central governing body. Consider in this regard that Italy ranks last in Europe for the presence of directors from other countries.

The crucial issue of **adequate information flows** to the board and between board members was mentioned. All observers recursively note critical issues related on the one hand to a certain 'distance' between the board and the organization – with the risk of a less than perfect alignment between management and organizational structure – and insufficient efforts to mitigate the inevitable information asymmetries within the board between executive and non-executive/independent directors, for which an adequate system of flows under the direction of the Chair seems the most suitable solution.

A final observation: in addition to its **management role**, the regulatory framework and international best practices emphasize the **control roles** entrusted to the board (consider the internal audit and risk committee) and the structure of the internal controls that should report to the board (Risk Management, Compliance and Internal Audit). This legislation is conceptually structured on systems that are different from the traditional system, which provides for a control body – that is ostensibly external – directly appointed by the shareholders' meeting (the board of statutory auditors). The consequences of this premise translate in practice into a system of controls that is too cumbersome and not always integrated, to which, moreover, are added controls related to the administrative responsibility of the company under Italian Legislative Decree no. 231<sup>4</sup> or institutional controls in public companies by the Court of Auditors. The adoption of integrated control systems clearly goes in the direction of system rationalization and simplification, but the basic thought remains as to whether (effective) control should be a foundational moment for business decisions and not the expenditure of energies that are not fully effective for true, concrete risk mitigation.

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4. The catalog of 'predicate' offenses for administrative liability has significantly expanded in recent years, encompassing, in addition to offenses that have always been given special attention internationally (e.g., HSE and corruption), very pervasive offenses, like tax crimes.

## 2. ONE BOARD, MANY MODELS: WHICH IS THE BEST?

In the context of the broad and dynamic legal/economic/business debate on corporate governance<sup>5</sup>, one of the queries usually raised concerns the effectiveness and efficiency of the Governing Body of joint-stock companies in the three different systems envisaged by the Italian legal system: the so-called one-tier (so-called *sistema monistico*), two-tier (so-called *sistema dualistico*), and traditional (so-called *sistema tradizionale*) systems. The Italian one-tier (also called unitary or single-tier) and two-tier systems, even if inspired by the well-known corporate governance systems used in major foreign jurisdictions and economies<sup>6</sup>, entails peculiarities and differences if compared to foreign ones (that operate in jurisdictions and markets with practices and experiences that are significantly, if not radically, different from the Italian ones).

However, this issue appears to be concrete and the related debate influences the evolution of the board of directors and of the management body, which, within the scope of its functions, must now assess the “*system of corporate governance that best serves the needs of the company and the pursuit of its strategies*”. Whether appropriate, the board shall propose to the shareholders’ meeting the choice of the most suitable corporate governance model from the three types available<sup>8</sup>.

It is worth mentioning that in the Italian corporate landscape, the traditional system (a model of corporate governance that appears not to be known outside Italy) has been in place for more than 130 years (hence the name ‘traditional’). The ‘traditional system’ was introduced into the Italian legal system – in its original French-inspired conception – by the Commercial Code of 1882, updated by the Civil Code of 1942, and renewed during the last century and systematically reinterpreted as part of the reform of the law on joint-stock companies and cooperatives (Italian Legislative Decree no. 6 of January 17, 2003 - the ‘Reform’). In addition, for the listed companies, the legislative excursus has been influenced by the relatively recent evolution of specific industry regulations (i.e., the well-known amendments to the Consolidated Law on Finance or TUF) and secondary regulations (Consob-issued regulations), statutory autonomy and codes of self-discipline<sup>9</sup> (specifically, the Corporate Governance Code issued in January 2020 and adopted by listed companies based on the “comply or explain” principle), as well as specific regulations issued by Borsa Italiana S.p.A..

On the contrary, the one- and two-tier governance types have been introduced into the Italian legal system relatively recently, on January 1, 2004, through the aforementioned Reform and with an unfortunate and inadequate legislative technique pursuant to which the relevant regulation is not expressly and organically provided but rather, for the majority of its aspects, inferred from the provisions relating to the traditional system, insofar as they are compatible. The above despite the fact that one- and two-tier governance systems are recognized as the two most widely used forms of internal corporate organizational structure in major economies, as well as they are those adopted by the EU legislature for the European Company by-laws and taken as a reference within the guidelines issued by international industry organizations.

The Italian lawmaker has thus attempted – not entirely successfully though – to emphasize the general principle of the adequacy of the internal organizational structure of the corporation, through the three different systems of administration and control, and by reshaping the relationship between the shareholders’ meeting and the governing body (giving the internal control function and its interactions with the governing body an essential and strategic role)<sup>10</sup>. In this brief paper, the governing body is to be understood only in its board composition, since the one- and two-tier systems do not provide for the possibility of adopting a single director for the administration function, and even in medium and large unlisted companies adopting the traditional system, though consented, the management function is generally assigned to a board. Moreover, specific industry regulations expressly preclude listed companies from appointing a sole director.

The legislature has sought greater organizational flexibility for corporate governance, better suited to the size, ownership structure, and needs peculiar to Italian companies, in the belief that systems closer to EU practices of modern market economies could improve the competitive ability of Italian companies in international markets<sup>11</sup>, and assuming for all models the common goal of efficient and effective administration. This allows businesses to “*respond effectively to the new and diversified needs of a now globalized market*”<sup>12</sup>.

As mentioned, even if for the boards of directors of listed joint-stock companies, the three models of administration and control are governed by the Civil Code, both industry regulations (i.e., the TUF) and codes the companies decide to adhere to have greater relevance with respect to the form of appointment and criteria for the composition of the board of directors. It is, therefore, “*a combination of statutory autonomy, legislative constraints and secondary regulation delegated to Consob*”<sup>13</sup> and in such respect, the new Code of Corporate Governance exercises a primary role. The board of directors must necessarily be a board of individuals appointed by the ordinary shareholders’ meeting according to the ‘slate method’ (taking into account the independence

5. Several definitions of corporate governance exist as it is an interdisciplinary topic that is greatly affected by the traditions and legislative, corporate and empirical experiences in each country. For an effective description of the topic of the notion of corporate governance, see BROGI, *Corporate Governance*, Egea, Milan, 2016.  
6. BLOCK-GERSTNER, *One-Tier vs. Two Tier Board Structure: A comparison Between the United States and Germany (2016). Comparative Corporate Governance and Financial regulation. 1*, available at <https://scholarship.law.upenn.edu/fisch-2016/1>.  
7. See *Rapporto 2020 Consob sulla corporate governance delle società quotate italiane 2020*, p. 4, available at [https://www.consob.it/web/area-pubblica/abs-rcg/-/asset\\_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973](https://www.consob.it/web/area-pubblica/abs-rcg/-/asset_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973).  
8. Corporate Governance Code – Borsa Italiana, January 2020, p. 5.  
9. AIDAF-Italian Family Business also issued a self-regulatory code for unlisted companies in October 2017.

10. ALVARO-D'ERAMO-GASPARRI, *Modelli di amministrazione e controllo nelle società quotate. Aspetti comparatistici e linee evolutive*, in *Quaderni giuridici Consob*, n. 7 maggio 2015, pp. 9 e ss., available at <https://www.consob.it/documents/11973/201676/qg7.pdf/ffff838f-c6c5-4d2c-a53e-f432a5bef738>.  
11. CHIAPPETTA, *Diritto Del Governo Societario*, Wolters Kluwer Italia, Milano, 2020, p. 74.  
12. ALVARO-D'ERAMO-GASPARRI, *Modelli di amministrazione e controllo nelle società quotate. Aspetti comparatistici e linee evolutive*, in *Quaderni giuridici Consob*, n. 7 maggio 2015, pp. 9 e ss., disponibile su <https://www.consob.it/documents/11973/201676/qg7.pdf/ffff838f-c6c5-4d2c-a53e-f432a5bef738>.

requirements for directors and gender distribution), as there is no possibility of adopting a sole director for listed companies (Art. 147-ter TUF).

The control function provided for in the traditional system focuses on the execution of the company contract and its organization through ex-post control by the board of statutory auditors of the decisions or conduct of the board of directors. This is a concept of control that is generally inadequate since it precludes immediate and preventive (ex-ante) control concerning the various phases of business in the context of internal board discussions assumed to be a forum for verifying and settling the interests of shareholders (and possible other stakeholders) as well as anticipating conflicts and potential abuses<sup>14</sup>. Therefore, by the introduction of adequacy of the organizational structure and internal control system's provisions, even in the Italian legal system the concept of the board of directors is evolving toward a board controlling the management function performed by the CEO<sup>15</sup>, including through the introduction of board committees and non-executive and independent directors (and minority directors for listed companies).

### MODELS OF ADMINISTRATION AND CONTROL IN THE ITALIAN LANDSCAPE

Without entering to the details of the legal framework of the systems of administration and control, find below a brief comparative survey of the relationship across the control and management functions. The purpose is to highlight the peculiar traits of each of them in order to understand whether there is or could be a model that is effectively 'better' than the others. The brief survey is based on limited empirical data, given the low uptake of one- and two-tier systems by Italian listed and unlisted companies (at the end of the year 2020, of the 228 companies listed on the MTA, only three had adopted the one-tier system and one of them the two-tier system)<sup>16</sup>.

It is useful to start with some brief considerations on the **traditional model** (Art. 2381 et seq. of the Italian Civil Code), considered not only as the main system (for seniority and numerical relevance) of corporate governance adopted in Italy, but also as the only model to have a complete regulatory framework.

This model provides two distinct corporate bodies directly appointed by the shareholders' meeting: the governing body – or board of directors – with management and administrative functions, and the board of statutory auditors, with a distinct control function by non-director auditors. Therefore, it is a system characterized by a formal and clear distinction between the management of the joint-stock company and the control over that management, which is deferred to as a separate supervisory body.

More specifically, the board of directors, in addition to its own administration and management functions, must also verify the adequacy of the company's organizational, administrative, and accounting structure and the effectiveness of the board committees. These committees are

mainly composed of independent non-executive directors with an advisory and proposal-making function (e.g., the Internal Audit and Risk Committee and the Appointments Committee, the Remuneration Committee and, when present, the Strategic Committee, and the Sustainability Committee).

One (or more) figure within the board of directors could have the role of 'first among equals'. In fact, if allowed by the by-laws or the shareholders' meeting, the board of directors may delegate its duties to one or more of its directors or to an executive committee composed of some of its members, retaining jurisdiction over the delegated powers. Thanks to this delegation of authority, it is possible to distinguish between executive and non-executive directors within the board other than the distinction between directors who do or do not meet the requirements of independence (i.e., independent directors) as established by law and industry regulations<sup>17</sup> (which for listed companies are supplemented by the provisions of the Corporate Governance Code).

Increasingly important in corporate governance, independent directors play a crucial role both in enabling executive directors to pursue the corporate interest and in benefiting the board of directors with their expertise and knowledge through a different perspective of judgment within board discussions.

Placed at the apex of corporate control systems, the board of statutory auditors has assessment, inspection, and reporting powers – including the obligation to report any administrative irregularities to Authorities in the case of listed companies – on the management and administration of the board of directors, as well as its compliance with the law and the dictates of the by-laws. Moreover, it has the power to supervise the adequacy of the company's organizational, administrative, and accounting structure and its actual operation. An external auditing firm performs the audit.

Although the most common in Italy, the traditional system has some structural flaws. The supervisory management function performed ex-post by a separate and external body such as the board of statutory auditors creates "*objective difficulties with respect to its recognizability by foreign investors and, in particular in the supervised sectors, with reference to the transposition of regulatory sources of a European, or international, nature*"<sup>18</sup>. Furthermore, the division of the organizational structure into three separate corporate bodies, as also empirically found, can significantly impact the speed of exchange of information flows between the bodies, often resulting in relatively long decision-making processes, with a decrease in the effectiveness and efficiency of information flows and corporate decisions.

The Italian **dualistic model** is inspired by 'two-tier' governance systems (Articles 2409-octies et

13. On this point see CERA, *Le società con azioni quotate nei mercati*, Zanichelli Editore, Turin, 2018, p. 99 ff.

14. ALVARO-D'ERAMO-GASPARRI, *op. cit.*

15. For a brief comparison with the US experience, see BLOCK-GERSTNER, *Op. cit.*

16. See *Rapporto 2020 sulla Corporate Governance delle società quotate italiane*, Consob, p. 26, available at [https://www.consob.it/web/area-pubblica/abs-rcg/-/asset\\_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973](https://www.consob.it/web/area-pubblica/abs-rcg/-/asset_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973).

17. RIVA-CORNO, *Il ruolo del Consiglio di Amministrazione (CdA) in Ruoli di Corporate Governance*, Egea, Milan, 2020, p. 66 ff.

18. ABRIANI, *Corporate governance e sistema monistico: linee evolutive*, in *Rivista delle Società*, n.2-3, Giuffrè, Milano, 2019, pp. 527 e ss.

seq. of the Italian Civil Code). This model, which constantly makes reference to the discipline of the traditional model, as long as compatible, provides for two distinct corporate bodies in addition to the shareholders' meeting: a supervisory board appointed by the shareholders' meeting, which appoints and subsequently controls a management board that differs in many aspects from the functions of the board of directors of the traditional system<sup>19</sup>. Specifically, this model provides that the shareholders' meeting elects a supervisory board with supervisory and, in some cases, strategic guidance functions, with the power of convening the shareholders' meeting and appointing (or dismissing, or taking legal action against) the members of the management board. The supervisory board – in which at least one of the regular members must be chosen among those enrolled with a specific register of auditors established at the Ministry of Justice – brings together functions traditionally attributed to the shareholders' meeting in the traditional model (Art. 2409-terdecies of the Italian Civil Code) with others ones peculiar to the board of statutory auditors of that system (control over management, organization of control systems and procedures, attendance at meetings of the management boards, acquisition of information, and, where envisaged, strategic policy functions). However, it is up to the management board “to perform all decision-making functions regarding corporate operations and carry-out the ordinary and extraordinary administration for the implementation of the corporate purpose, including the preparation of the draft financial statements, which, however, will be approved by the supervisory board”<sup>20</sup>, where the Chair plays a key role close to the figure of the CEO<sup>21</sup>. The board committees are composed of members of the supervisory board.

From the different statutory choices, it is possible to distinguish a ‘strong’ and a ‘weak’ dualistic model, i.e., a tri-partition could be observed at if the supervisory board has a role of pure control<sup>22</sup>.

The extensive separation of the company's shareholders from the management function is, thus, a unique feature of the dualistic model, with the peculiarity that strategic decisions – traditionally attributed to the shareholders' meeting – are in the hands of the supervisory board which also has managerial prerogatives typical of the board of directors in the traditional system.

On the contrary, and in extreme summary, the Italian **one-tier model** is inspired by foreign one-tier systems of governance (Articles 2409-sexiesdecies et seq. of the Italian Civil Code). This model is distinguished – again through a constant reference to the discipline of the traditional model to the extent compatible – for being composed of a single corporate body (obviously in addition to the shareholders' meeting, which appoints it): the board of directors, which appoints an internal Audit Committee. Thus, it is a separation by functions between (i) executive directors,

members of the board of directors (which maintains a role similar to the one provided in the traditional system), who are entrusted exclusively with the management of the company; and (ii) non-executive and independent directors who are members of the Audit Committee, whose functions are exclusively to supervise operations, the adequacy of the organizational structure and internal control and accounting (with at least one member of the aforementioned committee chosen from among those enrolled with the national register of auditors) and to liaise with those in charge of auditing the accounts (duties typical of the board of statutory auditors in the traditional model). Therefore, one-third of the directors must be both independent and non-executive directors, and in the case of listed companies, the Audit Committee must consist of no less than three directors who meet the requirements of honorability and one member must be elected by minority shareholders.

Thus, the main feature of this model is the concentration of administration and control functions in a single body. In fact, it is the board of directors that appoints an Audit Committee from among its members composed of “directors who are absolutely not involved in any executive functions (or committees) or in any management function or operation, either in the company or in companies that control it or are controlled by it”<sup>23</sup>. The main result of this is to facilitate the circulation of information, which increases in immediacy, quality, and quantity, allowing for a high degree of transparency within the company that benefits from the cognitive contribution and experience of the members of the Management Control Committee, with particular reference to strategic policy deliberations and with the additional benefit for the functioning of the board committees composed of the same independent non-executive directors. The absolute prominence of independent directors within the one-tier system thus makes it a particularly suitable model for all companies with widespread ownership, where the absence of a ‘managing shareholder’ may facilitate the use of independent directors<sup>24</sup>.

The monitoring of the legitimacy of the management is made at an early stage, instead of the subsequent (ex-post) control performed by auditors in the traditional model.

Other advantages of the one-tier system are: the extensive presence of independent and/or non-executive directors; a direct relationship between the shareholders' meeting, the board of directors, and the management function, with powers of the shareholders' meeting to scrutinize and approve the financial statements and to pass resolutions on the appointment and remuneration of directors. In addition, another advantage is the familiarity of this system of governance by EU regulatory and legislative authorities, as well as by institutional investors or in the context of multi-jurisdictional groups.

The main feature of the one-tier system is the supervisory role played by independent directors

19. VISENTINI, *L'Amministrazione della Società per Azioni* in Collana Professionale del Diritto Commerciale, Dike Giuridica Editore, Roma, 2016.

20. On this point see ABATECOLA-CAFFERATA-PANICCIA-POGGESI, *Le difficoltà del cambiamento dei sistemi di governance delle società italiane* *quotate*, p. 16 ff., available at: [https://www.researchgate.net/publication/268331846\\_Le\\_difficolta\\_del\\_cambiamento\\_dei\\_sistemi\\_di\\_governance\\_delle\\_societa\\_italiane\\_quotate?enrichId=rgreq-ad86dcd0ebcb93f4e04b0fa601606d4a-XXX&enrichSource=Y292ZXJQYWdIOzI2ODMzMTg0NjBUZoxNjQxMTQyOTkxMDUyODVAMTQxNjEzOTMwNjIxOQ%3D%3D&el=1\\_x\\_2&\\_esc=publicationCoverPdf](https://www.researchgate.net/publication/268331846_Le_difficolta_del_cambiamento_dei_sistemi_di_governance_delle_societa_italiane_quotate?enrichId=rgreq-ad86dcd0ebcb93f4e04b0fa601606d4a-XXX&enrichSource=Y292ZXJQYWdIOzI2ODMzMTg0NjBUZoxNjQxMTQyOTkxMDUyODVAMTQxNjEzOTMwNjIxOQ%3D%3D&el=1_x_2&_esc=publicationCoverPdf).

21. VISENTINI, *op. cit.*

22. MIOTTO, *Commento sub. art. 2409-octies*, in CIAN-TRABUCCHI (ed.), *Commentario Breve al Codice Civile*, XIV ed., Cedam Wolters Kluwer, Milan, 2020, p. 2893.

23. ABATECOLA-CAFFERATA-PANICCIA-POGGESI, *op. cit.*, p. 18.

24. For a brief comparison with the US experience see BLOCK-GERSTNER, *Op. cit.*

over the remaining board members, which is also the most critical factor, as belonging to the same body can prevent independent and non-executive directors' opposition to the choices of their colleagues.

An unresolved knot of the one-tier system concerns the potential conflict generated by the assignment of the management control function to a special internal committee of the board of directors composed of company directors. The consequence is that the director, on the one hand, administers by participating in operational decisions and, on the other hand, is called upon to monitor compliance with current primary and secondary regulations (in addition to any self-regulatory rules the company had adhered to)<sup>25</sup>. In fact, as it is often mentioned, the effectiveness of management control functions can be reconciled by assigning the Audit Committee tasks, which are often the responsibility of the Internal Audit and Risk Committee under the traditional system.

## CONCLUSIONS

Despite the initial assumptions, the use of alternative models of administration and control since 2004 has been very limited in Italy. Cases in which some companies adopting the one-tier and two-tier systems later decided to return to the traditional model are also common.

For example, for what concerns listed companies, based on data updated at the end of 2020, the traditional model is confirmed as the most popular, with only three companies having chosen the one-tier model and one company the two-tier model<sup>26</sup>. As to the world of unlisted joint-stock companies, the data clearly confirm the absolute prevalence of the traditional administration model<sup>27</sup>.

Less clear, however, are the reasons why the traditional system (and the board of directors - board of statutory auditors dichotomy) is still the most used form by Italian companies. Perhaps, as argued by some, *"more for cultural reasons than for genuine business convenience"*<sup>28</sup>, depending on our country's historical, institutional, and economic framework, suffering from the well-known inertia of *'path dependence'*<sup>29</sup>.

In general, however, the low uptake of alternative models of administration and control in the Italian landscape may be attributable to a number of factors. Some of them are common to both open and closed corporations; others affect purely joint-stock companies with listed securities. The first factor certainly includes a cautious attitude of operators, often bordering on 'cultural resistance', as well as a widespread knowledge gap regarding one- and two-tier models and how they work in practice (after all, foreign directors in Italian companies account for only about

6% of all members; therefore the exchange of administrative and management experience and knowledge with directors from other jurisdictions is rather rare).

On the other hand, with respect to listed companies, what seems to be the main reason for the low spread of the one- and two-tier models is that the legislative provisions contained in the Italian Civil Code, the TUF and the Corporate Governance Code relating to these systems *"do not constitute an autonomous and well-articulated body of legislation, but rather are limited to references to the traditional system"*. In fact, the lawmaker simply placed the one- and two-tier systems side by side with the traditional system, putting them all on the same level, in a competitive and alternative relationship, which ended up resulting in *"a flattening of the specificities of the two-tier and one-tier systems"*. For many scholars, such a circumstance has been misunderstood, and freedom in the choice of administration and control model – relevant element for competitive business-to-business perspective – has been perceived as an 'element of confusion', thus leading most companies (listed and unlisted) not to abandon the traditional Italian model.<sup>30</sup>

However, some legal and corporate doctrine authors and several practitioners in the field have begun to predict possible changes over the long run.

Under this view, the one-tier system could play a leading role, which is still unknown in Italy but popular across large foreign institutional investors<sup>31</sup> and the holding companies of multinational groups. As mentioned, the relevant element of the one-tier system lies in the fact that the directors of the management control committee – unlike the board of statutory auditors – are directors and participate in every decision of the company's governing body, including through the exercise of voting rights. Such a concentration of executive, non-executive, and independent directors in a single body would simplify *"that complex system of controls in large listed S.p.A.s that today leads to cross competencies, overlapping flows, and disorientation in the internal structures involved"*<sup>32</sup>. The one-tier governance model ultimately sets the stage for establishing specific relationships between the management control committee and the various corporate functions through formalizing specific information flows<sup>33</sup>.

The two-tier model responds to particular shareholder ownership's interests, fundamentally attracted by the prospect of accentuating its powers of control in the face of the potential regression of its administrative powers. Again, despite lacking significant evidence in application practice, juxtaposing the two-tier model to companies with shares listed on regulated markets comes naturally. Several also see specific advantages in adopting a two-tier model, also in closed, family-owned joint-stock companies. This model could be well suited to generational transitions. The gradual transfer of management powers to the head of the new generation

25. MARCELLO-SCOTTON, *Il sistema monistico e il nodo irrisolto dei conflitti d'interesse*, in *Il Sole 24 Ore*, April 14, 2021.

26. See *Rapporto 2020 sulla Corporate Governance delle società quotate italiane*, Consob, p. 24 ff., available at [https://www.consob.it/web/area-pubblica/abs-rcg/-/asset\\_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973](https://www.consob.it/web/area-pubblica/abs-rcg/-/asset_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973).

27. ALVARO-D'ERAMO-GASPARRI, *op. cit.*, pp. 20 e ss.

28. CERA, *Le società con azioni quotate*, *op. cit.*, pp. 110 e ss.

29. For more see ROE, *Political Determinants of Corporate Governance*, Oxford University Press, Oxford, 2003.

30. ALVARO-D'ERAMO-GASPARRI, *op. cit.*, pp. 22 e ss.

31. TOMBARI, *Il sistema monistico è una garanzia di efficienza e controllo*, in *Il Sole 24 Ore*, April 9, 2021.

32. CERA, *Il curioso caso del sistema monistico: negletto, ma efficace*, in *Il Sole 24 Ore*, April 3, 2021.

33. ABRIANI, *op. cit.*, p. 534.

of the management board is mirrored by the *“constant retreat of the previous generation in the supervisory roles of the relevant board... which still allows the possibility of exercising substantive direction as well as formal business activity, resulting in the safeguarding and protection of the invested capital”*<sup>34</sup>. The large ‘family’ shareholder-based company might be a possible habitat for the two-tier system in times of low relational fluidity between ownership and management. In the latter context, the governing body can encourage equilibrium between the different family branches. The supervisory board could play a key role, which could reconcile management differences among family members.

Moreover, based on limited Italian practice, the two-tier system would seem mainly functional in situations of comparison and reshaping of ownership structures following merger and/or incorporation operations. Under such circumstances, a share of ownership could find its place within the supervisory board. At the same time, entrepreneurial management could easily be referred to as a management board composed of individuals outside or not influenced by the corporate structure. However, it can be pointed out that this system has presented, and presents, numerous weaknesses in the ordinary course of management and administration, with particular reference to the information flows between the supervisory committee and its potential strategic supervision functions and the management board, as well as to the internal control functions, which is noted in numerous corporate governance reports of some Italian listed companies.

Thus, pulling together the threads of what has been said so far, while the traditional administration model remains the most popular, there is a re-evaluation of so-called alternative models both in the theory and recent practice of a few companies, with particular regard to the one-tier system.

However, it continues not to be easy to provide an answer to the first question in this paper. The clear preeminence of the traditional model might argue in favor of its designation as a litmus test across the various governance systems; however, it would be simplistic to de-qualify the other models simply because they are still not widespread.

Each of the administration and control systems examined has positive and negative aspects. There is no expressed and motivated market preference for one of the three systems regardless of the almost absolute use of the traditional system, which is more the child of the ‘path dependence’ of the Italian system than of thoughtful law choice and even more of an economic and industrial environment that does not reward changes in the governance model.

In fact, the ‘best’ governance model is likely the one that best respects the characteristics and ownership structure of the relevant company, resulting in a business concept and culture

that is more functional in pursuing the interests of the entire shareholder base (minority and majority), taking into account the interests of the relevant company stakeholders. Finally, the adoption of a good corporate governance system in itself could contribute to but not ensure efficient, effective, and law-abiding administration, which will always depend on the integrity, ability, professionalism, and propriety of the members of the various corporate bodies, board committees, and management of the company.

In any case, as long as the reference framework of the one-tier and dual-tier systems remains in its current state of incompleteness and uncertainty, there seems to be a long path before a significant number of Italian companies adopt the models.

From many points of view (theory, practitioners and investors), there are increasing calls for the Italian lawmaker to revisit the regulation of the one-tier, and two-tier systems in order to eliminate the unfortunate technique of reference. The aim is to produce an autonomous, complete regulation that makes possible in practice to adopt these systems, or rather the system most appropriate for each company’s characteristics, ownership structure, and stakeholders.

34. For an overview of the two-tiered administration and control system, see DI TERLIZZI-DI VIETO, op. cit., p. 175 ff.

### 3. A COMPARISON BETWEEN THE MADE IN THE USA BOARD AND THE MADE IN ITALY BOARD

This chapter takes a comparative look at some of the differences between the structure and operation of boards of directors in Italy and the US, particularly in relation to aspects that are in the spotlight of investors and policymakers these days.

As in the first chapter, several areas of interest were analyzed, divided into the following stages:

1. The Initiative Stage, on board **composition** and **operation** in the United States and Italy, with emphasis on the debate around board composition and the structure of governing bodies.
2. The Investigation and Deliberation Stages, in which the focus is placed on **environmental and social sustainability** issues and how these factors are taken into consideration within board's decisions.
3. The Implementation Phase, where the focus, also based on the experience of the past year, is placed on the role that the board plays in the context of the company's response to high-impact events (be it reputational, industrial, social or environmental events), attempting to outline a framework of action proposals functional to the fulfillment of the board's role both in the **resolution of the crisis** and in the driving role of the **preparation of internal protocols and procedures**, with a view to the **prevention** or otherwise **efficient management** of a subsequent crisis.

#### INITIATIVE STAGE

As part of the Initiative stage, it is relevant to address issues related to the composition of the board, with particular reference to the diversity of board members and the board's operation, by conducting an analysis of the structural differences between the one-tier model, widespread in the United States and generally in the Anglo-Saxon world, and the Italian system.

With reference to the first issue, it has to be noted that diversity can take a **variety of forms** within the board. The regulations on **gender** difference adopted in Italy and other European countries are well known, but diversity can have multiple meanings, such as for example the differences among board members with respect to **other factors**, including **age, ethnicity, or sexual orientation**.

In the US experience a **mixed composition** is one of the factors contributing ensuring that the board as a whole can outline an **innovative, long-term** corporate **strategy** that is responsive to the various needs of the stakeholders as well as shareholders.<sup>35</sup>

Indeed, a composition aimed at accommodating a greater number of 'differences' makes it pos-

sible to reduce the risk of groupthink, a felicitous American expression that sums up the concept of the risk for a company to act on the basis of a board belief that (as directors share the same cultural and social background) does not take into account all the variables at play, and where consensus is based on common experiences and consequently on a lack of true internal debate<sup>36</sup>.

While legislation in Italy regarding publicly traded and publicly controlled companies has made it possible to achieve encouraging results with respect to gender diversity,<sup>37</sup> the same cannot be said for the representation of other minorities on the board.<sup>38</sup>

A starting point, therefore, must be an effort to appoint boards with members that reflect the social base of the company's stakeholders. In this regard, it is appropriate to consider as candidates for board directors people:

1. **Of different ages** who can improve decision making and know the needs of customers and other stakeholders.
2. From (ethnic, cultural or social) **minorities** spread throughout society, to stimulate debate within the board and consider different points of view.

In addition to a board composition that reflects the diversity of the company, another element to be taken into account when selecting directors concerns **skill diversity**. In the United States, while boards continue to be composed of directors with financial expertise, there is a greater focus on different areas that enable companies to keep up with the challenges posed by the market. Specifically, the areas toward which the board's skills are directed include digital transformation, sustainability and technology. The trend toward qualified directors in diversified areas, combining managerial qualities with knowledge in more innovative fields, is likely to continue, given also the role and activism of investors who are increasingly attentive to the qualitative and quantitative composition of boards of directors and the governance of companies.<sup>39</sup>

35. See NYSE: Corporate Governance Guide, especially p. 72 ff, available at <https://www.nyse.com/cgguide>.

36. *Diversifying the board* – a step towards better governance, Acca Global, available at <https://www.accaglobal.com>. Furthermore, it is worth noting that in August 2020 the SEC amended Item 101 of the S-K Regulation, which governs the reporting requirements that listed companies must comply with. As a result of this change, companies' annual disclosures are now required to also report the number of employees, as well as the actions and/or goals set by them with regard to the so-called human capital. One of the most interesting results to look at concerns the factual data that have emerged from the implementation of the standard: companies have begun to include information related to staff diversity in their annual reports. On this topic, see SIEGEL, *The SEC's New Human Capital Disclosures: Year 1*, available at <https://www.financialexecutives.org/FEI-Daily/May-2021/The-SEC%E2%80%99s-New-Human-Capital-Disclosures-Year-1.aspx>.

37. Pursuant to Articles 147-ter and 148 of the TUF, corporate by-laws must stipulate that the mechanisms for appointing directors and auditors reserve at least two-fifths of the board members and standing statutory auditors for the less represented gender.

38. According to Consob, *Rapporto 2020 sulla Corporate Governance delle società quotate italiane*, available at [https://www.consob.it/web/area-pubblica/abs-rcg/-/asset\\_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973](https://www.consob.it/web/area-pubblica/abs-rcg/-/asset_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2020/11973), only 6% of the directors of listed companies have foreign origins.

39. On this topic see TONELLO, *Corporate Board Practices in the Russell 3000 and S&P 500: 2020 Edition*, available at <https://conferenceboard.esgauge.org/boardpractices>; MISHRA, *U.S. Board Diversity Trends in 2019*, Harvard Law School Forum on Corporate Governance, June 18, 2019, available at <https://corpgov.law.harvard.edu/2019/06/18/u-s-board-diversity-trends-in-2019/>.

The issue of diversity within the board is also addressed by Italian self-regulatory sources. The Corporate Governance Code dictates some (admittedly still limited) provisions both with respect to gender diversity and to other forms of diversity. In the latter respect, Principle VII states that “The company applies diversity criteria, including gender ones, to the composition of the board of directors, ensuring the primary objective of adequate competence and professionalism of its members.” Recommendation no. 8 states that it is the company's task to define diversity criteria for the composition of the boards of directors and statutory auditors. Finally, in accordance with Recommendation no. 23, the outgoing board of directors “sets forth guidelines on board composition deemed optimal before its renewal.”<sup>40</sup> However, for the time being there is no evidence of a particularly incisive change in the composition of our boards, where the most innovative skills still seem to be in short supply. An analysis of the data on the composition of the boards of Italian listed companies confirms this assumption: the majority of directors have managerial experience, while only 2% have education and expertise that pertain to different backgrounds, such as non-profit, technology or sports.<sup>41</sup>

Regarding the operation of the board of directors, the one-tier model represents **the most common governance system** in the international arena. The salient feature of this system lies in the **coexistence** of management and control within the same governing body: this results in greater efficiency than other corporate governance systems, such as the two-tier and traditional systems, which require a division of responsibilities among several bodies.

Given the newness of the one-tier model in the Italian legislative landscape, it seems appropriate to analyze its functioning in the US system, which influenced its introduction.

In the United States, the board is endowed with very broad functions, some of which in Italy are the responsibility of the shareholders' meeting and the control body. For example, it is the board that is responsible for approving the financial statements and the distribution of profits as well as for the management and control of the business.<sup>42</sup> Moreover, one of the tasks of the US board of directors is to prevent hostile takeovers at inappropriate prices (by means of the adoption of poison pills). The board also retains a more pervasive role compared to the Italian management body in the area of bringing liability actions against one or more directors (through the filter of the so-called demand requirement imposed on shareholders).<sup>43</sup>

However, the management of the company in the US model is not entrusted to the entire Board: it is the **management**, consisting of executives and executive directors,<sup>44</sup> that is in charge of

running the company, while the board has a supervisory role. And in fact, one of the functions of the board elaborated by North American scholars is that of so-called monitoring: more correctly, the paradigm of the legal model, accepted by the laws of the individual federal states, under which the board is recognized as a body fully inserted in the company management, contrasts with that of the board entrusted with supervisory functions (and, in the case of pathological social conduct, of intervention) on the work of the management.<sup>45</sup>

Furthermore, the **monitoring** function is joined in American listed companies by the additional, more pervasive function of the **audit committee**, thus constituting a third function within the board. Note that the establishment of the latter committee, first provided for only by way of self-regulation, found express legislative regulation with the Sarbanes-Oxley Act of 2002 for public companies.<sup>46</sup>

As a matter of self-regulation, the **listing standards** of US stock exchanges require the appointment of an audit committee, that the majority of directors meet independence requirements, and that the company make disclosures to the market about these requirements.<sup>47</sup>

In Italy, the introduction of the one-tier governance system along with the German-derived two-tier model as a result of the 2003 Reform brought a **new** element to the legislative landscape, despite their limited use in practice.<sup>48</sup>

In the Italian one-tier system, the management and control functions are exercised by the Board of Directors and the **Management Control Committee**, which is constituted within the Board of Directors. Precisely because of the fact that the control function is exercised within the board, according to the 2003 Reform Report, this model favors “information flows between the management body and the body in charge of control, achieving time and cost savings and a high degree of transparency between the management and control bodies.”

40. Note that in the United States it is the board itself that nominates candidates for directors. In this regard, there is a practice among some large Italian issuers of including a provision in the by-laws allowing the management body to submit its own slate of candidates when electing new members. In this regard, see the provision in Article 9.2 of the TIM S.p.A. by-laws, available at <https://www.gruppotim.it/it/gruppo/governance/strumenti-governance/statuto-sociale.html>.

41. *Spencer Stuart Board Index*, Italia 2020, available at <https://www.spencerstuart.com/research-and-insight/italy-board-index>, the source of the data reproduced here.

42. GHEZZI, *Commento sub art. 2409-Sexiesdecies*, in GHEZZI (ed.), *Sistemi alternative di amministrazione e controllo*, in Marchetti-BIANCHI-GHEZZI-NOTARI (ed.) *Commentario alla riforma delle società*, Egea, Milan, 2005, p. 195 ff; BERTOLOTTI, *Commento sub art. 2409-sexiesdecies*, in BERTOLOTTI (ed.), *Sistema dualistico. Sistema monistico*, in SCIALOJA-BRANCA-GALGANO (ed.), *Commentario del Codice Civile e codici collegati*, Zanichelli, Milan, 2020, p. 269-270.

43. Pursuant to rule 23.1 of the Federal Rules of Civil Procedure, the shareholder intending to propose a so-called derivative action on behalf of the company must make a request to the board. Therefore, a conflict of interest at least potentially arises when such an action is brought against one or more directors. To overcome this drawback, the practice has developed of entrusting the task of screening the shareholder's claim to a special litigation committee, which is called upon to assess the company's interest in bringing the liability action. However, note that a number of rulings by Delaware courts have intervened on this point, which, based on the so-called futility exemption, have established the exemption from the demand requirement in cases where the conduct of the directors themselves is the subject of dispute. On this topic see WILDER, *The Demand Requirement and the Business Judgment Rule: Synergistic Procedural Obstacles to Shareholder Derivative Suits*, in Pace L. Rev. 5:633, 1985, available at <https://digitalcommons.pace.edu/plr/vol5/iss3/5>.

44. GHEZZI, op. cit., p. 197; BERTOLOTTI, *ibid*.

45. EISENBERG, *The structure of the corporation: a legal analysis*, Boston, Little, Brown and Co., 1976, p. 164 ff; BAINBRIDGE, *Corporate law*, Foundation Press, New York, 2009, p. 89 ff.

46. Following the enactment of the Sarbanes-Oxley Act, the provision in Rule 10A-3 of the Securities Exchange Act was introduced. The Securities and Exchange Commission (SEC) report is available at <https://www.sec.gov/rules/final/33-8220.htm>.

47. See the NYSE Listed Company Manual and NASDAQ Listing Rules. Note also that in the United States, boards are predominantly composed of independent directors and the Chief Executive Officer. On this topic, see GIOVE-TREUHOOLD, *Corporate governance and directors' duties in the United States: overview*, available at [https://content.next.westlaw.com/9-502-3346?\\_lrTS=20201015103348319&transitionType=Default&contextData=\(sc.Default\)&firstPage=true](https://content.next.westlaw.com/9-502-3346?_lrTS=20201015103348319&transitionType=Default&contextData=(sc.Default)&firstPage=true).

48. The one-tier model has been adopted by four listed companies. On this point see TOMBARI, *Il sistema monistico è una garanzia di efficienza e controllo*, in *Il Sole24Ore*, April 9, 2021, available at <https://www.ilsole24ore.com/art/il-sistema-monistico-e-garanzia-efficienza-e-controllo-ADj4TEWB>.

Regarding the composition of the board, the law requires that at least one-third of the directors meet the independence requirements established for statutory auditors in Article 2399, paragraph 1, of the Italian Civil Code, in addition to any additional requirements set forth in the by-laws. This requirement, which is not provided for the traditional and two-tier models<sup>49</sup>, is due precisely to the need to establish the management control committee, consisting only of independent directors. With regard to the latter, in private companies the composition and number of members is determined by the board of directors, while in public companies the number of members cannot be less than three.

An element of criticism of the one-tier 'Italian-style' model can be found in the assignment of prerogatives to the management control committee: in a system where the management body is subject to more stringent limits than in the United States (think of the role of shareholders and the powers vested in the shareholders' meeting in Italy), the control committee has been endowed with **functions substantially coinciding** with those of the board of statutory auditors (so much so that at least one of its members must be a registered statutory auditor). This limitation of powers, also due in part to the **continuous cross-reference** in the legislation to the rules governing the operation, composition, and characteristics of the control body in the traditional system,<sup>50</sup> does not vest the members of the control committee with powers similar to a US-style audit committee. Indeed, audit committee members, in their capacity as directors, in addition to a duty of oversight over the work of the management, retain a set of managerial prerogatives necessary to carry out the company's business, concurrent with the executive directors, to be exercised when the latter's performance 'falls short of expectations.'<sup>51</sup>

In conclusion, the real difference between the original American model and the system imported into the Italian legal system concerns the **role** of the audit committee. Based on cultural heritage linked to the traditional model, there is a tendency to see an **opposition** between management and control, while the American experience teaches that the audit committee does not have an *ex-post* verification function with respect to the actions of the directors, but rather the **task of facilitating** the work of the board by monitoring the actions of the executive directors<sup>52</sup>, while maintaining management functions. Concurrently serving as directors thus enables the members of the audit committee to supervise the management more closely, and where necessary **intervene in the management** of the company.

## INVESTIGATION AND DELIBERATION STAGES

As mentioned, a differentiated composition of the board allows the company to take into account innovative and socially impactful issues into its decision-making process. Among them,

49. In the two-tier system, however, there is a special requirement for independence (applicable to all members) applicable to the company itself, its subsidiaries, and the companies under common control.

50. Note that the 2003 Reform Report states that "[t]he one-tier system provides for an administration model that is essentially the same as the traditional version: the main differences are the impossibility of entrusting management to a single director and the elimination of the board of statutory auditors."

51. GHEZZI, *op. cit.*, p. 198.

52. LORENZONI, *Il comitato per il controllo sulla gestione nel monistico: alcune riflessioni comparatistiche*, in *Giur. comm.*, 2006, I, p. 66 ff.

**ESG factors** have seen growing and consistent interest from institutional investors, non-profits, and other stakeholders in recent years. In such a vibrant environment, companies are called upon to take these issues into consideration when developing and implementing their strategy.

The second stage of the work, Investigation and Deliberation, thus aims at analyzing how ESG issues find their way into strategic board discussions in the United States, as an example for the Italian system to look to.

While there is a notion of corporate interest as an interest in the creation of shareholder value, corporate governance is affected by increasingly insistent pushes from institutional investors, as well as national and supranational legislators, aimed at a **long-term view** and the **integration of ESG factors** in the business. In this renewed context, directors consider stakeholder interests and sustainability risks in decision-making, including with a view to creating value for companies and shareholders.

The underlying belief is that while the identification of best practices related to ESG reporting taxonomy and mechanisms and the preparation of shared ratings are still evolving, boards should place considerations of the impacts that strategic choices may have with respect to environmental and social factors at the center of their actions.

It is now worth distinguishing between the ways in which these factors are taken into account in the United States and Europe.

The weight held by **institutional investors** has historically been greater in the US, where equity ownership of listed companies is usually widespread. It should come as no surprise, then, that the **activism** of such investors plays a key role in shaping the board's strategies.

In 2020, by means of its annual 'Letter to CEOs,' BlackRock sought to emphasize the need to focus attention on the profound change that the financial sector is going through, where the climate factor has become determinant in developing long-term strategies.<sup>53</sup>

Given the lack of a unified regime regarding the definition and disclosure of investments and information related to environmental issues, some financial giants have identified a number of soft law tools, including the principles of the Sustainability Accounting Standards Board (SASB) and the recommendations of the Task Force on Climate-related Financial Disclosure (TCFD), as indicators on the basis of which to guide social action.<sup>54</sup>

Within the European Union, where equity ownership is more concentrated and despite the increasingly pervasive engagement of institutional investors, it is **supranational institutions** that have a prominent role in the field of ESG issues. In March 2018, the European Commission published its Sustainable Finance Action Plan, which calls for the creation of a unified sustainable

53. LARRY FINK, *Letter to Ceos*, disponibile su <https://www.blackrock.com/corporate/investor-relations/2020-larry-fink-ceo-letter>.

activity ranking system and the promotion of sustainable investments and a corporate governance paradigm geared toward a long-term vision.

Further, Regulation (EU) 2019/2088 on sustainability disclosure of the financial services industry requires, in Article 3, market participants to publish information about policies on the integration of sustainability risks implemented in investment decision-making processes.

Moreover, Article 3-octies, paragraph 1, letter a) of Directive 2017/828 (SHRD II) requires institutional investors to publish an engagement policy describing how their investee companies are monitored on relevant issues, among which are social and environmental impacts. Investor activism, therefore, becomes a means and expression of control over the managerial decisions taken by management.

Finally, Directive 2013/34/EU, as amended by Directive 2014/95/EU (NFRD), requires large companies that are public interest entities to include in the management report “a non-financial statement containing information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, **environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters...**”<sup>58</sup>

Given the difference in the US and European experience, it is important to clarify that an environment driven by **market** insights has the characteristic of **adapting better and faster** to the changing needs of shareholders and stakeholders. The role of regulating authorities should be reserved for defining the legislative framework within which companies, including through soft law sources, can operate with regard to requirements related to ESG factors, including disclosure. This would allow for the **constant updating** of adopted measures, as well as the

54. *Climate Risk Governance: What Vanguard Expects of Companies and Their Boards*, Vanguard Investment Stewardship Insights, available at [https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/ISCLRG\\_062020.pdf](https://about.vanguard.com/investment-stewardship/perspectives-and-commentary/ISCLRG_062020.pdf); on this topic see CLARKIN-SAWYER-LEVIN, *The Rise of Standardized ESG Disclosure Frameworks in the United States*, Harvard Law School Forum on Corporate Governance, June 22, 2020, available at <https://corpgov.law.harvard.edu/2020/06/22/the-rise-of-standardized-esg-disclosure-frameworks-in-the-united-states/>.

55. At the national level, note that Article 1833 of the French Civil Code, as amended by the 2019 *Loi Pacte*, requires that when managing the company directors have to pursue the company's interest while at the same time taking into account the social and environmental implications of the company's business. Section 172 of the English Companies Act requires directors to have regard in their management to the company's impact on the environment and the community. Furthermore, in its Recommendations for 2021, the Corporate Governance Committee of Borsa Italiana invited member companies to consider the integration of the sustainability of the business in the definition of strategies and remuneration policy, also based on a relevance analysis of the factors that may affect the generation of value in the long term. On this topic, note that some listed Italian companies have included sustainability as an integral element of the corporate purpose or directors' duties. In this regard, see the by-laws of Snam S.p.A. (Article 2), available at <https://www.snam.it/it/etica-governance/corporate-governance/statuto/> and of SeSa S.p.A. (Article 20), available at <https://www.sesa.it/governance/statuto/>. Finally, there is an increasingly insistent push for legislative change to include social and environmental aspects within the scope of directors' fiduciary duties. In this sense, see *Doveri degli amministratori e sostenibilità*, Assonime, Note 6/21, especially p. 26-30, available at [http://www.assonime.it/attivita-editoriale/studi/Pagine/Note-e-Studi-6\\_2021.aspx](http://www.assonime.it/attivita-editoriale/studi/Pagine/Note-e-Studi-6_2021.aspx).

56. See also Article 3, paragraph 3 of Italian Legislative Decree no. 49/2019, implementing Directive 2017/828, which introduced paragraph 3-bis of Article 123-ter of the TUF, according to which “[t]he remuneration policy shall contribute to corporate strategy, the pursuit of the company's long-term interests and sustainability, and illustrate how it makes this contribution...”

57. As defined by Article 2(1) of Directive 2013/34/EU, and among others including listed companies, credit institutions, and insurance companies.

**creation of self-regulatory tools of a transnational nature** that are increasingly shared and uniform across different markets, **averting the risk of obsolescence** inherent by definition in the hard law approach.

Finally, it is important to point out that the expression ‘**take into consideration**’ often used with regard to ESG issues<sup>59</sup> refers to conduct aimed at determining **compliance** of business operations (and management decisions) with guidelines related to environmental and social factors. In this context, it is up to the board of directors to assess whether risks and opportunities related to these factors are included in the company's long-term strategy, whether and which procedures and controls are in place to ensure accurate **disclosure** of the impact of management decisions, which function is best suited to ensure that the company's culture also incorporates environmental and social issues, and whether the company's ESG strategy is aligned with the needs of shareholders and stakeholders.<sup>60</sup>

### IMPLEMENTATION STAGE

The Implementation stage focuses on the board's ability to **respond appropriately to unexpected events** that may have a negative impact on the company (**crisis management**).

Uncertainty in every system has resulted in the **multiplication of risks** that all companies are exposed to. In addition to ‘classic’ risks, such as financial and capital risks, a company's concerns must turn to a multitude of factors, such as cyber security and protection against cyber-attacks, reputational risk, business continuity (particularly topical as the pandemic continues), natural disasters, regulatory compliance, and protection of trade secrets.<sup>61</sup>

There is no denying that society's ability to respond to sudden high-impact negative events is contingent on the preparations made to cope with the state of crisis. Factors that have proven necessary for crisis management include the creation of **a crisis management-oriented culture** and, from a forward-looking perspective, the integration of a strategic approach within the company's management choices aimed at identifying techniques to be used in the event of the occurrence of unexpected events.

With regard to building a **crisis-oriented** culture, experience shows that an environment where the interests of workers and the company are substantially aligned allows for greater integration and prompts the former to come forward to report potential risks.<sup>62</sup>

58. On April 21, 2021 the European Commission published a proposal for a legislative amendment to broaden the scope of non-financial disclosure provisions. In this regard, see DOLMANS-BOURGUIGNON-CIBRARIO ASSERETO, *The Corporate Sustainability Reporting Directive: From ‘Non-Financial’ to ‘Sustainability’ Reporting*, Cleary Gottlieb Steen & Hamilton LLP, May 2021, available at <https://www.clearygottlieb.com/news-and-insights/publication-listing/the-corporate-sustainability-reporting-directive>.

59. Also by French and English legislators, see note 57 above.

60. See LOOP-DE NICOLA-BERLIN, *How Does the Board Oversee ESG?*, Harvard Law School Forum on Corporate Governance, December 21, 2020, available at <https://corpgov.law.harvard.edu/2020/12/21/how-does-the-board-oversee-esg/>.

61. FINOTTO, *I dieci rischi che corrono le imprese. E cosa fanno per proteggersi*, in *Il Sole24Ore*, November 6, 2018, available at <https://www.ilssole24ore.com/art/i-dieci-rischi-che-corrono-imprese-e-cosa-fanno-proteggersi-AEB6D4bG>.

The business strategy should include procedures for **planning** and **responding** to critical events. The ability of companies to respond to the occurrence of such events depends on having guidelines and protocols in place to identify and manage the risk and/or damaging event that gave rise to the crisis.

A key role in crisis management is played by **information flows** between corporate principals and corporate bodies: an adequate communication allows all relevant structures to be aware of the state of crisis and enables efficient and rapid action by the company. Moreover, the establishment of a risk management system and its monitoring should be integrated within the company's governance procedures. As the general management body, the **board** should be the body designated to receive all information on the state of the crisis<sup>63</sup> and stand as a body **with functions of support and supervision** of the activities put in place by the corporate structures.

An additional element of crisis prevention concerns the constant updating of disaster recovery and **business continuity** plans that enable the allocation of personnel and resources when a crisis emerges. When one considers the impact of the pandemic that companies had to deal with, for example, one can see how the establishment of protocols to regulate teleworking appears to be necessary as part of a business continuity plan, given the uncertainty generated by the spread of the Sars-CoV-2 virus and its consequences in the near term.

Moreover, an indispensable piece of crisis management is the **updating** of existing procedures. This cannot be achieved without an adequate risk mapping system based on internal checklists. The results of these checks should then be instrumental in revising existing protocols.

More generally, from a practical point of view the most virtuous behaviors that characterize efficient crisis management concern the company's ability to respond strategically, through the analysis of the critical situation, the assessment of the priority elements to be addressed, and the precise identification of the roles of the parties tasked with resolving the crisis; the involvement of the legal and risk management functions in both the pre-crisis and crisis phases; the protection and preservation of company documents and materials (especially in the case of data breaches); the maintenance of a constant flow of information within the company on the one hand, and an adequate system of communication with external parties such as authorities, media, and stakeholders on the other; the proactive nature of the company's reaction (think of the conversion of company facilities during the pandemic); and finally, an analysis of the reasons that led the company to face a state of crisis, with a view to updating the company's internal procedures accordingly.<sup>64</sup>

## CONCLUSIONS

The picture drawn with this review leads to some final brief considerations.

1. In terms of efficiency and speed in the management and supervision of companies, the **one-tier system** represents the preferable model because of the **coexistence within the board** of all the components that instead are divided among several bodies in the traditional model.
2. The **composition** of the boards of directors needs to be rethought with a view to achieving a fair **balance** with respect to:
  - The **diversity** of its members, so as to enable the company to interpret the needs of both the social base of stakeholders and shareholders, with specific regard to small shareholders. The skills of directors, **supplementing typically managerial** qualities with an array of **innovative skills** that will ensure a true renewal of the company's actions.
3. Whether due to the activism of large investors or new regulations, **boards of directors must increasingly take into account the impact** that management choices can have, with specific reference to **environmental and social factors**.
4. When a crisis emerges, the **function of the board of directors** must on the one hand be to coordinate the company's response, and on the other to **supervise** the work of the various corporate functions. Constant monitoring must be supported by an **adequate internal information flow** reporting all developments of the crisis to the board. In other words, the governing body should be regarded as the linchpin around which corporate functions act to reach a solution to the crisis.

62. BAMBERGER-KENNEDY-PARK, *Crisis Management in Unprecedented Times, in Selected Issues for Boards of Directors in 2021*, Cleary Gottlieb Steen & Hamilton LLP, January 2021, available at <https://www.clearygottlieb.com/news-and-insights/publication-listing/selected-issues-for-boards-of-directors-in-2021>.

63. KLEMASH-SMITH-LEE, *The Board's Role in Confronting Crisis*, Harvard Law School Forum on Corporate Governance, October 7, 2018, available at <https://corpgov.law.harvard.edu/2018/10/07/the-boards-role-in-confronting-crisis>.

64. On this topic see KALVAR-MYSORE, *Are you prepared for a corporate crisis?* in *McKinsey Quarterly 2017 Number 2*, available at <https://www.mckinsey.com/quarterly/the-magazine/2017-issue-2-mckinsey-quarterly>.

## 4. THE NEW NORMAL AND THE GLOBAL CONTEXT: THE BOARD 2.0

The Covid-19 pandemic had and continues to have a major impact on business performance and operations globally, as sudden as it is persistent.

Companies have been shocked by the health emergency and the subsequent countermeasures taken by governments. Most companies have experienced a negative shock related to business disruptions, altered supply and demand in their target market, restricted public access and also, internally, the health of their workforce. Such have been the companies operating, for example, in the tourism sector, aviation sector and fashion luxury. Conversely, other companies have experienced a positive shock as a result of the significant opportunities created by the crisis in their particular industry, the emergence of a new 'working-from-home economy' and consequently the pressure of managing unexpected growth. Examples of such companies include the digital, pharmaceutical-medical and online distribution sectors.

In both cases, however, a strong reaction of the body entrusted with the management of the enterprise, namely the board of directors, has been required.

The Covid-19 pandemic – which has impacted every country in the world – is triggering on a global scale an evolution in the role, composition and operating methods of the board of directors. This evolution is taking place in two stages:

- an ongoing change resulting from the immediate needs related to emergency management, in terms of securing business operations, financial performance and internal organizational structure;
- a future change to adapt to the post-pandemic reality, as that experience will definitely crystallize with changes in the market, business model and corporate organizational structures.

First it is worth noting that many of the changes that are underway and will be undergone by the board of directors can be traced back to trends that already existed but, until recently, were being implemented at a slower pace, such as social and environmental policies. The pandemic has been an accelerator of such instances because it has made them essential to better operations, capable of interpreting the new social and economic reality.

The following paragraphs will examine more in detail what transformations the board of directors of Italian companies is likely to undergo as a result of the evolutions of the business model and strategic planning due to the Covid-19 crisis, having regard both to the composition and operation of the board as well as to communications with shareholders and other stakeholders. Finally, the last paragraph will focus on the consequences related to non-adaptation to the ongoing evolutionary thrusts.

### ROLE OF THE BOARD 2.0 IN THE CONTEXT OF BUSINESS MODEL EVOLUTION AND STRATEGIC PLANNING

During the emergency, boards have ceased to prioritize long-term strategic planning being mainly absorbed in the adoption and implementation of crisis containment measures in the short term.

The above phase is forcing boards to rethink and change several aspects of their business model very quickly. Indeed, boards must ensure and will need to ensure that the organization always has a high degree of responsiveness and resilience to the occurrence of exceptional events. Good governance will require that in the event of severe discontinuity scenarios there should be mechanisms in place that allow for flexibility within a reasonably short period of time aimed at reorganizing the processes necessary to react promptly to changing circumstances. One can imagine, then, that in the best corporate governance systems Directors 2.0 will make sure to adopt effective crisis management plans on a permanent basis. For example, establishing dedicated crisis units, setting up dedicated budgets, procedures for timely communication both externally and internally. For this purpose, a streamlined structure that a management must have to be able to make decisions quickly, including through an effective and efficient system of delegations and powers, may be relevant. The system of delegations and powers will have to be rethought where it does not provide sufficient autonomous decision-making centers with power to intervene in emergencies without having to wait for the central decisions of the board, but with consequent reporting obligations, to ensure proper supervision and harmonious management of overall business operations.

Furthermore, the Board 2.0, which plays the role of guiding and assessing the adequacy of the internal control and risk management system, will need to focus on strengthening risk management systems (adapted to the size and complexity of each company) in order for these systems to be able to provide the correct view of the effectiveness of internal risk management, both overall and in detail. The pandemic-induced crisis has highlighted the need to better oversee risk management activities and systems, with empowerment not only of the technicians responsible for internal audits and controls but primarily of top management. In addition, with reference to risk hierarchy, we have witnessed the emergence of risks that, until recently, had often been overlooked. Indeed, many companies have realized that for some risks the potential impact had not been properly identified and adequately measured and managed, for example with respect to risks of third-party relationships (the risk of supplier and customer concentration, which also emerged with the loss of many suppliers and customers as a result of the pandemic), risks related to occupational accidents, IT risks dependent on the increased use of technology, and product liability risk.<sup>65</sup> Reorganizing risk management systems to increase their adequacy becomes a very important factor in enabling companies to have more resilient organizations.

Also in correlation with the purpose of emergency management, the Board 2.0 must increase

its support of management by intensifying opportunities for dialog and oversight, including for example by frequently inviting management to report on the status of business at board meetings or to send pre-board-meeting reports. For this reason, too, it can be expected in general terms that in the future board members will be required to make a greater commitment at the board level with respect to the frequency of meetings, where the monitoring of the management of exceptional events and risks can only take place through frequent discussions between those with ultimate managerial responsibility (and thus cannot be limited to sporadic meetings as is the practice in many Italian companies) and the management that deals with operations.

In recent times the majority of companies have simply focused on short-lived interventions, extraordinary measures aimed more at overcoming the emergency of the moment rather than laying the foundation for strategic growth. However, boards will soon have to return to long-term goals, and this is because the purpose of building value rather than 'preserving' it will become central again.

With regard to strategic planning, boards of directors now and in the near future cannot fail to take into account the fact that the economic, social and political reality has undergone a radical transformation and therefore that corporate priorities must be changed. Indeed, it is not possible to ignore the fact that we are witnessing a permanent mutation of, for example, work patterns, consumer and customer preferences as well as a centrality of environmentalist demands (trends that already existed before but were further underscored by the pandemic).

The Board 2.0 will increasingly need to focus strategic planning and the corporate mission on digitization, teleworking and sustainability (ESG policies), directions that are already the priorities of many companies and investors globally.

Digitization, which is aimed at automating activities and procedures and facilitating communication and information exchanges, can be a significant benefit for companies, both in terms of efficiency and cost reduction, and with respect to business operations in the strict sense (production, procurement, distribution, customer relations) and business organization (archiving and document management for administrative, accounting, and legal aspects). As part of the digitization process, information systems assume an important role and the adoption of best-in-class mechanisms of communication and data exchange platforms, as well as back-up, disaster recovery and protection against cyber-attacks will be crucial. In this regard, it may be useful – especially in view of the target market – to introduce a Chief Technology Officer who reports directly to the board so that the board can assess whether the IT systems are sufficient and up to date, whether they need to be upgraded and whether or not they are subjected to

65. See 8th Edition Cineas-Mediobanca Observatory on the spread of risk management in medium-sized Italian companies, November 2020, available at <https://www.cineas.it>.

potential threats of attack, as they are fundamental working tools to enable the goals of growth and value creation to be met.

Similarly, special attention deserves the phenomenon of smart working, which was only seldom applied in Italy before the pandemic. In fact, the sudden and rapid explosion of the crisis has led to a forced and abnormal use of this tool, which on the one hand is a confirmation of an already existing trend, but on the other hand has highlighted the need and urgency for a revision of operating methods in order to combine flexibility and productivity in the best possible way. Once again, the Board 2.0 is being called upon to rethink the structure and monitoring of work organization at the corporate level in a previously unprecedented way, laying the groundwork for an evolution away from a work structure with a traditional approach to a new form of flexible work that, with the help of technology, could boost productivity while safeguarding social values such as work-life balance.

Lastly, the Board 2.0 cannot overlook the fact that corporate value is no longer measured only in terms of profits but also in terms of social responsibility (ESG), as attention to environmental protection, worker care, and proper corporate governance have also become key growth factors. And it is also in this direction that the boards of directors of the future will have to focus with the understanding that sustainability is an attraction for both investment and human capital as well as improves the company's reputation and visibility. In this regard it is worth recalling that the Corporate Governance Code has dictated guidelines for listed companies that should shape strategic planning for sustainable success. Indeed, the Corporate Governance Code points out that the internal control and risk management system must also be structured in such a way that it can contribute to the sustainable success of the company as well as the policy for the remuneration of directors, statutory auditors and top management must also support the pursuit of this objective. Given the very general meaning of 'sustainability,' each board of directors is facing the challenge of articulating sustainability goals in a way that is compatible with the characteristics of the specific business and corporate structure.

### **COMPOSITION AND OPERATION OF THE BOARD 2.0**

At this point it is necessary to ask in which direction best practices related to corporate governance will be established. In particular, it is useful to question how the board should be composed in the near future to offer the best governance in response to new demands imposed by the market.

First, the composition of the boards should be such that they also include individuals who can bring their expertise to bear in new areas. It will probably no longer suffice to include individuals with expertise in financial, industrial, commercial and legal matters, but the optimum will also require the involvement on the board of digital or IT experts who are able to guide the technological evolution and innovation of the company or of experts in environmental or social issues who can provide input for the achievement of objectives related to sustainability. This

will also necessarily lead to a general reduction in the average age of board members. The 2019 Corporate Governance Report prepared by Consob notes that the average age of members of the boards of directors of listed companies is about 56 years old (this was also the case in the previous three years).<sup>66</sup> Where the governing body also needs to rethink its strategic planning in the sense indicated above, the inclusion of professionals who contribute their expertise in new areas must be contemplated, and experts in such areas are usually more common in the younger segments of the population (especially those related to digital aspects and innovation).

Furthermore, the presence of more directors with international backgrounds may also be important for the board in order to: (i) bring experience gained in other corporate and business models that have been subjected to the same evolutionary stimuli as a result of the global crisis and can provide a contribution in terms of better governance solutions as elaborated in other countries, as well as (ii) be able to help manage emergencies (and also crisis management system planning) that may affect other countries where there are significant subsidiaries of the group or where major production facilities have been relocated. In the recent past, many Italian companies, especially those with significant geographic diversification at the production level, were subjected to different pandemic containment measures in each country where they had operations, and sometimes suffered in the management of the anti-Covid solutions and measures proposed in each country, not being able to adopt the same decisions for all but having to diversify the response for each region.

At the level of Board 2.0 operations, it is reasonable to imagine that the technological development generating operational efficiencies for businesses may also facilitate board operations. In fact, the latter will make it possible to manage more effectively the sharing of pre-meeting information (including through the increasingly widespread creation of virtual spaces that allow for the timely uploading of pre-meeting documentation while safeguarding the necessary confidentiality requirements, especially for listed companies), the holding of meetings also remotely (to allow for physical distancing), and the transmission of data, information and reporting (so as to intensify and streamline the information flow of management data to top management for monitoring management's actions).

### **IMPORTANCE OF DIALOG WITH SHAREHOLDERS AND OTHER STAKEHOLDERS**

The global pandemic has made the importance of communication to internal realities (e.g., to management and employees) as well as to external realities (e.g., to shareholders, customers, and suppliers) even more pronounced. Companies that better managed communications were often able to contain the alarmism generated by the health emergency that had negative effects on business and/or stock market value.

Indeed, communication with shareholders has already taken on a central role in corporate governance in recent years, partly as a result of recent laws and regulations. As a reminder,

Directive (EU) no. 828/2017 (Shareholder Rights Directive II) has introduced provisions aimed at increasing the active involvement of shareholders in corporate governance as a factor that can help improve companies' financial and non-financial performance, especially with regard to institutional investors and asset managers (transparency requirements for engagement policies). Many organizations and associations have adopted best corporate governance principles that also focus on engagement and stewardship policies with investors.<sup>67</sup> The topic is also found in the Corporate Governance Code, which stipulated that "employing the most appropriate forms, the board of directors promotes dialog with shareholders and other stakeholders relevant to the company" (Principle IV) and that "upon the proposal of the chair and in agreement with the Chief Executive Officer, the board of directors: - In the corporate governance report adopts and describes a policy for managing dialog with the generality of shareholders, including taking into account the engagement policies adopted by institutional investors and asset managers. In the next meeting the chair ensures that the governing body is in any case informed of the development and significant content of the discussions that took place with all shareholders" (Recommendation no. 3).

Note that in Italy Assonime has recently established an Observatory on Shareholder Dialog Policies, active since March 2021, with the aim of investigating issues related to the definition and implementation of shareholder dialog policies and creating a database aimed at studying practices and critical issues.

As a result of the aforementioned increasingly relevant trend, we can therefore imagine a Board 2.0 that will be focused on:

- the creation of an effective dialog with shareholders that goes beyond the mere dynamics of the shareholders' meeting, by organizing opportunities for periodic meetings (both in person and remote) directly with the board or with directors competent to do so;
- the identification of competent directors to be tasked with this dialog since it is unlikely that this activity can be delegated to the full board. Specifically, these directors could be the CEO, the Chair of the board of directors, or, more likely, non-executive directors with a subsequent requirement to report on the outcomes of these meetings during board meetings;
- mapping the areas that can be the subject of such a dialog, distinguishing between those that are strictly relevant to board responsibilities and those that are not. Such areas could be, for example, strategies, financial and equity performance, objectives related to sustainability, governance structures and improvements thereof, director succession plans and the risk control system;

66. 2019 Report on Corporate Governance of Italian Listed Companies, Consob, available at [https://www.consob.it/web/area-pubblica/abs-rcg/-/asset\\_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2019/11973](https://www.consob.it/web/area-pubblica/abs-rcg/-/asset_publisher/D4UvV7Ug51WY/content/report-corporate-governance-2019/11973).

67. EFAMA Code for external governance (2011); OECD Principles of Corporate Governance (2015); ICGN Global Governance Principles (2017).

- the development of the role of investor relator (a function that is already mandatory for companies that are listed on the STAR segment of the MTA market) as an effective tool for implementing continuity of dialog and as a first line for gathering shareholder requests and views;
- supervision of the dialog's compliance with the principles of confidentiality of inside information, equal treatment of investors and protection of commercially and industrially sensitive information;
- the adoption of policies formalizing the dialog process outlined above and the manner and degree of transparency.

The traditional view that saw benefits from limiting the sharing of information about the company, believing that opacity could limit liability and expand the board's room for maneuvering, is outdated. There is now a growing recognition that active shareholder dialog brings significant benefits because active shareholder involvement results in greater shareholder understanding and thus support for the growth strategies being pursued and their implementation. Management can learn more about the demands of generality or at any rate institutional investors who in any case may represent qualified minorities.

But the dialog cannot be limited to shareholders in general. Given that value creation must take into account the interests of all the various stakeholders for the purpose of 'sustainable' success (not just shareholders) as the mission of the Board 2.0, the board will be responsible for ensuring that the business model is permanently structured to ensure dialog not only with shareholders but with all other stakeholders relevant to the company (employees, suppliers, customers, market).

### **CONSEQUENCES OF THE BOARD'S FAILURE TO EVOLVE**

At the end of this analysis of the evolutionary instances accentuated or brought about by the Covid-19 crisis within the board of directors, it is necessary to ask what can be expected to happen to those companies that do not intend to adapt to the pressing transformation taking place. Dwelling on the latter allows us to measure the degree of need and permanence of the changes taking place, in order to begin to define the contours of a new normal.

It is clear that a board that hesitates in incorporating technological solutions into its business organization, that resists organizing work in a flexible manner or that procrastinates in adopting business procedures aimed at a better social and environmental approach will find itself unprepared for the challenges of the market. Such a company risks losing market share to more efficient competitors because they are more advanced, will have difficulty attracting talent and will respond late to changing conditions in its industry. Resistance to evolution is sanctioned by the ultimate penalty: exit from the market.

But there is more. Even companies with functional business models and attractive margins will suffer, and are already suffering, market sanctions in a broader sense. Imagine, for example, how the failure to adopt functional, effective and appropriate ESG policies for the relevant industry can affect the appeal to third-party investors and the criteria and parameters they apply in the company valuation process. In this sense, it is also worth mentioning that the Corporate Governance Code – which, as anticipated, recommends that companies adopt governance in line with many of the instances set forth in the preceding paragraphs – is not binding in nature, but as a result of Article 123 bis, paragraph 2, letter a) of the TUF entails an obligation on the part of companies listed on regulated markets to provide information to the market in relation to their adherence to the Code, giving reasons for any deviations. It follows that, in addition to civil and administrative effects resulting from the dissemination of incorrect information, the disclosure to the market of the failure to adhere to certain principles or recommendations of the Corporate Governance Code (including for example those related to the pursuit of a sustainable success or the policy of dialog with shareholders) may generate penalizing behavior by market investors, with consequent negative effects on market capitalization. Change is inevitable and the Covid-19 crisis has highlighted this both suddenly and unequivocally.

## 5. RECOMMENDATIONS FOR THE BOARD 2.0

The findings of the analyses proposed in this position paper regarding the role of the Board in the era of the 'new normal' have identified some areas of particular interest.

These are issues that 'Boards 2.0' will increasingly have to consider in the future.

The board of directors remains the sole instrument charged with providing strategic direction and controlling the actions of a company's management. However, the complexity of economic and financial variables and new contexts make it increasingly necessary to identify the fundamental characteristics that a board should be equipped with in order to best exercise its function.

The conclusions below are a summary of what emerged in the course of the work, but in part, they also provide a number of suggestions for improving the role and function of tomorrow's boards of directors, with the aim of bringing them increasingly in line with international standards, and above all with the expectations of all stakeholders.

The areas of focus identified can be grouped into three strands:

- The skills of board members, diversity, and minority representation are three key aspects that should be addressed without further delay by Italian companies. On the whole, these could be introduced without too much difficulty.
- The second strand includes the debate on the most appropriate model for boards of directors, the openness to the internationalization of boards, and the length of board tenure harmonized with business plans. These topics are likely to require more in-depth reflections and may perhaps need legislative changes as well.
- Finally, the third category includes two suggestions that are not obvious subjects of the Italian governance debate, but which would bring Italian companies closer to those in more sophisticated financial markets. These are annual board reappointment voting and/or preference voting of individual board members, as well as the purchase/possession of company shares which can result in a greater alignment of directors' interests with those of stakeholders.

In this regard, subject to the changing regulatory environment at national and international levels, as well as the changing dynamics of financial markets and the impact of new contexts such as Covid-19, the Committee identified some possible suggestions:

### 1. THE SKILLS OF BOARD MEMBERS

There is a consensus that boards should be composed of members who bring a mix of skills and experience, which is a combination that is more difficult to achieve with a small number of board members. However, there are a number of new skills that boards often lack, which are made even more relevant by new contexts such as cybersecurity, digitization, crisis management, and sustainability. The issue of board expertise, together with board compensation, seems to be critical to ensure that boards are capable of dealing effectively with current and future or unexpected challenges. The multiplicity and combination of skills are considered a factor in the growth of board leadership.

### 2. DIVERSITY

It will be crucial for the boards of the future to recognize diversity as a concept that needs to be interpreted across the board, without limiting it to gender difference alone. A perfect example is age diversity, whereby directors of different ages can offer innovative visions and approaches to business.

### 3. GREATER REPRESENTATION OF MINORITY SLATES

This is perhaps the area where the debate is at its most advanced stage. Also, during the work of the AmCham Italy Governance Committee, it was observed that the presence of only one minority director does not guarantee an adequate level of 'challenge' on the board, diminishing the necessary critical capacity. More minority directors, together with a higher level of director independence, would ensure a variety of judgments that would maximize value creation for all stakeholders. A single minority director now seems to be a practice that cannot be reconciled with the current economic and financial environment.

### 4. THE BEST MODEL

In Italy, as shown in the analyses in this position paper, the most widely adopted model is the traditional model. However, there is ample room to consider adopting alternative models depending on certain contexts. While the one-tier system has some critical issues, it could be very effective in the subsidiaries of a holding company. As for the two-tier system, hastily abandoned by Italian companies, it may be the best model for managing generational transitions within a company. Specifically, the leverage of the supervisory board could be left to the family-shareholders, with the addition of external professionals diversified by expertise, leaving the management board dedicated to management.



## **5. INTERNATIONALIZATION OF THE BOARD**

Few countries in the world have boards with a pronounced presence of foreign administrators, and Italy is not among them. Comparisons with international business approaches and views, experience in other financial markets, and the application of established solutions are factors of great value and help to boards. There may be language and logistical barriers to be considered but even these can be greatly mitigated by innovations in remote communications.

## **6. BOARD TENURE SHOULD BE CONSISTENT WITH THE STRATEGIC PLAN**

The experiences of the Committee have raised the issue of aligning the tenure of boards with the timing of business plans. Perhaps the three-year board tenure could be replaced by different time frames, allowing shareholders to evaluate directors' performance and results more consistently.

## **7. ANNUAL BOARD REAPPOINTMENT VOTE**

Similar to the previous point, the introduction of an annual board reappointment vote by the shareholders could ensure more consistent scrutiny of performance without resulting in short-termism on the part of the directors themselves.

## **8. PREFERENTIAL VOTING FOR INDIVIDUAL DIRECTORS**

Going even further, as is the case in many countries, shareholders could also vote on the individual members of the board and not just on a group of directors included in one or more slates. The provision of an 'advisory vote' that results in a diversity of opinion could induce companies to make a more appropriate evaluation of directors and thus boards with higher mixes of expertise, skills, and abilities.

## **9. DIRECTORS' OWNERSHIP OF COMPANY SHARES**

International experiences regarding various forms of ownership and/or the purchase of company shares are harbingers of strong alignment among directors, shareholders, and all other stakeholders. While there are cases where remuneration is composed solely of shares, companies could identify diversified forms of compensation that would lead directors to make decisions that could impact not only all stakeholders but also themselves.

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