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DELEGATION OF POWERS AND CONSEQUENCES FOR NON- EXECUTIVE DIRECTORS' LIABILITY UNDER ITALIAN LAW

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Introduction

The Court of Cassation (Italian Supreme Court) recently reaffirmed some important principles on the civil and criminal liability of directors (including non-executive directors) of Italian companies' boards. The topic is sensitive not only for directors of domestic companies but also for multinational groups which often designate non-Italian managers to serve on the board of their Italian subsidiaries.

The Supreme Court ruled that the members of a board of directors may be subject to different grounds of civil and criminal liability depending on whether the board delegated some of its functions to one or more directors, and clarified the conditions for non-executive directors' liability to be affirmed in both situations.

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The Court of Cassation ruling No 11087 of March 28, 2022

The case before the Supreme Court involved a member of the board of directors of an Italian consortium (that follows the same rules of joint-stock companies) who was under investigation – together with other subjects – for criminal tax violations for having recorded invoices for non-existent transactions. In particular, the Court had to decide an appeal by a non-executive director against the decision of the Judge for Preliminary Investigations ordering the seizure of his personal assets. The appellant claimed that the seizure order was not legitimate as he had not had an active role in the alleged tax crime, nor had any delegated powers in that respect, and that all allegations were based solely on his formal position as director, and therefore that there were no elements to establish that the director had knowledge or awareness of the crime committed by others.

The Supreme Court rejected the appeal, confirming the preventive seizure against the non-executive director for the tax offence he had been charged with, given that there were no delegation of powers and – like any other member of the board – the appellant was entrusted with direct administrative duties: even if the decisions regarding tax obligations were not in fact taken directly by him, the director had breached his obligations to supervise and prevent harmful acts from being carried out or avoid their harmful consequences.

As a general principle under Italian law, similar to what happens in other jurisdictions, the board of directors has a collective responsibility for managing the company through the decisions taken through its resolutions. Italian law allows the board of directors to delegate specific functions and grant the relevant powers to an executive committee or to a managing director, in accordance with certain rules and subject to some limitations¹.

¹ Under Article 2381, paragraph 4 of the Italian Civil Code the board of directors cannot delegate certain specific functions, such as: issuing bonds, if delegated to the board; drafting financial statements; increasing the share capital, if delegated to the board; reducing the share capital for losses, also in the case of losses involving a decrease of the share capital below the legal minimum threshold; and drafting merger or demerger projects.

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In examining the specific case at hand, the Supreme Court clarified the conditions for criminal liability of the members of the board (including non-executive directors) when the illicit act was part of the functions which have been delegated, and when it was not or was delegated to another director.

In the absence of a specific delegation of powers, all members of the board are jointly liable² for any illicit actions decided or carried out by the board or also only by some of its members. The members of the board may avoid liability solely if they have expressed in writing their specific dissent vis-à-vis the specific resolution, as provided by article 2392 of the Italian Civil Code, and have not been negligent.

On the contrary, if the board properly delegated specific matters to certain directors, then those directors will be liable for illicit acts carried out within those matters. However, under some circumstances, notwithstanding the delegation of powers, the non-executive directors/other directors may be held jointly liable and considered conspirators in a crime.

The exercise of the power of delegation does not discharge the other directors from the duty to act with care and to “oversee” the management of the company. Based on this principle the Court clarified that even if some matters have been attributed to one or more directors, the non-executive directors (and the executive directors who were attributed different powers) must diligently exercise, in particular, two duties: they must act in an informed manner, pursuant to Article 2381 of the Italian Civil Code and, in the presence of any red flags, they must ask additional information to the executive directors and do everything within their power to prevent harmful acts from being carried out or to avoid their harmful consequences (Article 2392, second paragraph of Italian Civil Code). If a director is found to have breached (for negligence or willful misconduct) his/her duties of acting in an informed manner and of intervention in the presence

² Directors may be held liable (i) towards the company itself, e.g. if they have caused damage to the company due to a breach of law, the company’s by-laws or other general duties (article 2392 of the Italian Civil Code), (ii) towards the company’s creditors, e.g. if the directors have breached the specific rules regarding the preservation of corporate assets, and those assets are insufficient to satisfy the creditors (article 2394 of the Italian Civil Code), (iii) towards individual shareholders or third parties, e.g. if the latter have suffered direct damage from any acts performed with fraud or gross negligence by the directors (article 2395 of the Italian Civil Code).

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of red flags, he/she may be subject to liability jointly with the executive directors who had the delegated powers over the matter at hand.

On the contrary, the members of the board may not be blamed and face no liability in cases where the executive directors omit or provide false information and no red flags emerge from a diligent control – given that, in those cases, there is no indication that they knew or could have known that something improper was going on.

Conclusion

Boards of Italian companies must put in place a proper system of delegation of powers and functions that could not only assist in enhancing the decision-making processes, but also limit the indiscriminate exposure of all the directors of the board to all the aforementioned liabilities. Any delegation must be reasonable in scope and admissible by the law and the company's By-laws, the delegated persons must be competent and trustworthy, and the board must supervise how the company is managed.

Even though they are not directly involved in the ordinary management of the business, non-executive directors may not remain passive and consider themselves discharged from any liability for the sole fact that there is a managing director or an executive committee. On the contrary they should exercise thoroughly and diligently their duties of care and intervention. In particular, non-executive members must carefully review the information provided by executive directors, ask for information if the executive directors did not provide any, and require additional information if those provided are insufficient or raise doubts or red flags. Lastly, in the presence of red flags also non-executive directors must intervene in a timely fashion, regardless of how they became aware of said red flags.