

**Italian Civil Code:
Duties and Obligations of Company's Board of Directors**

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I) Duties and obligations of the directors of a joint stock company

In the organized structure of a company, the board of directors's task is to conduct the business of the company. The directors' functions, therefore, are based on a complex of powers and duties.

SPECIFIC DUTIES, as provided by specific law or by the deed of partnership. The respect of the internal rules of organization related to the elaboration and externalization of the company's will, represents one of these duties, so as the elaboration of the balance sheet project, or the convening of the Assembly in the event the company's capital suffers a reduction for more than one third. In accordance to this approach, the DILIGENCE STANDARD is considered a kind of duty performance, in other words "the measure of the engagement asked to the directors". From this point of view, liability can be verified in accordance with section 1218 of the Italian civil code where the failure of the performance is caused by an event that could not be avoided neither overcome through the requested diligence. The director will be responsible to the extent that he does not respect the rules as provided by law or indicated in the deed of partnership, except when he will prove that the default has been caused by an event unchangeable to him.

GENERAL DUTIES are defined through the recourse of general clauses, such as the duty to carefully manage the company or to conduct the business with no conflict of interests.

In accordance with this approach, the liability of the company's directors will be more difficult to be verified. Diligence represents from this point of view the purpose of the performance. The simple business conduct without the utilization of carefulness causes a default. It is necessary to analyze the directors' behaviour and distinguish the company's risk from the damage suffered because of a lack of diligence. On the basis of such considerations, "the liability of the director must be connected with the violation of the general duty of diligence in the management choices, therefore, the good business conduct of the director is sufficient enough to exclude the default, nevertheless the result of the choice made (..)" (*Civil court of Cassation n. 5718/2004*).

II) Liability of the directors

In accordance with section 2392 of the Italian Civil Code, the director is responsible for the violation of the duties as provided by law or indicated in the deed of partnership. Though the Reform in force, enacted on January 17th 2003 n.6, the legislative preserved directors liability for damages caused by violation of rules, but provided for the possibility for the director to prove his innocence. This kind of responsibility is in fact considered a liability for own fault.

The directors' responsibility is a liability for damages, in particular, a liability for contractual default based on the fact that the director is bound to the company through a contract of MANDATE.

Section 2932 of the Italian civil code, as above indicated, states that the directors must abide by their duties, as imposed by law and indicated in the deed of partnership, through the “*mandatary's diligence*”. The standard of good and correct management does not mean profitable business but highlights a certain kind of attention, efficiency and respect to the company's rules.

Before the Reform, the discussion was focused on the nature of diligence requested of the director. Some authors (Galgano), emphasized the diligence of the *bonus pater familias* (the director's duty was in fact considered a duty based on the measures utilized and not a duty based on the reached result). Most of the doctrine and court decisions agreed on the necessity to lay out a qualified diligence based on the professional nature of the business conduct. Other authors sustained the importance of a diligence based on a technical appraisal or specific competence on the account, financial, industrial and trade field.

As a result of the Reform, the discussion as above outlined, has been over-passed through the intervention of the legislature who under section 2392 c.c. today requires a PROFESSIONAL DILIGENCE. The new section in fact states that the directors must accomplish their duties through the diligence requested in accordance with the “nature of the task and their own specific ability”. Liability has been created that refers to the position that each director has inside the board (president, director with particular power, manager) and to the specific knowledge of each one of them.

The Report which supports the legislative decree n.6/2003, states that technical knowledge of the directors does not mean that “the directors must necessary be experts in accountancy, financing or in any other area of the company management, but that their choices must be informed and meditated or based on their respective knowledge as a result of a calculated risk and must not seem to be the result of an irresponsible or negligent improvisation”.

Another problem is to understand the grade of IMPEACHABLE that the judge can exercise toward the directors' choices. The Reform has not solved the question related to the nature of the judge's control over the director's conduct. Under this approach the *business judgement rule* represents one of the new standards that is taking place. In accordance with this criteria, the judge, in order to verify the correctness of the directors' decisions, cannot enter into the heart of such company's decisions unless these decisions are considered totally irrational. The Court's decisions have constantly been consolidated in asserting the necessity to make a control *ex ante* and *in abstract*, in order to take into consideration the lines which guide the choice and not the choice

itself. The director's business conduct is necessarily connected to a risk. His liability cannot be simply presumed from the reached profits/results (Court of Cassation n. 3652/97). As a result, there is a liability of the director when the business conduct that has caused the damage, should have not been made based on those conditions that he instead accepted for negligence.

The standard of unpeacheability on the director's choice finds its ratio in the directors' meditated and INFORMED DECISIONS.

An informed decision underlines also the important role of the director inside the company and puts into light the problem related to the duty of vigilance of the NON DELEGATE DIRECTORS toward the delegate ones. The new paragraph 2 of section 2392 of the Italian civil code, eliminates the hypothesis of liability for lack of vigilance and introduces a more specific liability in the event the directors, informed of the prejudice facts, have not acted as they could, in order to impede such facts, or eliminate/mitigate the consequences. This modification thus preserving the jointly liability, tries to avoid an incorrect extension of the responsibility as an objective liability.

Section 2381 of the Italian civil code works as a counterpoise to the elimination of the *culpa in vigilando*. This section states in fact that the only actions which cannot be transferred to other directors are those related to the operations on the share capital, and on the elaboration of the balance sheet project. Therefore, all the extraordinary/ordinary operative management can be commissioned to the delegate directors or to the executive committee.

Section 149 of the TUIF requires delegate directors to periodically inform the principal director on the management conduct and on the most important operations. The principal will inform the internal auditing every three month. The section as above indicated also determines the power for each director to ask to the delegate organs to give more information during the board of directors.

III) Civil liability of the Directors

The elements on which the directors' liability is based on are:

- default (breach of a duty as imposed by law/statute);
- damage caused against the company/creditor/shareholder/third party;
- the causal connection between the breach and the damage

it is a difficult profile because characterized by several liability based on different titles:

- concurrent liability between directors and internal auditors;
- concurrent liability between directors and outside auditors;
- concurrent liability between delegate directors and principal.

The liability of the directors is articulated into three directions:

a) contractual liability toward the company:

This kind of liability comes to light when the director does not respect the duties as imposed in the contract through which he has accepted the charge. In accordance with section 2392 of the Italian Civil code, paragraph 1, the directors are JOINTLY responsible toward the company when they fail to perform the duties as imposed in the DEED'S INCORPORATION or in LAW. When several functions have been delegated to an executive committee or to particular directors, the liability of the directors is excluded for any default made by these delegated persons. This approach is tempered by the following paragraph 2 which states that "considering steady section 2381 of the Italian civil code, the directors will be jointly responsible if, aware of the prejudice facts, they did not do anything to prevent such events neither to mitigate or eliminate the negative consequences". On the basis of such rule, the directors will be liable for not having made any kind of control on the business entrusted to the charged persons.

Sect. 2393 of the Italian civil code "liability action"

- action filed after the deliberation of the ordinary Assembly (this deliberation is included ex lege into the agenda when the balance sheet is the discussed subject);
- action can be filed within 5 years from the discontinuance of the director's office;
- the REPEAL follows automatically the filing of such claim only if such decision is supported by a favourite vote of one fifth of the share capital;
- the company has the possibility to decide to renounce/settle this action through an Assembly deliberation at the condition that the contrary votes won't reach one fifth of the share capital.

b) tort liability toward the company's creditors

Action filed in order to claim against the liability of the directors for their non compliance to the duties on the COMPANY'S TOTAL ASSETS INTEGRITY in accordance with section 2394 of the Italian civil code.

- fundamental element necessary for the filing of this action is the INSUFFICIENCY of the total assets of the company for the creditor's benefits.
- Subjects entitles to act are: a)the COMPANY'S CREDITORS: they don't substitute themselves to their company, therefore, they will independently and directly file claims against the directors. As a result, the directors won't object against them the exceptions related to the company itself; b) TRUSTEE in bankruptcy or liquidator or extraordinary commissioner in the event of bankruptcy, winding up or extraordinary administration;

- The SETTLEMENT, on the contrary, obstructs the action of the creditors. This latter, have the possibility to attack the settlement only through an avoidance action when the settlement provokes a prejudice against them.

c) tort action toward the single shareholders or third parties

This rule has not been modified by the Reform of 2003 except for the five years term fixed for the filing of such action that confirms its tort nature. It is a civil action which aims to assure, to a single shareholder or third party, the damages suffered for NEGLIGENCE OR FRAUD by directors. It is a personal liability of the directors. The main conditions on which such action is based on are the negligence or the fraud of the directors; a direct loss into the person asset and a chain of causation between the fraud and the loss. The rules that govern the directors behaviour are extended toward the officers too (sect. 2396). Regarding the Internal auditing liability, it is necessary to highlight how, in accordance with section 2407 of the Italian civil code, the internal auditing of a company is jointly responsible with the directors for the directors' misconduct, when the injury would have not been suffered if they would have correctly controlled the management people of the company. The INTERNAL AUDITING liability is not equivalent to the directors' liability because these two kind of categories have different tasks as the internal auditing does not have any management function but a legal and substantial control over them. The Italian legislative has put on the same level these two categories only on the repairing damage side of view. The joint liability of the internal auditing, for the illegal behaviour conducted by the directors, is modelled on the directors' liability. Therefore, they may be called to answer jointly with the directors, for the damage caused not only against the company but also against third parties or single shareholders, for the directors misconduct (Court of Cassation n.2624/2000). The jointly liability is in fact an external liability toward the damaged person. The lack of recall in accordance of the second paragraph of sect. 2407 of the Italian civil code in the TUIF (Financial compilation) means that the OUTSIDE AUDITING is responsible in a direct way and not jointly with the directors. In this field, a phenomenon that takes place is the deep pocket though which the person who will pay of the damage will not be the real person responsible but the one who has the financial means to pay. In other words, between a director and an external auditor the most simple choice falls into this latter.

IV) Criminal liability of the Directors

In accordance with sect. 2621 of the Italian civil code, directors, officers, internal auditors and liquidators, who deceive shareholders or the public by publishing fraudulent reports, balance-sheets, or other economic statements as fact may be punished with the arrest for one year and six months.

Such criminal liability is excluded if the falsity and the forbearances don't alter in a sensible way the economic situation of the company or of the group. The liability is however excluded if falsity and forbearance provoke a modification of the economic result not greater than 5% gross or 1% net. *“The liability of the directors of a joint stock company toward single partners or third parties is an extra-contractual liability and provides the completion of fraudulent or negligent behaviours which have directly damaged the partner or the third party. For direct damage is meant a damage which has directly weighed on the third's patrimony, impoverishing it (Court of Appeal of Milan, 11 July 2003).*

If the criminal conduct of the directors, the officers, the internal auditors and the liquidators as described in sect. 2621 results in economic damage to shareholders, creditors, the punishment will be the arrest for six months to three years (sect. 2622 of the Italian civil code).

As a result of the new regulation as introduced by the legislative decree of April 11th 2002 n. 61, the area of the old sec. 2621 of the Italian civil code has been strongly limited and contemporary articulated in two sections 2621 (as a technical offence) and 2622 (as a criminal charge). (Court of Cassation 3.26.2003 n. 25887).

Before the Reform, the main interest guaranteed by section 2621 as above indicated was transparency. It was considered an ultra-individual interest, a collective interest in accordance to which the firmness of the economic system was guaranteed through the balance truths. An indirect interest was the one concerning those creditors, third parties and shareholder who had entrusted the company. The time of the exhibition of the false elements was considered the moment in which the crime was intended to be committed. Therefore, the main consummation of the offence coincide with the exhibition of the data and not with the perception of such elements of a third party. The only alteration of the balance was sufficient enough to consider the company guilty for attempting the economic system stability.

Through the Reform, the new sect. 2621 describes a simple offence based on an intentional fraud. The reform legislature has in this way reduced the criminal area legally relevant. This new crime as described in sect. 2621 does not represent an *abolitio criminis* respect the previous one but a sequence of criminal laws in accordance with sect. 2 of the Italian criminal code.

Another crime that today has particularly importance is the one related to FALSE PROSPECTUS. This crime finds its regulation in section 2623 of the Italian civil code in accordance to which one who is aware of the forgery and with the intent to defraud persons, tries to obtain an unfair profit for himself or others, by exhibiting false information into requested reports on investment solicitude or on ordinary market quotation, or in documents to be published during

the public offering, or hides such information in order to induce in error the addressees of such information, causing an economic loss against them is subjected to the arrest for one year.

Today a relevant role is played also by the MANIPULATION crime as regulated by sect. 2637 of the Italian civil code. In accordance with such rule, one who divulges false notices, or sets out simulated operations or other artificial conducts able to concretely provoke a sensible alteration of the price of financial means, may be imprisoned for five years. This crime takes into consideration not only simulated operation but also other artificial conduct. Therefore, market manipulation can be obtained also through single legal activities whose combination or the time in which they are set provoke a distortion of the mechanism of the prices elaboration (Court of Milan, 11.11.2002).

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V) Autonomy and Independence of each company

A) GENERAL PART

1. The definition of group in the contemporary jurisdiction.

The concept of group is to be found in the company field, in which the company, in order to achieve a high level of organization, has the opportunity and the convenience to organize itself and create corporate groups, among which it provides a thick net of connections.

As a matter of fact, the parent company controls its subsidiaries and the whole structure is perceived, by this latter, as a unitary economic body, even though the financial, fiscal and administrative aspects of the different companies remain separate.

In the last years, the debate on corporate group, which recognizes the group as a single economic unit and, at the same time, maintains a rigid position on the legal autonomy of each company, improved a lot, both on the legislative and jurisdictional side.

Considering the first view, it is necessary to underline that in the Italian law a definition of corporate group does not exist.

Law Prodi bis: the concept of group has been studied for the first time by the legislative decree n.270/99 (Sections 81, 82), known as *Prodi-bis*. The new provision is reserved to the insolvent companies whose perspectives for a renewal of the economical activity are concrete. This law allows the submission of the other companies of the group to insolvency administration, as the unitary management of these companies is considered the instrument able to achieve the aims towards the procedure is headed.

Reform - legislative decree n. 6/2003: the Reform of the Italian civil code on companies, enacted through legislative decree n. 6/2003, contributed to enforce the concept of corporate group, based on a regulation of the connections among the parent company and its affiliates which work under the control of the first one. The relations among the companies need to be examined both on

the economic and legal aspect. Chapter IX of the Reform of the Civil Code, entitled “DIRECTION and CO-ORDINATION”, gives an imprecise profile of the corporate group. This represents a serious choice made by the legislative which intended to leave to the doctrine and Courts’ decisions the hard work to define the concept so that the notion could be more flexible and able to adapt itself to the continuous economic, social and legal evolution.

Dlgs. n. 347/03: Also the decree-law n. 347/2003, issued for the **Parmalat** case, because law on 18 February 2004 n. 39, integrated by the decree law 3 May 2004, converted in law 5 July 2004 n. 166 (known as Marzano law), modified through the decree law 29 November 2004 n. 281 converted in law 28 January 2005 n.6 (known as Marzano bis) concerning urgent measures for the industrial reorganization of big companies in crisis, deals with corporate groups but, it does not provide any definition of the corporate group structure, nor of the unitary direction of the companies, or of the relations among them. As a result of the modifications made by the laws as above indicate, the last one Law n. 6/2005 issue for **Volare Airlines**, is applied toward those companies which jointly have: a) not less than 500 of employers (L. Marzano provided instead 1000 employers); b) a total amount of debts not less than three billions euro (L. Marzano was settled for 1 billion of euros).

The Italian **Commission** for the Reform of the Bankruptcy Law, known as the Trevisanato Commission, deeply discussed the matter related to group insolvency. The provisions included in the Reform of the Bankruptcy Law do not add other definitions of unitary direction which remains the one drawn by legislative decree n. 270/99. A Commission argued that the group should not be bound by rigid rules, but should be premised on the continuous evolution characterising the groups of companies as legal entities.

2. The concept of group in accordance with the doctrine and court’s decisions: the Unitary direction

In accordance with most of the **Court’s decisions**, the corporate group is perceived as an aggregation of productive bodies, legally self-governing, but managed in a unitary way in order to better accomplish the objectives aimed by the group. The fundamental characteristics of the group are as follow: a) legal autonomy of each company belonging to a group; b) control by the parent company of the subsidiaries; c) direction and coordination of the management of the group.

The contemporary **doctrine** is still debating on defining the content of the connections between the concepts of group and control. Part of the doctrine perceives the group as a whole corporation in which all the bodies are equal; other parts of the doctrine highlight how the parent company holds effective control of the subsidiaries as a presumption with no possibility to give contrary proof. The

second option should be preferred, with several limitations in respect of the directors' liability, both of the parent and of the subsidiary. In accordance with this approach, each company has a different grade of integration in the group. It is necessary to clarify the parent's influence over its affiliates in order to understand if the group corporation really exists. A pure integration from the parent company, does not identify such phenomenon. In any case, a group comes into existence under a legal perspective, in the event the parent controls the subsidiaries through a unitary management. The unitary direction is therefore considered a value to protect and a vehicle of economic evolution and more stability inside the group. Nevertheless, the company autonomy must be saved because the hypothesis of a "destructive abuse" against each single unit will have to be avoided.

The **Reform** of the corporate law (legislative decree n. 6/2003) describes the CO-ORDINATION and DIRECTION ACTIVITY and introduces a presumption of law in the conduct of such activity of direction, if:

- the companies are obliged to draw up a consolidated balance sheet;
- the company is expected to exercise the activity of direction as provided in sect. 2359 of Italian Civil Code;
- one company holds the majority of the votes of an other company, or votes sufficient to exercise a position of direction in the Shareholders' Assembly, or there are liens among the companies whose direct consequence is the acquisition of a controlling stake in other companies;
- general clauses in order to acquire a position of direction as arranged in the agreements negotiated between the companies.

The legislature does not provide the exact content of the conduct of the direction. Such information must be contained in a special section of Public Registers of the Companies held in the Chambers of Commerce of each chief town or province where the details related to organs conducting the activities of direction and co-ordination, and companies subjected to them, are contained. The mention of such connections among the companies has to be inserted in the letter-head, the agreement-head and the document-head. The balance sheet of the parent company will have to contain the essential details related to the activity carried by the subsidiaries. The choice of the legislature is to privilege publicity, public information and transparency in order to inform the parties interested, in particular creditors, that a single company is part of a complex corporate structure.

3. The concept of group in the insolvency procedure

The studies conducted on the Italian experience, represented by approximately 3000 groups of joint-stock companies plus an undefined number of groups which heads are natural persons,

show the wide structure adopted by the companies. The phenomenon has characteristics mostly connected to a temporary and peculiar strategy of business, so that the management conducted by the parent could be, more or less, unitary according to the main aims. On the same matter, it is also important to highlight an increase of agreements of temporary aggregation subscribed by companies whose financial and economic objectives are similar. The adoption of such kinds of agreements do not involve any change in the original company structure. Therefore, if under a legal perspective, the belonging of a company to a group might be excluded, the unitary direction could be temporary admitted for a single business conduct.

Courts' decisions, in contrast with the doctrine, underline the autonomy, both legal and patrimonial, of each company being part of a group, so that the assets and the personality of each one will remain separate in the event of bankruptcy. The consequence of such a provision is that the same Court, whose territorial jurisdiction depends on the residence of each single company, will have to judge on each proceeding filed and will declare the insolvency for each different company. The separation among the jurisdiction and the places in which the company conducts its business, has relevant contents. In fact, if the subsidiary has its own residence in a place different from the parent's one, and this latter is subjected to the extraordinary administration, the commissioner will have to demand to the Court, where the subsidiary is located, the bankruptcy declaration of the affiliate.

The **Project of the Reform of Bankruptcy Law** gives the possibility to assure: a) the same temporary management to all the companies whose insolvency is declared: b) the sale in bulk at the same time of the assets of the company so that the restart of the entire enterprise will be guaranteed; c) the fees for the unitary management of the different bankruptcy proceedings which will be charged on the basis of the amount of the bankrupt's estate of each company. This new approach is invoked by the experts because, as we said before, both the Law n. 95/1979 and the legislative decree n.270/99 faced the matter of the insolvency for corporate group, but did not succeed in solving the pre-said matter.

4. The directors' liability of the Parent company.

When the holding company conducts the main management of the group, a SUBJECTIVE RELATIONSHIP is established with its subsidiaries and has the primary task to realize the group interest through the satisfaction of the subsidiary's interest. The parent company must abide by specific duties of correctness toward its affiliates. These duties represent constraint obligations which if not performed, may cause ABUSIVE conduct. In this hypothesis, the parent company will have to indemnify the damage jointly with its directors and the subsidiary's directors. Each director

may be excluded from responsibility if, in contrast with some deliberations/directives of the company, he expressly indicated its negative decision. However sect. 2497 of the Italian civil code, underlining the standard of “COMPENSATE ADVANTAGE”, excludes any kind of liability of the directors if the sacrifice is compensated by the enrichment of a group interest.

In order to examine closer what was said before, the main part of the reasons for a decision pronounced by the Court of Milan, whose activity has always focused on the analysis of the matters related to advanced economy and enterprises, has been reported hereby: “The bankruptcy trustee of a failed company, being part of a corporate group, will be able to enact liability actions either towards the DIRECTORS of the parent company or towards the PARENT COMPANY. The trustee will have the opportunity to file a claim against the parent company only in the event the company ABUSED of the UNITARY DIRECTION and of its position of supremacy. The directing body entities of the subsidiaries must had subscribed dangerous transactions or they could had not done anything necessary for the economic health of the company”.¹

Such a decision highlighted the enlargement of the duties among the organs being part of a group: since the matter related to responsibility used to concern exclusively the company as a legal person, nowadays the liability has been extended to those who owned the companies or abused of them, without any respect of the law. The *ratio* of the decision of the Court of Milan, has to be researched in the willing of the Italian legislature (sect. 2497, part 2, of the Italian Civil Code) to charge with responsibility for any fault, the one who effectively committed it.

The provision of a general duty of control conducted by the parent on the subsidiaries, has been adopted by the Italian jurisdiction (the same provision is also contained in the American jurisdiction, as we will examine later) and the Courts have perceived it as a specific obligation of the parent.

Thus, the creditors will have the opportunity to claim their rights, both against the parent company and its directors. The origin of the liability has to be searched, as said before, in the abuse of the activity of unitary direction as a vehicle for prejudicing the activity of the subsidiary.

The provision through which the responsibility of the directors is sanctioned, is contained in **Sect. 90 of the Legislative Decree 270/1999** (known as *Prodi-bis*). This section expressly states that, in the event of a unitary direction, the directors of the parent who, abusing of their position of supremacy, fraudulently induced the directors of a subsidiary to subscribe to dangerous transactions, are responsible together with the directors of the failed company, for the damages caused to the company itself. This kind of responsibility is not considered to be objective. The

¹ Tribunale di Milano 22-1-01 in Il Fallimento n.10 del 2001, pg. 1143.

behaviour of the directors will be prosecuted only if they act with awareness and fraudulently conduct their business.

Thus, it is fundamental to look at the managing plan proposed for the company in order to verify whenever the directors effectively acted without considering the interests of the company, violating the rights of both, the shareholders and the creditors.

With regard to the liability of the parent company, of its administrators and of anyone who abused of the power of unitary management, the Trevisanato Commission proposed to Italian Parliament a range of options. Two hypothesis are particularly important. The first one, provides the extension of the insolvency proceeding to all the companies that are part of the corporate group, or to the natural persons who caused the insolvency of the parent or of its affiliates by their own behaviour. The second hypothesis, supported by many commissioners, transfers the civil aspect of the liability and of damage compensation, the assessment and the condemn of those responsible, in accordance with the Italian Civil Code so as reformed in Section 2497. In fact, the legislature, through this Section (2497) enlarged the responsibility of directors, both of the parent and of the subsidiary, towards shareholders and creditors who have been damaged by the directors' illegal behaviours. In my view, the second approach should be preferred, so to avoid to give extraordinary powers to the Bankruptcy Courts and to those proceedings characterized by an incomplete right of controverting (or adversary system). Therefore, not only limits of coherence of the system, and of respect of the rights to defence, suggest to keep distinct the bankruptcy plan from the civil one, without providing the Bankruptcy Court extraordinary powers, especially in a delicate matter such as the corporate group.

There are no doubts on the **tort** nature (*ex* Sect. 2043, 2049 Italian Civil Code) of the action that creditors may enact. The Courts, on the contrary, have not yet reached a unitary position on the legal qualification (tort or contractual, *ex* Sect.1218 Italian Civil Code) for the action shareholders may be able to file.

The qualification of the direction, exercised by the directors, as a TORT activity depends on the occasionally on the instructions given. The illicit conduct violates the general principle represented by the *neminem laedere*. On the contrary, the illicit conduct led by directors will have to be intended as CONTRACTUAL liability if the directors' duty of direction is expressly contained in a contractual agreement.

The discipline related to the *onus probandi* depends on the qualification attributed to the activity of direction. In the event the liability of the parent company is qualified as extra-contractual, the damaged party will have to prove the fault of the parent (so hard to be proved!),

otherwise, in the event the liability would be qualified as contractual, the *onus probandi* would only consist in the proof of the violation of the contract.

Part of the doctrine, though the minority, perceives that also in the case of contractual liability, it will be necessary for the damaged party to prove the fault making a comparison between the effective conduct held by the directors and the abstract model of conduct perceived as the fair one.

Moreover, **Sect. 90**, Law n.270/1999 proposes two different solutions. The first solution is based on the liability both of the directors of the parent and of the parent itself. The liability of this latter is proved if the directors are re-known to be responsible for abusing of the unitary direction. In this case, the liability of the directors is extra-contractual for behaving fraudulently towards the company, while the liability of the parent is contractual. A second view, instead, applies Section 90 only to directors (in accordance to Sections 2049 or 2043 c.c.). Parent's liability would not have any connection with these sections and would be regulated through the obligations that this latter assumes towards its affiliates. It is clear, under the procedural profile, (particularly on the probative level), the importance, of a casuistry based on the evident negative and illegal behaviours of directors, that the Court's decisions may offer not only on a national level; the legislature realized the concrete possibility to create real *standards of review* able to immediately punish the board of directors, as a preventive measure, every eccentric, contrary conduct of the directors.

5. Parent Company's liability and Creditors' protection on insolvency proceeding

Part of the Italian doctrine, extends the liability of the parent directors to the parent company itself in accordance to the principle of the organic unification (Section 2049 c.c.) or of the direct liability, as described in Section 2043 of the Italian Civil Code. The shareholder and the creditor may act against the parent company only if their credits will not be satisfied by the subsidiary. However, they will have to prove the concrete and permanent damage they suffered, otherwise, they will not have the possibility to enact the claim.

The Court of Milan, in the sentence above mentioned, considers, on the contrary, the parent company as the candidate for forbidden behaviours held by subsidiary's directors. The Italian Court, in fact, agrees with the opinion that the party who gives illicit directives is the company which conducts its business through its own representatives. The unitary direction is organized by the controller company, therefore, the abuse required as necessary raises from the activity of this latter.

A particular problem concerns parent's liability and its directors' for bad business conducted by one of its subsidiaries. In accordance to the majority of Court's decisions, it will be necessary to

consider each controlled company as a single unit among the whole relations inside the corporate group. In the individual relations, instead, damaged creditors and shareholders have the possibility to call on the proceeding the subsidiary's directors, the parent's directors, and the parent itself. This latter, therefore, will have to answer jointly with its own directors.

B) SPECIFIC PART

THE PERILS OF ZEUS

As I argued in the foregoing pages, the corporate group is perceived as an aggregation of productive bodies, legally self-governing, but managed in a unitary way in order to better accomplish the objectives aimed by the group. The fundamental characteristics of the group are as following: legal autonomy of each company belonging to a group; control of the parent company on the subsidiaries; direction, and coordination in the management of the group. Regarding the specific case as elaborated into the "Perils of Zeus" an eventual decrease of production and a financial distress of the group forces "Zeus subsidiaries" to stretch trade creditors". As I explained above, the Italian law regulates the corporate group only through a few sections. Therefore, the following outline is based on the fact that most of the relations and connections between the subsidiaries of a group, included the holding company, receive their regulation through specific individual terms of contracts.

1. Can the company in crisis should enter into new contracts or accept new goods without knowing she will have the money in the future to perform?
 - if the Group is in crisis or has already filed bankruptcy, the management conduct of each **subsidiary** (such as Zeus Italy) will be valued independently from the general business conduct of the entire group. Preventive measures and precautions will be taken into consideration and will be applied in accordance with the grade of financial difficulties each company is facing. As a matter of fact, if this financial difficulty is a temporary condition that can be easily over passed, then the company's directors may stipulate new contracts or accept new goods or services. A company even though has no liquidity may have a sufficient economic capacity which allows the company itself to continue its business conduct. On the contrary, if the company is facing serious economic distress, any stipulation of new contracts or the acceptance of goods or services during a crisis won't be considered a correct business conduct toward third parties who enter into contracts with the company.

2. At what point should the company in crisis stop the automatic sweep of money to the concentration account? Should the company create a reserve in its country?

It is necessary to understand at what title Zeus subsidiary's money are swept into a consolidated account, if it can be considered a contract, or articles of incorporation, or terms of contracts. For example, if this automatic sweep is considered an agreement between the subsidiary and the Holding, it is important to analyze the conditions of such agreement. In the event Zeus Italy stops giving the money to the Central Bank of New York, the single company will be considered responsible for the breach of the above contract. This default regards the single subsidiary involved that will be responsible for the violation of the agreement conditions. The consequences of such failure of performance are different depending on the kind of relation that has been established between the involved parties. In accordance with the Italian law, the subsidiary does not have any prohibition to create a reserve of money in its country unless it is not interdicted through the specific agreement above mentioned.

3. If Zeus Italy stops the automatic sweep of money to the concentration, the Italian company will be considered negligent for its misconduct. Remaining steady for what has been said in the general part, the Italian law does not regulate such phenomenon. Therefore, it is important to analyze the contract between the parties. As a contractual party Zeus Italy can sell product directly to an affiliate at an artificial low price only if this is authorized in the terms of contract agreed with the Holding.

4. If Zeus Italy stops the automatic sweep and other Zeus subsidiaries are harmed

- **Zeus Italy** (subsidiary company) will be responsible in a **contractual** way for having violated the terms of the eventual stipulated negotiation within the group. It would be interesting to verify the specific conditions of such agreement and understand for example if the holding company has made different contracts with each subsidiary or if the contract involves the entire group;
- The **directors** of Zeus Italy, will be responsible toward the shareholder or any third party who has suffered a loss as a direct result of the misconduct of these directors. Therefore, the damaged persons have the right to act against Zeus Italy's directors through a **tort** action in order to repaired the damage suffered. The harmed parties will have to prove that the damage suffered is considered a direct consequence of the misconduct of the Italian company directors.

5. If Zeus Italy will have to leave some creditors unpaid, it is not important if they are foreign creditors or local ones. In accordance with sec. 52 b.l. the bankruptcy proceeding opens the

concurrency of the creditors on the debtor's assets. The Court decision which declares bankruptcy gives to each creditor the right to participate, in accordance with their own credit, at the distribution of the proceeds obtained from the liquidation of the debtor's assets. The amount of each credit is valued at the moment of the bankruptcy declaration (sect. 55 b.l.). This concurrency is based on the *par condicio creditorum* standard in accordance to which once the bankruptcy is declared, the creditors cannot count on any individual action against the debtor's goods (sect. 51 b.l.). The *par condicio creditorum* has effects only toward the unsecured creditors (local or foreign). The secured creditors, whose claim is based on specific title such as pledge, mortgage, liens, will be satisfied for first and they will participate currently with the unsecured creditors only for the amount of credit which remains excluded for the first guarantee. It is necessary to underline that in accordance with such criteria, in the debtor's assets are included not only the goods which belong to the debtor at the time bankruptcy is filed, but also goods that don't belong anymore to the debtor at the time before bankruptcy was filed. For this reason, any sale/purchase made by the bankrupt company, within one year before the declaration of bankruptcy, will be subordinated to avoidance action. This action represents an instrument able to reorganize the debtor's assets in favour of all the creditors and may be filed only by the bankrupt receiver.

b) Liability

1. - If Zeus Italy does not handle this correctly and becomes insolvent, the Italian law provides that the company's interest will be guaranteed by the receiver. The receiver will have the power to file claims (in accordance with sect. 2393-2394) against the company's management, the internal auditing, the officers, and the liquidator, after the authorization of the judge and the consent of the creditors' committee. The judge may grant to the liquidator provisional remedies (art. 146 b.l.).
If an officer of Zeus Italy is not able to handle this correctly, any shareholder or third party who has suffered a loss as a direct result of the misconduct of the director, can file a claim against this latter in accordance with sect. 2395 of the Italian civil code.
2. The penalties are various and the directors and internal auditing of the subsidiary may go to jail.
3. In accordance with the Italian law, **INSOLVENCY** mostly refers to the entire economic situation of the debtor. A debtor is insolvent when he is not able anymore to regularly satisfies his duties. A default related to one single event does not represent an insolvency condition. This condition, as above described, becomes judicially prominent when it exteriorizes outside. It is therefore necessary an embodiment of the insolvency condition whose main example is represented by repeated defaults as a dangerous and serious evidence of the financial distress of the debtor. Insolvency is measured

through the examination of the involved company's balance sheet or can be easily verified when the company goes into default regarding any title which remains unpaid. Other examples are: the the escape or the fugitiveness, of the entrepreneur, the closing of his business premises, the stealing, the substitution or the fraud decrease of the assets (sec. 7 b.l.), swindle, ruinous sales of the company's goods.

c)Indemnity

1-2 in accordance with the Italian law there is no indemnity provided in favour of the subsidiary company. If a claim is filed against Zeus Italy by any unpaid party, the Zeus Parent will not indemnify the subsidiary. Zeus Italy has therefore no title to be indemnify for any wrongful acts.

3. The insurance may work in these kinds of damages. It is necessary to verify what kind of insurance the real responsible are entitled. The Italian law allows directors and the company to have an insurance for contractual liability, a second one for tort liability. It also possible to have an insurance on the single credit.