Department of Business and Management

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Top executive's compensation, a focus on Italian public listed companies

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Introduction

A popular assumption in economic thought is that cash is better than any good, implying that through it people are able to consume more and that cash is the principal means for exchanges.

Relating this assumption to the way firms structure the compensation and incentives of its managers, it might be argued that cash works at best to motivate and reward top executives.

However, most companies apply other remuneration and incentive schemes rather than cash, for instance equity based incentives or different types of bonuses such as fringe benefits.

Previous research tried to assess which kind of compensation system is the best to align the performance of the managers with the interests of the shareholders, leading to a higher firm performance. Most studies tried to view this problem under the principal agent framework.

The central premise of this framework, defined by Jensen and Meckling (1976), is that shareholders have not full knowledge of the daily activities of a firm and that managers, being in a position of trust by acting on behalf of the shareholders, might abuse their power to the detriment of the company.

This paper aims to provide insight into the impact of three different top executives' compensation systems (*fixed salary, variable compensation and fringe benefits*) on firm performance over a sample of Italian public listed companies in 2016 according to the agency theory perspective.

The first chapter has an introductive quality starting with the analysis of the main tasks of the board members and the potential conflict of interest that might arise. It follows illustrating the main structure and the different composition characteristics of the board of directors. Finally, it outlines the main characteristic of the board of directors' counterparty, the CEO.

The second chapter starts determining the general reward system applied to workers and follows analyzing the role of the remuneration committee as a guarantor for fair and attractive remuneration package for top executives. Lastly, a literal review is provided analyzing the impact of top executive's compensation on performance from an academic point of view.

The third chapter is the core of the research and consists of the formulation of the hypothesis and of the study and the analysis of the variables used for the regression and of the final discussion about the results found from the sample of firms.

This work provides an analysis of the Italian market that is not common in the literature.

1. Chapter: Importance of Board of Directors and CEO

1.1 Main Tasks

In the last decades the phenomenon of globalization has deeply affected society, economy, business life and environment in many different ways.

Globalization brought to an increased competition, for instance, affecting target market, product and services, technological development, cost and price and quick response to global changes. Globalization enabled customers to have a broader choice in the market and affected their behaviors. Customers aim to obtain goods and services quickly and in a more efficient way than before, expecting higher quality and lower prices.

A company has to be ready to adapt price, product and service to customer's needs in order to accomplish demand on the international market.

Therefore, the board of directors plays a vital role in the company's success to guide and adapt the company's objectives. It is the highest decision authority, that supervises and controls firm's management and protects shareholders' interests. The primary concern for shareholders is that the capital invested will generate enough returns. The board of directors, on behalf of the shareholders, sets up an effective governance structure by balancing the interests of its different beneficiaries including customers, staff, investors and local societies.

The board must be entrepreneurial and lead the firm ahead while simultaneously keeping it under careful control. It has to be sensitive to short-term pressure and be ready to take due account of long-term trends. Constantly monitoring the external operating environment, it assesses the current and future strengths, weaknesses and risks relating to the company. In this way, the board of directors ensures that the organizational strategic directions remain both appropriate and achievable. Furthermore, the board of directors establishes and protects the company's vision, mission, and values. This is of utmost importance, since the board of directors must grant that the company operates in line with them. It shall form the basis for planning, monitoring and reviewing all activities, expenditures, policies and decision making. The board of directors has to be familiar with the vision, mission, and values of the company and ready to review these in the light of current and impending circumstances.

Generally speaking, a Mission statement answers the following questions:

- What do we do?
- Whom do we serve?
- How do we serve them?

It points out the core business of the company, setting a strong mission statement and adjusting the objectives to the company's culture, leading the team to accomplish the set goals. On the flip side, a weak mission can generate unmotivated feelings, resulting in an opposite effect. For instance, the mission statement of Ferrari is the following: “We build cars, symbols of Italian excellence the world over, and we do so to win on both road and track. Unique creations that fuel the Prancing Horse legend and generate a “World of Dreams and Emotions” ”[1].

Instead, the vision statement gives the company direction, responding to the following questions:

- What are our dreams and ambitions?
- What issue are we solving for a better good?
- Who and what are we addressing to change?

By setting a visioning, it conveys aspiration to the company’s employees, stimulating internal and external growth. This, in turn, boosts innovation and helps the team to concentrate on the real interest of the company. For example, the vision of Samsung states: “Inspire the world. Create the future”[2].

Finally, the values can be regarded as the company’s fundamentals, the pillars of the organization inspiring its action. As the president of Calzedonia Group Sandro Veronesi says to its employees: “In life as in work we must be actors and not spectators”[3].

The board of directors is faced continuously by challenges and responsibilities.

[1] http://corporate.ferrari.com/en/about-us/ferrari-dna
[2] https://www.samsung.com/us/aboutsamsung/vision/vision2020/
[3] http://www.businesspeople.it/People/Protagonisti/Chi-e-Sandro-Veronesi-mr-Calzedonia-103862

1.2 Conflict of Interest

Speaking of the tasks of the board of directors, it is necessary to shed some light on the possible drawbacks that might arise.

In particular, as they are in a position of trust, by managing the company on behalf of the shareholders, they might take advantage of their job to make a profit to the detriment of the company and the shareholders. This kind of behavior could trigger a conflict of interests, for instance when a board member acquires confidential information and uses it for personal purposes or, to put it differently, when a board member or a close relative draw a financial advantage from any business, dealing or service of the organization.

The company's rules should be established in such a way that directors can exercise their power freely without abusing them.

The board is bound to lead the organization according to law and observing moral principles to serve the interests of the company and of the shareholders. They must act honestly and in good faith in exercising their responsibilities towards the company's best interests.

Furthermore, board members should always demonstrate an ethical behavior according to their responsibilities in the company.

They must not misuse critical information obtained through their position to take advantage directly, indirectly, for personal purposes or third parties.

This issue can be better pictured by considering a scandal that broke out in December 2001, the collapse of the Texan Giant American corporation Enron.

The history of the Enron group is one of the most iconic events of the excesses of American capitalism of the 1990s. Traditionally born as an energy producer, the group began progressively to strategically diversify its business in investing almost in all energy sectors, but above all in brokerage, trading, and finance. Enron became the world's largest intermediary supplier of oil, gas and electricity becoming a trader of energy derivative contracts, hedging the risk and speculating on indices and future trends in energy prices. Through its high knowledge of the web and its mastery of new technologies, Enron turned to almost a self-sufficient Energy Exchange where world demand and supply met, and prices were formed. In few years Enron had become a myth, as its stock market capitalization was being studied and exalted as a model, for inventing a mostly new and highly sophisticated business.

Enron went bankrupt in few weeks, due to a ruthless management that for many years rigged the budgets and hid a mountain of debt, particularly using a market to market accounting method, that involves accounting assets and liabilities at its current market values.

This type of mechanism allowed Enron to calculate revenues from long-term contracts and register them as immediate profits, without being sure if they were ever recovered. More specifically, in late 2001 when the company was under investigation by the SEC (Securities and Exchange Commission), it came out that the company had overestimated the earnings for the past four years by $586 million[4].

Enron political implications with the White House by financing the Bush 2000 campaign in exchange of consideration also emerged.

In the same time span, another scandal broke out in Italy, concerning the listed Italian company Parmalat.

Parmalat was founded by Calisto Tanzi in 1961, close to the city of Parma, in northern Italy. The family business grew exceptionally in the following years, to become one of the most significant food and dairy companies in Italy and a multinational company operating in 2003, when the scandal burst out, in 48 different countries through 214 subsidiaries.

According to PwC, the last reviewer of Parmalat's financial reports before the crisis, the company made false statement on its balance sheet since 1990 until 2003. In twelve of those thirteen years, Parmalat experienced considerable losses and the fraud started to cover the losses of a South American subsidiary. Instead of concentrating on the organizational problems or revising their strategic decisions, the management deliberately tried to camouflage the company's failures through fraud and conspiracy. During this period the company's executive adopted multiple tactics to extend the scam. Specifically, they overstated revenues by forming fictitious transactions through a double-billing scheme using receivables as guarantee dealing with the banks. They recorded fictitious assets to improve their reported assets.

The turning point of the Parmalat crisis was in November 2003, when the previous reviewer Deloitte & Touch refused to approve the half-year financial statement. One month later, Parmalat declared to be insolvent and went under extraordinary administration procedures. At the end of December 2003 Calisto Tanzi was indicted for fraud, arrested and sentenced in 2010 to eighteen years in prison[5]. In 2005 the new Parmalat S.p.a was quoted on the Milan Stock Exchange together with sixteen companies of the old Parmalat Group. Since July 2011 Parmalat has been controlled by the Lactalis Group, which at the time of the takeover held approximately 83% of the share capital[6].

[4] Weitz, E. et.al,2004," Misbehavior in Organization: Theory Research, and Management," Lawrence Erlbaum Associates, p.212-15
[5] Rimkus, R.,2016, "Financial Scandals, Scoundrels & Crises: Parmalat", econcrises
[6] http://www.parmalat.com/it/il_gruppo/storia/storia_di_parmalat/

A more recent scandal that its worth to be considered is the one concerning the German automobile manufacturer Volkswagen.
The issue was raised in 2013 when the researchers of West Virginia University and the International Council on Clean Transportation observed discrepancies between nitrogen oxide emissions (NOX) measured by Volkswagen vehicles on the road and in lab tests.
In May 2014 also the Environmental Protection Agency (EPA) began an investigation and confirmed that VW vehicles were found to violate the Clean Air Act.
In September 2015 VW admitted that since 2009 it had deliberately placed "defeat devices" in nearly 600.000 vehicles sold in the US with the intent of making the emission control test ineffective[7].
As soon as the scandal went public, the CEO Martin Winterkorn resigned, and his place was taken by the head of the sister brand Porsche Matthias Mueller. In October 2016 the US court settled a $15bn fine to VW.[8]

[7] Legget, T., 2018, "How VW tried to cover up the emission scandal," BBC News Business
[8] Dean, S., 2017," Volkswagen hit with further €2.5bn charge over 'dieselgate' scandal - taking total damages to more than €25bn", The Telegraph Business

1.3 Corporate Governance

Corporate governance is widely seen as tracking the rights and responsibilities of the company's major shareholders and it setting out the rules and procedures in corporate business decisions.

Alternatively, it can be seen as "the design of institutions and mechanism that induce or control board directors and management to best serve the interests of shareholders and other stakeholders in a company and to resolve conflicts among them, subject to the constraints of economic legal and ethical norm"[9].

Good corporate governance maximizes shareholder value and companies' productivity.

It can differ by country due to legal, economic and social factors mirroring the specific economic system and corporate traditions. For instance, there is a distinction between civil and common law countries.

The first is usually characterized by a dualistic model, or two-tier system, where the shareholders appoint a supervisory board, which ensures that the company is managed according to the company's by-laws and laws. Subsequently, the supervisory board selects a controlling body, the management board, which is responsible for the day-by-day management.

There is a neat distinction between the two control bodies, which operate alongside without imposing each other's binding commands.

Interdependence is a leading structural weakness of dualistic board structure. The management board submits its strategic decisions to the supervisory board for approval, but the latter is not involved in the decision making. This interdependence can be detrimental to the quality of control, leading to mistakes due to the poor communication between the boards and the unclear responsibilities of the board members. Moreover, it might be that some members of the supervisory board are part of the management board of other companies (interlocking directorates), likewise limiting the quality of control. On the other hand, including board members external to the company enables them to be more independent in representing shareholders' interests and more objective in analyzing the business. This type of governance is usually applied in countries such as Germany, Austria, and France.

In common law countries, such as UK and US, the most popular governance structure is the one-tier system, or monistic model. It follows almost the same logic as the two-tier one, but it concentrates the management and supervisory functions in one body.

This provides significant advantages for the members of the board of directors performing supervisory functions, enabling them to have full knowledge about the daily business of the company.

[9] W.Lin, T., 2004

Though it could rise some issues about independence and separation of responsibilities. For instance, the CEO might also be the chairman of the board, making it difficult to have a proper separation of powers in the boardroom and to run it effectively.

However, another aspect to be considered is that the decision-making process is far quicker and faster to put in practice since no approval is needed from another body.

Mention is due to the Chinese corporate governance system, with its high degree of state ownership concentration. Over the past several years the Chinese tried to align with the western style corporate governance mechanism, but the policies created remained weak.

One aspect is related to the absolute control of the state, which significantly influences the management of the company. Around two-thirds of the companies listed in the Chinese stock market are state-owned. As suggested by Conyon and He (2011), that the stock ownership in China follows two different patterns. One is related to State-owned shares, controlled by government agencies. Another is linked to the ownership of legal entities, obtained through both state-controlled and privately controlled legal persons. Lastly, shares can be owned by private organizations, institutions, and individuals.

In case a government-owned business is listed, a minimum share is sold in the IPO process to private investors. The government and parent owned government businesses control the majority of the shares, obtaining a high degree of voting rights, influencing the running of the business. The authors argue that usually, the largest shareholder controls approximately 43% of the company's shares, the second about 9% and the third roughly 4%[10].

The role of independent directors in China is quite questionable, since the state nominates and removes directors and supervisors alike. Due to the high degree of State ownership, the chosen independent directors can be viewed as a symbolic figure. As Zheng (2003) argues, supervisors are typically nominated by either company's personnel or previous communist cadres in government-owned businesses, leading as a result to a potential conflict of interests[11].

Indeed, insider trading is another major issue in Chinese corporate governance. In general, in the 1990's there was a boom in insider trading, becoming a hugely debated topic at a global level. One of the first cases, undertaken in 1993 by the Chinese Regulatory Commission (CSR), was an investigation into the share deal by the Xiangfan Investment Company of Chinese Agricultural Bank ("Xiangfan Shangzhen"). The investigation revealed that Xiangfan Shangzhen had a business meeting with another company in the Health Care business and they became aware that the latter company was about to purchase a significant amount of shares of another joint stock company. As a consequence, Xiangfan Shangzhen bought a substantial amount of shares of this joint stock company,

[10] Conyon, M.J. et.al, 2011
[11] Kang, Y. et.al., 2008

around 627,000, and later sold them for a profit of more than 16 million yuan. The CSRC revealed that Xiangfan Shangzhen had committed insider trading[12].

As a result, China and many other countries adopted laws to limit the insider trading trend, changing stock markets regulations significantly by the year 2000[13]. Another motivation for China to do so was its exceptional economic growth and its membership in the World Trade Organization in December 2001, becoming an increasingly attractive investment decision[14].

The main rules on Insider Trading in China are provided by the Security Law of July 1999, sharing many norms of the US regulation. The central controlling body is the CSRC, that regulates the exchanges and is responsible for the application of insider trading provisions[15].

However, Chinese trading law focuses on the major trading situations and sets the corresponding liability to those that abuse of trading information's to their advantage. For instance, Article 67 of the Securities Law forbids people in possession of inside information for trading securities to use such inside knowledge. Article 68 identifies the supposed holders of such information as the directors, supervisors and shareholders that own more than 5% of companies shares, or senior management that issues shares or corporate bonds.

Also employees can be insiders if they have obtained inside information concerning their job[16]. In particular, article 75 further specifies insider information as any confidential information that may put pressure on the shares price, for instance, utilizing restructuring, M&A, dividend announcements, abnormal earnings or changes in the board of directors. Anybody involved and found guilty in insider dealings has to pay the government a fine up to three times the profit made. The Criminal Law in China extends this by sentencing inside dealers up to ten years in prison.

Furthermore, in December 2002, in order to identify more effectively illegal inside trading, the CSRC established the Administration of Disclosure of Information on the Change of Shareholdings in Listed Companies, forcing shareholders with a majority of 5% ownership of the company to declare their interests in due time. Subsequently, the stock exchange shares the information on his web platform.

Despite the enormous effort of the CSRC and other regulatory authorities in 2009, the Shanghai and Shenzhen Stock exchange revealed 45 and 39 enforcement actions, specifically, against violations of corporate insiders' transaction for instance in trading ban periods or swing transactions.

Moreover, as the Chinese court system does not permit investors to file a private lawsuit against insider traders, present sanctions like fines, professional discharges or criticism are not enough to avoid insider misbehavior[17].

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[12] Huang, H., 2007
[13] ibidem
[14] https://www.wto.org/english/thewto_e/countries_e/china_e.htm
[15] He, Q. et.al, 2014
[16] Huang, H., 2005
[17] He, Q. et al., 2014

Another major issue in Chinese corporate governance is the fraudulent financial reporting. The central notion of corporate financial fraud was defined in the Provisional Measures on Prohibition of Securities Fraud in 1993, and it encoded the first rules for financial fraud in the first national securities law in 1998. One of the first scandals in corporate financial fraud was the one related to the DaMing group, which misstated the firm's listed outstanding shares by omitting crucial material information and by falsifying the initial public offering prospectus statement in 1996, resulting in a sanction of 2 million yuan. One of the most critical cases that marked the first criminal sanctions against senior management of public listed companies was that of Hainan Minyuan Modern Agricultural Company in 1998. The company's administration ruthlessly manipulated financial accounts by 1.2 billion yuan[18].

Besides these issues, there is a positive future trend in corporate governance developments in China. Chinese listed companies entering into overseas markets improved the transparency and accountability of their corporate governance practices.

[18] Yiu, D.W. et al., 2018

1.4 Board of Directors' Characteristics Component

The company's success is based not only on his governance and good performance, but also on the board of director's effectiveness and characteristics. The formation of a good board strengths the firm's decision-making and may improve the firm's capabilities.

This topic was largely debated in the existing literature resulting in different views.

The main variables under examination are the size of the board and the proportion of independent and dependent directors.

Furthermore, a great effort has been made to analyze the impact of diversity (gender, cognitive factors) on the board composition.

Beginning with the size, some researchers see an adverse correlation between the board size and the financial performance of a company. As suggested in such studies, the bigger the size of the group, the greater communication, and coordination problems are. Therefore the ability of the group to control the management decrease[19].

Small boards are likely to have a better communication system, enabling a quicker internal decision-making process and making it easier to solve agency problems.

The opponents of this theory notice that larger boards allow different opinions effect, bringing more thought and expertise into the company, reducing the likelihood of accepting bad projects. Moreover, in the effort of compromising different opinions, large boards are less risk-taking.

The above comparison suggests that none of the two board sizes is optimal. Some researchers, Coles, Daniel & Naveen (2008), consider the size of the board as a black and white issue, depicting it as a U-shaped form relationship: effective boards are either small or large. Specifically, they analyzed the relationship between board size and firm performance measured by Tobin's Q performance indicator. This relationship derives from the differences between simple and complex firms. This denomination of two distinctive firms is determined by unobserved complexity factor of a firm such as diversification, firm size, and leverage by using the method of factor analysis. Factor analysis is a system used to reduce a great number of variables observed by grouping them into an index of common factors.

As a result, companies showing a higher than average degree of complexity are named "complex," whereas those under the average are named "simple." Based on their analysis they suggest that simple company's, needing less advice than complex ones, have smaller boards with less outside directors. Indeed, Tobin's Q varies according to the board size decreasing in simple companies and increasing in complex companies. It is also influenced by the number of outside directors.

[19] Sahin, K. et.al, 2011

The authors also detected a weak indication that companies with a high degree of R&D, which attach particular significance to the firm's special know-how, result in a higher proportion of inside members of the boards[20]. Nevertheless, it is at the discretion of the company to choose the best size for the board. The analysis moves on to the board independence factor.

Independent directors are those members of the company that do not have any material relationship with it and are chosen following the shareholder's interest. Their role is to monitor the company and participate in the decision making if they are asked to.

Empirically, the effect of board independence on performance is mixed. One part of the academic research suggests that there is a positive statistically significant relationship between the two variables: the greater the independence of board member is, the better financial decisions are taken, translating into a greater performance. On the other hand, some researchers found no empirical results of such relationship and indicated a negative correlation between independent board members and firm performance.

It shall be mentioned that this somewhat mixed empirical results may be influenced in part by the different governance mechanism (one or two-tier system) existing in the analyzed countries. For instance, a monistic structure may benefit of additional independent directors in the decision making, whereas in the dualistic system they can be viewed as unnecessary.

However, the actual trend is to make the board as independent as possible. Essentially, independent members, coming from different professional backgrounds bring diversity and a different knowledge, allowing transparency, higher accountability and improving corporate governance mechanisms[21].

Concerning diversity, another topic is worth to be mentioned.

Generally speaking, diversity can be split into observable (gender, race, and ethnicity) and non-observable (knowledge, education, values, perception, affection and personality characteristics) variables[22].

Moreover, the world's community is demographically and cognitively diverse, therefore
the company's attempt to build a diversified boardroom can be viewed from the outside as an effort to tackle discrimination and as an open-minded approach.

In the light of this, organizations can exploit distinctive capabilities such as innovation, creativity, a better understanding of the marketplace, leading to a higher global network.

For this reason, nowadays a person with a high degree of cognitive factors is regarded very positively by firms because it can bring that unique added value that companies seek.

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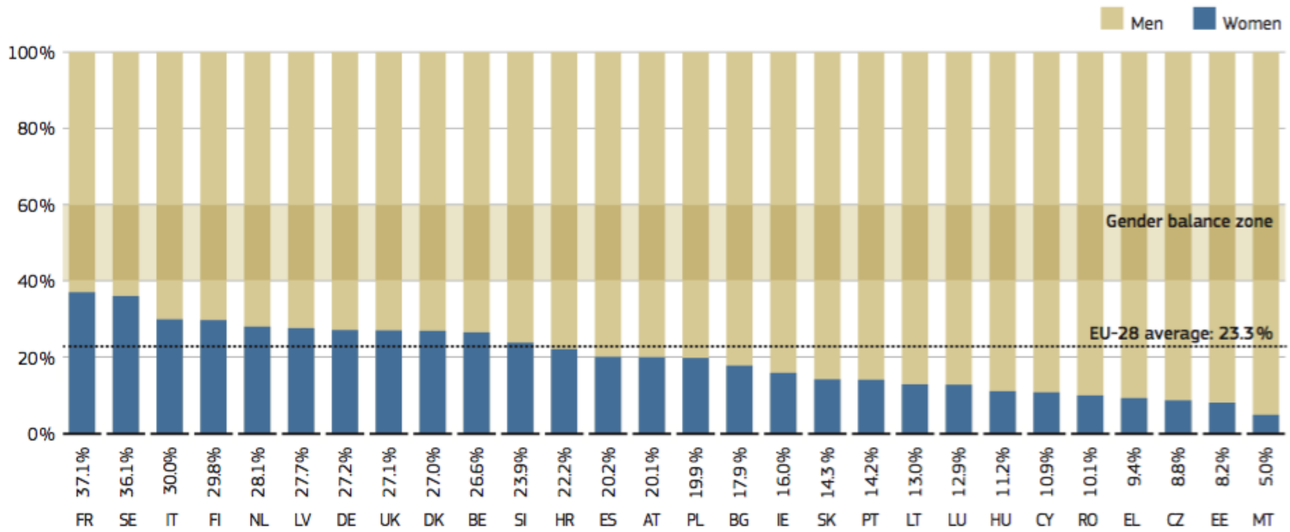
[20] Coles, J.L. et.al, 2008
[21] Veklenko, K., 2016
[22] Navjeet, S., 2018

After all, a right balance of diversity should be maintained. Otherwise, it can contribute to communication breakdown and lack of cooperation between Board members, due to different ethical backgrounds.

Despite this, in the recent years, a lot of effort has been made to increase the presence of women as board members, so gender diversity has become an issue. Most academics see gender diversity as a positive influencer in the decision-making process, transferring values and attitudes that create a more different debate, a more significant number of alternatives and a better quality of ideas. Furthermore, women tend to be more interpersonally oriented than men, more compassionate and focused on developing interpersonal relationships. Equally important, the presence of women on the board shows an increased commitment to corporate social responsibility, providing a signal that a firm agrees with regulations, embraces diversity and has appropriate working conditions without gender discrimination and is therefore socially responsible.

For instance, at European level, the ratio of women to men on the board of the biggest listed firms is still deficient. The figure 1.1 below displays this issue.

Figure 1.1- Representation of women and men on the boards of large listed companies in the EU, April 2016



Source: European Commission, Database on women and men in decision making

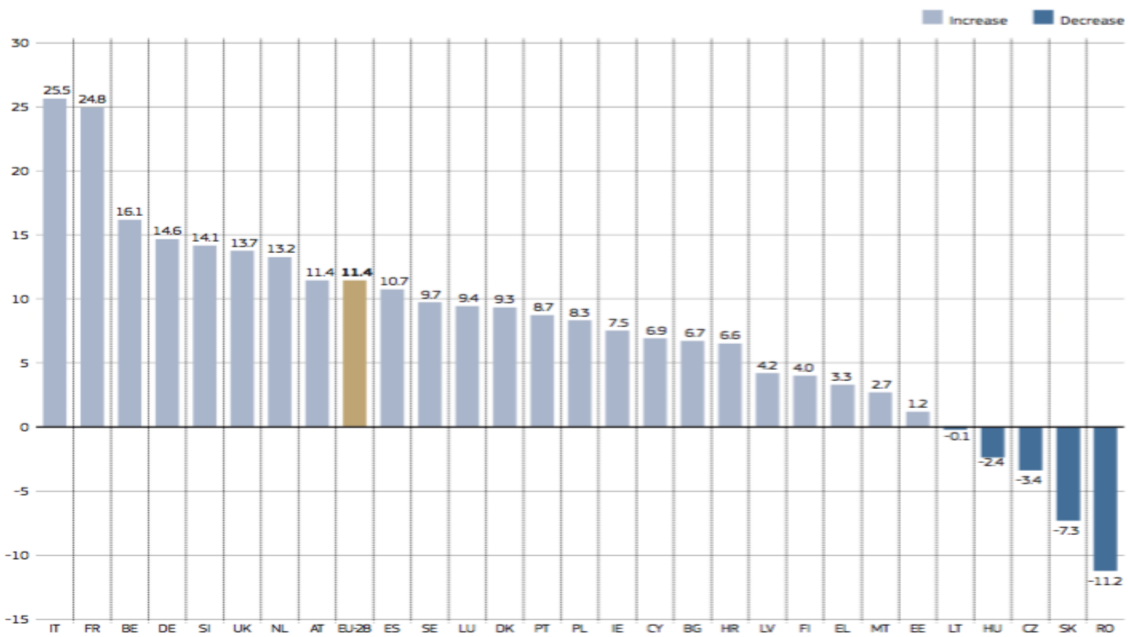
From the chart, we can see that on average in 2016 the presence of women on the committees of large listed companies in the EU amounts to 23.3%, marking a considerable improvement of 11,9% since 2010, when the EU commission put the issue on his political agenda[23].

[23] Jourová, V., 2016

The highest share of women on boards is mainly visible in ten countries, accounting for at least a quarter of board members. Beginning in France with a 37.1% quote and ending up in Belgium with 26.6%.

However, more needs to be done to have gender balance, especially in those countries that have very low female shares, such as the Czech Republic, Romania, Hungary and Montenegro which are below 10%. For this reason, the EU commission in November 2012 proposed a Directive aimed to accelerate the progress of gender balance by setting a 40% female share as non-executive directors of the biggest listed companies by 2020. Over the period of October 2010 and April 2016, the degree of females on boards grew in 23 out of 28 Members States. From the figure 1.2, we can grasp this change.

Figure 1.2- Change in the share of women on boards of largest companies, EU-28, October 2010-April 2016 in percentage points (pp)



Source: European Commission, Database on women and men in decision making

In particular, countries like Italy and France registered a dramatic growth in percentage points reaching 25pp. However, countries like the Netherlands, Germany, Belgium, Slovenia and the UK, which is going to exit EU in March 2019, reached important levels that ranged from 11.5 to 16 pp. The majority of countries that have taken legislative action registered significant improvements having an intensive public debate on the issue.

Indeed, considering Italy, the Italian government issued the legislative decree n.120/2011 also known as "Golfo Mosca Law" which established in 2012 that the boards of the Italian public listed companies should include at least one-fifth and, from 2015, one-third of women until 2022, when the law will expire[24]. With the law becoming effective in August 2012 a significant increase in the women's share in Italian public listed companies began, also where both genders were already present.

Especially compelling evidence of this emerges from a paper of Pastore and Tommaso (2016) investigating whether imposing gender quotas in the management and supervisory board has been successful in reducing disparities in Italian public listed companies.

Specifically, the paper analyzes the structure of Italian public listed companies' boards over the period 2008 to 2014 including June 2015.

The study, based on Consob data, as highlighted in the following table, shows that female ratio on boards committee of publicly listed companies has increased notably.

Table 1.3- Female representation on corporate boards of Italian listed companies

Listed companies		*Listed companies where at least one female director sits on the board*		*Board seats held by women*	
*Year**	*no.*	*no.*	*Weight on total number of listed companies*	*no.*	*Weight on total number of board seats*
2008	288	126	43.8	170	5.9
2009	278	129	46.4	173	6.3
2010	268	133	49.6	182	6.8
2011	261	135	51.7	193	7.4
2012	253	169	66.8	288	11.6
2013	242	202	83.5	421	17.8
2014	243	217	91.9	521	22.7
*2015**	235	232	98.7	621	27.6

** end of June 2015.*

Source: Author's elaborations on Consob data (Report on corporate governance of Italian listed companies several years)

As we can see, from 2011 to July 2015 the share of women on boards rose significantly respectively from 51.7% to 98.7% and 7.4% to 27.6%.

A further aspect is the presence of women holding executive positions in Italian listed companies from 2013 to the end of June 2015, highlighted by the next table.

[24] Solimene, S. et.al,2017

Table 1.4- Positions held by female directors in Italian listed companies at the end of June 2015

Positions	2015		2014		2013	
	Female directors	*Listed companies where at least one female director sits on the board*	*Female directors*	*Listed companies where at least one female director sits on the board*	*Female directors*	*Listed companies where at least one female director sits on the board*
	no. of directors *(Weight on board seats held by women)*	no. of companies *(% market cap)*	no. of directors *(Weight on board seats held by women)*	no. of companies *(% market cap)*	no. of directors *(Weight on board seats held by women)*	no. of companies *(% market cap)*
CEO	16 (2.6)	16 (0.9)	16 *(3.1)*	15 *(1.0)*	13 *(3.2)*	12 *(0.7)*
Chairman or honorary chairman	17 (2.7)	16 (22.1)	16 *(3.1)*	15 *(27.5)*	10 *(2.5)*	9 *(0.4)*
Deputy chairman or member of the executive committee	36 (5.8)	34 (9.6)	32 *(6.1)*	32 *(7.5)*	33 *(8.1)*	33 *(8.2)*
Independent director	424 (68.3)	199 (98.3)	333 *(64.0)*	168 *(93.5)*	244 *(59.8)*	138 *(63.1)*
Minority director	42 (6.8)	34 (58.0)	37 *(7.1)*	32 *(58.9)*	20 *(4.9)*	18 *(26.9)*

Source: Author’s elaborations on Consob data (Report on corporate governance of Italian listed companies several years)

According to the authors’ analysis, in June 2015, only 2.6 % (down from 3.2% in 2013) of female on boards were in CEO position in sixteen firms, accounting for 0.9% of total market capitalization. Moreover, the positions in which the female presence increased substantially were those of independent director and minority director.

In the first case the increase was dramatic, from 244 women holding the position in 2013 to 424 in June 2015, and their weight on board changed from 59.8% in 2013 to 68.3% in June 2015.

Similarly, the number of female minority directors doubled from 20 women (equal to 4.9%) in 2013 to 42 (equivalent to 6.8%) in June 2015.

Women hold mainly non-executive positions in public listed companies, generally as independent directors.

In the final analysis, the authors are questioning whether this temporary provision will be enough to achieve the objective of removing gender diversity barriers in public listed companies.

According to them, the appointment of women in a board's must mirror the true aim of the firm to become gender diverse and more effective, rather than being a symbolic means to enhance corporate reputation and image[25].

All in all, the participation of women on boards has become a hugely debated issue at EU and corporate level.

[25] Pastore, P. et.al.,2016

1.5 CEO Characteristics

After discussing the board composition characteristics, it is necessary to shed some lights on the significant counterpart of the board, the CEO.

The CEO is accountable for the whole management of a firm and usually designated by the shareholders and the board of directors. In smaller companies, the CEO deals often with the everyday tasks of the business. In larger public listed companies, the CEO plays a leadership and policy role without being involved in daily operations. It sets the company standards and general development plans, leading managers and directors to implement them. Consequently, the CEO must choose executives apt to realize those plans developing an effective and efficient communication with them. In particular, another aspect of CEO's role in small and large companies is the distinctive engagement in transformational leadership. The transformational leadership refers to the CEO qualities of charisma, inspirational motivation, intellectual stimulation, and individual consideration. The first quality displays CEO's capacity to shape and to give an attractive vision for the time to come and to deliver to his associates emotional arguments to enhance loyalty, trust, enthusiasm, pride, and respect. The second quality reflects CEO's ability to stimulate collaborators by establishing high expectations and giving reassurance that obstacles can be overcome. The third one focuses on the CEO's efficiency in stimulating colleagues to see problems from a new perspective, by challenging assumptions and not taking them as given. Moreover, the fourth points out the CEO's ability to enhance workers progress by giving coaching support and encouragement.

Previous studies tried to assess the transformational leadership of CEOs in sizeable organizational contexts finding no influence on firm performance in large companies (Agle et al., 2006; Tosi et al., 2004)[26].

Ling et al (2008) found instead a significant relationship in small-medium-sized enterprises (SME). They argue that in SME CEOs enjoy more managerial freedom, they are mainly more empowered and also able to empower. On the contrary, in larger companies' CEOs may limit their discretion to justify their actions to an active governing board and have a more evaluative role, assessing the achievements of corporate manager's divisions and allocating capital and change managers correspondingly. Without such restrictions, the CEO is more free in the implementation of the company's strategy and takes more direct part in the day by day implementation of those strategies. The CEO enjoys a more significant opportunity to install individual commitment and building high expectations by encouraging more innovative ideas in employee's minds.

[26] Ling, Y. et.al, 2008

Furthermore, provided that the SME context is structurally less complex and increases role opacity, in an SME the CEO may be a reference point for the workers seeking illumination and encouragement.

Nevertheless, the authors also suggest that transformational CEOs in SME are influenced to some extent by firm size, CEO founder status (founder or non-founder) and CEO tenure.

Doing so, they associate their analysis from a theoretical perspective to the debate between population ecologists and upper echelon theory. According to the population ecology theory the CEO's role is merely an organizational assignment that does not impact firm performance, while environmental factors do play a significant role (Hannan & Freeman, 1984; Meindl & Ehlrich, 1987). The upper echelon theory by D.C. Hambrick et al (1984) initially stated that "organizational outcomes-strategic choices and performance levels-are partially predicted by managerial background characteristics"[27] and was revised by Hambrick in 1994: "the executives' experiences, values, and personalities greatly influence their interpretations of the situations they face and, in turn, affect their choices"[28].

Specifically, associating the latter definition of Hambrick with the three aspects mentioned before, we find support to this new view. The authors suggest that transformational leadership may be limited by company size, with a more significant impact on SMEs than on larger companies.

Moreover, the study shows that the CEO founder status has a notable effect on SMEs; founder CEO was transformational, having a more significant impact than non-founder CEO on firm performance. When CEOs are also founders, they can better imprint their leadership style and succeed in making employees identify themselves with these values, obtaining a stronger affiliation.

Similarly, another study made by Wang, H et.al (2010) tried to assess the CEO characteristics during a period of instability, specifically in China, where traditional firms are faced with new corporate transformations as well as an increase of new entrepreneurial companies. In this context of uncertainty, companies need a leader with the managerial freedom and ability to affect the firm's outcomes. Moreover, leaders in China are seen by company's employees with full respect and attach great values to it, being the top authority and primary decision maker of the company.

The final results of this study, based on Western literature, suggest mainly two types of CEO leadership behaviors in the Chinese environment. The first is related to task-focused CEO leadership behaviors, where CEO articulates the vision, monitors operation and being creative and risk-taking affecting directly firm performance. The second relationship-focused behavior reflects CEO ability to be both authoritative and benevolent, establishing a direct relation with the employees' indirectly influencing the company's performance.

[27] Hambrick, D.C. et.al, 1984
[28] Hambrick, D.C et.al, 1994

This result supports the primary hypothesis of the authors that a high company's performances can be obtained when CEOs focusing on both task performances in a direct way and encourage constructive mindset in workers via relationship-oriented behaviors.

Previous studies inquired other aspects of CEO qualities, linking the organizational features with the background qualities of the new CEOs.

The main argument was that firms display different operating features in distinctive contexts and employ top managers with different circumstances and skills. It follows that the CEO succession outcomes may depend on the prior conditions found in organizations. The paper of Datta, D.K. et.al (1994), investigates whether a positive relationship exists within a set of prior organizational successions such as firm growth, profitability, and R&D intensity and selected CEO characteristics, for instance, insider/ outsider functional experience and educational level.

This inquiry was based on 195 succession events reported in Business Week concerning 1000 US firms in the years 1980-1989.

The decision to hire an internal or an external CEO may be influenced by the firm's objective to realize particular performance outcomes.

An insider CEO is more familiar with firm's products/market and operating procedures. Hiring an insider CEO yields firm-specific benefits, such as reduced costs in acquiring firm-specific knowledge. On the other side a long permanence of members in an organization, to reduce the chance of developing original ideas to respond to with new realities. It follows that insider CEO may have a limited perspective if they have already spent an entire career within the same organization.

The authors categorized as insider CEOs the subjects staying more than 5 years in an organization. Hiring an external CEO may have instead an emblematic value, conveying to the company's members the idea that an organizational change is about to come. Firms that experience lower profitability may indeed rely on outsider CEO in order to give a new imprint to the company's strategy. This hypothesis has been confirmed in the final results of the study, suggesting that there is a strong relationship between poor performance companies and the desire to hire outside CEOs. To be more specific, firms do not price and award firm-specific knowledge in a situation of low performance.

Furthermore, the conclusions of the study that the view of R&D quality is linked in a positive relation to hiring CEOs with a high degree of education and specific experience in technical, functional areas.

A study by Roth, K. (1995) went a step further, analyzing the ideal CEO characteristics in medium-sized firms with a predominant presence in the international context. Moreover, the author conceptualizes the managing of international interdependence under the resource-based view framework.

The resource-based view sees the company as a collection of heterogeneous resources, tangible and intangible. Defined as internal resources, managers can use a set of criteria to assess the quality of resources and their potential to generate superior returns under the Value Rarity Imitability Organization framework. Only in presence of these four requirements it's possible to produce above-average returns for an extended period. The value of a resource is assessed by the ability of the resource itself to create value by generating revenues. The rarity and imitability factor refers to the degree by which competitors try to appropriate the resource and therefore to imitate a firm's competitive advantage. Lastly, the organization has to be able to integrate and exploit the resource with its structure and management systems. The resource-based view evolves into the capability-based view, because when a company puts resources together, this translates into a capability for the firm, that is the ability to combine resources and produce an extra value.

The firm's CEO will presumably influence the management, directing resources and combining them to create extra value in an international firm. Notably, international firms have operations and resources stocks in different countries. According to this study stocks in different areas have to be in some way connected or integrated, to exploit the maximum returns from the international accumulation of intangible and tangible assets. The author emphasizes the concept that an international firm is not a multinational collection of independent resources stocks, but rather an interdependent, geographically dispersed, resource stock.

The management of this related international interdependence is centralized in the hands of a firm's CEO by influencing the company's performance. Specifically, the relationship between the distinctive characteristics of a CEO and a company's performance is supposed to be related to the degree of a company's international interdependence.

As a firm grows internationally more interdependent, it needs to boost its information process capacity. Thus, according to the author, the CEO plays a significant role in the creation of lateral processes to sustain a large amount of information processing. A CEO must be internationally networked in order to improve the international communication mechanism. An intuitive CEO will manage international interdependence better, dealing with problems in their whole complexity, seeing integrate meanings and relationships, rather than single details. Moreover, the external environment shows cultural, regulatory, language and operational differences and a global approach imposes the selection of Intermarket segments in which well defined, similar groups of customers exist across national borders.

2. Chapter: Reward Management and Executives literal review

2.1 Reward system

Reward management sets out the guidelines, strategies, and procedures needed to make sure that the input of company's employees is assessed as both in financial and non-financial levels.

The primary purpose is not only to compensate workers correctly, evenly and coherently, according to the value they provide to the company, but also to enhance their involvement and their dedication by developing a high-performing work culture that helps the company to attract and retain the best employees. Reward management does not only concern employees' benefits and pay, it involves ”non-financial rewards such as recognition, learning and development opportunities and increased job responsibilities”[29]. The management of reward is an integral component of the Human Resource Management approach to managing people.

Moreover, internal and external factors can considerably influence the reward strategy and policies of a company. The first ones can refer to the corporate culture, that is to the core shared values, norms and attitudes, which impact the company's record on items such as care and consideration for people, equal treatment between employees and stakeholders, equal opportunity or social responsibility and teamwork.

Equally important, the adopted technology may require different skills and a workforce with distinctive capabilities to align with the business goal and strategy.

Reward policies and strategies may be influenced also by external factors such as globalization, increased competition or governments interventions. Referring to government interventions, the UK introduced a National Minimum Wage and the Transfer of Undertakings (protection of employment) in order to preserve the continuity of work and “the terms and conditions of those employees who are transferred to a new employer (except for certain occupational pension rights)”[30].

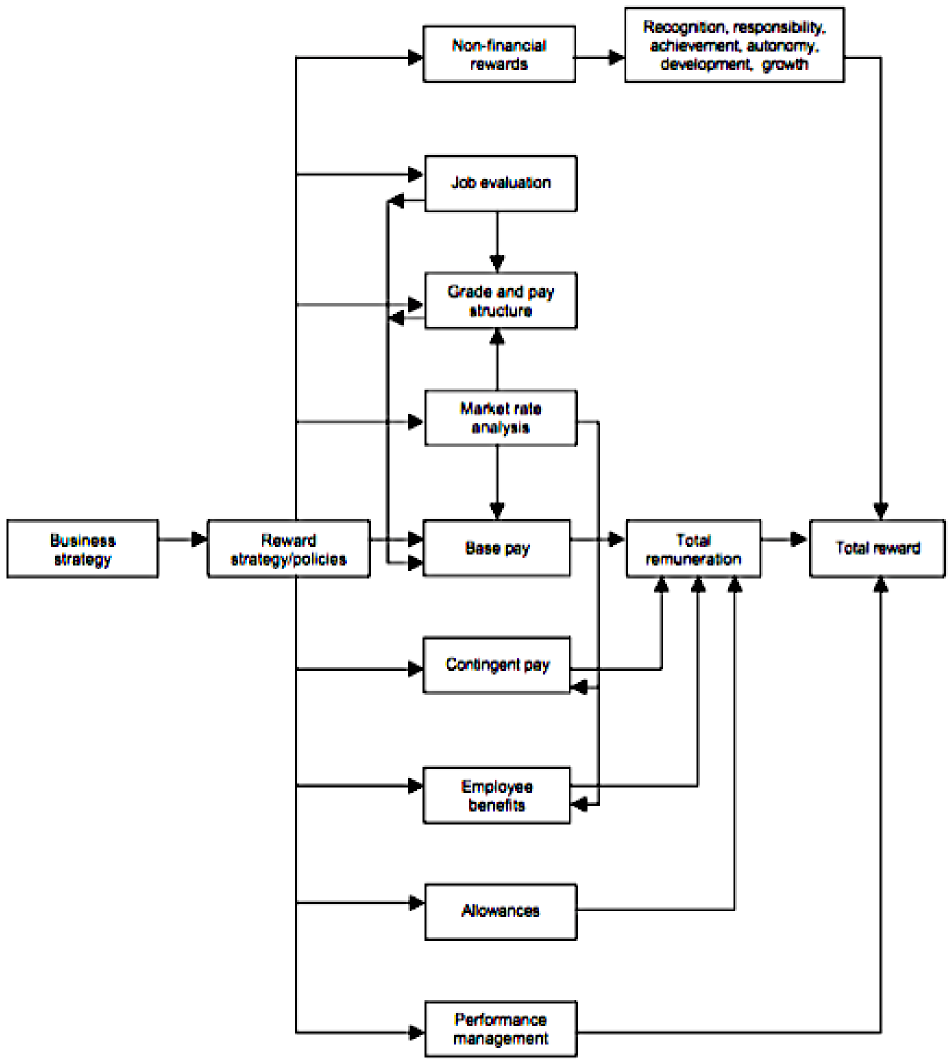
The aforementioned points, should be taken into account to reflect at best the various elements of an organization's reward system.

[29] Armstrong, M., 2007

[30] Department for Business, Innovation and Skills, 2014, “Employment Rights on the Transfer of an Undertaking”, Crown copyright

Figure 2.1 provides an overview of the interrelationship between the many factors that characterize the reward system.

Figure 2.1- Reward system and interrelationship



Source: Armstrong, M., 2007," Employee Reward Management And Practice," Bell& Bain , p.9

As we can see, the reward system starts with the business strategy. It defines the basis of competitive advantage (cost leadership/ differentiation advantage), and its main drivers such as productivity, innovation, and quality that are unique to any organization, to meet its business goals.

The reward strategy delineates the long-term schemes in pay structures, with the aim to boost participation and devotion of workers taking into account an all-embracing remuneration approach. Reward policy is concerned with pay levels such as fair, equal pay, job valuation, market surveys and contingent pay.

From this point on, the interrelation effect spreads out between the various elements.

For instance, the base pay or fixed salary is linked to the job evaluation. The wages may vary according to the job degree, the required skills and external factors assessed by tracking market rates. Job valuation is crucial to accomplish fair pay and is a fundamental way to deal with issues like same wage for equal work value. There are three main categories of job valuation, the first two, analytical and non- analytical, rely on an internal comparison, whereas the third, “Market pricing”, is based on an external comparison. The analytical valuation breaks down jobs into various factors or elements that are assumed to be present in each position, such as physical/mental effort, working conditions, and other related factors. These are ranked, compared with each job and evaluated, giving each of them a score. This method is systematic, consistent and less subjective, providing a defense against equal pay claims, but it is costly, time-consuming and extremely complicated to be implemented.
The non-analytical job valuation approach compares jobs producing a hierarchy that the company’s management considers fair. This classification does not include the various elements or factors characterizing the job. As a result, this system is easy to be developed, providing a quick and straightforward ranking method of employment. The approach is though very subjective, and there is no defined standard to judge the relative worth of a job.
Lastly, the market pricing view is generally set out as a not reliable work evaluation scheme, as it depends entirely on exogenous factors. This method analyses job by reference to market values.
Despite this, it is a realistic job evaluation, since it is determined by the marketplace and can be used as a reference for internal comparisons. Although this could be true, not always accurate market data are ready available, leading to misleading analysis and creating unequal pay.
In support of this, a market rate analysis is needed to monitor, compare and to collect information’s about the rates and benefits available for comparable professions in different companies and by which criteria wages are growing. Henceforth the quality and accuracy of market rate data are underpinned by mainly three features: job matching, sample frame, and timing.
Inadequate job matching can bring to misleading results, and the objective is to properly compare the jobs within the firms and those outside so that accuracy is granted. The sample frame has to be the most representative as possible to reflect at best the comparison needs of the organization concerning sector, technology, business, size, and location. The timing can be understood as the capacity to reliably update the information scale.
Other reward systems worth to be mentioned are contingent pay and employee benefits.
Individual performance, competency, expertise or contribution are extra financial rewards in a contingency pay framework. They can vary in the form of cash bonuses (variable pay) or increases of fixed salaries or a combination of the two. The main idea is to pay more those who contribute more to the company. This can highlight the value of performance, motivating employees with the aim of

attracting and retaining high-quality workers. This pay scheme may result dissatisfactory when the bonus is considered biased, not suitable or badly managed. Furthermore, it might militate against quality and teamwork.

Unlike performance or contribution related pay, bonus schemes have to be re-earned. They are not included in the base pay and only attributed if the individual performance of a worker is sufficiently high, having an immediate impact on worker's motivation and engagement in the company or team. Retribution linked to the performance may encourage teamwork and enhance flexible working and multiskilling, but workers might prefer to raise their base pay rather than receive potential bonus incentives that can be viewed as biased. Referring to "team pay ", it can be challenging to detect clearly-defined teams with concrete and quantifiable targets, and members may feel that their performance is not recognized. In particular, Balkin and Montemayor (2000) tried to explain team-based pay under a contingency framework, putting it in relation with the firm life cycle and team task design. The contingency approach provides a framework to analyze in which ways the company's strategies and structures accommodate to changes in their internal and external environment.

The contingency perspective does not support the idea that there is a single valid set of organizational systems in all cases. Compensation systems should be adopted following the firm's strategy and structure. The compensation system, in particular, may also differ in the company life cycle.

The stages of the corporate life cycle are start-up, growth, maturity, and decline. The authors focused on how team pay varies depending on the organizational life cycle. In the startup phase the primary concern is to create a business plan, looking for financial resources or trying to develop a service or product. Moreover, there are few structural policies and procedures in place, and compensation systems are limited to basic pay or eventually stock options, which can be used to keep critical workers in the initial growth phase. However, this does not presuppose that workers work individually at this startup phase in the same way they may cooperate as a team. Notwithstanding this, the authors argue that team-based pay is unlikely applied at this stage, due to a low degree of formal structure, but even because of the scarce cash resources that, if available, would be mostly invested for business growth.

In the growth stage, companies are focused on the distribution, production, and selling of their products and services on the market. As the company grows in the volume of sales and the number of workers, functional and hierarchy structure are needed to differentiate jobs, however there it is present an enormous need to integrate and to coordinate the job done in various units and organization levels. On this matter, teams can give a value-added to the company, in connecting employees from different functional groups and contributing with their brainstorming to meet the customers' needs.

Notably, the growth phase teams can provide significant advantages through innovation and boundaries spanning activities, enabling companies to expand their business to uncontested market space. Moreover, at the growth stage, firm's profit and wealth is higher, therefore greater financial resources are available to finance team-based compensation. Under those circumstances, the authors suggest that team-based pay is more likely adopted in the growth stage than in the startup phase.

At the maturity stage of the firm's life cycle, the company's growth is gradual and more steady, having reached its maximum size and the ability to take advantage of economies of scales, resulting in stable and predictable profits. This notwithstanding, the administrative control system and the compensation systems may be routinized and bureaucratic. At this stage, companies are focused on developing new products that may improve existing ones already enjoying a high degree of customer acceptance. Teams may be very beneficial in reducing the product development process and increasing the quality of products and services. Moreover, the identification of savings in labor cost in the manufacturing process through the aid of cross-functional teams leads to lower staff requirements. Furthermore, the engagement in self-management activities reduces the number of managers charged to oversee the team job. In the authors' view, provided that at the maturity stage companies reach their most profitable level, operating conditions to implement team-based compensations are likely to be adopted.

Finally, in the decline phase, companies suffer financial losses, a significant reduction in market share and product demand due to a change in the environment or within the company, possibly as a result of competitors' conduct, obsolete strategies or declining industry. In other words, the company is in a survival phase, where it focuses on reducing anything that might not be beneficial for the firm's continuity. Specifically, labor cost or compensation reductions may be necessary as survival tools.

Hence, the adoption of team-based pay is less likely at the decline stage than at the maturity and growth stage.

The second aspect of the contingency perspective analyzed by the authors is the team task design used as a proxy for estimating the probability of team-based pay adoption. The team task design refers to the kind of job that is entrusted to the team. Team work is influenced mainly by two types of team task designs. The team autonomy is the first, involving the level of management duty entrusted to the team. Generally speaking, the freer a team is, the less supervision is required, and as a consequence, more managerial skills are developed within the group in organizing the work.

The second aspect refers to the time dimension of the team task, that is time commitment and time horizon. Time commitment is intended to be the part time or full time needed to perform the task inside the team, while time horizon is the short or long term that is set for the teamwork.

To analyze the different implications of teamwork the authors focused on three major types of team used in organizations, namely, work teams, project teams and parallel teams.
Work teams are liable for producing goods, for instance assembling vehicles, or providing services, like in hospital, giving necessary medications to patients in the emergency room. Work teams are embedded in the design of a company's structure and are probably to stay as long as the company's framework remains the same. The authors suggest that employees in work team task design dedicate their job commitment to the team over an extended period and indefinite time. Provided that employees working in a group invest the majority of their time in the team with a modest to a high degree of autonomy, company's might consider being convenient to additionally compensate team members through team-based pay. In short, this type of team design seems favorable for team-based compensation.
Alternatively, project teams work for a specific period with the full job commitment of its members to the project. The project may be supervised by a project manager, whose role is to monitor and control team members chosen from distinctive organizational, functional areas, such as marketing, finance or engineering. Generally speaking, project teams are used to work out new product and services, rearrange a business operation or other functions within a limited period. As a result, project teams are less autonomous than work teams. So team-based pay scheme may be used as a performance incentive to the project members. Although this may be true, the authors emphasize the obstacles that can generate administrative complexity by limiting the concomitant use of team-based pay with project teams. For instance, project teams usually include individuals with a restricted role and competence which are vital in other company's areas. These kind of people have variable tasks and frequently change project, without going all the way through a whole project cycle.
As a consequence, these non-core members can have a limited but essential effect on projects outcomes, but then again, they may be more linked to their specific job area. To assess their performance in the team in order to establish a team-based pay is very difficult. It may be more beneficial to apply other compensation schemes that are easier to be implemented, for example, profit sharing. The authors conclude that there is a mix of favorable and unfavorable factors in the use of team-based pay as an incentive for project works, and they classify it as moderately favorable.
Finally, parallel teams gather employees from different company's areas together for specific works on a particular issue that require a broader vision for instance in job evaluation, product quality, technology adoption, plant expansion, safety and so on.
It’s important to realize that parallel teams work in parallel with the functional organization structure, whereas work teams and project teams are a way out from a functional structure, to another possible structure design. So parallel teams can be seen as marginal.

It is difficult to set an incentive system for parallel teams, given that some may produce tangible results, for instance, enhancing the quality leading to cost reduction while others may only provide reports, giving suggestions to solve a problem. In this sense parallel teams can give only a marginal contribution and do not behave as a decisional authority. In the light of this, the authors suggest that the adoption of the team-based incentive compensation is very unfavorable for parallel teams, mainly because it is difficult to assign a monetary value to the output of parallel teamwork and for the short period in which workers are employed in parallel team’s activities.

In short, work teams are the most apt to team-based pay, followed by project teams. The least apt are parallel teams.

An extension of the previously mentioned contingent pay and bonuses, including team pay, are the financial rewards consisting in giving the workers a share in the company, as well as granting them extra payments. The idea behind is to enhance the workers’ recognition in the company and to show that the firm has the moral duty to share its success with its employees. There are mainly three forms of organizational schemes: profit sharing, stock ownership, and gain sharing.

Profit sharing is a plan where a principal reward to qualified workers a certain sum, related to the proceeds of the firm, additional to their regular remuneration. The specific amount is entirely at the will of the board, it can be a fixed percentage, or calculated on the basis of a threshold formula, determining a profit level below which profit won’t be distributed and a maximum payable sum.

Stock ownership plans are another tool for providing additional benefits to the employees, stimulating their interest in the company’s affairs. For instance, a direct purchase program allows workers to buy a company stock directly from the company, avoiding brokerage fees and commissions.

Similarly, a stock option gives the employee the possibility to purchase company shares at a predetermined price for a set period.

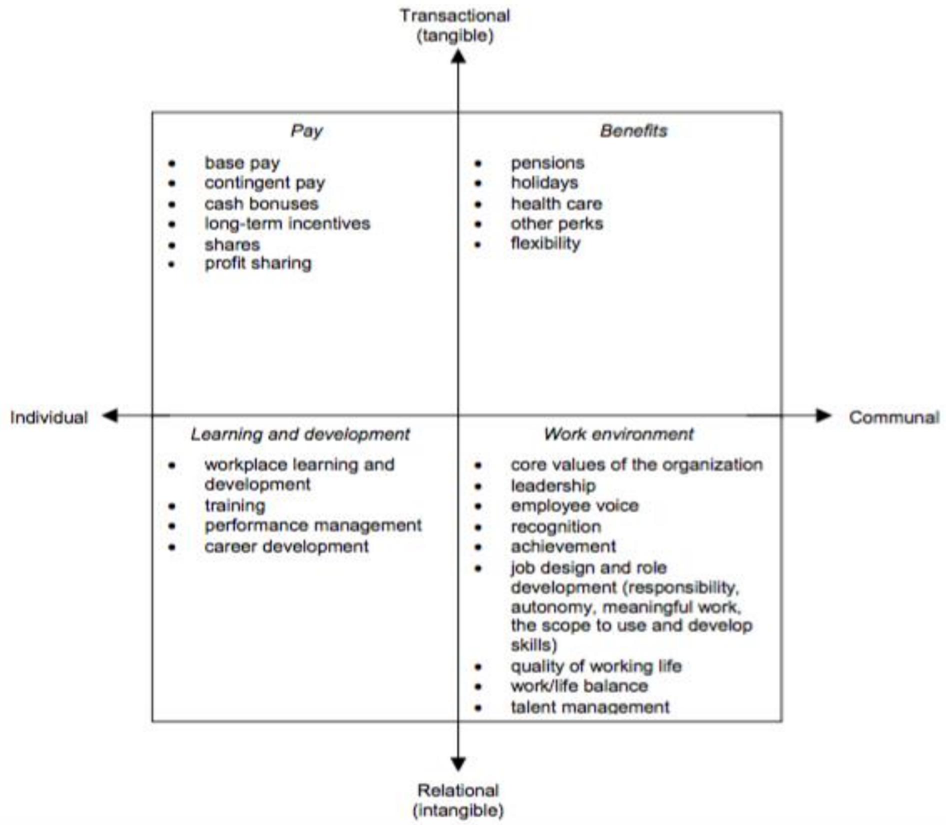
These are one of the many forms of ownership scheme that can be provided to workers at the discretion of the company.

Finally, as before mentioned, employee benefits or fringe benefits are another critical reward system to be analyzed. They may be part of the total remuneration package, covering several non-wage compensations such as company car, pension scheme, sick pay, maternity or insurance coverage.

A company providing fringe benefits testifies to its care for the well-being of its employees, and seeks to increase their commitment to the organization. The formulation of employee benefits is in line with the company's strategy and this, in turn, determines the scale and range of the benefits provided and the costs it can cover up. They can be very expensive, and it is essential to have a constant monitor routine. In particular pension schemes are a notable aspect of the additional reward benefits. It is a long-term benefit that, if reasonably structured, can enable to keep and attract workers by preserving

competitive levels of total compensation. Organizational retirement schemes differ from state pension scheme. Individually, the UK, USA, and Canada have mainly two kinds of corporate pension schemes: defined benefit and defined contribution.
The first is based on an employer’s guarantee to provide a specific retirement amount, calculated on the employee's salary. The primary risks are borne by the employer, that must ensure the set benefit amount to the retired employee. In this sense, the employee has little control over the funds until he receives them.
Whereas the "defined contribution" is principally funded by the employee and matched by the employer to a certain amount. The pension sum is related to the total contribution, the rate of return on the investment of the accrued fund and the rate of return on an annuity acquired by the employer. It is not dependent on the worker's wage. In contrast, the cost of the employer is predictable and lower than the previously mentioned scheme. In this case, the risk falls on the employee.
Italy has instead a two-pillar pension system, consisting of a compulsory public scheme and a private one. The first is a defined benefit system, assuring a minimum pension despite the size of the installments paid by the employee or by the employer. It functions as a "pay-as-you-go" system: the contributions of current workers finance current pensions; public expenditure covers any deficit.
The second instead is a defined contribution system, running through funding deriving from the employees and, usually, from the employers as well.
Nevertheless, the sum of all rewards mentioned leads to the total remuneration as illustrated in figure 2.1 and to the total reward. Total reward includes every aspects of reward: individually base pay, contingent pay, fringe benefits and non-financial rewards, including intrinsic rewards from the job itself, all connected jointly and treated like an integrated and consistent set. Interesting to consider is a model developed by Towers Perrin shown in Figure 2.2 in the next page.

Figure 2.2- Model of total reward



Source: Armstrong, M., 2007," Employee Reward Management And Practice," Bell& Bain,p.34

The transactional rewards, benefit and pay, are shown in the two upper tables. These are crucial to recruit and retain workers and, at the same time, can without difficulty be imitated by competitors. Conversely, the relational (intangible) rewards represented in the two bottom tables are fundamental to increase the value of the upper two tables and are harder to be copied.

The combination of relational and transactional rewards creates the real power of total reward.

In this sense, performance management plays an essential role, enhancing the relational rewards.

It can be understood as a series of actions for building a common understanding about what has to be met, training people to accomplish short-long term goals. It is concerned with the stimulation of productive discretionary behaviors, in the shape of acknowledgement through feedback, enabling employees to develop their skills, recognizing people’s achievement and strengths, discussing the development of the single careers.

It is a continuous process, aiming to grant the individuals the opportunity to develop and grow.

Overall, turning rhetoric into reality is much more compelling. To work, total reward requires a lot of effort by top managers and line managers, under the lead of human resource management.

2.2 Remuneration Committees

The efficient supervision of the executive function performed by a qualified and independent board of directors under the chairmanship of the CEO is considered the primary tool aiming to protect the interest of the organization and of the shareholders. Notably, the feedback between CEO and board is considerably intense, due to the complex, ambiguous and volatile market settings faced by many companies. This unique relationship must not alter the balances between the board and CEO, especially regarding the compensations to be assigned to executives. A proper balance of the oversight responsibility of the board is encouraged by Corporate governance laws leading to the creation of sub-board committees to carry out the remuneration function.

The reward of executive directors is managed by the remuneration committee, that should include only non-executive directors determining both the remuneration policy and the compensation packages which will be published in a section of the annual report. For public listed companies it is mandatory to develop a remuneration report. The remuneration committee must offer a reward package attractive enough to keep and motivate directors with attention to not settle compensations too high. Also, performance related rewards should be introduced to link directors with shareholder’s interests. The remuneration committee should include at least one individual with financial expertise and eventually external help from consultants to assess fair compensation packages.

Remuneration committees aim to provide an independent view on establishing wage levels, incentives, benefits and contract provisions for the management. The remuneration forms for directors and senior executives manly include a fixed and variable compensations, fringe benefits and ownership schemes such as the stock option or share ownership. Furthermore, the remuneration committee acts on behalf of shareholder’s interests and should not have any material relationship with the company.

Failing a remuneration committee senior executive’s directors could attribute themselves salary increases that are not in accordance with the shareholder’s interests.

It follows without saying that the remuneration committee significantly reduces agency conflict of interests. In this respect, it is opportune to mention that the remuneration report by the remuneration committee, it enhances the transparency and accountability of the company's corporate governance practices. The voluntary disclosure of remuneration policies and the extent of such exposure are linked to the efficiency of the remuneration committee as a central corporate governance body established by the board.

The voluntary disclosure by the remuneration committee has been studied by Kanapathippllai et al. (2016) developing a "composite measure as a proxy for remuneration committee efficiency" considering remuneration committee size, independence, chairman's independence, expertise, and diligence[31].

The research was based on market capitalization for each of the years from 30th June 2007 to 2011, on a sample of the top 200 listed companies in the Australian Securities Exchange.

This time span was chosen to effectively include periods with different macroeconomic conditions, namely, before, during and after the global financial crisis.

The study suggests that the presence and the quality of a remuneration committee contributes undoubtedly to the decision of providing voluntary disclosure of remuneration actions and the scope of such disclosure. Moreover, it appears that the number of independent directors, the degree of independence of the remuneration committee and the number of remuneration committee meetings and firms size are all statistically significant and positively linked with narrative voluntary executive remuneration action disclosure. In conclusion, the final results reflect author's expectations, namely that the presence of a remuneration committee will lead boards to voluntarily disclose more information.

Nevertheless, let's focus on the structure of the remuneration report, of the Italian public listed companies. All public listed companies in Italy have to show and prepare once a year the remuneration report according to the art 123-ter of "Testo unico della Finanza" that comprehends all the documents under the legislative decree n.58/1998[32].

The first section should illustrate the society remuneration policy for the administrative board members, the general directors and the directors with strategic responsibilities. Furthermore, it has to show the used procedure for the adoption and implementation of this policy.

The second section offers an adequate representation of the different entries that make up the remuneration. Specifically, it includes all treatments in case of office termination or resolution of the employment relationship, highlighting its consistency with the company's reward approved in the previous year. Besides, it represents analytically the compensations paid by the company and by subsidiaries or associates during the reporting period in any capacity and in all forms, stating any components of the fees mentioned above that refer to activities carried out in the years before the reference year.

It compares the fees to be paid in one or more subsequent financial years against the activity performed in the year in question. Eventually it also indicates an estimated value for the components that cannot be objectively quantified in the year under consideration.

[31] Kanapathippllai et al. (2016)
[32] https://www.borsaitaliana.it/comitato-corporate-governance/documenti/relazioniremunerazioni.htm

2.3 Literature review on director's remuneration

The topic of top executive's pay has received widespread attention both from academics and society at large. Literature focused predominately on the issue of managerial compensation and incentives from a "principal-agent" point of view.

Among the first academics who shed light on this subject were Michael C. Jensen and William H. Meckling with the publication in 1976 of "Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure". It distinguished itself from the former literature stream focusing on the "property rights" issue, impacting significantly the theory of the firm.

According to the authors the subject discussed is much broader than the term suggests. The main focus here is on the specification of the individual rights, establishing how rewards and cost will be assigned among the company's members. As the designation of rights is generally influenced through explicit and implicit contracting, individual behavior in organizations, along with the manager's behavior, will be related to the nature of these contracts. Jensen and Meckling focused therefore on the implications of the property rights included in the contracts on the shareholders and managers' behaviors. They define the agency relationship as an arrangement between the owner (principal) and the manager (agent) to perform some activities, where the owner delegates to the agent some decision-making-authority on his behalf. However, if in this relationship both parties maximize their utility, the potential risk incurred is that the manager will not behave in the owner best interests.

The owner may mitigate this opportunistic behavior by granting sufficient awards to the manager and controlling his behavior imposing budget restrictions, compensation policies, operating rules and so forth.

Notwithstanding this, it is very difficult for the owner to make sure, at zero cost, that the manager choices will be optimal from the owner's perspective. Also, Jensen and Meckling argue that in most agency relationship the shareholders and the managers will incur positive monitoring and bonding costs (non-pecuniary as well as pecuniary) and furthermore there will be some disparities between the manager's decisions and those decisions which could not maximize shareholder's welfare.

They consider the reduction in the shareholder's satisfaction due to this divergence as a cost, specifically as a "residual loss".

Agency costs are defined as the sum of:

- monitoring expenditures by the principal
- bonding expenditures by the agent
- residual loss

They also note that agency costs occur in whatever circumstance concerning a joint work by two or more individuals, even when there is no an apparent relationship between a principal and an agent.

Jensen and Meckling claim that manager's compensation, ownership structure, and board composition are mutually influenced and according to the quality of a business, for instance firm size, business risk, cash flow pattern and others. They argue that these factors may impact a company's performance. So the critical question for shareholders is how to incentive managers so that their performance leads to wealth maximization.

In the literature, top executives are portrayed as being risk-averse. As Harris and Raviv (1979) discuss, managers prefer a remuneration structure by bearing less personal risk as possible. In other words, for a given certain amount of remuneration they may opt for a fixed base pay rather than equity-based pay. The latter is strictly linked to the firm's stock return thus beyond managers' control. As a result of this, the value of an executive's human capital will also change according to the firm's stock performance. So as Jensen and Meckling (1976) argue, to mitigate their compensation risk managers may undertake actions which reduce the company's risk.

Consequently, this risk-averse behavior by managers can in turn negatively impact shareholders' wealth. Although this may be right, shareholders are seen as risk neutral, since they can hedge the firm-specific risk by merely diversifying their portfolio. Furthermore, shareholders will anticipate the risk-averse attitude of managers potentially reducing the firm value.

In general, there are various forms to wind down this conflict over risk, one stream of research conveys to link executive's compensation to firm performance to maximize the value of decision making. This view has been discussed by authors such as Holmstrom (1979), Harris and Raviv (1979) and Grossmann and Hart, (1983)[33]. Other researches, such as Jensen and Murphy (1990), theorized to tie the performance pay on managers to a more significant percentage of equity-based compensation such as through stock options[34]. In their analysis, they compared the various compensation policy incentive mechanism generated by cash compensation, stock options, insider stock ownership and so forth. The sample of cash compensation was based on data reported in Forbes concerning 1,668 CEOs serving in 1049 firms in the years 1974-1986, whereas the sample for stock option and insider stock ownership was based for CEOs active in 73 manufacturing firms in the years 1969-83[35].

The general hypothesis was that to every $1000 change in shareholders' wealth corresponds an average increase in CEO's total wealth.

For instance, the value of CEO's stock options increases on average of 14,5 cents per year for each $1000 increase in shareholder's wealth, while annual cash compensation rises to 3,3 cents per $1000. Whereas, considering stock ownership, the value of the stock owned by the CEO changes by $2.5

[33] Mehran, H., 1995
[34] ibidem
[35] Jensen, M.C et.al., 1990

whenever the value of the firm changes by $1000, implying that CEO held on average 0,25 % of a firm common stock[36].

Another interesting study made by Abowd (1990) focused on whether the level and the mode of top executive compensation has any influence on future performance. The author constructs the database considering more than 16,000 managers in 250 large corporations from 1981 to 1986.

He suggests that a reward of 10 % good performance translates into an increase of 0,3% - 0,9% in economic performance in the next year. Likewise, a 10% bonus for good stock performance leads to an increase of 4% - 12% increase in stock performance for the next financial year[37].

The studies mentioned above focused on US corporate sectors and shed light on the importance of analyzing the relationship between pay and performance and the effects of remuneration modes to structure suitable remuneration contracts with the aim to limit the principal-agent problem.

Other researches tried to contextualize this, in other countries such as in the UK, India, Australia, and China, by including other variables, as company size, board independence, remuneration committee, board structures and critical corporate governance characteristics.

Shareholders are not the competent authority to set executive compensations, but they generally rely on outside directors that have no link with the company.

A study conducted by Peck and Conyon (1998) using a panel data of public listed companies in the UK between 1991 and 1994 examined the role of board control and remuneration committees in determining top executive's compensation. Board monitoring measured as the ratio of non-executives' directors on board and the presence of remuneration committees and CEO duality had only a limited effect on the level of executives' pay. Their results appear consistent with other US studies that have tried to analyze this issue with similar methods. For instance, Westphal and Zajac (1995) found little effect that the level of pay of CEOs changes according to the ratio of inside directors and by the same token Hambrick (1989) found no indications of a link existing between compensation and rate of outside directors in the company. Notwithstanding this, Peck and Conyon were in line with Main and Johnston report (1993), stating that businesses including remuneration committees with a higher proportion of outside directors generally had higher levels of top executives pay.

An important conclusion of Peck and Conyon study suggests that executives' pay and organizational performances are more aligned in businesses with a higher ratio of independent directors in the board or high proportion of independent directors serving on a remuneration committee. This view results

[36] ibidem
[37] Parthasarathy, A. et.al, 2006

consistent with Tosi and Gomez-Mejia's report (1989) that "monitoring is positively related to the influence of the compensation committee"[38].

All in all, previous research has tried to understand manager's compensation concerning agency theory and investigated relationships between various forms of firm performance and executive's incentives. At the same time, the academic research on executive's compensation is mostly focused on American and European organizations. Academics like Khanna and Palepu (1997) have stressed the importance of the differences in institutional settings in which businesses in emerging countries operate. The Institutional context consist of capital, product and labor markets and their related legal and regulatory systems. In other words, this "closed system" view, widely based on Anglo- American agency literature pays not enough attention to the different context in which businesses are embedded. Aguilera et al. (2008) criticize agency theory approach pointing out its "under-contextualized" nature and therefore its failure to precisely explain and compare the differences of corporate governance arrangements across distinctive institutional and organizational contexts.

Filatotchev and Allcock (2010) propose an "open system" approach, aimed to understand the interrelationship between the manager's compensations practices and the organizational and institutional framework in which these practices are conducted. In other words, the efficient implementation of executive's incentives can differ in the various stages of company's development, according to the degree of innovation in different markets and sectors but also to the size or age of the firm among many other factors.

With this in mind, an empirical analysis made by Parthasarathy et al. (2006) investigated the determinants of executive compensation in the Indian context. The database was constructed for a single period from 2004 to 2005 considering listed companies traded on the Bombay Stock Exchange. The authors tried to considerably add to some previous papers of Indian academic research by incorporating multiple factors such as firm performance, shareholder's wealth changes and corporate governance parameters to create a model that explains more consistently the executive's compensation in Indian businesses. The authors point out that none of the profitability indicators (ROA and NPM) can explain the differences in total CEO pay across Indian firms, in contrast with previous research that hypothesized ROA to be statistically significant for CEO compensation. Besides, they found that firm size is an essential factor for explaining both total CEO pay and the share of variable or incentive compensation that a CEO is given.

The idea behind is that larger companies can provide the executives with higher rewards due to the larger size of their businesses resulting in higher sales and total income. This result was consistent with some previous studies, but for instance, Ramaswamy et al. (2000) claimed that firm size was not

[38] Conyon, M.J, et.al, 1998

a critical explanatory variable for CEO compensation. They also found that top executives that are promoters or owners receive compensations on the basis of a higher incentive clause compared to other CEOs. This result may indicate that the monitoring process in a sizeable institutional organization is either absent or very weak[39].

Alternatively, a study made by Janet Lee (2009) compares the share of performance-based compensation given to CEO by Australian and Singaporean firms experiencing enhancement in financial performance and the degree to which such payment is established by the difference in performance and board structure. The sample consists of 47 performance improving firms and 19 declining firms in Australia, along with 52 performance-enhancing firms and 32 declining firms in Singapore over the period 2001 to 2003, using Osirus database containing company data in different countries[40].

Even if the regulatory framework is similar, the degree of ownership in Singapore firms is more concentrated than in Australian companies since most Singaporean firms are predominately state-owned or family businesses. In particular, this has a significant impact on the structure of the firm board as a monitoring mechanism and leads to the creation of an independent committee to establish executive remuneration.

The author highlights that performance improving firms in both countries show a higher rate of CEO performance-based compensation than performance declining firms, indicating that performance pay is not only associated to the level of performance, as previously stated in research, but it might also be linked to performance changes. Furthermore, the study suggests that in both countries the proportion of performance pay for CEO increases in larger companies and with larger sales revenues. Finally, the board structure seems not to influence the proportion of performance pay received by CEO in both countries. The author gives two possible explanations, the first is related to a regulatory perspective, the designation of independent directors on the board might differ by state as a statutory requirement.

The second is based on a theoretical perspective: the objective approach of independent directors to the performance outcomes does not always reward the true capability, effort, and responsibility of a CEO as Kren and Ker (1977, p.308) suggests[41].

Likewise, a study made by Conyon and Lerong (2011) analyzed on one side executive compensation and corporate governance in China's public listed company, on the other side it compared executive pay in China and in the USA. The database was based on the two major Chinese stock exchanges, the Shanghai- Shenzhen Stock exchange from 2001 to 2005.

[39] Parthasarathy, A. et.al., 2006
[40] Lee,J.,2009
[41] ibidem

The research demonstrates that executives' pay and CEO incentives are lower in government-owned company's and businesses with concentrated ownership structure. Boardroom governance is essential mainly because the higher the proportion of independent directors on the board the more top pay-performance link are attributed. Private, controlled businesses and businesses with a higher proportion of independent directors on the board can to a higher extent change CEO for poor performance. Finally, they suggest that in the US salary and bonuses are approximately seventeen times larger than in China. They argue that the pay differences in China-US. They suggest that unobserved factors, for instance, social norms and institutions in China might be relevant[42].

This study has to be taken with a grain of salt as the authors rightly point out, since it is limited to 2001 to 2005 and data on stock options and other equity pay at time were not available. Notwithstanding this, it is the first evidence of comparison of CEO compensation in China and the US, including compensation for performance relation and monitoring businesses' and executive's quality.

[42] Conyon,M.J. et.al.,2011

3. Chapter: Empirical study, findings and discussion

3.1 Research hypothesis

After an analysis of the main features of the different reward systems and a closer look to the compensation system of top executive directors based on an academic point of view it is now possible to go deeper in the topic with an empirical analysis conducted on a sample of public listed Italian firms in 2016.

This study is especially aimed to analyze the types of compensation systems of the board of directors of Italian public listed companies under an agency theory perspective.

In the 2.3 paragraph of the second chapter, the agency relationship, is defined as an arrangement between the owner and the agent to perform some activities, where the owner delegates to the agent some decision-making authority on his behalf. However, if in this relationship both parties maximize their utility, the potential risk incurred is that the manager will not behave in the owner best interests. So the critical question is which type of compensation is best to align the interests of the shareholders with those of the directors sitting in the board so that it leads to a higher firm performance.

Academics tried to link executive's compensation incentives to firm performance through equity based compensation (Jensen & Murphy 1990) rather than cash compensation.

Abowd (1990) focused on whether the level and the mode of top executives' compensation has any influence on future performance. He suggests that a reward of 10 % good performance translates into an increase of 0,3% - 0,9% in economic performance in the next year. Likewise, a 10% bonus for good stock performance leads to an increase of 4% - 12% increase in stock performance for the next financial year.

In this study, three remuneration types are taken into consideration: fixed salary, variable compensation and fringe benefits. This study tries to approach the agency problem from different perspective, focusing on variables that were not considered so relevant in past research and contextualizing it in the Italian environment where little or no evidence of such studies is found.

Fixed salary represents the major component of a remuneration system, so if properly structured it may contribute to increase directors' motivation in performing their work leading potentially to a higher firm performance. In the light of this what is expected is that:

Hypothesis 1: Is firm's performance affected in a positive way by fixed salary?

In this study the variable remuneration considers cash compensation on an annual basis under a system of "Management by objective" attributed only by the achievement of predefined company's objectives. The variable compensation is measured by company's indicators such as EBITDA, Net Cash flow before Dividend or by individual objectives associated with operational outcomes and plans that sustain the firm's economic performance on the market.

Hypothesis 2: Is firm's performance affected in a positive way by variable compensation?

Fringe benefits is an increasing adopted incentive system valid as variable compensation.
The fringe benefits are differentiated by management level and consist in insurance or healthcare plans, company car, laptop, mobile phones, sometimes accommodation and child care center.

Hypothesis 3: Is firm's performance affected in a positive way by fringe benefits?

3.2 Data and Methodology

The Empirical analysis was carried out on a sample of 165 Italian public listed companies in 2016. The source of data for the companies listed is Borsa Italiana and for the financial data is Thomson Reuters Datastream.

The database focuses on some Board characteristics and some Corporate financial data.

For every single firm analyzed for the research, the 2016 annual report has been used to find information about the numerical composition of the board and other characteristics related to board members such as date of birth, nationality, gender, level of education, educational background, international work experience, tenure firm, if independent member, remuneration types: fixed and variable compensation and fringe benefits, if president or vice president and if CEO.

Financial data include market capitalization, common equity, total assets, leverage, ROA, ROE, long term debt over common equity and Tobin Q.

Finally, three simple linear regressions were created in order to understand the impact of fixed salary, variable compensation and fringe benefits on firm performance measured by Tobin Q indicator.

The linear regression is helpful in order to understand the bivariate and multivariate relationship between variables which are dependent, independent and control variables correlated by a coefficient. The correlation coefficient is non-parametric and just states that the two variables are associated with one another without explaining what kind of relationship exists between them.

The linear regression analysis is a linear relationship between X, the independent variable and Y, the dependent variable. Epsilon represents the random component of the linear relationship between X and Y.

$$\gamma = \alpha + \beta x + \varepsilon$$

Where Y is the value of the dependent variable in the observation. Alpha is a constant, or the intercept, and measures the value where the regression line crosses the y-axis. Beta is the slope, or coefficient, and measures the steepness of the regression line. Epsilon is the random component, or disturbance error term in the observation.

3.3 Variables

Dependent variable:

The Tobin's Q ratio is the performance index used as dependent variable in this study.

The Tobin Q formula measures the total market value of a company, divided by the total value of the company's assets. It calculates the worthiness of a firm over its assets. More specifically, the value of a firm should be equal to its replacement cost.

A value of Q between 0 and 1 implies that the company's worth is undervalued with respect to its possessed assets. It follows that it becomes an attractive investment opportunity for potential buyers. Instead a value of Q above 1 means that the company is overvalued in relation to its assets, implying that it generates more earnings than its replacement costs, which would induce other companies to create similar businesses trying to capture some of the profits. A consequence of this would lead to reduce the firm value and cause its Tobin's Q to fall.

Independent variables:

In the study the three linear regressions are carried through different independent variables.

The first is based with fixed compensation, the second with variable compensation and the third with fringe benefits. Generally speaking, a change in the independent variable, it reflects also a change in the dependent variable.

Control Variables:

Control variables are different from independent variables, because their effect on the dependent variable does not change. Control variables have to be held constant and are not relevant in the specific analyses but at the same time they indirectly influence the dependent variable. So they enhance the accuracy of the relationship between the dependent and independent variable.

The control variables included for each of the three regressions are: ROA, Financial Leverage and Firm size.

Firm size is computed in this research as the logarithm of total assets and represents the total resources, capital and assets available to the company. Size may have a mixed impact on firm performance. Larger firms' may take advantage of economies of scale and learning effects but the dimensions can negatively impact the firm performance due to the increased complexity to manage the firm's assets specially to monitor the information process capacity between the different firm's departments.

ROA or Return on Assets measures how much of the firm's profit is generated by the use of the company's assets. ROA is a profitability indicator and calculated as net income over total assets.
It assesses the amount of earnings generated from the invested capital. The last control variable taken into consideration is Financial leverage.
Generally speaking, Financial leverage assesses the volume of additional debt taken by the company over its net worth. If the Financial leverage ratio is high, it means that the company has accumulated debt to finance its business and may not be able to generate enough cash flows. A declining cash flow can lead to an increased risk of insolvency. Financial leverage can be calculated in many forms. In this study the ratio considered is Long-term Debt over Common Equity. This type of leverage ratio assesses more accurately the leverage level of a company compared to its competitors.

3.4 Results and Discussion

Table 3.1- Descriptive statistics

Variable	obs	mean	std. Dev	Min	Max
ComponenteFissa2016	1.490	133514,5	294685,7	0	3.514.497,00
ComponenteVariabile2016	1.485	38138,5	336775,6	0	1,10E+07
Fringebenefits2016	1.472	8934,299	260675,5	0	9993000
ROA_2016	1.411	3,211906	11,34795	-36,07	117,61
Financial Leverage_2016	1.449	96,90244	148,0738	-686,25	647,7
size2016	1.464	13,47508	1,944688	8,288283	18,81899

The above table gives an overview of the variables used in the study. For each variable are provided observation, mean, standard deviation, minimum and maximum value. The observation for the different variables are almost in line. We can see that board members in our sample perceive on average a fixed compensation of 133.514,5 Euro, a variable cash compensation of 38.138,5 Euro, fringe benefits of 8.934,3 Euro and a maximum amount of 3.514.497 Euro, 11.000.000 Euro and 9.993.000 Euro respectively.

On average ROA, Financial leverage and Firm size have a value of 3,21, 96,9 and 13,5 respectively and a minimum and maximum value of -36,07 and 117,61, -686,25 and 647,7, 8,29 and 18,82 respectively.

The next tables will show the results of the three linear regressions in relation to Tobin's Q indicator.

Linear Regression 1:

$$Tobin\ Q_{2016} = Componentefissa_{2016} + ROA_{2016} + Financial\ Leverage_{2016} + Constant + \varepsilon$$

Linear Regression 2:

$$Tobin\ Q_{2016} = Componentevariabile_{2016} + ROA_{2016} + Financial\ Leverage_{2016} + Constant + \varepsilon$$

Linear Regression 3:

$$Tobin\ Q_{2016} = Fringebenefits_{2016} + ROA_{2016} + Financial\ Leverage_{2016} + Constant + \varepsilon$$

Table 3.2- Linear Regression 1

		Number of obs	=	1.372		
		F(4, 1367)	=	71,26		
		Prob > F	=	0		
		R-squared	=	0,263		
		Root MSE	=	0,67624		
					95% conf. Inter	
TOBIN_Q_2016	**Coeff**	**Rob. Std. Err**	**t**	**P>|t|**	**min**	**max**
Componentefissa2016	0.000**	5,27E-08	3,11	0,002	6,08E-08	2,68E-07
ROA_2016	0.033***	0,0030574	10,68	0	0,0266626	0,0386582
Financial Leverage_2016	-0.001***	0,0000754	- 14,21	0	-0,0012185	-0,0009228
size2016	-0.040***	0,0103444	-3,85	0	-0,0600769	-0,0194917
Constant	1.894***	0,1512083	12,52	0	1,597054	2,190304

$p< 0.1^{+}$, $p<0.05^{*}$, $p<0{,}01^{**}$, $p<0{,}001^{***}$

The first linear regression analyses whether fixed compensation affects positively firm's performance.

1.372 observations were considered for this linear regression constructed under a 95% confidence interval. A 95% confidence level implies that the results obtained from the analysis are statistically sound and confident at 95%. To have a more proper evaluation of the linear regression analysis along with the p value, an F-test was conducted. The upper part of the table shows the results of the F-test. This holds for all the three regression considered in the analysis.

The F-test must be used in combination with the p value in order to make sure that all the variables overall are statistically significant, because sometimes a significant result does not imply that all the variables are significant.

The F-test reduces the random chance between variables. The p value measures the probability whether the initial hypothesis is supported or not given the analysis made. The lower the p value is, the stronger is the evidence of the hypothesis.

From the table 3.2 we can see that all the variables coefficient is statistically significant, especially ROA, Financial Leverage and size at a p < 0,01% which is the maximum reachable confidence level. Focusing on the control variables, we see that ceteris paribus an increase of ROA increases the firm performance by 0.033, whereas an increase in Financial Leverage and size decreases firm performance by -0.001 and -0.040 respectively.

The fact that ROA is positively associated to firm performance makes sense, since if the company is able to generate earnings from its assets the firm performance increases.
The fact that the coefficient of Financial leverage impacts negatively firm performance makes sense since if the company is taking additional debt to finance its business it may imply that it does not generate enough revenues leading to a lower performance and increasing its financial risk.
The coefficient of Firm size is negative implying that the complexity factor in managing the firm's resources and assets affects negatively firm performance.
The positive effect of ROA and the negative effect of Financial Leverage and size on firm performance holds also in the next two linear regressions changing partially their coefficient values respectively.
The independent variable Fixed compensation is significant at a p < 5% implying that it influences firm performance. We can see that the coefficient is near zero, having practically a neutral effect on the performance but influencing it all the same in a positive way. This result supports our first hypothesis that fixed compensation affects positively firm performance.

Table 3.3- Linear Regression 2

		Number of obs	=	1.368		
		F(4, 1363)	=	69,31		
		Prob > F	=	0		
		R-squared	=	0,2593		
		Root MSE	=	0,67869		
					95% conf. Inter	
TOBIN_Q_2016	**Coeff**	**Rob. Std. Err**	**t**	**P>|t|**	**min**	**max**
Componentevariabile2016	0	6,85E-08	0,53	0,595	-9,80E-08	1,71E-07
ROA_2016	0.033***	0,0030584	10,69	0	0,0266821	0,0386816
Financial Leverage_2016	-0.001***	0,0000754	-14,13	0	-0,0012126	-0,0009169
size2016	-0.036***	0,0103005	-3,48	0,001	-0,0560319	-0,0156187
Constant	1.862***	0,1509895	12,33	0	1,56548	2,157874

$p < 0.1^{+}$, p<0.05*, p<0,01**, p<0,001***

The second linear regression focuses on whether variable compensation has an effect on firm performance. The analysis has slightly less observations than the preceding one and as before ROA, Financial Leverage and size are statistically significant with a p < 0,01 %.
The independent variable the "variable compensation" is not significant on firm performance.

This means that an increase or decrease of variable compensation has no effect on the firm's performance. This result does not support our initial hypothesis. This surprising result may suggest that variable compensation may be absorbed by other factors that makes it irrelevant.
For most Italian public listed companies, the attribution of variable compensation to members of the board, as previously mentioned in the paragraph 3.1, is based on a system called "Management by objectives" and given only by the achievement of predefined company's objectives.
Variable compensation is measured by some company's indicators or by individuals' objectives associated with operational outcomes and plans that sustain firms' economic performance on the market. The fact that the variable reward is given only if objectives are achieved, is perceived by the members of the board as a hypothetical and not certain compensation.
Relying on company's indicator's the variable compensation does not mirror the individual performance of a board member and if the individual's objectives are set too high the variable compensation might be difficult to be achieved.
When variable compensation is based on individual objectives the compensation line may result unclear, since it is expressed in percentage on an amount varying from a minimum to a maximum value. Furthermore, objectives may be revised during the year making it quite difficult for board members to rely on those rewards.
Board members may prefer more secure compensation systems or incentives so that their individual performance is better recognized.
In most Italian public listed companies fixed compensation covers the risk that the variable component is not awarded because of failed performance objectives.
This may explain the irrelevance of variable cash compensation. Furthermore, it reinforces the fixed compensation system as a valuable reward for compensating management according to their role and responsibilities leading to a reliable and equitable reward system.

Table 3.4 - Linear Regression 3

		Number of obs	=	1.357		
		F(4, 1352)	=	214,22		
		Prob > F	=	0		
		R-squared	=	0,2592		
		Root MSE	=	0,67698		
					95% conf. Inter	
TOBIN_Q_2016	**Coeff**	**Rob. Std. Err**	**t**	**P>|t|**	**min**	**max**
Fringebenefits2016	0.000***	5,67E-09	12,45	0	5,94E-08	8,17E-08
ROA_2016	0.032***	0,0030756	10,56	0	0,0264505	0,0385175
Financial Leverage_2016	-0.001***	0,0000754	- 14,16	0	-0,0012149	-0,0009192
size2016	-0.034***	0,0103149	-3,32	0,001	-0,054523	-0,0140532
Constant	1.843***	0,1510062	12,21	0	1,547225	2,139689

$p < 0.1^{+}$, $p<0.05$*, $p<0,01$**, $p<0,001$***

The last regression of the study analyses whether fringe benefits positively affects firm performance. The number of observations are slightly inferior to the previous two regressions, but all coefficients are statistically significant at a p < 0,01% level.

Fringe benefits definitely affect positively firm performance. This result supports the initial hypothesis that an increase in the use of fringe benefits, even if the coefficient is near zero, influences positively firm performance.

This type of incentive system is an alternative way to reward individuals as compared to cash compensation. Fringe benefits may provide an enhanced working environment offering services that are more suitable for board members enhancing their performance.

Fringe benefits being additional elements going along with fixed compensation may explain the irrelevance of variable compensation.

In conclusion, what emerges is that fixed compensation and fringe benefits are a valuable reward system in enhancing positively firm performance leading to a potential reduction of agency costs.

Conclusion

This paper aims to provide insight into the impact of three different top executives' compensation systems (*fixed salary, variable compensation and fringe benefits*) on firm performance over a sample of Italian public listed companies in 2016 according to the agency theory perspective.

Before going into the outcomes of the empirical research, different topics have been addressed in the previous two chapters.

The first chapter outlined the importance of the board of directors and the CEO.

The board of directors is the highest decision making authority, that supervises and controls the firm's management by taking the most relevant managerial and financial decisions and protects the shareholder's interests.

Conflict of interests arise when board members do not act honestly and in good faith in exercising their responsibilities towards the company's best interests and they misuse critical information obtained through their position to take advantage directly or indirectly, for personal purposes or third parties.

Corporate governance structures of a board differ by country due to legal, economic and social factors mirroring the specific system and corporate traditions. A distinction of corporate structures in civil (two-tier system) and common law (one tier system) countries has been made. Interdependence is a leading structural weakness of dualistic board structure. The one-tier system provides significant advantages for the members of the board of directors performing supervisory functions, enabling them to have full knowledge about the daily business of the company, though it could rise some issues about independence and separation of responsibilities. Chinese corporate governance system was also analyzed, with its high degree of state ownership concentration. There are three main issues of Chinese corporate governance: the absolute control of the state, which significantly influences the management of the company, insider trading and the fraudulent financial reporting.

The characteristics of the board of directors' composition differ in the size of the board, the proportion of independent and dependent directors and in diversity (gender, cognitive factors).

Empirically the size factor and the number of independent directors on the board has mixed results on firm performance. As Coles, Daniel & Naveen (2008) explain, simple companies, with a low degree of unobserved complexity factors (firm size, diversification and leverage), need less advice than complex ones, have smaller boards with less outside directors. This holds also for the reverse situation.

Diversity, can be split into observable (gender, race, and ethnicity) and non-observable (knowledge, education, values, perception, affection and personality characteristics) variables. The company's attempt to build a diversified boardroom can be viewed from the outside as an effort to tackle discrimination and as an open-minded approach. A right balance of diversity should be maintained. If not balanced diversity can contribute to communication breakdown and lack of cooperation between board members, due to different ethical backgrounds. Gender diversity in a board is extremely important. The EU commission and EU countries like Italy, made a great effort to increase the presence of women as board members. However, the appointment of women in a board must mirror the true aim of the firm to become gender diverse and more effective, rather than being a symbolic means to enhance corporate reputation and image.

The CEO is accountable for the whole management of a firm and usually designated by the shareholders and the board of directors. The CEO characteristic in small vs large firms may differ in his degree of transformational leadership.

Transformational CEO are more present in small- medium-size enterprises(SME), provided that SME context is structurally less complex and increases role opacity. The Transformational quality of a CEO is influenced to some extent by firm size, CEO founder status (founder and non-founder) and CEO tenure as stated by Ling et. al (2008). In the Chinese environment Wang, H et.al (2010) assessed the CEO characteristics, suggesting mainly two types of CEO leadership behavior: task-focused CEO leadership behavior and relationship-focused behavior. Previous studies inquired other aspects of CEO qualities including the CEO succession outcomes, that may depend on the prior conditions found in organizations. The decision to hire an internal or an external CEO may be influenced by the firm's objective to realize particular performance outcomes. CEO characteristics are influenced also by the level of a firm's international interdependence, as Roth, K. (1995) states. A CEO must be internationally networked in order to improve the international communication mechanism of a firm's multinational collection of interdependent, geographically dispersed, resource stock.

The second chapter focused on the Reward Management and executives literal review.

The main reward systems are: basic pay, contingent pay (variable pay (cash bonuses), team pay), fringe benefits (employee benefits), and financial rewards consisting in giving workers a share in the company (profit sharing, stock ownership and gain sharing) showing that the company has the moral duty to share its success with its employees.

Job evaluation is crucial to accomplish fair pay, and cash bonuses are attributed to the performance of a worker if sufficiently high. Especially team based pay can differ in a company's life cycle and team task design.

In the company's life cycle, team based pay is less likely at the decline stage than at the maturity and growth stage, whereas in the team task design, team based pay is most apt for work teams, followed by project teams and least apt to parallel teams.
Fringe benefits may be part of the total remuneration package, covering several non-wage compensations such as company cars, pension scheme, sick pay, maternity or insurance coverage.
The real power of the Reward management of a company is the effective combination of transactional (pay and benefits) and relational (learning and development and work environment) rewards.
Relational rewards are crucial to increase the value of the transactional rewards and are more difficult to be copied by other firms.
The reward of executive directors is managed by the remuneration committee, that should include only non-executives' directors and at least one individual with financial expertise, determining both the remuneration policy and the compensation packages. The remuneration committee acts on behalf of the shareholder's interests and should not have any material relationship with the company.
The remuneration committee contributes undoubtedly to the decision of providing voluntary disclosure of remuneration actions and the scope of such disclosures, as the study made by Kanapathipplai et.al (2016) states.
The focus of the literature on top executives pay was predominately based from a "principal agent" point of view. The central premise of this framework, defined by Jensen and Meckling (1976), is that shareholders have not full knowledge of the daily activities of a firm and that managers, being in a position of trust by acting on behalf of the shareholders, might abuse their power to the detriment of the company. Research therefore tried to understand manager's compensation on the basis of the agency theory and investigated the relationship between various forms of firm performance and executive incentives.
Most studies concluded that equity-based incentives are the best solution to reduce agency costs. However, the efficient implementation of executive's incentives to reduce agency costs may differ in the various stages of company's development, according to the degree of innovation in different markets and sectors but also to the size or age of the firm among many other factors.
This being said, it is now possible to go back to the research carried out, in order to draw up the conclusion of the empirical study. This study gives insight of a new approach to analyze the agent problem by focusing on Italian public listed companies.
What emerges from the study is that, fixed compensation and fringe benefits are a valuable reward system in enhancing positively firm performance leading to a potential reduction of agency costs.

Fixed salary is statistically significant at a p value < 5% and fringe benefits is statistically significant at a p value< 0,1%, the maximum reachable statistical significance level.

The variable compensation has no effect on firm performance, meaning that an increase or decrease of variable compensation does not impact on the firm's performance.

This suggest that the effect of variable compensation on firm performance is absorbed by other factors that makes it irrelevant.

In most Italian public listed companies fixed compensation covers the risk that the variable component is not awarded because of failed performance objectives. This may explain the irrelevance of variable cash compensation.

Furthermore, fringe benefits are an alternative way to reward individuals as compared to cash compensation and, being additional elements going along with fixed compensation, they may explain the irrelevance of variable compensation.

For future research it might be interesting to analyze whether equity based incentives (share ownership or stock options) have an impact on firm performance in the Italian context, in association with the agency theory perspective.

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Paper summary

Introduction

A popular assumption in economic thought is that cash is better than any good, implying that through it people are able to consume more and that cash is the principal means for exchanges.
Relating this assumption to the way firms structure the compensation and incentives of its managers, it might be argued that cash works at best to motivate and reward top executives.
However, most companies apply other remuneration and incentive schemes rather than cash, for instance equity based incentives or different types of bonuses such as fringe benefits.
Previous research tried to assess which kind of compensation system is the best to align the performance of the managers with the interests of the shareholders, leading to a higher firm performance. Most studies tried to view this problem under the principal agent framework.
The central premise of this framework, defined by Jensen and Meckling (1976), is that shareholders have not full knowledge of the daily activities of a firm and that managers, being in a position of trust by acting on behalf of the shareholders, might abuse their power to the detriment of the company.
This paper aims to provide insight into the impact of three different top executives' compensation systems (*fixed salary, variable compensation and fringe benefits*) on firm performance over a sample of Italian public listed companies in 2016 according to the agency theory perspective.
The first chapter has an introductive quality starting with the analysis of the main tasks of the board members and the potential conflict of interest that might arise. It follows illustrating the main structure and the different composition characteristics of the board of directors. Finally, it outlines the main characteristic of the board of directors' counterparty, the CEO.
The second chapter starts determining the general reward system applied to workers and follows analyzing the role of the remuneration committee as a guarantor for fair and attractive remuneration package for top executives. Lastly, a literal review is provided analyzing the impact of top executive's compensation on performance from an academic point of view.
The third chapter is the core of the research and consists of the formulation of the hypothesis and of the study and the analysis of the variables used for the regression and of the final discussion about the results found from the sample of firms.
This work provides an analysis of the Italian market that is not common in the literature.

1. Chapter: Importance of Board of Directors and CEO

1.1Main Tasks

The board of directors is the highest decision making authority, that supervises and controls the firm's management by taking the most relevant managerial and financial decisions and protects the shareholder's interests. The board of directors has to be familiar with the vision, mission, and values of the company and ready to review these in the light of current and impending circumstances.

1.2 Conflict of Interest

Conflict of interests arise when board members do not act honestly and in good faith in exercising their responsibilities towards the company's best interests and they misuse critical information obtained through their position to take advantage directly or indirectly, for personal purposes or third parties. Three conflict of interest scandals were analyzed Enron, Parmalat and Volkswagen.

1.3 Corporate Governance

Corporate governance structures of a board differ by country due to legal, economic and social factors mirroring the specific system and corporate traditions. For instance, there is a distinction between civil and common law countries.

The first is usually characterized by a dualistic model, or two-tier system, where the shareholders appoint a supervisory board, which ensures that the company is managed according to the company's by-laws and laws. Subsequently, the supervisory board selects a controlling body, the management board, which is responsible for the day-by-day management.

There is a neat distinction between the two control bodies, which operate alongside without imposing each other's binding commands. Interdependence is a leading structural weakness of dualistic board structure.

The one-tier system follows almost the same logic as the two-tier one, but it concentrates the management and supervisory functions in one body. The one-tier system provides significant advantages for the members of the board of directors performing supervisory functions, enabling them to have full knowledge about the daily business of the company, though it could rise some issues about independence and separation of responsibilities. Chinese corporate governance system was also analyzed, with its high degree of state ownership concentration. There are three main issues of Chinese corporate governance: the absolute control of the state, which significantly influences the management of the company, insider trading and the fraudulent financial reporting.

1.4 Board of Directors' Characteristics Component

The characteristics of the board of directors' composition differ in the size of the board, the proportion of independent and dependent directors and in diversity (gender, cognitive factors).
Empirically the size factor and the number of independent directors on the board has mixed results on firm performance.
As Coles, Daniel & Naveen (2008) explain, simple companies, with a low degree of unobserved complexity factors (firm size, diversification and leverage), need less advice than complex ones, have smaller boards with less outside directors. This holds also for the reverse situation.
Diversity, can be split into observable (gender, race, and ethnicity) and non-observable (knowledge, education, values, perception, affection and personality characteristics) variables. The company's attempt to build a diversified boardroom can be viewed from the outside as an effort to tackle discrimination and as an open-minded approach. A right balance of diversity should be maintained. If not balanced diversity can contribute to communication breakdown and lack of cooperation between board members, due to different ethical backgrounds. Gender diversity in a board is extremely important. The EU commission and EU countries like Italy, made a great effort to increase the presence of women as board members. The EU commission in November 2012 proposed a Directive aimed to accelerate the progress of gender balance by setting a 40% female share as non-executive directors of the biggest listed companies by 2020. The Italian government issued the legislative decree n.120/2011 also known as "Golfo Mosca Law" which established in 2012 that the boards of the Italian public listed companies should include at least one-fifth and, from 2015, one-third of women until 2022, when the law will expire. With the law becoming effective in August 2012 a significant increase in the women's share in Italian public listed companies began, also where both genders were already present. According to the study of Pastore and Tommaso (2016), investigating whether imposing gender quotas in the management and supervisory board has been successful in reducing disparities in Italian public listed companies, women hold mainly non-executive positions in public listed companies, generally as independent directors.

However, the appointment of women in a board must mirror the true aim of the firm to become gender diverse and more effective, rather than being a symbolic means to enhance corporate reputation and image.

1.5 CEO Characteristics

The CEO is accountable for the whole management of a firm and usually designated by the shareholders and the board of directors. The CEO characteristic in small vs large firms may differ in his degree of transformational leadership. The transformational leadership refers to the CEO qualities of charisma, inspirational motivation, intellectual stimulation, and individual consideration.

Transformational CEO are more present in small- medium-size enterprises(SME), provided that SME context is structurally less complex and increases role opacity. The Transformational quality of a CEO is influenced to some extent by firm size, CEO founder status (founder and non-founder) and CEO tenure as stated by Ling et. al (2008).

In the Chinese environment Wang, H et.al (2010) assessed the CEO characteristics, suggesting mainly two types of CEO leadership behavior: task-focused CEO leadership behavior and relationship-focused behavior. Previous studies inquired other aspects of CEO qualities including the CEO succession outcomes, that may depend on the prior conditions found in organizations. The decision to hire an internal or an external CEO may be influenced by the firm's objective to realize particular performance outcomes. CEO characteristics are influenced also by the level of a firm's international interdependence, as Roth, K. (1995) states. A CEO must be internationally networked in order to improve the international communication mechanism of a firm's multinational collection of interdependent, geographically dispersed, resource stock.

2. Chapter: Reward Management and Executives literal review

2.1 Reward system

The main reward systems are: basic pay, contingent pay (variable pay (cash bonuses), team pay), fringe benefits (employee benefits), and financial rewards consisting in giving workers a share in the company (profit sharing, stock ownership and gain sharing) showing that the company has the moral duty to share its success with its employees.

Job evaluation is crucial to accomplish fair pay, and cash bonuses are attributed to the performance of a worker if sufficiently high. Especially team based pay can differ in a company's life cycle and team task design.

In the company's life cycle, team based pay is less likely at the decline stage than at the maturity and growth stage, whereas in the team task design, team based pay is most apt for work teams, followed by project teams and least apt to parallel teams.

Fringe benefits may be part of the total remuneration package, covering several non-wage compensations such as company cars, pension scheme, sick pay, maternity or insurance coverage.

The real power of the Reward management of a company is the effective combination of transactional (pay and benefits) and relational (learning and development and work environment) rewards.

Relational rewards are crucial to increase the value of the transactional rewards and are more difficult to be copied by other firms.

2.2 Remuneration Committees

The reward of executive directors is managed by the remuneration committee, that should include only non-executives' directors and at least one individual with financial expertise, determining both the remuneration policy and the compensation packages. The remuneration committee acts on behalf of the shareholder's interests and should not have any material relationship with the company.

The remuneration committee contributes undoubtedly to the decision of providing voluntary disclosure of remuneration actions and the scope of such disclosures, as the study made by Kanapathipplai et.al (2016) states.

2.3 Literature review on director's remuneration

The focus of the literature on top executives pay was predominately based from a "principal agent" point of view. The central premise of this framework, defined by Jensen and Meckling (1976), is that shareholders have not full knowledge of the daily activities of a firm and that managers, being in a position of trust by acting on behalf of the shareholders, might abuse their power to the detriment of the company. Research therefore tried to understand manager's compensation on the basis of the agency theory and investigated the relationship between various forms of firm performance and executive incentives.

Most studies concluded that equity-based incentives are the best solution to reduce agency costs. However, the efficient implementation of executive's incentives to reduce agency costs may differ in the various stages of company's development, according to the degree of innovation in different markets and sectors but also to the size or age of the firm among many other factors.

3. Chapter: Empirical study, findings and discussion

3.1 Research hypothesis

After an analysis of the main features of the different reward systems and a closer look to the compensation system of top executive directors based on an academic point of view it is now possible to go deeper in the topic with an empirical analysis conducted on a sample of public listed Italian firms in 2016.

This study is especially aimed to analyze the types of compensation systems of the board of directors of Italian public listed companies under an agency theory perspective.

The agency relationship, is defined as an arrangement between the owner and the agent to perform some activities, where the owner delegates to the agent some decision-making authority on his behalf. However, if in this relationship both parties maximize their utility, the potential risk incurred is that the manager will not behave in the owner best interests.

So the critical question is which type of compensation is best to align the interests of the shareholders with those of the directors sitting in the board so that it leads to a higher firm performance.

Academics tried to link executive's compensation incentives to firm performance through equity based compensation (Jensen & Murphy 1990) rather than cash compensation.

Abowd (1990) focused on whether the level and the mode of top executives' compensation has any influence on future performance. He suggests that a reward of 10 % good performance translates into an increase of 0,3% - 0,9% in economic performance in the next year. Likewise, a 10% bonus for good stock performance leads to an increase of 4% - 12% increase in stock performance for the next financial year.

In this study, three remuneration types are taken into consideration: fixed salary, variable compensation and fringe benefits. This study tries to approach the agency problem from different perspective, focusing on variables that were not considered so relevant in past research and contextualizing it in the Italian environment where little or no evidence of such studies is found.

Fixed salary represents the major component of a remuneration system, so if properly structured it may contribute to increase directors' motivation in performing their work leading potentially to a higher firm performance. In the light of this what is expected is that:

Hypothesis 1: Is firm's performance affected in a positive way by fixed salary?

In this study the variable remuneration considers cash compensation on an annual basis under a system of "Management by objective" attributed only by the achievement of predefined company's objectives. The variable compensation is measured by company's indicators such as EBITDA, Net Cash flow before Dividend or by individual objectives associated with operational outcomes and plans that sustain the firm's economic performance on the market.

Hypothesis 2: Is firm's performance affected in a positive way by variable compensation?

Fringe benefits is an increasing adopted incentive system valid as variable compensation.

The fringe benefits are differentiated by management level and consist in insurance or healthcare plans, company car, laptop, mobile phones, sometimes accommodation and child care center.

Hypothesis 3: Is firm's performance affected in a positive way by fringe benefits?

3.2 Data and Methodology

The Empirical analysis was carried out on a sample of 165 Italian public listed companies in 2016.

The source of data for the companies listed is Borsa Italiana and for the financial data is Thomson Reuters Datastream.

The database focuses on some Board characteristics and some Corporate financial data.

For every single firm analyzed for the research, the 2016 annual report has been used to find information about the numerical composition of the board and other characteristics related to board members such as date of birth, nationality, gender, level of education, educational background, international work experience, tenure firm, if independent member, remuneration types: fixed and variable compensation and fringe benefits, if president or vice president and if CEO.
Financial data include market capitalization, common equity, total assets, leverage, ROA, ROE, long term debt over common equity and Tobin Q.
Finally, three simple linear regressions were created in order to understand the impact of fixed salary, variable compensation and fringe benefits on firm performance measured by Tobin Q indicator.
The linear regression is helpful in order to understand the bivariate and multivariate relationship between variables which are dependent, independent and control variables correlated by a coefficient. The correlation coefficient is non-parametric and just states that the two variables are associated with one another without explaining what kind of relationship exists between them.
The linear regression analysis is a linear relationship between X, the independent variable and Y, the dependent variable. Epsilon represents the random component of the linear relationship between X and Y.

$$\gamma = \alpha + \beta x + \varepsilon$$

Where Y is the value of the dependent variable in the observation. Alpha is a constant, or the intercept, and measures the value where the regression line crosses the y-axis. Beta is the slope, or coefficient, and measures the steepness of the regression line. Epsilon is the random component, or disturbance error term in the observation.

3.3 Variables

Dependent variable:

The Tobin's Q ratio is the performance index used as dependent variable in this study.
The Tobin Q formula measures the total market value of a company, divided by the total value of the company's assets. It calculates the worthiness of a firm over its assets. More specifically, the value of a firm should be equal to its replacement cost.
A value of Q between 0 and 1 implies that the company's worth is undervalued with respect to its possessed assets. It follows that it becomes an attractive investment opportunity for potential buyers. Instead a value of Q above 1 means that the company is overvalued in relation to its assets, implying that it generates more earnings than its replacement costs, which would induce other companies to

create similar businesses trying to capture some of the profits. A consequence of this would lead to reduce the firm value and cause its Tobin's Q to fall.

Independent variables:

In the study the three linear regressions are carried through different independent variables.

The first is based with fixed compensation, the second with variable compensation and the third with fringe benefits. Generally speaking, a change in the independent variable, it reflects also a change in the dependent variable.

Control Variables:

Control variables are different from independent variables, because their effect on the dependent variable does not change. Control variables have to be held constant and are not relevant in the specific analyses but at the same time they indirectly influence the dependent variable. So they enhance the accuracy of the relationship between the dependent and independent variable.

The control variables included for each of the three regressions are: ROA, Financial Leverage and Firm size.

Firm size is computed in this research as the logarithm of total assets and represents the total resources, capital and assets available to the company. Size may have a mixed impact on firm performance. Larger firms' may take advantage of economies of scale and learning effects but the dimensions can negatively impact the firm performance due to the increased complexity to manage the firm's assets specially to monitor the information process capacity between the different firm's departments.

ROA or Return on Assets measures how much of the firm's profit is generated by the use of the company's assets. ROA is a profitability indicator and calculated as net income over total assets.

It assesses the amount of earnings generated from the invested capital. The last control variable taken into consideration is Financial leverage.

Generally speaking, Financial leverage assesses the volume of additional debt taken by the company over its net worth. If the Financial leverage ratio is high, it means that the company has accumulated debt to finance its business and may not be able to generate enough cash flows. A declining cash flow can lead to an increased risk of insolvency. Financial leverage can be calculated in many forms. In this study the ratio considered is Long-term Debt over Common Equity. This type of leverage ratio assesses more accurately the leverage level of a company compared to its competitors.

3.4 Results and Discussion

Table 3.1- Descriptive statistics

Variable	obs	mean	std. Dev	Min	Max
ComponenteFissa2016	1.490	133514,5	294685,7	0	3.514.497,00
ComponenteVariabile2016	1.485	38138,5	336775,6	0	1,10E+07
Fringebenefits2016	1.472	8934,299	260675,5	0	9993000
ROA_2016	1.411	3,211906	11,34795	-36,07	117,61
Financial Leverage_2016	1.449	96,90244	148,0738	-686,25	647,7
size2016	1.464	13,47508	1,944688	8,288283	18,81899

The above table gives an overview of the variables used in the study. For each variable are provided observation, mean, standard deviation, minimum and maximum value. The observation for the different variables are almost in line. We can see that board members in our sample perceive on average a fixed compensation of 133.514,5 Euro, a variable cash compensation of 38.138,5 Euro, fringe benefits of 8.934,3 Euro and a maximum amount of 3.514.497 Euro, 11.000.000 Euro and 9.993.000 Euro respectively.

On average ROA, Financial leverage and Firm size have a value of 3,21, 96,9 and 13,5 respectively and a minimum and maximum value of -36,07 and 117,61, -686,25 and 647,7, 8,29 and 18,82 respectively.

The next tables will show the results of the three linear regressions in relation to Tobin's Q indicator.

Linear Regression 1:

$$Tobin\ Q_{2016} = Componentefissa_{2016} + ROA_{2016} + Financial\ Leverage_{2016} + Constant + \varepsilon$$

Linear Regression 2:

$$Tobin\ Q_{2016} = Componentevariabile_{2016} + ROA_{2016} + Financial\ Leverage_{2016} + Constant + \varepsilon$$

Linear Regression 3:

$$Tobin\ Q_{2016} = Fringebenefits_{2016} + ROA_{2016} + Financial\ Leverage_{2016} + Constant + \varepsilon$$

Table 3.2- Linear Regression 1

		Number of obs	=	1.372		
		F(4, 1367)	=	71,26		
		Prob > F	=	0		
		R-squared	=	0,263		
		Root MSE	=	0,67624		
					95% conf. Inter	
TOBIN_Q_2016	**Coeff**	**Rob. Std. Err**	**t**	**P>|t|**	**min**	**max**
Componentefissa2016	0.000**	5,27E-08	3,11	0,002	6,08E-08	2,68E-07
ROA_2016	0.033***	0,0030574	10,68	0	0,0266626	0,0386582
Financial Leverage_2016	-0.001***	0,0000754	-14,21	0	-0,0012185	-0,0009228
size2016	-0.040***	0,0103444	-3,85	0	-0,0600769	-0,0194917
Constant	1.894***	0,1512083	12,52	0	1,597054	2,190304

$p < 0.1^{+}$, p<0.05*, p<0,01**, p<0,001***

The first linear regression analyses whether fixed compensation affects positively firm's performance.

1.372 observations were considered for this linear regression constructed under a 95% confidence interval. A 95% confidence level implies that the results obtained from the analysis are statistically sound and confident at 95%. To have a more proper evaluation of the linear regression analysis along with the p value, an F-test was conducted. The upper part of the table shows the results of the F-test. This holds for all the three regression considered in the analysis.

The F-test must be used in combination with the p value in order to make sure that all the variables overall are statistically significant, because sometimes a significant result does not imply that all the variables are significant.

The F-test reduces the random chance between variables. The p value measures the probability whether the initial hypothesis is supported or not given the analysis made. The lower the p value is, the stronger is the evidence of the hypothesis.

From the table 3.2 we can see that all the variables coefficient is statistically significant, especially ROA, Financial Leverage and size at a p < 0,01% which is the maximum reachable confidence level. Focusing on the control variables, we see that ceteris paribus an increase of ROA increases the firm performance by 0.033, whereas an increase in Financial Leverage and size decreases firm performance by -0.001 and -0.040 respectively.

The fact that ROA is positively associated to firm performance makes sense, since if the company is able to generate earnings from its assets the firm performance increases.

The fact that the coefficient of Financial leverage impacts negatively firm performance makes sense since if the company is taking additional debt to finance its business it may imply that it does not generate enough revenues leading to a lower performance and increasing its financial risk.
The coefficient of Firm size is negative implying that the complexity factor in managing the firm's resources and assets affects negatively firm performance.
The positive effect of ROA and the negative effect of Financial Leverage and size on firm performance holds also in the next two linear regressions changing partially their coefficient values respectively.
The independent variable Fixed compensation is significant at a $p < 5\%$ implying that it influences firm performance. We can see that the coefficient is near zero, having practically a neutral effect on the performance but influencing it all the same in a positive way. This result supports our first hypothesis that fixed compensation affects positively firm performance.

Table 3.3- Linear Regression 2

		Number of obs	=	1.368		
		F(4, 1363)	=	69,31		
		Prob > F	=	0		
		R-squared	=	0,2593		
		Root MSE	=	0,67869		
					95% conf. Inter	
TOBIN_Q_2016	**Coeff**	**Rob. Std. Err**	**t**	**P>|t|**	**min**	**max**
Componentevariabile2016	0	6,85E-08	0,53	0,595	-9,80E-08	1,71E-07
ROA_2016	0.033***	0,0030584	10,69	0	0,0266821	0,0386816
Financial Leverage_2016	-0.001***	0,0000754	-14,13	0	-0,0012126	-0,0009169
size2016	-0.036***	0,0103005	-3,48	0,001	-0,0560319	-0,0156187
Constant	1.862***	0,1509895	12,33	0	1,56548	2,157874

$p< 0.1^{+}$, p<0.05*, p<0,01**, p<0,001***

The second linear regression focuses on whether variable compensation has an effect on firm performance. The analysis has slightly less observations than the preceding one and as before ROA, Financial Leverage and size are statistically significant with a $p < 0,01$ %.
The independent variable the "variable compensation" is not significant on firm performance.
This means that an increase or decrease of variable compensation has no effect on the firm's performance. This result does not support our initial hypothesis. This surprising result may suggest that variable compensation may be absorbed by other factors that makes it irrelevant.

For most Italian public listed companies, the attribution of variable compensation to members of the board, as previously mentioned in the paragraph 3.1, is based on a system called “Management by objectives” and given only by the achievement of predefined company’s objectives.

Variable compensation is measured by some company’s indicators or by individuals’ objectives associated with operational outcomes and plans that sustain firms’ economic performance on the market. The fact that the variable reward is given only if objectives are achieved, is perceived by the members of the board as a hypothetical and not certain compensation.

Relying on company’s indicator’s the variable compensation does not mirror the individual performance of a board member and if the individual’s objectives are set too high the variable compensation might be difficult to be achieved.

When variable compensation is based on individual objectives the compensation line may result unclear, since it is expressed in percentage on an amount varying from a minimum to a maximum value. Furthermore, objectives may be revised during the year making it quite difficult for board members to rely on those rewards.

Board members may prefer more secure compensation systems or incentives so that their individual performance is better recognized. In most Italian public listed companies fixed compensation covers the risk that the variable component is not awarded because of failed performance objectives.

This may explain the irrelevance of variable cash compensation. Furthermore, it reinforces the fixed compensation system as a valuable reward for compensating management according to their role and responsibilities leading to a reliable and equitable reward system.

Table 3.4 - Linear Regression 3

		Number of obs	=	1.357		
		F(4, 1352)	=	214,22		
		Prob > F	=	0		
		R-squared	=	0,2592		
		Root MSE	=	0,67698		
					95% conf. Inter	
TOBIN_Q_2016	**Coeff**	**Rob. Std. Err**	**t**	**P>|t|**	**min**	**max**
Fringebenefits2016	0.000***	5,67E-09	12,45	0	5,94E-08	8,17E-08
ROA_2016	0.032***	0,0030756	10,56	0	0,0264505	0,0385175
Financial Leverage_2016	-0.001***	0,0000754	- 14,16	0	-0,0012149	-0,0009192
size2016	-0.034***	0,0103149	-3,32	0,001	-0,054523	-0,0140532
Constant	1.843***	0,1510062	12,21	0	1,547225	2,139689

$p< 0.1^{+}$, $p<0.05^{*}$, $p<0,01^{**}$, $p<0,001^{***}$

The last regression of the study analyses whether fringe benefits positively affects firm performance. The number of observations are slightly inferior to the previous two regressions, but all coefficients are statistically significant at a $p < 0,01\%$ level.
Fringe benefits definitely affect positively firm performance. This result supports the initial hypothesis that an increase in the use of fringe benefits, even if the coefficient is near zero, influences positively firm performance.
This type of incentive system is an alternative way to reward individuals as compared to cash compensation. Fringe benefits may provide an enhanced working environment offering services that are more suitable for board members enhancing their performance.
Fringe benefits being additional elements going along with fixed compensation may explain the irrelevance of variable compensation.

Conclusion

This study gives insight of a new approach to analyze the agent problem by focusing on Italian public listed companies.
What emerges from the study is that, fixed compensation and fringe benefits are a valuable reward system in enhancing positively firm performance leading to a potential reduction of agency costs.
Fixed salary is statistically significant at a p value $< 5\%$ and fringe benefits is statistically significant at a p value$< 0,1\%$, the maximum reachable statistical significance level.
The variable compensation has no effect on firm performance, meaning that an increase or decrease of variable compensation does not impact on the firm's performance.
This suggest that the effect of variable compensation on firm performance is absorbed by other factors that makes it irrelevant.
In most Italian public listed companies fixed compensation covers the risk that the variable component is not awarded because of failed performance objectives. This may explain the irrelevance of variable cash compensation.
Furthermore, fringe benefits are an alternative way to reward individuals as compared to cash compensation and, being additional elements going along with fixed compensation, they may explain the irrelevance of variable compensation.

For future research it might be interesting to analyze whether equity based incentives (share ownership or stock options) have an impact on firm performance in the Italian context, in association with the agency theory perspective.