



Report on the governance of quoted companies

Executive summary

(English version)

A report for the **European Commission**, submitted by **Fondation pour le droit continental** and written by **Michel Germain, Véronique Magnier** and **Marie-Aude Noury**.

This study was commissioned by the **Fondation pour le droit continental** [Foundation for Continental Law]; this document presents a summary of that study. The aim is to promote the techniques of continental law on an international level in order to demonstrate their effectiveness and the security they contribute to business relations. Following the plan of action in European corporate law of December 2012, the Fondation pour le droit continental wanted to contribute to this thought process in order to **provide a vision of the governance of commercial companies which makes best use of the legacy of French law and its continental tradition** by presenting the particular features and attractions of French corporate law. The Fondation thus hopes it can propose some possibilities for development to the Commission.

The report was entrusted to a working party led by **Professor Michel Germain**, lecturer in corporate law at the Université Paris II-Panthéon-Assas where he also supervises the master's degree for corporate jurists and an MBA in Law and Management. The group also included **Professor Véronique Magnier**, lecturer in French and Community corporate law at the Université Jean Monnet Paris-Sud where she supervises the Master's degree in Business Law [Master 2] for corporate jurists, and **Maître Marie-Aude Noury**, barrister at the Paris Bar. The three authors then endeavoured to highlight some significant points of French law with a view to enabling advances in governance in European law.

Based on that report, the Fondation has identified certain strong points in French law which might be of interest to the European Commission within the context of implementing its plan of action in corporate law.

The debate is structured around three seats of power: the directors themselves, the shareholders and the stakeholders.

I. Governance as regards directors

This is the area which has seen the most significant changes, on account of the emergence of what is known as “soft law”, which has been formalised via “codes of governance” and sanctioned by the rule of “comply or explain”.

1. The assimilation of soft law by French law

The difficult challenge faced by French law has been to assimilate the Anglo-Saxon culture of soft law within an essentially legislative corporate law, specific to the continental legal culture. It seems that this challenge has been largely met.

1.1. The effectiveness of a juxtaposition of standardisations

This juxtaposition of two different standardisation systems, even of a “graduated standardisation” according to the terms used by the French Conseil d’Etat in its 2013 annual study on soft law, is successful and seems to provide an **effective system**. This juxtaposition however, requires delicate adjustments.

Community law has already opted for “mixed” corporate laws, combining laws and soft law, since the rule of comply or explain has been extended to Member States by means of a Directive. By allowing companies to dismiss certain recommendations of codes of governance, on the condition that they justify doing so, this rule offers them the possibility of replacing them with rules more specific to their areas of activity. The rule of comply or explain allows **adaptable governance**.

1.2. The variable intensity of the rules of soft law: example of the rule of “say on pay”

The intensity of the rule of say on pay is very **variable** depending on the country, due to its combination with legislative law. At this specific point, the agreement is that it is no doubt necessary to allow changes that are quite natural and purely sociological.

In French law, the rule of say on pay currently takes the form of a subsequent consultative vote on an already established remuneration. Everything suggests that its terms and conditions can evolve on a gradual basis.

1.3. The useful complementarity of soft law in matters of conflict of interest

French law experiences a rather original system known as **related-party agreements**, consisting of initially authorising agreements that are entered into between the company and its directors. This system is sometimes criticised for being cumbersome, but seems to provide relative **legal certainty due to its foreseeable nature**.

For less obvious cases of conflict of interest, French law sanctions **the individual liability of the director**, which operates subsequently and is a useful complement to the first system. This complementarity seems to be a realistic solution and builds an effective instrument.

2. The relevance of harmonisation of rules of governance by European law

It seems that it would be paradoxical to harmonise, by European law, rules of governance which are legitimate due to their proximity to the business world, since harmonisation of concepts of soft law is also much more delicate than that of legal concepts.

However, the advantage of harmonisation is clearly revealed within the context of **controlling the effective application of the rule of comply or explain** which may be provided for by law. In France, this control exists both in the register of soft law, provided for by the code of governance, and in the register of legislative law, where it is entrusted to the public authority of the AMF [French financial markets supervisory authority]. This dual control is an original way of organising a kind of co-supervision of the rule of comply or explain.

Reflecting French law, European law could provide for a **dual system for controlling** the application of the rule of comply or explain and thus become guarantor of genuine governance, which would combine the advantages of **certainty** and **foreseeability** of a legal framework with those of the **flexibility** and **adaptability** of soft law. The Commission's action could then seek to harmonise the mechanisms for controlling the application of the rule of comply or explain.

II. As regards shareholders

In France and in Europe, increasing emphasis is being placed on the long term.

1. Establishing shareholders' loyalty

For a long time, French law has had a **double voting right** and, more recently, a **preferential dividend** which compensates the loyalty of shareholders. This French experience, once decried in Europe, seems advantageous and could even, apparently, be improved relatively easily.

2. Identification of shareholders

The **transparency of the shareholders' identity** is an option which French law offers all companies. It would seem strange to us if European law were to go back on this principle, when transparency is so valued elsewhere.

III. As regards stakeholders

A distinction needs to be made between two types of stakeholder: salaried employees, who may contribute to governance, and civil society, which legitimately has a kind of right to monitor the action of companies. Their statuses could be improved in European law.

1. The participation of salaried employees

French law has always taken an interest in the participation of salaried employees. This can be understood in more ways than one. French law offers at least two systems for participating on the board of directors: a specific system for participation of salaried employees-shareholders and a quite recent system for participation of all salaried employees through appointing their representative on the board of directors.

These two systems are possible models for Europe. We might legitimately hesitate between the two. But we might also think that the participation of salaried employees-shareholders is a more limited, but no doubt more effective, expression of the shareholders' interest.

2. Liability vis-à-vis civil society: corporate social responsibility

Recent corporate social responsibility law, of which **French law is one of the precursors**, along with the 2001 Law on New Economic Regulations, is also a possible source of inspiration.

In the light of a proposal for a Directive of 16 April 2013 proposing that companies submit a non-financial declaration with the annual report, European law seems to be going in the direction of a principle of transparency in social and environmental matters. The antecedence of French law on this subject should enable it to propose relevant solutions for improvement.

Conclusion: Proposals which could be accepted

- As regards the rules of **soft law**, the French Conseil d'Etat talks about a “**graduated standardisation**”. Codes of governance would have to **set out these different levels clearly**, which is not always the case. Otherwise, there is a high risk that the distinction between these levels lacks clarity.
- In matters of **conflict of interest**, the **combination of laws and rules of soft law** as it exists in French law is a very effective harmonious solution.
- Reflecting French law, European law may envisage a **dual level of control**, in law and in soft law, in order to guarantee the genuine application of the rule of comply or explain by companies.
- In matters of **establishing shareholder loyalty**, French law proposes solutions that may usefully inspire the European Commission, which seems to want to favour a long-term structure.
- The French system of **participation of salaried employees-shareholders** could be an example from which it would be interesting to draw inspiration with the intention of reinforcing a social consensus that is lacking in a certain number of companies.
- **The French law on corporate social responsibility**, one of the rare laws which has had some practical experience, is expressed through an **elaborate legal framework**. It can thus claim to be an effective source of inspiration for the European Commission in matters of companies' transparency in social and environmental terms.