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# *Do socially responsible managers violate their fiduciary responsibilities?*

Daniel Hurstel

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# I. “Fiduciary duties” in a European context

# I.1 The importance of “corporate purpose”

- The present situation with respect to “management autonomy” is the result of two opposite basic features in French History of corporations:
  - Since the French revolution, ownership has been considered an absolute and exclusive right, and the Civil Code reflects the importance of shareholders in corporations
  - Stakeholders primacy in France – the law on commercial companies of July 24th, 1866 enshrined the corporation as a “stand alone institution” independent from its shareholders
- Under the influence of the American trend towards shareholder primacy, as well as, more generally, Anglo-American conceptions of corporate governance, and in the context of globalization and the liberalization of financial markets from the 1980s onwards, a more shareholder-centered vision has had a real influence in France since the 1990s
- More recently the trends went again towards stakeholders capitalism

# I.1 The importance of “corporate purpose”

- Fiduciary duties to shareholders do not exist as such in a civil law context
- Under the law on commercial companies of July 24th, 1966, the corporation although the result of a contract between shareholders can be viewed as a stand-alone “institution” independent from its shareholders
- The primacy of stakeholders allows significant level of autonomy to corporate managers, who have to act in the corporate interest of the company
- The French commercial code provides:
  - “*The president, directors or general managers of a corporation to make, in bad faith, a use of the property or credit of the corporation that they know to be* ***contrary to the interests of the corporation****, for personal purposes or to favor another corporation or enterprise in which they are directly or indirectly interested* ”. (L. 242-6, 3)

# I.2 Corporate interest as measure to managers' liability

- Corporate purpose is the basis for courts to determine whether a manager is liable for mismanagement. So to determine the liability of a manager, the courts will not analyze the quality of the management but only whether or not it violated the corporate interest
- Despite the fundamental importance of the concept, debate continues about the extent of the "corporate interest"
- Perspectives range from: the corporate interest is the interest of the shareholder to the interest of the enterprise itself, a synthesis of the different categories of stakeholders interests
- The primacy of the shareholder has never completely replaced the traditional French understanding of the corporate interest as representing a distinctly independent interest of the corporation, informed by different stakeholders' interests
- [The obligations to act in the corporate interest are in addition to specific statutory or court-based specific obligations but they are not relevant here]

# I.3 Recent evolution of corporate interest

- On April 11th, 2019, France passed the so-called “PACTE” law, which amended Article 1833 of the French Civil Code to require that a corporation not only have a lawful purpose and be incorporated in the common interest of shareholders, but also that the corporation be “*managed in its corporate interest, while taking into account the social and environmental issues related to its activity*”
- Thus by taking into account the relationship between the corporation and greater social concern
- The French Commercial Code was simultaneously modified to specifically require the governing bodies of the company to consider these issues in their decision-making
- The consecration of the corporate interest would confirm at the legislative level a fundamental aspect of the management of companies :
  - *"the fact that they are not managed in the interest of particular persons, but in their autonomous interest and in the pursuit of their own ends”*
- The draft enshrines the concept of corporate interest without defining it because:
  - *“the relevance of its practical application rests on its great flexibility, which makes it resistant to any confinement in pre-established criteria. The elements necessary to determine whether or not a decision is contrary to the social interest depend too closely on the protean and changing characteristics of the activity and environment of each company*”

# I.3 Recent evolution of corporate interest

- In addition, Article 1835 of the French Civil Code was amended at the same time to permit a company to set out its "*raison d'être*" (or corporate purpose) in its articles of incorporation, consisting of the principles governing the company's conduct, including how the business allocates resources
- A company's "*raison d'être*" can be described as what is essential to fulfil its "*intérêt social*"
- A well-drafted "*raison d'être*" may provide the board and management with an additional justification of adopting a broader view of the corporate purpose, distinct from that of the shareholders
- However, in the same way, a "*raison d'être*" will limit the board's and management's flexibility, as they will indeed be obliged to take the "*raison d'être*" into account in their decision-making, with potential implications both for their personal liability and changes to the "raison d'être" thereafter (noting the high threshold for modifying the articles of incorporation)
- Lastly, the disregard of the raison d'être by a director would constitute a violation of the articles of association likely to engage his liability towards the company and the partners (cf. in particular C. com. art. L. 223-22 and art. L. 225-251)

# II. In addition to acting in the corporate interest, managers have specific CSR obligations

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- Over the last 20 years, the trend to enshrine ESG principles into law has taken a more dramatic turn in France. In that case, the liability again is clear – shareholders interest does not allow to disregard the specific obligation
- As examples:
  - in 2001, certain listed companies were required to include qualitative and quantitative information on the social, societal and environmental consequences of their activity in the management report*
  - this reporting obligation has progressively been reinforced and expanded to cover non-listed companies (exceeding certain thresholds) and to require data verification by an independent third-party organization**
  - at a European level, the Non-Financial Reporting Directive imposed requirements for the disclosure by large companies of non-financial and diversity information. This directive was transposed into French law in 2017
  - the need for boards of directors to consider not only the shareholders' short-term interests but also long-term social and stakeholder concerns
  - listed companies and, since the 2019 PACTE law, other companies meeting certain thresholds in terms of number of employees, have an obligation to include employee representatives in the management bodies, gender diversity and employee welfare
  - regarding gender diversity, for companies whose shares are admitted to trading on a regulated market or which meet certain financial metrics and employment conditions, the proportion of directors of each gender must be at least 40%



*« NRE » law, 2001
** Grenelle 2 Act, 2010

# III. New sources of pressure on managers obligations

# III.1 Pressure from Courts

- In December 2019, a judge in the Hague ordered the Anglo-Dutch Shell to reduce its CO2 emissions by 45% by 2030 and to comply with the law
- A similar lawsuit opened against TotalEnergies in January 2020
- The court acted upon a claim from Milieudefensie, the Dutch branch of the environmental action group, Friends of the Earth.
- Very recently that Dutch group sent a letter to 29 multinational companies (car industry, chemical industry, banks, investors, etc.) active in the Netherlands requesting a stronger involvement in climate change actions
- “One of the big reasons for the judiciary to exist is to bring balance in society and to protect us from human rights violations from our governments and other large entities that dictate our world and our wellbeing”
- “It is just a matter of time [before] the same kind of approaches will also be successful in other countries.” (Cox, a Dutch lawyer, author of “Revolution justified: why only the law can save us now”
- The legal basis for the courts’ actions is the “widespread human rights violations”
- This mean of pressure is also used by other societal activists: last month in Germany, Greenpeace sued Volkswagen to end the production of combustion – engine cars and cut totals emissions by 2030. Comparable cases have been opened against BMW and Daimler

# III.2 Pressure from Society

- There is a growing link between trust and share price. If trust is broken, share price falls immediately and more then is the past overreaction to media buy market players fear also for their images.
- One recent and interesting example: Orpea is a listed company operating care homes. A book published a few days ago "*Les Fossoyeurs*" (the Gravediggers) describes alleged mistreatments of elderly residents of Orpea nursing homes. After publication, the share lost 60% of its price in a few days. Where is the interest of shareholders? At what stage did managers become liable?

# III.3 … and from social activism

- Operating in countries where human rights are violated. The most recent example is Myanmar
  - Total and Chevron have announced their withdrawal from the country: point to abuses and human rights violations. These companies faced strong pressure from human rights activists and decided to divest their position in the gas industry; EDF has suspended its dam project; Japan's Kirin is in a long process of extracting itself from its long-criticised joint ventures with a military company that makes what used to be Myanmar's top-selling beer; Norway's Telenor is trying to sell its Myanmar business after facing regime pressure to install eavesdropping equipment
  - The activities in Myanmar were profitable, a narrow understanding of shareholders interests would have remained present
- Climate:
  - The **UN-convened Net-Zero Asset Owner Alliance**, made up of 69 large institutions, said its members would aim to reduce emissions linked to their investments by between 49 per cent to 65 per cent by 2030, after including a broader range of carbon-intensive sectors within its target framework
  - Fifteen institutional investors and individual shareholders gathered within the "ShareAction" collective have obtained the vote, at HSBC's general meeting, of a project committing the bank to stop financing fossil fuels at the latest in 2040

# IV. Shareholders' expectations tend to change

# IV.1 Shareholders express new interests

- In 2021, major investors took major steps through engagement and proxy voting efforts, to demonstrate their commitment to addressing climate transition and board and workforce diversity and inclusion, with a focus on disclosure and reporting of key ESG metrics and how the board, including its committees, oversees these issues
- In 2022, major investors have indicated that they plan to revisit the same issues, but with focus on strategy, innovation, and harnessing stakeholder capitalism to guide long-term value creation
- BlackRock and State Street's recent CEO annual letters clarify:
  - Decarbonization, not divestment, should be the primary solution for "brown" assets
  - The net zero transition will not be uniform, and companies will need to disclose their own transition plans, targets and progress
  - The green race will reward leaders, not followers
  - Boards will be at the forefront of the transition to the new economy : the role of boards has become ever more expansive and challenging, with investors expecting boards to oversee ESG issues alongside traditional strategic and financial matters
- Annual letter of Larry Fink explains:
  - "a company must create value for and be value by its full range of stakeholders in order to deliver long-term value for its shareholders"
  - "putting your company's purpose at the foundation of you relationships with your stakeholders is critical to long-term success"
  - "ESG, sustainability and long-term growth in value of the corporation reflects the now-widespread abandonment of a myopic focus on shareholder profits"
- The UK concept of "enlightened shareholder values"

# IV.1 Shareholders express new interests

- Many large investor groups have formed around attempts to limit the risks of climate change to the global economy. The largest of these groups is the "**Climate Action 100+**", which represents $60 billion in assets, including many of those at the United Nations conference

# IV.2 Activism has an influence over all shareholders

- France has a long-standing and vigorous tradition of activism, and French and European laws and regulations furnish both the activist and the target company's board and management with a variety of tools
- In Europe, the number of activist campaigns is steadily increasing. France is the third European country where activists are the most active
- Activism may have a short term profit goal but it raises issues (governance and strategy mainly but also transformation and climate) that management has to take into account and address
- To a certain extent, all institutional investors are under pressure to become active if not activists

# V. The manager's responsibility regime is an open question

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- Not satisfactory because exposure is extremely broad and evolution of the courts' position is unpredictable and not determined under French law. We need management who can take risks but not uncertainty about their liability
- Managers will have to privilege some interests over others and such prioritization may vary from one project to other and over time. How to answer this challenge? What governance structure will enable managers to adequately prioritize between various interests?
- The role of managers is growing, as is their discretionary capacity. Are we heading towards a new period of strong management power? What type of relations between board and shareholders, and between board and CEOs?
- Are we also leaning towards strengthened managers liability?
- How to arbitrate between profit and consideration of social issues?
- How to acquire knowledge of the shareholders interests?
- How to monitor so many interests without losing the fundamental features of businesses: delegation of authority and efficiency of decision taking process?



*Le Monde, « *Les mégaprofits du CAC 40 et le débat récurrent sur le partage des bénéfices* », 31 janvier 2022