Corporate governance: changing the paradigm

by

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Introduction

"Two institutions overdetermine the fate of the human being at work and on the planet Earth: what economists call the labor market and the company" (1).

If we admit that the company and the markets on which it interacts have a determining impact on our lives and our future, then the composition and legitimacy of the bodies that govern it represent a major challenge. We can then understand that the evolution of governance constitutes a powerful lever to initiate and accelerate the transformation of our society and to act effectively on the ecological transition and the reduction of inequalities.

In the first part, we shall see whether the new provisions of section 3 of the Pact Law, devoted to corporate governance, are equal to this ambition and whether they mark a real evolution, or even a breakthrough, in corporate governance or, on the contrary, whether they are the result of an adroit and seductive communication strategy without any real desire to change the lines. In the second part, we will examine the conditions for a paradigm shift in this area, which will lead us to question the notion of "common good" and to ask ourselves the central question of corporate ownership, from which stems any reflection on a fairer and more indispensable representation of stakeholders within governance bodies and contribution to strategic decision-making. Five proposals will be formulated, some of them based on the need for a profoundly renewed institutional scheme and not on the search, undoubtedly illusory and certainly insufficient, for good practices within an unchanged framework.

I. The Pact Law: "A rethinking of the place of the company in society": ambition or discourse? (2)

Part 3 of the Pact law enacted in 2019, entitled "fairer companies", inspired for the most part by the recommendations of the Notat/Sénart report, displays the ambition of a rethought place of the company in society.

1.1. Presentation of the main provisions of section 3 of the Pacte 3 law devoted to corporate governance and inspired by the report prepared by Nicole Notat/Jean-Dominique Sénart

The Pact law enacted in 2019 takes note of the recommendations of the report drawn up in 2018 by Nicole Notat and Jean-Dominique Sénart and states in particular:

- A lowering of the number of directors from twelve to eight as the threshold for appointing two employee directors, a change which in reality does not call into question the way in which boards of directors and supervisory boards operate today and the way in which managers are appointed.
- The recognition by the Civil Code of a "raison d'être" for the company, which is explicitly stated in the articles of association. The amended article 1883 of the Civil Code introduces the quality of "company with a mission", which refers to a desirable progress, a desirable future, a "common" objective of an environmental, societal or cultural nature. It specifies that: "the company must be managed in its own interest, taking into account the societal and environmental stakes of its activity". It should be noted that the Nanterre judicial court, whose jurisdiction was challenged by Total SE in a case opposing it to several stakeholders, relied on this article to declare itself competent in the matter (order of February 2021). A new governance structure is proposed, the mission council, composed of members representing employees, other stakeholders such as NGOs and representatives of local authorities. The authors of the report also insist on the need to revalue the role of managers, in the spirit of the work of the Collège des Bernardins, which considers the manager today to be the agent of the shareholders (agency theory) to the detriment of "the effectiveness of management power" and the "creative dimension of the managerial function"(3)

1.2 "A new form of law being created"(4) or the search for the lowest common denominator on the subject of governance?

Do these provisions represent a real innovation in terms of the representation of stakeholders other
than shareholders within the company's governance bodies?
If the concept of mission is undoubtedly attractive, what is important is to appreciate in what way the
mission council would constitute an effective counterweight to the power of the shareholders and to
measure the binding force of its opinions in the event of "conflicts" between the expectations of the
shareholders and the objectives of the mission which it monitors. But what does the Notat/Sénard
report say on this subject? What role does it intend this mission council to play and what power does it
confer on it? According to the authors, its purpose is to allow "managers to take a step back from their
decisions", "to obtain additional opinions on the company's raison d'être", "to provide an external
stimulus in favour of Corporate Social Responsibility (CSR) and sometimes to find solutions to
difficult situations". Finally, "the Board of Directors would be informed by the management of the
possible conclusions of this committee".
This mission council would play the role of a good conscience for managers and the board of
directors. The authors of the report speak of "awareness" and of "the company's taking a step back
from the risks and opportunities caused by its social and environmental positions and activities",
formulations whose vague and non-binding nature underlines the desire not to call into question the
existing and very unbalanced balance of power between the shareholders and the other stakeholders,
and therefore the lack of real power of this committee.
It is striking to note that the authors of the report have left out of the discussion what should be the
central element of governance, namely the confrontation between several conceptions and visions of
the role and place of the company in society, as expressed and embodied by the various stakeholders.
The authors presuppose a "natural" and therefore non-conflicting articulation between at least two
goals, pretending to forget that they are often opposed and that they are part of different time frames,
namely the one defined by the medium- and long-term social utility mission, and the other the short-
term maximization of profits expected by shareholders.
However, as Olivier Favereau points out, "it would be naïve to believe that we could correct such
stabilized practices without changing the ideas that give them meaning and justification" (5) since it is
not only a matter of negotiating but also "of influencing strategic decisions" (6).
In March 2021, two investment funds obtained the ouster of Emmanuel Faber, Chairman and CEO of
the Danone group, the first listed mission company. It is difficult to affirm the existence of a link
between the two. However, it is possible to argue that, despite the status of a company with a mission,
financial logic has once again imposed itself.
This logic is also reflected in the France stratégie reports on corporate governance and employee
participation, which also state the principle of favouring an approach based on the dissemination of
good practices through a so-called "integrated" approach (better information, employee consultation,
employee shareholding) and limiting legislative and regulatory changes to a minimum.
In short, the authors of the report, and the Pact law which is inspired by it, refer to ideas in the air of
time, and make a set of attractive recommendations, but whose formulation and contours empty them
of any substance or binding force. By avoiding a debate and a reform on the substance, they are in line
with a logic of marginal adjustments in an unchanged framework of governance, while giving the
illusion of a rethought place of the company in society.

II. In search of the conditions for a paradigm shift in governance

If we accept as a basic premise and a fundamental requirement the search for a new growth model for
companies, respectful of the environment and socially equitable, then we must recognize that the
primary role of the company can no longer be the maximization of profits but the sustainability of its
growth mode fully integrating "the societal and ecological stakes of its activity" to use the terms of the
Notat/Sénart report.
If we consider that this more virtuous and less costly model at the macro level for our society, i.e.
beyond the limits of the company, resulting from the elimination or at least the reduction of negative
externalities generated by a growth model that essentially ignored them, leads to a surplus of
investments and additional expenses for some of the actions of the virtuous company, then we need to
imagine specific financing modalities to put them back on an equal footing with other companies.
2.1. Changing the rules of corporate governance in depth

Talking about changes in corporate governance (in large companies and not in SMEs/SMBs, for which the subject of governance is posed in rather different terms) implies first of all defining and asking the question of the nature and ownership of the company: what is the company and who owns it?

A research group, led by Olivier Favereau, has been working for several years on the notion of the firm, essentially a legal UFO, distinct from that of the company, which is recognized by law. The former constitutes a common good, the latter is considered the property of the shareholders, who are in law only the owners of their shares. According to Olivier Favereau, the main consequences of this legal artifice are: "the primacy of the irresponsible shareholder over any other stakeholder in the company", "the alignment of the interests of managers with those of shareholders" and finally "the misunderstanding of the company as a collective" (7).

Company law confirms that the company belongs only to the contributors of capital and ignores (for the most part) the contribution of employees' skills (engineers, managers, employees, workers), and the contributions of public services "offered" by the State and local authorities. Commercial law does not recognize the existence of a "common good" or the notion of "stakeholders" that might be associated with it. It recognizes only the shareholders.

As commercial law stands, only the shareholders appoint the members of the board of directors, and in fact ensure, through the intermediary of the managers they have chosen, the running of the business.

According to Isabelle Ferreras, "There can be no real corporate governance in a framework of unrecognized capital sovereignty. In this logic, she proposes to apply political bicameralism to the field of business, with the consequence of creating two chambers of equal power, that of the "representatives of the capital contributors" and that of the "representatives of the investors in labor" (8). These two chambers appoint the corporate government that reports to them. Bicameralism differs from the principle of co-determination as it exists in countries such as Germany, insofar as the latter gives the shareholder a final casting vote.

Olivier Favereau, who endorses this bicameral logic, affirms that "the exit from the great deformation of the enterprise will be achieved through politics" and that it is "on new rules of responsibility, not derived from the right of ownership, that it is advisable to rely in order to release both new sources of legitimacy and new factors of collective efficiency. (9)"

If another path is possible (10), to use the title of a recently published work, and if it is imperative to commit to it, should we propose an institutional evolution applicable to all companies, which is highly desirable but difficult to achieve, or on the contrary, should we take a more gradual approach based on exemplarity? It is the second choice that we favor. The idea is to demonstrate, in an experimental way, that another model can work and coexist with the current dominant model, before proposing to generalize it. This is why we propose, first, the creation of a new legal status for the social-ecological enterprise (11) whose corporate governance bodies, board of directors or supervisory board, would ensure an equal place for employees in relation to shareholders and a right of representation for other stakeholders, in particular local authorities.

In an economy as globalized as ours, which favors social and fiscal dumping practices and where "States are now in competition with companies", (12) how can we not mention the need to engage in a second phase of advocacy with European institutions for the creation of a "social-ecological" European company that can benefit from privileged access to European funding? In this case, the example and the demonstrative force of the reform would come "from above". Note the existence of Cooperative and Participative Societies (SCOP) which partly correspond to this type of model, but which seems at this stage to be a form of company favoured by small companies with an average workforce of less than 20 people.

2.2. Ensure the conditions for the financial sustainability of a new mode of business growth

We have assumed that this new growth model, which fully integrates social and environmental issues into its mode of development, requires specific investments and additional costs to avoid or correct
what we have called the negative externalities linked to the activity.
Access to specific financing is therefore a condition for the sustainability, this time financial, of this model of social-ecological growth: public financing, a lighter tax regime (reduced rate, exemption, franchise), ethical funds.
In practice, the new status of "social-ecological" enterprise(13) would entail a certain number of obligations subject to certification, thus ensuring that these specific provisions have unquestionable probative force and eligibility, including

- Formalize the company's new social-ecological reference framework by means of a charter (or other document) that includes the commitments made in this area. This charter would be fully enforceable against third parties.
- Draw up a medium-term budget forecast (for a period of three to five years) detailing the investments and expenses planned for the period related to the achievement and respect of these commitments, as well as an annual statement showing the amounts recorded for this purpose in the company's accounts. These documents would form an integral part of the company's financial appendix and would be subject to certification by the statutory auditors.

These obligations would be the counterpart to privileged access to inexpensive sources of financing and to advantageous taxation, proportionate to the scale of the investments and expenditures allocated to achieving the objectives. The principle of a scale structured around different investment and/or expenditure thresholds could be considered.

Obtaining public financing and benefiting from a reduced tax burden for this new company status could be considered and perceived as an attack on "free competition". On the contrary, we consider that these provisions would not only re-establish the conditions for nominal competition but would be similar to a system of reallocation of avoided expenses in the form of specific and dedicated financing. However, it would be necessary to have an opposable and shared measurement system that would allow them to be quantified and accounted for! While it is not the purpose of this article to deal with accounting standards and principles, it must be noted that they do not adequately reflect the "non-market" costs and debts generated or created by business activity and, consequently, the cost of negative externalities borne by the community. (14).

Finally, the use of ethical funds would be facilitated by an institutional communication around this new status of companies and by obtaining a certification with a higher probative force than that given by the existing labels. The creation of a specific "stock exchange" to facilitate access to these ethical funds should be explored.

In summary, five proposals are formulated and should be considered as possible courses of action:

- **Proposal 1**: Create a new form of company whose governance is based on equal representation between shareholders and employee representatives. Members of a single board of directors or supervisory board, they appoint the company's management, which reports to them. The local authorities interested in the development project have a right of representation and a privileged right to act.

- **Proposal 2**: Associate with this new company status the obligation to formalize a social-ecological frame of reference and a medium-term budget forecast. The commitments made by the company in terms of business sustainability and social justice constitute the company's social-ecological reference framework. The investments and associated expenses are formalized in a medium-term budget forecast. The whole is submitted to the vote of the Board of Directors.

- **Proposal 3**: Submit to the certification of accounts the control of the reality and conformity of the investments made and the expenses incurred in relation to the commitments defined in the social-ecological pact. The scope of this certification covers the provisional medium-term budget, the annual monitoring of investments made and expenses incurred.

- **Proposal 4**: Ensure financial sustainability through public funding and favorable tax treatment. Eligibility for public funding and/or tax relief is conditional on obtaining certification, the subject of proposal 3.

- **Proposal 5**: Promote, through institutional communication, this new status of "social-
ecological" company to encourage access to ethical funds.

As a provisional conclusion, the adoption by the company of a virtuous mode of growth, with the objective of significantly reducing the negative externalities generated by its activity, requires, as we have tried to demonstrate, a profound change in the rules of corporate governance, which the Pact Law, beyond a clever discourse and a seductive concept of "the company with a mission", has not wanted. But as we have seen, this necessary condition is far from sufficient. It must be accompanied by the mobilization of other actors, local authorities, ethical funds and finally the State. The European Union, which is certainly dominated today by the major principles of a neo-liberal economy, must eventually constitute the institutional space of reference and propose a European statute for the social-ecological enterprise.

Notes and Bibliography
(2) the quotations in paragraphs 1.1 and 1.2 refer essentially to the minutes of the council of ministers of 18 June 2018 and to excerpts from the Notat/Sénart report, cited by Danièle Linhart in her article "Un rapport de plus sur l'entreprise" *les possibles été 2018*, and her book *l'insoutenable subordination du salarié*, editions cires, 2021.
(4) The lawyer Jean-Philippe Robé, in an article in *Le Monde* of March 21, 2021 entitled "la revanche du droit" (the revenge of law) wonders in these terms: "perhaps we have before our eyes a new form of law being created".
(6) and (8) Ferreras Isabelle, *Gouverner le capitalisme ? Pour le bicamérisme économique*, PUF, 2012.
(10), (11) and (13) Heyer Eric, Lokiec Pascal and Méda Dominique, *Une autre voie est possible, vers un modèle social-écologique*, Champs actuel, 2018 édition augmentée 2020.
(14) Kuhanaathan Ano, Métadier Benjamin, "How to accelerate the implementation of ecological accounting," Rousseau Institute, March 2021.