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The Role of Corporate Law in French Corporate Governance (reprinted in *The Legal Basis of Corporate Governance in Publicly-held Corporations: A Comparative Approach* (A.R. Pinto & G. Visentini eds. 1998))

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James A. Fanto*

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Introduction

This Article evaluates how well French corporate law creates a corporate governance favorable to capital market investors.¹ French corporate gov-

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1. French corporate law and securities law are not separate legal topics, but are part of the same legal code. All references to this law are to CODE DES SOCIÉTÉS [C. SOC.] (Paul Le Cannu ed., 14th ed. Petits Codes Dalloz 1997) (Fr.).

ernance is a timely subject because it currently has the attention of members of the French legal, business and financial communities.² French legal thinkers are increasingly examining corporate governance both in their country and in other countries to understand solutions to corporate governance problems and to reflect generally on the French situation.³

This Article makes three assumptions. First, the separation of management and ownership is characteristic of large corporations. Second, there is no single, economically superior answer to the agency problem that arises from the differences between manager and shareholder interests. Third, technological changes and the globalization of the economy are pushing corporate governance worldwide towards a U.S.-style market capitalism.

As to the first assumption, economists, finance theorists, and management scholars who study large public corporations have identified a central corporate characteristic that arises from the legal and practical nature of the corporate "personality": the general separation between the interests of managers who operate an enterprise and shareholders who own it. Corporate governance involves designing or altering a firm's governing structure to ensure that managers, as the shareholders' "agents," operate the firm for shareholders/owners, and not for other purposes.⁴

Corporate law creates the corporate personality and establishes legal relationships between shareholders and managers. Thus, from an agency perspective, the efficacy of this law can be judged by how well it both facilitates the alignment of managers' interests with those of shareholders and addresses abuses in the relationship. Yet law is only part of corporate governance. Because a corporation exists in many domains, such as in product, service, and capital markets, other forces pressure managers to respond to shareholders. From an agency perspective, corporate governance thus implicates many social activities and benefits from study within

2. For recent reform proposals concerning French corporate governance, see COMMISSION DES OPÉRATIONS DE BOURSE, 27ÈME RAPPORT AU PRÉSIDENT DE LA RÉPUBLIQUE 85-89 (1994); CONSEIL NATIONAL DU PATRONAT FRANÇAIS & ASSOCIATION FRANÇAISE DES ENTREPRISES PRIVÉES, THE BOARDS OF DIRECTORS OF LISTED COMPANIES IN FRANCE (July 10, 1995) [hereinafter Viénot Report] (named after Marc Viénot, the chief executive of Société Générale, who presided over the committee that prepared the report); PHILIPPE MARINI, RAPPORT AU PREMIER MINISTRE SUR LA MODERNISATION DU DROIT DES SOCIÉTÉS (13 juillet 1996) (reform proposal on French corporate law) [hereinafter Marini Report]. See generally JAMES A. FANTO, CORPORATE GOVERNANCE IN AMERICAN AND FRENCH LAW (1997); James A. Fanto, *The Transformation of French Corporate Governance and United States Institutional Investors*, 21 BROOK. J. INT'L L. 1 (1995) [hereinafter Fanto, *Transformation of French Corporate Governance*]. See *infra* Conclusion.

3. See, e.g., Olivier Pastré, *Le gouvernement d'entreprise: questions de méthodes et enjeux théoriques*, 31 REVUE D'ÉCONOMIE FINANCIÈRE [R. ÉCON. FIN.] 15 (1994); Jean-Marie Thiveaud, *De la gouvernance des grandes sociétés: un incessant différend dans l'espace et le temps*, 31 R. ÉCON. FIN. 243 (1994).

4. See generally Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308-10 (1976).

numerous disciplines.⁵ This Article focuses only on the law's contribution to the alignment of shareholder and managerial interests.

The second assumption is that, to date, there has not been one economically superior answer to the agency problem. At any specified time, in different countries, and even within the same country, numerous solutions to the problem of ensuring that managers operate firms for the shareholders' benefit have been, and continue to be, employed. The success and profitability in national and world markets of corporations based in different countries, at the very least, suggests that several approaches to aligning management and shareholder interests have worked.⁶ According to an evolutionary metaphor used in economics and legal studies, countries and companies, like biological organisms, have adapted different corporate governance practices to their circumstances.⁷

If different corporate governance practices exist in corporations and countries throughout the world and firms successfully function in their markets despite these differences, then corporate governance must be subject to, although not entirely dictated by, cultural or situational influences. An understanding of corporate governance in any country should identify the cultural forces that, at a given time, push relationships between shareholders and managers in a particular direction.⁸ These forces include legal doctrines which influence shareholder/manager relationships, pressures from groups and individuals who have a stake in a particular governance solution or structure, and a country's traditions of firm ownership.

This Article's presentation of the role of law in French corporate governance acknowledges this cultural background. Yet, like economic destiny, corporate governance is no longer entirely under the control of any nation state. Indeed, corporate law scholars debate whether a transformation in the world business environment has caused a "convergence" of corporate governance whereby cultural factors are losing their influence. The industrial world is in the middle of a massive restructuring that began around the middle of the 1970s.⁹ Developments in technology (particularly in communications technology) now allow economic tasks to be both

5. See, e.g., Michael C. Jensen, *The Modern Industrial Revolution, Exit, and the Failure of Internal Control Systems*, 48 J. FIN. 830 (1993) (discussion from finance perspective); John Pound, *The Rise of the Political Model of Corporate Governance and Corporate Control*, 68 N.Y.U. L. REV. 1003 (1993) (discussion from public policy perspective).

6. See, e.g., Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737, 769-73 (1997) (discussing success of different kinds of corporate governance).

7. See generally Ronald J. Gilson, *Corporate Governance and Economic Efficiency: When do Institutions Matter?*, 74 WASH. U. L.Q. 327 (1996); Mark J. Roe, *Chaos and Evolution in Law and Economics*, 109 HARV. L. REV. 641 (1996).

8. See generally James A. Fanto, *The Absence of Cross-Cultural Communication: SEC Mandatory Disclosure and Foreign Corporate Governance*, 17 NW. J. INT'L L. & BUS. 119, 134-37 (1996). Culture does not determine corporate governance arrangements, but it strongly influences them. Cf. Michael C. Jensen & William H. Meckling, *The Nature of Man*, J. APPLIED CORP. FIN., Summer 1994, at 4, 10 (observing that the social exists in a dialectic with the individual).

9. See Jensen, *supra* note 5, at 835-47.

completed at lower-costs and connected where they were previously separate. This results in overcapacity, making some enterprises, and indeed entire industries, obsolete. The technology can also lead to more flexible, less hierarchical work environments that facilitate rapid product changes and responses to customer needs.¹⁰ Other events, such as the breakdown of the Socialist block and the reduction of trade barriers, heighten global product market competition, which is already exacerbated by technological and organizational change. Businesses that use technology and human resources efficiently stand a better chance of prevailing in their product markets.

Technological changes also create different ways to raise both capital and invest. Investors, whether individually or through financial intermediaries, have increased access to investments throughout the world. Further, because companies can raise capital in different markets, they are no longer limited to domestic investors.¹¹ The companies best able to utilize new capital-raising opportunities and financial innovations gain an advantage over their competitors because they can pay less for capital and use it more efficiently.¹² For maximum financing flexibility, a company must find ways of bringing in capital market investors.¹³ Thus, as investment alternatives expand, this competition for capital market investors often subjects companies to new, or at least increased, pressures. No one has yet identified the corporate governance system that will best aid companies (and thus countries) to survive in these circumstances.¹⁴

As a third and final assumption, this Article assumes that the above forces are pushing corporate governance throughout the developed world towards a market capitalism similar to what has long existed in the United States. It argues that, at least for the past two decades, French legal policymakers have attempted to create a legal environment favorable to both market capitalism and the corporate governance that accompanies it. Such a legal environment would seek to enhance shareholder rights and to address the kinds of agency problems typical of this market capitalism. Further, Anglo-American corporate finance has generally involved raising money from capital market investors.¹⁵ On the basis of these notions, French

10. See *A Fortress Against Change, A Survey of Business in Europe*, *ECONOMIST*, Nov. 23, 1996, at 3-5.

11. See generally ROY C. SMITH & INGO WALTER, *GLOBAL BANKING* 3-15 (1997) (describing growing internationalism in financial services).

12. See Frank H. Easterbrook, *International Corporate Differences: Markets or Law?*, *J. APPLIED CORP. FIN.*, Winter 1997, at 23, 27.

13. Cf. Shleifer & Vishny, *supra* note 6, at 769. Not every company must use domestic or global capital markets. However, they should be used by world-class companies that need a competitive advantage. Cf. Marco Pagano et al., *Why Do Companies Go Public? An Empirical Analysis*, 53 *J. FIN.* 27, 60-61 (1998).

14. See, e.g., RAFAEL LA PORTA ET AL., *LAW AND FINANCE* (National Bureau of Econ. Research Working Paper No. 729, 1981) (reviewing shareholder and creditor rights). See also Rafael La Porta et al., *Legal Determinants of External Finance*, 52 *J. FIN.* 1131 (1997) (comparing which legal systems are most favorable to market finance).

15. See ADOLF A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (Murray L. Weidenbaum & Mark Jensen trans., Transaction Publishers,

legal policy makers have borrowed laws from Anglo-American legal traditions. It is therefore sensible to review how successfully they have done their work.¹⁶

Part I provides the cultural and historical background of French corporate governance and an overview of the ownership structure of large French firms. This Part explains how State influence and concentrated ownership (whether by the State or a family) have characterized French corporate governance. It then identifies who generally replaces the State as its ownership of French firms declines and the implications of such ownership for French corporate governance. In the ensuing Parts, the Article examines whether French policy-makers have been successful at creating legal solutions to the specific agency problems that arise in a corporate governance of market capitalism.

Part II analyzes how well French corporate law provides the basic methods whereby dispersed shareholders address their lack of control over an enterprise: the right to information about the firm and its governance and the related right to vote, generally through a proxy. It finds that, although French law requires public companies to supply a considerable amount of information to capital market investors and provides for methods to facilitate their voting, these rules are relatively new and need to be enhanced to encourage capital market investing.

Part III considers how French law aligns the interests of shareholders with their elected representatives in a corporation, the directors. It observes that French law imposes a serious "duty of care" upon directors, but the duty has not been developed in situations involving capital market investors. Similarly, the law also prohibits directors and managers from engaging in conflict-of-interest transactions. Yet the law could further market capitalism if it increased the corporations' disclosure obligations with regard to both these transactions and executive compensation. This Part also explains how monitoring by French company accountants supplements, rather than replaces, director activity on behalf of capital market investors.

Part IV studies the related subject of whether French corporate law enhances the directors' obligations to minority shareholders in the special, but important, case of a change in control or restructuring. It notes that shareholders do not receive the protection of enhanced duties by directors or a court-supervised right of exit from the company. They do, however, receive both a right of exit in certain change-of-control situations and eval-

reprinted 1991) (classic statement on U.S. corporate governance or market capitalism, with its dispersed shareholders and strong managers).

16. See also James A. Fanto, *The Role of Corporate Law in the Adaptation of French Enterprises*, 1998 COLUM. BUS. L. REV. ____ (forthcoming 1998) (presenting a general argument concerning the efforts of French legal policy-makers to design a corporate law that promotes market capitalism and thus helps French enterprises adapt to current economic circumstances). This Article, by contrast, evaluates in detail what these policy makers have done.

uation of the exit price by French market authorities, which may be adequate protection for capital market investors.

This leads to Part V, which analyzes the role of French law in a central phenomenon of market capitalism: the takeover, whether friendly or hostile. It finds that the law gives managers considerable, but not unlimited, opportunity to defend against hostile takeovers. This law also compels companies to give shareholders both the time and the information to consider a bid and any competing offers. Yet this Part observes that French takeover law is generally used to eliminate capital market investors after controlling shareholders have decided upon a transaction, not as an instrument whereby a bidder effects a change in control. It thus suggests that the law gives too much protection to managers whose companies lack controlling shareholders when they face hostile offers.

Part VI explores the availability of shareholder suits under French law and observes that French shareholders can engage in collective legal action for harm done either to themselves or to the corporation. Restrictions on these suits and uncertainty over recovery of expenses, as well as the absence of a clearly defined shareholder plaintiffs' bar, discourage the use of this legal right by small shareholders. This Part considers whether such lawsuits will become more prevalent with the increase in capital market investors and the possible "decriminalization" of French corporate law.

Finally, this Article concludes with a brief critical review of recent proposals for legal and other reform to French corporate governance and corporate law. It observes that these proposals clearly intend to promote market capitalism in France and that, if implemented, they would be valuable for French enterprises. It suggests, however, that the proposed reforms do not go far enough because they do not squarely confront obstacles to market capitalism in the form of concentrated ownership and continuing State influence on business and the law. It argues that a public French examination of the role of law in corporate governance is needed.

I. The Cultural Background to French Corporate Governance

Corporate governance practices are partly cultural and historical products. In this context, culture can be defined as the conceptual framework whereby individuals, generally of the same country, understand and mediate the pressures of the world and motivate as well as explain their actions. As the corporation is a meaningful and purposeful human response to economic and social pressures, culture clearly informs corporate governance practices. The relationship between owners of capital and the managers who use it — the heart of corporate governance — is part of the response. Law, for example, gives shareholders certain rights and responsibilities as to the corporation, their fellow owners, and sometimes nonshareholder citizens. Members of the culture understand what it means to be a shareholder in these terms, and this understanding motivates the actions of both shareholders and their agents.

These observations are not new to anthropologists and cultural his-

torians.¹⁷ Under the influence of a biological evolutionary model,¹⁸ some economists and legal scholars have also suggested that the existence and endurance of such phenomena as corporate governance require a historical explanation.¹⁹ An economic discussion should take precedence in any analysis of corporate governance practices because these human creations are central in a country's economic life and because it is important to understand the cost-minimizing purposes of the practices.²⁰ That discussion, however, can be complemented by cultural and historical explanations that account for the endurance of certain features of these practices.

An authoritative account of Western corporate governance marks the emergence of the corporation as the dominant form of business organization in the nineteenth century.²¹ According to this account, technological developments made possible the accomplishment of large, complex economic tasks, such as the construction and operation of national railroads. Firms needed to grow significantly in order to attain the size necessary to use these technologies and to accomplish efficiently the tasks in national, as opposed to local, markets. Since technologies and related business practices worked successfully in many areas of economic life, small businesses increasingly ceded the field to large businesses as the latter could integrate many production and distribution functions into single firms in a cost-effective manner.

These developments brought specialization to the large corporation, and separated ownership from control. The increased size of enterprises demanded more capital than local financing or even retained earnings could generally provide. Firms often had to turn to outside investors, who were dispersed throughout the nation and beyond its borders and who would not necessarily commit all their funds to any single investment.²² Since any one investor generally provided a small proportion of the total capital of an enterprise, he or she did not have the same involvement in the business, nor the incentive to monitor its employees as had an owner of a smaller business. The new technologies, moreover, demanded specialized management training and expertise to ensure the efficient operation of a

17. See, e.g., CLIFFORD GEERTZ, *AFTER THE FACT: TWO COUNTRIES, FOUR DECADES, ONE ANTHROPOLOGIST* 43 (1995).

18. See, e.g., STEPHEN JAY GOULD, *THE PANDA'S THUMB: MORE REFLECTIONS IN NATURAL HISTORY* 19-26 (1980).

19. See, e.g., DOUGLASS C. NORTH, *INSTITUTIONS, INSTITUTIONAL CHANGE AND ECONOMIC PERFORMANCE* 3-10 (1990); Gilson, *supra* note 7, at 331-34; Roe, *supra* note 7, at 643-46.

20. See OLIVER E. WILLIAMSON, *THE MECHANISMS OF GOVERNANCE* 233 (1996).

21. See, e.g., ALFRED D. CHANDLER, *SCALE AND SCOPE: THE DYNAMICS OF INDUSTRIAL CAPITALISM* 2-13 (1990); ALFRED D. CHANDLER, *THE VISIBLE HAND: THE MANAGERIAL REVOLUTION IN AMERICAN BUSINESS* 1-12 (1977) [hereinafter CHANDLER, *VISIBLE HAND*].

22. Dispersed investors could only invest in large enterprises if a capital market infrastructure and/or financial intermediaries existed to move their funds efficiently to the firms. This infrastructure also permitted investors, in Professor Gilson's words, to "specialize in risk bearing," i.e., to diversify their investments over numerous large enterprises in order to reduce the firm-specific risks of their portfolio. See Gilson, *supra* note 7, at 331.

complex enterprise. A new professional management class appeared, with all of the features that characterized professional expertise, such as professional schools and organizations.²³ The new large firm thus separated ownership from control, a situation distinct from the traditional overlap between the two functions in smaller firms.

In the United States, the separation was acute and had certain consequences for owners. Adolf A. Berle and Gardiner C. Means observed some sixty years ago that, as a result of the separation, the general rule that a business was governed for its owners was not necessarily the case for a large corporation.²⁴ Managers could operate large corporations for significant periods of time for their own benefit and without particular concern about dispersed shareholders who could rarely mobilize to challenge or replace them.²⁵ The rise of the corporation and the separation of ownership and control in large firms also occurred in Western European countries, including France. This occurred even though the smaller size of these countries' markets initially limited the impact of the scientific and management technologies in creating large enterprises there.²⁶ Nonetheless, while specialization in investment and management functions occurred outside the United States, it did not necessarily lead to the opposition between powerful managers and powerless shareholders characteristic of U.S. corporations.

In his authoritative account of U.S. corporate governance, Professor Mark Roe explains that U.S. cultural forces helped maintain the separation between corporate ownership and control.²⁷ In his view, as the examples of corporate governance in other countries demonstrate, financial institutions could address this separation and bridge the gap. A financial institution could make a large equity investment in a corporation and thereby act

23. On the professionalization of engineers and business managers, see generally BURTON J. BLEDSTEIN, *THE CULTURE OF PROFESSIONALISM: THE MIDDLE CLASS AND THE DEVELOPMENT OF HIGHER EDUCATION IN AMERICA* (1978); MAGALI SARFATTI LARSON, *THE RISE OF PROFESSIONALISM: A SOCIOLOGICAL ANALYSIS* (1977).

24. See BERLE & MEANS, *supra* note 15, at 78-82.

25. Thus, a serious corporate governance problem developed, the disenfranchisement of the owner:

In examining the break up of the old concept that was property and the old unity that was private enterprise, it is therefore evident that we are dealing not only with distinct but often with opposing groups, ownership on the one side, control on the other — a control which tends to move further and further away from ownership and ultimately to lie in the hands of the management itself, a management capable of perpetuating its own position. The concentration of economic power separate from ownership has, in fact, created economic empires, and has delivered these empires into the hands of a new form of absolutism, relegating "owners" to the position of those who supply the means whereby the new princes may exercise their power.

Id. at 116.

26. See CHANDLER, *VISIBLE HAND*, *supra* note 21, at 499 ("Smaller and slower growing domestic markets in Western Europe and Japan lessened the interest of manufacturers in adopting new mass production techniques and also reduced the incentive to build large marketing and purchasing organizations.").

27. See MARK J. ROE, *STRONG MANAGERS, WEAK OWNERS: THE POLITICAL ROOTS OF AMERICAN CORPORATE FINANCE* 26-49 (1994).

as a financial intermediary for smaller investors. Its significant stake in an enterprise would give it the incentive to monitor management closely, and it could thus act as a counterweight to management's power.²⁸ However, the U.S. cultural forces of populism and federalism shaped U.S. law to keep financial institutions from assuming a role in corporate governance.²⁹

A similar cultural-economic story explains French corporate governance.³⁰ A brief outline, based upon accounts by economists, historians, and legal scholars of French business and business law,³¹ might proceed as follows. Separation of ownership from control arising from the modern large firm and the specialization of management appeared in French firms before the 1940s. Yet, for a number of reasons, it was not until after World War II that this enterprise structure began to produce the large vertically-integrated firm with mass-produced, consumer-oriented or technologically sophisticated goods, numerous diversified product lines, and a coordination among operating divisions that was similar to firms in other developed economies. Even then, this kind of firm did not dominate the French economy.³² Firms operated originally in a small, primarily rural market and only gradually grew to a size that could efficiently use management expertise. While mergers and the funding of large projects facilitated the growth of large firms in other countries, the weakness of French capital markets and the small size of banks hindered the growth of French firms.³³ French business growth came not within hierarchically organized firms, but through projects funded and owned by different groups of industrial firms with financing capabilities.³⁴ Furthermore, family ownership in France did not evolve into manager-dominated firms, and the development

28. See, e.g., Jonathan R. Macey & Geoffrey P. Miller, *Corporate Governance and Commercial Banking: A Comparative Examination of Germany, Japan, and the United States*, 48 STAN. L. REV. 73, 90-99 (1996) (questioning whether financial institutions are beneficial monitors of management for other shareholders).

29. See ROE, *supra* note 27, at 53-145. To take only one example, from an early date U.S. commercial banks (i.e., those that make commercial loans and take demand deposits) were not allowed to own shares in industrial companies, were prohibited from expanding nationally, could not join together in expansive holding company systems, and were separated from investment banks.

30. On non-U.S. corporate governance systems, see, for example, ROE, *supra* note 27, at 169-86; Macey & Miller, *supra* note 28. Like most U.S. scholars, however, Roe, Macey, and Miller focus on German and Japanese corporate governance. See Fanto, *supra* note 8, at 120 n.4 (listing citations); Edward B. Rock, *America's Shifting Fascination with Comparative Corporate Governance*, 74 WASH. U. L.Q. 367, 367 n.1 (1996) (listing citations). The volume of work by scholars in countries outside the United States is starting to grow. See, e.g., THEODOR BAUMS ET AL., *INSTITUTIONAL INVESTORS AND CORPORATE GOVERNANCE* (1994) (surveying corporate governance in numerous countries).

31. For a brief comparative history of French corporate law, see Claude Ducouloux-Favard, *L'histoire des grandes sociétés en Allemagne, en France et en Italie*, 44 REVUE INTERNATIONALE DU DROIT COMPARÉ [R.I.D.C.] 849 (1992).

32. See Maurice Lévy-Leboyer, *The Large Corporation in Modern France*, in *MANAGERIAL HIERARCHIES: COMPARATIVE PERSPECTIVES ON THE RISE OF THE MODERN INDUSTRIAL ENTERPRISE* 117 (Alfred D. Chandler, Jr. & Herman Daems eds., 1980) [hereinafter *MANAGERIAL HIERARCHIES*].

33. See *id.* at 124, 146.

34. See *id.* at 139-45.

of projects and expansion of firms often resulted from family relationships.³⁵ In fact, technologically competent managers — who in other countries took control of companies — often worked in France under the supervision of family owners. Because managers generally received their education and professional training in the State bureaucracy, they often relied upon State contracts and aid and never developed the marketing skills that might have led them to create large consumer-oriented firms.³⁶

One distinguishing feature of French corporate governance's solution to the management agency problems of large firms was the role of the French State. Since the seventeenth century, the State has been involved in, and has directly or indirectly owned, large economic undertakings. Although there have been periods of classically liberal markets with private ownership of major enterprises in France,³⁷ the State's influence was still felt in both these firms and the economy in general. The *économie mixte* of the post-war years with its State ownership and control, either direct or through financial institutions, was the most recent example of the State's traditional corporate governance role.³⁸

From the agency perspective, in State-oriented corporate governance, management was subject to the oversight of a powerful shareholder. Using methods available to a controlling shareholder, as well as special ownership rights arising under nationalization laws, the French State kept management in check for much of the post-war period; because of its direct or indirect controlling interest in a company, it appointed managers and directors and replaced them by decree.³⁹ State representatives also had the legal right to oversee and inspect the operations of a firm. The State's influence additionally arose from the identity of corporate agents: managers and directors were typically former State bureaucrats who, by background and training, shared the State's goals and were inclined to favor State purposes.⁴⁰

State ownership and control evolved during the post-war period from dominance of companies to "relational" investing;⁴¹ the State made capital investments in nationalized companies available to private investors, and

35. See Alain Alcouffe & Christiane Alcouffe, *Control and Executive Compensation in Large French Companies*, 24 J.L. & Soc'y 85, 88 (1997); Alfred D. Chandler, Jr. & Herman Daems, *Introduction*, in *MANAGERIAL HIERARCHIES*, *supra* note 32, at 1, 7.

36. See Lévy-Leboyer, *supra* note 32, at 132-37.

37. See William N. Goetzmann & Philippe Jorion, *A Century of Global Stock Markets* 19 (Dec. 1996) (unpublished paper, on file with author) (showing data on French stock market going back at least until 1921).

38. See JEAN-FRANÇOIS ECK, *HISTOIRE DE L'ÉCONOMIE FRANÇAISE DEPUIS 1945*, at 4-39 (1994); Fanto, *Transformation of French Corporation Governance*, *supra* note 2, at 28-40.

39. See generally JEAN KERNINON, *LES CADRES JURIDIQUES DE L'ÉCONOMIE MIXTE* 73-81 (1992). In some cases, a business enterprise would simply become part of a French State department or ministry.

40. See generally MICHEL BAUER, *LES 200: COMMENT DEVIENT-ON UN GRAND PATRON?* 123-97 (1987) (describing State path to executive success).

41. See Jill E. Fisch, *Relationship Investing: Will It Happen? Will It Work?*, 55 OHIO ST. L.J. 1009, 1010 (1994) ("Relationship investing may be described as a large long-term financial commitment by an investor to a portfolio company in exchange for a say as to how it is run.") (footnote omitted).

gave management more freedom to pursue business strategies with State approval of long-term goals and intervention only in the event additional capital was needed or problems developed. The French "Statist" corporate governance was highly successful as the economic results of the three decades following World War II ("*Les Trente Années Glorieuses*") demonstrated. Collaborating with the State, managers exercised their business expertise to produce "national champions" that, in many cases, competed successfully in the world markets.

Today, in all but several "sensitive" economic sectors, the State's ownership and control of private companies are diminishing. In France, as elsewhere in Europe and around the world, there has been a loss of confidence in the State's competence to manage enterprises in the new global market.⁴² The State often operated a profit-making business for purposes unrelated to the specific financial well-being of the firm, such as to address unemployment, distribution of credit, and public services. This approach worked when France was reconstructing and modernizing its war-torn economy and when its markets were highly regulated and closed. In contrast, it can be argued that the approach does not work when private companies must compete in international markets and rapidly adapt to new technologies.⁴³ With its market liberalism, its goal of reducing European trade barriers, State subsidies of industry and budget deficits, the European Union has also pressured the State to sell off its interests in enterprises. Privatization of State-owned companies took place between 1986 and 1988, resumed in 1993, and despite occasional delays, shows no sign of ending.⁴⁴

What will constitute corporate governance in large French companies once the State's influence declines? To answer that question, it is useful first to explain the importance of these companies in the French economy

42. See, e.g., John Vickers & Vincent Wright, *The Politics of Industrial Privatisation in Western Europe: An Overview*, in *THE POLITICS OF PRIVATISATION IN WESTERN EUROPE* 1, 6 (John Vickers & Vincent Wright eds., 1989); Shleifer & Vishny, *supra* note 6, at 767-69.

43. This statement oversimplifies a complex matter. Firm success depends upon the goals that are set for it, the definition of such goals and the monitoring of those entrusted with achieving the goals. Under this definition, state-owned firms could be said to have achieved success — it all depends upon their goals. In certain situations, they might be the most appropriate for achieving specific goals. See Saul Estrin & Virginie Pérotin, *Does Ownership Always Matter?*, 9 INT'L J. INDUS. ORG. 55, 58-64 (1991). See also WILLIAMSON, *supra* note 20, at 241 ("Whether public ordering can do better depends on whether (i) the public sector is better informed about externalities, (ii) the requisite collective action is easier to orchestrate through the public sector (possibly by fiat), and/or (iii) the social net benefit calculus differs from the private in sufficient degree to warrant a different result.").

44. See Fanto, *Transformation of French Corporate Governance*, *supra* note 2, at 49-56. Just recently a Socialist government has again taken power in France. At first it stated that it might well bring the French privatization program to a halt. See *Bad for Business?*, *ECONOMIST*, June 7, 1997, at 51. Recent signs reveal, however, that the new government has no choice but to continue privatization in some form if it wants to comply with European Union restrictions on state support of firms and its guidelines on reducing state budget deficits. See *France Still Trapped*, *ECONOMIST*, July 5, 1997, at 51.

and to provide current information concerning their capital and ownership structure.

Stock market capitalization of French companies⁴⁵ accounts for approximately 32% of France's gross domestic product,⁴⁶ reflecting the significant role that large companies play in the French economy. Although it is not possible to obtain an exact understanding of the capital structure of listed companies, available data suggest that nonfinancial industrial companies have decreased their debt financing, increased their funding from equity capital, and retained earnings over the last ten years.⁴⁷ Like U.S. companies, French companies secure approximately 30-40% of their capital from equity and retained earnings.⁴⁸ Numerous factors, including high interest rates (which discourage continued debt financing), increased emphasis on privatization, and improvement in French stock markets, have influenced this increase in equity financing.⁴⁹

Stock ownership in these large firms is concentrated, but not in the hands of financial institutions. Of the 120 listed nonfinancial companies in an index of the Société des Bourses Françaises, the weighted average percentage holding of the five largest shareholders was 48.2% in 1995.⁵⁰ Other data suggest that, out of the 416 largest French firms in 1995/1996, 24% of the identifiable stockholders in these firms had holdings of more than 50% in a given firm, with 16.5% of the stockholders having holdings larger than 75%.⁵¹ Depending on the data source, financial institutions –

45. Listing on France's "first market" (*La Cote officielle*) requires that at least 25% of the company's share capital be held by the public and that the company have three years of published financial accounts (the last two of which must have been audited). See CMF Règlement Général, arts. 3-1-11, 3-1-14, C. soc., *supra* note 1, at 913. French market authorities demand that the share capital of a listed company be substantial. See HUBERT DE VAUPLANE & JEAN-PIERRE BORNET, DROIT DE LA BOURSE 350 (1994).

46. This is out of a GDP of FF 7,681 billion. See OECD ECONOMIC SURVEYS: FRANCE 1997, at 166 (1997) [hereinafter OECD FRANCE]. This represents a significant shift from the 20% figure of approximately ten years ago (1986). See Raghuram G. Rajan & Luigi Zingales, *What Do We Know About Capital Structure? Some Evidence from International Data*, 50 J. FIN. 1421, 1448 (1995).

47. Rajan and Zingales do note that, from 1982 to 1991, French companies decreased their leverage. Further, from 1984 to 1991, the external financing of French companies was primarily equity, although as a fraction of total financing it was a relatively small amount. See Rajan & Zingales, *supra* note 46, at 1432, 1439. In contrast, financial companies, such as banks, generally have a highly leveraged financial structure.

48. See OECD FRANCE, *supra* note 46, at 123-25 (French non-financial companies have 36.2% of their capital structure in equity (share capital and retained earnings) in comparison to 37.4% for U.S. companies). Looking at data primarily from 1987 to 1991 and attempting to be more restrictive in their definition of debt, Rajan and Zingales find that companies in the G-7 countries have similar leverage (with the exception of companies in Germany and the U.K. which have lower leverage). See Rajan & Zingales, *supra* note 46, at 1438. This result cautions against a ready characterization of countries with relatively small capital markets as necessarily having more leveraged companies.

49. See OECD FRANCE, *supra* note 46, at 124-25.

50. See *id.* at 113. This number can be contrasted with comparable U.S. figures of 25.4%. See *id.*

51. See Paul Windolf, *The Governance Structure of Large French Corporations: A Comparative Perspective* 17-19 (March 1997) (manuscript on file with author). Profes-

such as banks, insurance companies, and mutual funds — own approximately 20-37% of the equity capital in listed companies, but due to legal controls, these holdings are generally not controlling positions.⁵² Another significant class of shareholders is French nonfinancial companies, which also own approximately 20% of the listed companies and whose holdings are more concentrated than those of financial institutions.⁵³ Households own 34% of listed companies, and of these, wealthy individuals and families have significant stakes.⁵⁴ Foreigners own approximately 20% of listed French firms.⁵⁵ Since large French companies are currently seeking equity capital, both French investors and non-French investors are becoming critical as capital providers.

The question is whether the State's declining ownership really signifies its abandonment of its customary corporate governance role. Statistics show that the State is no longer mediating, and given the trend toward liberalized markets, cannot mediate, this investment. As the recent French parliamentary elections show, many French citizens continue to turn to the State as a problem solver. French history of a centralized State and social acceptance of concentrated financial power, for example, differs from the U.S. populist preference for local centers of power and fear of centralized financial institutions. Moreover, the State retains the possibility of influ-

sor Windolf's data suggest that 63% (262 firms) of the large French firms in his sample have a majority shareholder, and 87% (373 firms) have one shareholder with a holding greater than 25% (in the United States, this figure is approximately 4% (9 firms)). *Id.*

52. For the general breakdown, see Andrea Goldstein, *Privatizations and Corporate Governance in France*, 48 BNL Q. REV. 455, 475 (1996) (chart based upon 1994 data prepared by OECD). See also OECD FRANCE, *supra* note 46, at 111. Professor Windolf's data produce slightly different results: banks own 20.2% of the 416 largest French firms, insurance companies own 12.1%, and funds own 5.2%. His database may be more restricted than that of the OECD. These institutions do not generally have controlling positions. Together, they are controlling shareholders in only 48 out of 416 companies in his database. See Windolf, *supra* note 51, at 19. The limited control position of French financial institutions is related to legal obstacles that keep their holdings at the noncontrolling level (e.g., banks are generally limited to holding 10% of any nonfinancial company, insurance companies and mutual funds are limited to a 5% holding). See Goldstein, *supra*, at 477.

53. See Goldstein, *supra* note 52, at 475; OECD FRANCE, *supra* note 46, at 111. Of the 262 companies in his database with a majority shareholder, approximately 59 have a French industrial company as such a shareholder. See Windolf, *supra* note 51, at 19.

54. Goldstein's data indicate that households (including ownership through financial intermediaries) own 34% of listed company stock. See Goldstein, *supra* note 52, at 475. See also OECD FRANCE, *supra* note 46, at 111. In Professor Windolf's database, direct individual and family ownership (which does not include ownership through financial intermediaries) is 12.8%. Moreover, individuals and families have controlling positions (greater than 50% stakes) in 29 companies, and significant stakes (between 10% and 49%) in 56 others. See Windolf, *supra* note 51, at 19. Professor Windolf feels that his database in fact understates family ownership, since many shares are held by nonfinancial companies where the actual ultimate owner is unknown. See *id.* at 18 n.25.

55. See Goldstein, *supra* note 52, at 475; OECD FRANCE, *supra* note 46, at 111. Professor Windolf's data show that some foreign shareholdings are concentrated (e.g., of the 180 firms with a 75% shareholder, 40% (72 firms) had a non-financial foreign firm in this position, which suggests that the firm is a subsidiary of a foreign firm). See Windolf, *supra* note 51, at 19. See also Alcouffe & Alcouffe, *supra* note 35, at 89 (giving a similar breakdown of ownership of the largest French companies).

ence in some privatized firms.⁵⁶ In firms where it no longer has, or never had, direct or indirect ownership, its influence may be exercised through other means, such as the awarding of contracts and through managers still largely originating from the State bureaucracy.⁵⁷ Thus, it is hard to imagine France without State influence over the policies of major French enterprises.

Yet with the State abandoning, or at least reducing, its corporate governance role, will other institutions fill its place as a strong counterpart to French management? As noted above, an account of corporate governance in large French enterprises should not ignore the importance of family ownership.⁵⁸ Windolf and Bauer argue that family ownership has been an enduring and dynamic form of capitalism in France, and not merely a stage on the road to an inevitable capitalism of dispersed shareholders and strong managers. Even in recent years, families continue to own and control, often through complex pyramids of ownership, some of the most profitable large French companies.⁵⁹ Families could replace the State's ownership role in large firms because their ownership has always existed side-by-side with that of the State. Since families both cultivate from within and recruit managers from the State career path, they are not passive owners and present yet another solution to agency problems in the French corporation.

Financial institutions could also assume a new corporate governance role in France.⁶⁰ On a practical level, banks and insurance companies could act as vehicles for small investors, either by managing specific equity investments or by investing the proceeds of deposits. Further, a strong single investor, such as a bank, may be more welcome in France, where historically the State and single family ownership of firms has dominated. In fact, many French observers hold that despite the withdrawal of the State from capital investment, this characteristic of French corporate governance, the acceptance of centralized financial power, distinguishes it from a classic Anglo-American market capitalism and may favor creating a role for

56. See generally Alice Pezard, *The Golden Share of Privatized Companies*, 21 BROOK. J. INT'L L. 85 (1995) (describing the "golden share" used, for example, in the privatization of the Société Nationale d'Elf Aquitaine, which gives the State a veto on major transactions involving Elf). The actual State shareholding of listed firms is not significant (2% of listed firms), but such figures do not necessarily reflect indirect State ownership and influence. See Goldstein, *supra* note 52, at 475; OECD FRANCE, *supra* note 46, at 111, 118-22. Professor Windolf's data suggest that the State still controls (greater than 50% shareholding) 32 of the 416 largest French firms. See Windolf, *supra* note 51, at 19.

57. See BAUER, *supra* note 40, at 170-91. See also Goldstein, *supra* note 52, at 479.

58. See BAUER, *supra* note 40, at 51-120; Windolf, *supra* note 51, at 15-16. See also Morton Keller, *Regulation of Large Enterprise: The United States Experience in Comparative Perspective*, in MANAGERIAL HIERARCHIES, *supra* note 32, at 161, 164.

59. See OECD FRANCE, *supra* note 46, at 127 (pointing out the good results of family-owned companies, such as LVMH, L'Oréal, Carrefour, Castorama). See also Alcouffe & Alcouffe, *supra* note 35, at 90 (noting that French family groups have proved to be dynamically efficient because, with centralized control, they can respond rapidly to changes in markets and technology, but that such control is often incompatible with rights of minority shareholders).

60. See OLIVIER PASTRÉ, *LES NOUVEAUX PILIERS DE LA FINANCE* 101-31 (1992).

financial institutions in corporate governance.⁶¹ Those hostile to market capitalism particularly prefer the emergence of a capitalism of strong financial intermediaries.⁶² Use of financial institutions to regulate agency problems may thus be one of the most favored solutions to France's corporate governance problems.

The monitoring of financial institutions is not without practical and theoretical difficulties, however, some of which are specific to France. Although bank-centered corporate governance appeared preferable to U.S. governance during the early 1990s,⁶³ problems are now appearing in the main models of this form, prevalent in Germany and Japan. Bank-centered corporate governance is suited to temporary economic circumstances (such as reconstruction), closed national markets, and preferences for debt financing. It may not, however, be well adapted to present economic conditions.⁶⁴

Of further relevance, France has no tradition or experience with financial institution capitalism. As explained above, the shareholding percentage of financial institutions has been insignificant due to legal constraints, and their role has generally been one of financier and advisor to a strong shareholder, such as a family or the State.⁶⁵ Moreover, from the perspective of controlling management, the possible involvement of financial institutions in corporate governance has a dark side.⁶⁶ François Morin has drawn attention to the creation, at the time of privatization, of the *noyaux durs* or cross-shareholdings of companies structurally "centered" around a financial institution (or group of such institutions). In these instances, financial institutions provide companies with financial and restructuring advice. However, since no financial or industrial shareholder controls another company in the network, cross-shareholding protects the managers of each networked company from capital market pressures.⁶⁷ This "capi-

61. See, e.g., Olivier Pastré, *Les dix commandements du gouvernement d'entreprise*, in RAPPORT MORAL SUR L'ARGENT DANS LE MONDE 1996, at 201, 203 (1996) [hereinafter RAPPORT MORAL] ("Quatrième commandement: tu assumeras la spécificité du capitalisme à la française.").

62. See, e.g., MICHEL ALBERT, *CAPITALISME CONTRE CAPITALISME* 117-92 (1991).

63. See Roberta Romano, *Corporate Law and Corporate Governance*, 5 INDUS. & CORP. CHANGE 277, 297-313 (1996) (summarizing scholarly work favoring bank-centered capitalism). See also Rock, *supra* note 30, at 375-86.

64. Market capitalism is making inroads, albeit slowly, in both countries. See, e.g., *Making Companies Efficient: The Year Downsizing Grew Up*, ECONOMIST, Dec. 21, 1996, at 97-99.

65. See OECD FRANCE, *supra* note 46, at 111, 125; Windolf, *supra* note 51, at 16. Crédit Lyonnais was the one French example of a bank with significant equity stakes, but its spectacular failure has cast doubt in France on the wisdom of this form of corporate governance. See Goldstein, *supra* note 52, at 475-76.

66. Edward B. Rock, *Controlling the Dark Side of Relational Investing*, 15 CARDOZO L. REV. 987 (1994).

67. See FRANÇOIS MORIN & CLAUDE DUPUY, *LE COEUR FINANCIER EUROPÉEN* 47-54 (1993). See also François Morin, *Le règle capitaliste entre laxisme et détournement*, in RAPPORT MORAL, *supra* note 61, at 207, 210-11. The Viénot Report offers the view of the cross-shareholdings often heard in French business circles, i.e., it is a temporary phenomenon that will disappear when French companies can raise capital from other French sources (pension funds, once they are created, and other financial institutions

talism à la française" produces and maintains a management oligarchy, for managers are subject to no countervailing power. It may also allow the State to influence industrial policy covertly through friendly managers and indirectly to protect national industries against foreign "invaders." Yet if financial institution monitoring takes this form, where institutions favor rather than check management control, capital market investors will suffer and French companies with such ownership structures will feel product market discipline too late.⁶⁸

Yet another French corporate governance outcome could be possible, a market capitalism that also has French cultural origins.⁶⁹ As noted above, for maximum financing in global competition, French world class companies need to attract capital market investors whose investment presumes a liquid and well-regulated stock market and non-French investors who also make significant investments in these companies and favor market capitalism.⁷⁰ Since, moreover, the State can no longer fulfill the retirement demands of an aging population and still meet European Union budget restrictions, there is a need for private pension funds, which must make equity investments to maximize their returns.⁷¹ On the basis of an Anglo-Saxon model, these funds apparently prefer a shareholder and market-based corporate governance system and, because of their mobility, will penalize countries and companies producing less than adequate returns. French persons and organizations, particularly the Commission des Opérations de Bourse,⁷² are also pushing for a market capitalism solution and emphasizing the development of French capital markets and the availability of those markets to foreign, as well as domestic, investors.

French corporate law will play a role in determining the French corporate governance "outcome."⁷³ For example, corporate law of the post-war years had a "Statist" character that both reflected and promoted the State's

that have not traditionally invested in equity). See Viénot Report, *supra* note 2, at 14 ("In this respect, the existence of cross-shareholders may be viewed as a transitional phenomenon in French capitalism, and one whose elimination as quickly as possible would appear highly desirable.").

68. See generally François Morin, *Privatisation et dévolution des pouvoirs: Le modèle français du gouvernement d'entreprise*, *RÉVUE ÉCONOMIQUE* 1253, 1263-66 (1996). As Jensen observes, product market discipline is inevitable. When it strikes, it may destroy an enterprise, with great human cost. It is thus useful to have other management control systems that would permit a more rational and productive transformation of an enterprise. See Jensen, *supra* note 5, at 850-51. French privatized companies have recently been the least profitable of large French firms. See OECD FRANCE, *supra* note 46, at 125-26.

69. See WILLIAM JAMES ADAMS, *RESTRUCTURING THE FRENCH ECONOMY: GOVERNMENT AND THE RISE OF MARKET COMPETITION SINCE WORLD WAR II* 249-54 (1989) (describing the historical strength of economic liberalism in France). See also Keller, *supra* note 58, at 164.

70. See generally Fanto, *Transformation of French Corporate Governance*, *supra* note 2, at 22-28; Jean-Paul Valuet, *Fonds de pension américains: incidences de leur politique d'actionnariat sur les sociétés françaises*, in *BOURSE ET PRODUITS FINANCIERS* (1996).

71. See CENTRE FOR EUROPEAN POLICY STUDIES, *WORKING PARTY REPORT NO. 12, CORPORATE GOVERNANCE IN EUROPE* 29-30 (1995).

72. See COMMISSION DES OPÉRATIONS DE BOURSE, *supra* note 2, at 85-89.

73. See generally Fanto, *supra* note 16.

control of enterprises. The concept of the *intérêt social*, which permeates the French corporate code, permits directors to consider the interests of all constituencies in deciding upon corporate strategy.⁷⁴ This concept allowed the State-owner to use controlled corporations for purposes other than profit-making. For the past two decades, however, French legal policy-makers have changed corporate law to make it more hospitable to capital market investors. Part II examines whether they have achieved their goals.

II. Information and Voting

If market capitalism separates shareholder ownership from management control, corporate law should help shareholders to monitor and discipline managers. A main monitoring method is shareholder voting, whereby shareholders elect, or reelect, the agents who oversee the corporation's operation and approve decisions by these agents on major corporate actions. In order for such monitoring to be meaningful and effective, shareholders must have information. In fact, control of management is based upon shareholder access to, and expertise in understanding, corporate information. As Robert Clark explains in his classic hornbook on corporate law, "[t]he basic reason for a shareholder inspection right is to insure managerial accountability to shareholders."⁷⁵

A. French Shareholders' Legal Rights to Information

Professor Conard once observed that U.S. state corporate law rules on the provision of information to shareholders were "rudimentary" compared to those of many other industrialized countries, including France.⁷⁶ Under the basic French corporate law governing public companies, the *société anonyme*, the shareholder has the right to see a significant amount of information. A shareholder can inspect, at the company's main place of business, minutes of the shareholder meetings, a list of those present, and documents prepared prior to the company's annual shareholder meeting for the last three years. Among other things, the documents include the company's financial statements, a list of directors, any reports by the directors or by the statutory auditors (*les commissaires aux comptes*), any explanation of resolutions submitted at the meeting, together with background information on the candidates for board membership, and total compensation to directors.⁷⁷ A shareholder can also obtain the company's certificate of incorporation (*les statuts*) and a list of directors and statutory auditors.⁷⁸ Directors who prevent this disclosure are subject to criminal sanctions.⁷⁹

74. See Viénot Report, *supra* note 2, at 5.

75. ROBERT C. CLARK, *CORPORATE LAW* 103 (1986).

76. See ALFRED F. CONARD, *CORPORATIONS IN PERSPECTIVE* 325-27 (1976).

77. See Loi N° 66-537 du 24 juillet 1966, [1966] JO 26 juillet 6402, arts. 168-170 (Fr.), C. soc., *supra* note 1, at 114, 328-30 [hereinafter Loi N° 66-537]. See also MICHEL JEANTIN, *DROIT DES SOCIÉTÉS* 104 (2d ed. 1992). See *infra* Part IV. Section C.

78. See Décret N° 67-236 du 23 mars 1967, [1967] JO 24 mars 2843, art. 153 (Fr.), C. soc., *supra* note 1, at 599, 641 [hereinafter Décret N° 67-236].

79. See Loi N° 66-537, art. 445, C. soc., *supra* note 1, at 569-70.

A shareholder of a French company has the absolute right to undertake, without justification, an inspection of records and to have the information ready for his or her perusal. It is unclear, however, how effectively a shareholder can use the inspection right to identify other shareholders in order to encourage them collectively to oppose or replace managers. In his recent proposal to reform French corporate law, Senator Marini suggests that the law should be amended to compel a company to give a requesting shareholder all the information it has about shareholders' identities (not just the few names actually registered on the company's books). This proposal indicates that problems exist under the current disclosure laws.⁸⁰ Shareholder information rights under French corporate law are thus likely to be more useful to shareholders in a closely-held corporation or to large shareholders in a large public corporation (for example, a family owner) than to capital market investors. Such limited utility is perhaps explained by the fact that these laws originated in a time when firms were controlled by the State or a family unit. While a shareholder in a closely-held corporation or a large shareholder may use these rights to safeguard its ownership stake and to contest other shareholder factions, it is difficult to imagine that a capital market investor, with minor holdings in a company, would have the necessary economic incentive to exercise these informational rights.⁸¹

The most important legal means whereby capital market investors acquire information about publicly-traded firms is through mandatory disclosure. While only recently developed and not as extensive as that required of companies under U.S. law and regulation, such disclosure has gradually developed in France. The addition of this safeguard suggests that French legal policy makers are incrementally creating a legal climate favorable to capital market investing. That before 1967 securities regulation was not an identifiable area of French law, and that no specialized government regulator existed to ensure the flow of accurate information to capital market investors, underscores the historical insignificance of such investors in French corporate governance as compared to other shareholders (such as the State, financial institutions and controlling families). Since that time, the major government market regulator, the Commission des Opérations de Bourse (the COB) has gradually grown in power and size, particularly due to laws passed in 1988 and 1989.⁸² Two other mar-

80. See Marini Report, *supra* note 2, at 89-90. See also Philippe Merle, *Les contrôles internes*, in LA MODERNISATION DU DROIT DES SOCIÉTÉS: PREMIÈRES RÉFLEXIONS SUR LE RAPPORT MARINI 41, 42 (Jean-Jacques Daigre ed., 1996) [hereinafter MODERNISATION DU DROIT] (agreeing that there are problems with access to shareholder lists in French companies).

81. In France, small shareholders can act collectively through shareholder associations, but this is a recent legal power. See generally Loi N° 66-537 (as amended by Loi N° 94-679 du 8 août 1994), C. soc., *supra* note 1, at 114-599.

82. Two major legal reforms, the Loi N° 88-70 du 22 janvier 1988 and the Loi N° 89-531 du 2 août 1989, significantly increased the oversight, investigatory and enforcement powers of the COB with respect to disclosure and market manipulation. See THIERRY SCHOEN, THE FRENCH STOCK EXCHANGE: A PRACTICAL GUIDE FOR INVESTORS AND ADVISORS 4-10 (1995); Michel Germain, *Les sociétés qui font appel public à l'épargne*, in MODERNISA-

ket authorities succeeded earlier self-regulatory organizations and complement the COB's oversight of the securities markets by regulating market participants in the stock exchanges (for example, brokers and listed companies) and exchange issues. The Conseil des Bourses de Valeurs, renamed the Conseil des Marchés Financiers (CMF)⁸³ in 1996, and the Société des Bourses Françaises (SBF) were established in 1988 and progressively acquired powers in matters such as broker regulation, listing procedures, and tender offers.⁸⁴ Shareholder disclosure improved with the increased power of these French market authorities.

The initial public sale of securities in France, which exemplifies the cooperation of these market authorities, requires the disclosure of information in a prospectus (*note d'information*) that, pursuant to COB regulations, includes business, financial, and offering information.⁸⁵ Without COB approval, the company can use neither the prospectus nor the summary prospectus that is disseminated to the public to generate interest in the securities. The listing of securities, which generally accompanies or precedes their issuance, also involves considerable disclosure. Under the direction of the CMF, the SBF prepares a *dossier* of historical, financial, and business information supplied by the company.⁸⁶ The listing is subject to COB veto.⁸⁷ French listings also require the company to continue to provide exchange authorities with interim financial results as well as information about corporate events which substantially affect the company and its shareholders.⁸⁸

Yet French mandatory disclosure, while increasingly comprehensive, may not fully promote capital market financing. The COB believes that more progress is needed with what is called "continuous reporting" in the United States. The COB has observed that, while information flows to investors from several sources in French companies, it is not well-organized. The investor or the market professional⁸⁹ has no single company document detailing the overall business, financial situation and governance of

TION DU DROIT, *supra* note 80, at 31, 32 (pointing out that the COB's regulations constitute another corporate law for listed companies); Leslie Goldman, *The Modernization of the French Securities Markets: Making the EEC Connection*, 60 *FORDHAM L. REV.* S227, S237-S245 (1992).

83. See Loi N° 96-597 du 2 juillet 1996, [1996] JO 4 juillet 10063 (Fr.), C. soc., *supra* note 1, at 1047-49.

84. See generally CMF Règlement Général, C. soc., *supra* note 1, at 911-46.

85. See COB Règlement N° 91-02, C. soc., *supra* note 1, at 957-59 (Fr.); SCHOEN, *supra* note 82, at 149-56.

86. See Arrêté du 6 juillet 1988, art. 3-1-1, C. soc., *supra* note 1, at 911.

87. See SCHOEN, *supra* note 82, at 156.

88. See Arrêté du 6 juillet 1988, art. 3-1-2, C. soc., *supra* note 1, at 911-12.

89. Evidence suggests that the French securities markets are efficient. See William J. Baumol & Burton G. Malkiel, *Redundant Regulation of Foreign Security Trading and U.S. Competitiveness*, J. APPLIED CORP. FIN., Winter 1993, at 19, 25-27. Thus, investors rely upon market price, which is established by the activity of market professionals (e.g., doing fundamental analysis about companies and trading on their research). See generally Ronald J. Gilson & Reinier H. Kraakman, *The Mechanisms of Market Efficiency*, 70 *VA. L. REV.* 549, 557 (1984).

a French company.⁹⁰ To remedy this informational gap, the COB thus encourages companies to file with it a *document de référence* based on the annual report customarily prepared for shareholders at the annual meeting.⁹¹ The COB recognizes the capital market investor as an increasingly important figure in French corporate finance, which is not surprising because, without such investors, the COB would have little purpose for its existence.

B. Shareholder Voting

Since voting is one of the few legal methods whereby the shareholder can directly influence the policies of the corporation, a significant corporate governance concern is focused on which subjects a shareholder of a large corporation is permitted to vote. The corporate form takes advantage of centralized and specialized management, which must be free to operate the business to effectuate the purpose of a corporate form. As a result, the subjects of shareholder voting are limited, with the most important being the election of directors. French corporate law is generally in line with the laws of other countries in allowing shareholders to vote on only a few subjects. At meetings, whether ordinary or extraordinary, French shareholders vote only on major decisions affecting an enterprise (election of directors, changes to its certificate of incorporation, and mergers).⁹²

The highly regulated French voting procedures ensure that shareholder voting is not an empty formality.⁹³ Some aspects of the French law on shareholder voting, however, suggest that, until recently, the system was designed to regulate the relations between management and a small group of concentrated owners, rather than management's relations with numerous shareholders. These aspects have led some scholars to conclude that the French legal tradition is not favorable to capital market investors.⁹⁴ In the United States, for example, capital market shareholders are protected through the practice of "one share, one vote," that is, all common or "ordinary" shares have equal voting rights.⁹⁵ In contrast, French corporate law

90. See COMMISSION DES OPÉRATIONS DE BOURSE, 26ÈME RAPPORT AU PRÉSIDENT 44 (1993) (discussing lack of such company document).

91. See COMMISSION DES OPÉRATIONS DE BOURSE, *supra* note 2, at 23.

92. See Loi N° 66-537, arts. 153-157, C. soc., *supra* note 1, at 309-15.

93. See Loi N° 66-537, arts. 160-177-1, C. soc., *supra* note 1, at 319.

94. See LA PORTA, *supra* note 14, at 18-20.

95. State corporate law enables a corporation to be structured by classes of shares, each with differing voting and economic rights. See, e.g., DEL. CODE ANN. tit. 8, § 151(a) (1996). However, the SEC and the major U.S. stock exchange, the New York Stock Exchange (the latter through its rules), traditionally opposed the use of "dual-class" common stock, where some shareholders have no or fewer voting rights, in large publicly-owned companies. The dual-class issue surfaced in U.S. corporate governance in the 1980s when management sought in some cases to recapitalize their companies' capital structure with dual-class stock so as to maintain control in the face of the threat of hostile takeovers. See, e.g., *Williams v. Geier*, 671 A.2d 1368 (Del. 1996). While the story of the SEC's opposition to dual-class stock is an interesting one, see RICHARD W. JENNINGS ET AL., *SECURITIES REGULATION: CASES AND MATERIALS* 714-716 (1992) (summarizing the story), it suffices to say that, while shares with unequal voting rights are not prohibited in the United States, whether they arise from dual-class stock or some other

allows a company to grant a shareholder double voting rights if he or she holds shares in registered (as opposed to bearer) form for at least two years. This legal possibility does not seem particularly well-suited to, and may even harm, capital market investors who buy and sell shares frequently and who are more likely to hold shares through financial intermediaries rather than directly with the company.⁹⁶

Capital market shareholders' weakness arises from their number, geographical dispersion, and small holdings. Such characteristics make it unlikely that they will act as a cohesive group at shareholders' meetings. In fact, there is little economic incentive for them to attend meetings at all, or even to vote, so long as they can easily sell their shares.⁹⁷ To facilitate shareholder participation in the corporate enterprise, corporate law should allow a shareholder to vote by proxy, that is, to instruct another individual to cast his or her votes on particular resolutions or in director elections. Yet French regulation akin to full proxy voting is of relatively recent origin. Under French law, a shareholder could always give his or her vote to a spouse or another shareholder, or simply provide a "blank" power to management.⁹⁸ Only in 1983 did French corporate law allow a shareholder to vote by mail (*par correspondance*), and it was not until 1988 that detailed rules were instituted regulating the manner of, and management's conduct regarding, this kind of voting.⁹⁹

The relatively recent origin of this French proxy-like regulation and the "relative lack of use" of the French proxy process again suggest that capital market investors are only gradually becoming significant in French corporate finance. If major French companies increasingly seek equity capital from these investors in the national and global market, more legal and regulatory attention must be given to this process. Recent use of proxy solicitation by shareholder activists in the Eurotunnel context suggests that French shareholders are discovering the advantages of organizing themselves through proxies.¹⁰⁰ Capital market investors may also become more assertive and begin to oppose current French corporate voting practices, such as the double voting privilege¹⁰¹ and the ability of a company to limit

attribute (such as the length of shareholding), they are the exception, rather than the rule.

96. See Loi N° 66-537, art. 175, C. soc., *supra* note 1, at 334-35. See also *infra* note 224 and accompanying text (describing principle of "one share, one vote" in France).

97. This is the classic collective action problem. See JAMES D. COX ET AL., CORPORATIONS 335-36 (1997).

98. See Loi N° 66-537, art. 161, C. soc., *supra* note 1, at 321-22; MAURICE COZIAN & ALAIN VIANDIER, DROIT DES SOCIÉTÉS 310 (9th ed. 1996). A single shareholder can thus obtain the proxies of many fellow shareholders.

99. See Loi N° 83-1 du 3 janvier 1983, [1983] JO 4 janvier 162, art. 161-1 (Fr.), C. soc., *supra* note 1, at 323; Décret N° 67-236, art. 131-1 to 131-34, C. soc., *supra* note 1, at 632 (as amended by Décret N° 86-584 du 14 mars 1986 and Décret N° 88-55 du 19 janvier 1988).

100. See Joel Chernoff, *Shareholder Power Grows: France's First Proxy Solicitations Are Big Step Forward*, PENS. & INV., June 10, 1996, at 19 (this technique was designed by the U.S.-trained shareholder activist, Sophie L'Hélias).

101. See Loi N° 66-537, art. 175, C. soc., *supra* note 1, at 334-35. See also *infra* note 223-24 and accompanying text.

the number of votes a shareholder can cast at a shareholders' meeting,¹⁰² which, in the circumstances of market capitalism, help protect management from collective shareholder action.¹⁰³

Senator Marini recommends making the French proxy process more responsive to and more protective of capital market shareholders. He suggests one reform, based on a Swiss model, that would involve appointing an independent official (a *mandataire indépendant*) for shareholders' meetings, to whom capital market investors could send their "blank" powers and who would be more inclined than management to act on their behalf.¹⁰⁴ He also suggests facilitating the formation of shareholder associations to enhance the ability of small shareholders to act collectively in their shareholder and investor organizations.¹⁰⁵ In addition, inspired by U.S. law on pension voting,¹⁰⁶ Senator Marini recommends that French institutional investors, such as mutual funds and private pension funds, be legally obligated to vote and to explain to their clients their voting policies.¹⁰⁷

102. See Loi N° 66-537, art. 177. See also *infra* note 215 and accompanying text.

103. See Loi N° 78-741 du 13 juillet 1978, [1978] JO 14 juillet 2799, art. 177, C. soc., *supra* note 1, at 726-28 (Fr.). In effect, the legal ability to put a ceiling on voting by any single shareholder suggests that French corporate governance is changing (i.e., that there is no longer a controlling shareholder, like the State, in a company's capital. If there were such a shareholder, no protective ceiling would be necessary). Further, it shows that French company managers are afraid of the outcome of this transformation (i.e., they want the protection from takeovers that the ceiling gives them when there is no dominant shareholder).

In addition, French law allows a company to require that shares other than those registered on a company's books be "immobilized" for five days up to the date of the meeting, if a shareholder holding such shares wants to vote. See Décret N° 67-236, art. 136, C. soc., *supra* note 1, at 636. This process deters market capitalism, since capital market investors may well be reluctant to immobilize their shares for even a short period. See LA PORTA, *supra* note 14, at 19.

104. See Marini Report, *supra* note 2, at 92.

105. See, e.g., *id.* at 94-95 (recommending that these organizations include bearer, as well as registered, shareholders).

106. See, e.g., Department of Labor, Pension and Welfare Administration Interpretive Bulletin, 59 Fed. Reg. 38,860 (1994) (stating that fiduciaries of private pension plans have responsibility to vote proxies of shares held by the plan).

107. See *id.* at 99. See also Jean-Paul Vauet, *L'identification des actionnaires des sociétés cotées*, *RÉVUE DES SOCIÉTÉS*, oct.-déc. 1996, at 707, 725-28. The article discusses legal problems that may hinder voting in French companies by nonresident shareholders and the need for a solution since these shareholders are increasingly likely to exercise their voting rights. It further proposes that financial intermediaries be allowed to transmit the vote of shareholders, if these intermediaries receive the permission of shareholders and disclose their intermediary status to the issuer. See *id.* In commenting upon the Marini Report, Professor Merle suggests that more emphasis should be placed on the better use of voting *par correspondance*, rather than on new methods of shareholder voting. He also cautions against pushing French institutional investors to vote before installing safeguards to prevent their abuse of the vote. See Merle, *supra* note 80, at 45-47. The French legislature has recently passed a law authorizing the creation of private pension plans. See generally *Plan épargne retraite: Mode d'emploi*, *LE POINT*, Mar. 15, 1997, at 81-86.

III. Directors and Other Supervisors of Managers

Directors are of critical importance in the corporate governance of publicly-owned firms. Elected by shareholders, they are expected to represent shareholder interests, even if their primary obligation runs to the legal "personality" of the corporation. Although they do not manage the corporation's operations, directors are supposed to "direct," or to supervise, its business. A corporate director thus occupies the ideal middle position between management and shareholders. He or she can generally supervise the former on behalf of the shareholders. Further, even if he or she cannot pay the same amount of attention as management to the business, it is at least more attention than the owners themselves can give. Directors often have considerable business experience, making them well-suited to this role. As a corporate structural matter, therefore, the directors could address the agency problems presented by market capitalism.

In practice, however, the director in France has often been a corporate governance disappointment. A typical director does not necessarily have the same interests as shareholders and also is not directly answerable to them (again, the director's primary responsibility is to the corporation). In fact, the director is much more likely to be a representative of management than of shareholders. Managers, not shareholders (except shareholders contesting management), have the main say in nominating directors, and thus directors are beholden to management for their position. Directors frequently come from management ranks (the chief executive of a French company is also its chairman of the board) or former management. They may also be business executives at other companies, who, on account of their own positions, are sympathetic to management's desire to run a company without interference. Lastly, directors may be in occupations whose business success may depend upon management's good graces, such as investment banking, law, or business consultation, that provide services to a corporation.¹⁰⁸

Even if directors were focused upon protecting shareholder interests against managerial overreaching, they are at a disadvantage for logistical reasons. Corporate boards act only at meetings and since, except in a "crisis," meetings occur infrequently, directors (who generally have other full-time positions) do not have much time to supervise management. It is also questionable whether this meeting time, as well as the necessarily limited premeeting preparation, is adequate to enable them to comprehend the complex business of a large public company. Directors have a right to information about the corporation. The information, however, generally

108. General research on boards of directors suggests that the director's background, as well as other social factors, such as group behavior and loyalty, conspire to ensure that boards are deferential to management and passive in protecting shareholder rights. See generally ADA DEMB & F.-FRIEDRICH NEUBAUER, *THE CORPORATE BOARD: CONFRONTING THE PARADOXES* (1992); JAY W. LORSCH & ELIZABETH McIVER, *PAWNS AND POTENTATES: THE REALITY OF AMERICA'S CORPORATE BOARDS* (1989). The French situation is more acute since chief executives in large French companies have almost dictatorial powers. See *infra* Part IV.A.

comes not from an independent directorial staff, but from management, which can therefore control its content and presentation.¹⁰⁹

Much corporate legal (and other) scholarship in the last three decades suggests ways to minimize the passivity of boards of directors functioning in market capitalism and to make boards more responsive to shareholder interests. One reform, which has now become a reality in many Anglo-American jurisdictions, mandates that the majority of directors be "outside" directors, individuals not drawn from management.¹¹⁰ This reform has not proved to be a panacea because it fails to deal with the indirect influence of managers on directors and the issues of directors' lack of time and expertise. Another suggestion is to have "professional" directors, whose full-time job would be to direct several companies and who could thus develop expertise in monitoring company management.¹¹¹ Furthermore, to help insulate outside directors from management influence, the chairperson of the "supervisory board" could be required to be an outsider as well.¹¹² Current research also identifies the importance of tying board compensation to company share performance, thus linking the interests of board members and shareholders more closely.¹¹³ While legal and nonlegal efforts to make corporate directors more effective monitors for shareholders continue,¹¹⁴ basic corporate law addresses the agency problem by imposing upon directors specific duties and establishing guidelines by which directors can satisfy these legal obligations.

A. The General Obligations of a Director

By setting standards for director conduct, French corporate law attempts to ensure that directors (*administrateurs*) will take their positions seriously and thus monitor management for the benefit of shareholders. As a prelim-

109. The Viénot Report recognizes these problems with board operation, although it does not consider that they require changes to French corporate law. For example, it observes that French company boards "meet three to four times a year, and in practice meetings last around two hours." See Viénot Report, *supra* note 2, at 16. It also recognizes that directors receive information about the company only from management. See *id.* at 17.

110. See generally 1 AMERICAN LAW INSTITUTE, PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS 110-14 (1994) [hereinafter PRINCIPLES] (discussing recommendation from a group of legal practitioners and scholars that corporate boards in large public companies should consist of a majority of outside directors).

111. See Ronald J. Gilson & Reinier Kraakman, *Reinventing the Outside Director: An Agenda for Institutional Shareholders*, 43 STAN. L. REV. 863 (1991). See also Laura Lin, *The Effectiveness of Outside Directors as a Corporate Governance Mechanism: Theories and Evidence*, 90 NW. U. L. REV. 898 (1996).

112. See 1 PRINCIPLES, *supra* note 110, at 115-33 (discussing the function and composition of audit, nominating and compensation committees). See also WILLIAM A. KLEIN & JOHN C. COFFEE, JR., *BUSINESS ORGANIZATION AND FINANCE: LEGAL AND ECONOMIC PRINCIPLES* 151-52 (1996).

113. See Charles M. Elson, *Shareholding Directors Create Better Corporate Performance*, ISSUE ALERT, May 1996, at 3 (describing report of the National Association of Corporate Directors' Commission on Director Compensation). See generally Romano, *supra* note 63, at 284-97.

114. For a discussion of the impact of this research on reforming French boards, see *infra* Conclusion.

inary matter, it is useful to explain French corporate board structure. Although there are two possible legal structures,¹¹⁵ the following summary concerns only the form that is widely used. Under French law, a board of directors or "*conseil d'administration*," elected by shareholders, "administers" the affairs of the French *société anonyme*.¹¹⁶ The law gives the *conseil* broad powers to act on the company's behalf.¹¹⁷ It elects from its members a president, who "is responsible for general management of the company," who acts for the company with respect to third parties, and who can essentially exercise all powers not reserved to the shareholders or to the board.¹¹⁸ The actual direction and operation of a company thus lie in the president's hands, subject to the board's supervision. The board can also grant the president the ability to appoint one or more individuals, known as *directeurs généraux*, to assist him in company management.¹¹⁹ These "directors" work with non-*directeur* executives and the president, who is himself a general director and goes by the title of "*président directeur général*" or the "PDG." The PDG thus has considerable statutory powers and is perceived to be all powerful in his company.¹²⁰

A director's responsibility to the corporation (and thus to the shareholders) is stated in the French corporate code and explained in the related jurisprudence. In particular, the code provides that, "The directors are responsible individually or as a group, depending upon the situation, to the company or third parties, for (1) violations of laws or regulations applicable to corporations, (2) violations of the certificate of incorporation, and (3) errors committed in the course of management."¹²¹ Shareholders cannot relieve directors of this responsibility by ratifying an action or decision

115. French law provides for two board structures: a board of directors (*conseil d'administration*) which selects one of its members as the chairman and chief executive (*président directeur général* or "PDG"), see Loi N° 66-537, art. 89-117, C. soc., *supra* note 1, at 230-90, and a supervisory board (*conseil de surveillance*), which names an executive board (*le directoire*) and selects a president thereof, see *id.* art. 118-150, C. soc., *supra* note 1, at 290-308. The second structure, which is infrequently used in France, is modeled on the German system. See CLAUDE DUCOULOUX-FAVARD, *SOCIÉTÉ ANONYME, AKTIEN GESELLSCHAFT, SOCIETÀ PER AZIONI* 120-29 (1992).

116. Loi N° 66-537, art. 89, C. soc., *supra* note 1, at 230.

117. Loi N° 66-537, art. 98, C. soc., *supra* note 1, at 250-57 (from Loi N° 67-559 du 12 juillet 1967 and Ordinance Loi N° 69-1176 du 20 décembre 1969) (Fr.) ("Le conseil d'administration est investi des pouvoirs les plus étendus pour agir en toute circonstance au nom de la société; il les exerce dans la limite de l'objet social et sous réserve de ceux expressément attribués par la loi aux assemblées d'actionnaires.").

118. Loi N° 66-537, art. 113, C. soc., *supra* note 1, at 281-84 (from Loi N° 67-559 du 12 juillet 1967).

119. See Loi N° 66-537, art. 115, C. soc., *supra* note 1, at 285-87.

120. See Ducouloux-Favard, *supra* note 31, at 872 (describing how the PDG structure during the Vichy regime was based upon German corporate law). As Senator Marini has observed, French corporate law gives the PDG and the board almost equal power. In some cases, managers of large French companies now use this power unchecked by State oversight, the former means of internal control. See Marini Report, *supra* note 2, at 8-9, 39-40.

121. Loi N° 66-537, art. 244, C. soc., *supra* note 1, at 408-11 (from Loi N° 67-559 du 12 juillet 1967) (translation by author). As the late Professor Jeantin remarked, "company directors (managers or a board of directors (or a supervisory board) of a corporation) have a positive obligation to act, under all circumstances, in the company's

of the directors which is allegedly in violation of their duties.¹²²

The closest of the above three "duties" to a basic "duty of care" is the last obligation of directors — to avoid any "*fautes commises dans leur gestion*."¹²³ The French corporate code, however, fails to define this concept. In his treatise, Professor Gibirila explains that a director is expected to act as a prudent, diligent and active person would in similar circumstances (that is, as a corporate director would act), and that he or she cannot use lack of experience or knowledge as an excuse.¹²⁴ He admits that this *faute* is difficult to establish with precision, particularly for acts of *administrateurs*, as opposed to proving the misconduct of *directeurs* who are actively engaged in business management. He also acknowledges that French courts apply the doctrine on a case-by-case basis.¹²⁵ Directors must take an active interest in the enterprise and scrutinize the actions of the PDG and the other *directeurs généraux*. An important part of their *gestion* is to ensure that they have adequate information about the business and the PDG's conduct thereof.¹²⁶

The liability imposed upon a director if a company becomes bankrupt exemplifies the seriousness with which French law treats a director's obligation to supervise company management. Under French bankruptcy law, a director is personally liable if there are insufficient assets to cover creditors' claims, if he or she committed a *faute de gestion*, and if the *faute* "contributed" to the deficiency.¹²⁷ In this context, too, the statutory law fails to define what constitutes a *faute de gestion*. Case law suggests, however, that a director may be liable even on the basis of simple negligence.¹²⁸ Although it is difficult to prove director error and many reported cases deal with gross nonfeasance or malfeasance,¹²⁹ this legal obligation and penalty reinforce the supervisory responsibilities of a French company director.¹³⁰

At first glance, the French legal "duty of care" is puzzling from a corporate governance perspective. One might predict that there is no developed duty in French corporate law, because the duty would seem to go hand in hand with the protection of capital market investors. Yet the opposite is

interest. If they fail to do this, their responsibility is engaged." See JEANTIN, *supra* note 77, at 134-35.

122. See Loi N° 66-537, art. 246, C. soc., *supra* note 1, at 413 ("Aucune décision de l'assemblée générale ne peut avoir pour effet d'éteindre une action en responsabilité contre les administrateurs pour faute commise dans l'accomplissement de leur mandat.").

123. *Id.* art. 244, C. soc., *supra* note 1, at 408-11. Professor Gibirila admits that the obligation of a director to avoid the *faute de gestion* sometimes overlaps with his other duties (i.e., to avoid breaking the law and committing a *violation des statuts*). See DEEN GIBIRILA, *LE DIRIGEANT DE SOCIÉTÉ: STATUT JURIDIQUE, SOCIAL ET FISCAL* 439 (1995).

124. See GIBIRILA, *supra* note 123, at 430, 439.

125. See *id.* at 439-40.

126. See *id.* at 441.

127. See Loi N° 85-98 du 25 janvier 1985, [1985] JO 26 janvier 1985, art. 180, C. soc., *supra* note 1, at 794, 812-19 (Fr.).

128. See GIBIRILA, *supra* note 123, at 479.

129. See *id.* at 480.

130. Directors are also subject to considerable criminal penalties for abuse of their functions. See *id.* at 540-64.

true: the duty to avoid *fautes de gestion* is at least as severe as any "duty of care" in the Anglo-American legal context.¹³¹ A duty of care does not, in fact, implicate only a corporate governance of capital market investors. A legal obligation like the duty of care is useful in every corporate situation, because, by definition, the corporate form involves a delegation of responsibility to those who manage property that they do not own. After all, the foundation of the duty of care, as with other corporate duties, lies in basic agency law. One should thus expect to see the duty wherever the corporate form exists. In economic terms, a general, open-ended obligation imposed upon directors, like the duty of care, is the most cost-efficient manner of monitoring their behavior for long periods of time in unforeseeable circumstances.¹³²

The use or enforcement of the duty, not its existence, makes the difference. In a country like the United States where market capitalism has a long history, the duty has been refined to protect capital market investors during different events that involve public companies, (including proxy contests, mergers, and hostile takeovers), without deterring management from making business decisions. In France, the duty has not similarly developed because controlling shareholders, like the State and families, had other means to police and direct management. The French duty of care will become an important protection for French and non-French capital market investors as these investors begin to play a larger role in the capitalization of French companies.¹³³ In fact, both the Viénot Report and the Marini Report urge French directors to take their basic duty of care more seriously.¹³⁴ Given the attention this duty has attracted from French legal policy makers, it may soon assume a more important role in French corporate governance.

B. A French Director's Duty of Loyalty

Since the corporate form uses agents and thus implicates an inevitable conflict of interest between agents and principals, directors owe a duty of loy-

131. Under Delaware law, for example, the duty of care requires that a director not be grossly negligent and that he or she act reasonably under the circumstances of the director's position (e.g., size of the corporation). See, e.g., *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985). A director's compliance with the duty of care often turns on whether the director adequately informed himself and debated with his peers before taking action (generally before voting for a resolution proposed by management). The American Law Institute (ALI) further qualifies the definition of the duty of care, by specifically stating that it "includes the obligation to make, or cause to be made, an inquiry when, but only when, the circumstances would alert a reasonable director or officer to the need therefor." 1 PRINCIPLES, *supra* note 110, §4.01(a)(1) at 138-39.

132. See FRANK H. EASTERBROOK & DANIEL R. FISCHEL, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* 91 (1991).

133. In both the United States and France, directors are under an obligation to obey the law and the corporate certificate or articles of incorporation. These obligations, while important, are at the outer bounds of corporate governance, governing only egregious management abuse.

134. See Marini Report, *supra* note 2, at 42-43; Viénot Report, *supra* note 2, at 20-21.

alty to, or a duty to deal fairly with, the corporation.¹³⁵ Officers and directors of large public corporations with capital market investors should bear this obligation because they control the property of shareholders who cannot individually monitor their agents' behavior, and thus managers have the opportunity to engage in opportunistic behavior at shareholders' expense.¹³⁶ For example, a director or officer may directly or indirectly do business with the corporation on terms which are personally beneficial but are not favorable to the corporation. This may take the form of extraordinarily high executive or director compensation, personal use of corporate property, or use of corporate information for his or her benefit.¹³⁷ Since disclosure discourages self-serving management actions, disclosure obligations help to prevent these abuses in large public companies.

Similarly, French corporate law imposes upon managers and directors a duty of loyalty and regulates their conflicts of interest. As a general matter, it limits the number of comparable positions that an officer or director may occupy, although the limitations are not particularly restrictive. No individual can be a member of more than eight boards of directors of *sociétés anonymes* in France,¹³⁸ nor can he or she occupy the position of PDG in more than two companies.¹³⁹

French conflict of interest rules also reach management and director self-interested transactions. Subject to certain exceptions, French law prohibits a director or an executive (and any of their relatives) from borrowing money, or receiving a guaranty, from his or her corporation.¹⁴⁰ This rule not only protects shareholders and creditors from an improper use of corporate funds, but stands upon a moral ground. It prevents improper management and director behavior that may injure a corporation's reputation

135. The ALI uses the term "duty of fair dealing" to emphasize the obligation of officers, directors and control persons to avoid conflicts of *pecuniary* interest with the corporation. See 1 PRINCIPLES, *supra* note 110, at 199-200.

136. Some academic literature criticizes the imposition of this duty upon managers. The reasoning is that, if managers divert wealth from shareholders through conflict of interest transactions, shareholders can simply reduce management compensation accordingly. Other scholars believe that management's diverting wealth to itself hurts shareholders. For a summary of the debate, see LUCIAN AYRE BEBCHUK & CHRISTINE JOLLS, *MANAGERIAL VALUE DIVERSION AND SHAREHOLDER WEALTH* 1-3 (Harvard Law School John M. Olin Center for Law, Economics, and Business, Discussion Paper No. 179, 1996).

137. See CLARK, *supra* note 75, at 141-46.

138. See Loi N° 66-537, art. 92, C. soc., *supra* note 1, at 236. This restriction excludes board positions that a natural person occupies as a representative of a company, and up to five additional positions in companies that are at least 20% owned by a company in which one is already a board member. *Id.*

139. See Loi N° 66-537, art. 111, C. soc., *supra* note 1, at 280. Senator Marini proposes restricting this *cumul des mandats* so that the eight board membership restriction would include board positions which are now exempted from it and that a PDG would be restricted to four board positions (not counting his board seat in the company and membership on boards of its subsidiaries). See Marini Report, *supra* note 2, at 45. His reason for this recommendation, however, is not to address conflicts of interest, but to "upgrade" the quality of French board members and executives.

140. See Loi N° 66-537, art. 106, C. soc., *supra* note 1, at 270-71.

and thus its ability to raise capital.¹⁴¹ In the event of a violation, the company can either declare the contract void or seek damages from the offending officer or director.¹⁴² In addition, this misfeasance subjects a director or manager to criminal sanctions for improper use of corporate property, particularly the crime of *abus de biens sociaux*.¹⁴³

French law does not prohibit all transactions between a director or officer and a corporation; it simply subjects them to a prior approval process. Other than contracts in the ordinary course of a corporation's business,¹⁴⁴ the following contracts must be preapproved by a specific procedure: those between a director or executive and his or her corporation; those between the corporation and another corporation or business in which he or she is an owner, director or executive; and those between the corporation and someone with whom the director or executive is directly or indirectly linked.¹⁴⁵ This rule applies to any special compensation for members of the board of directors, other than directors' fees (the *jetons de présence*),¹⁴⁶ but does not apply to the board's determination of compensation for the PDG.¹⁴⁷ French law broadly defines the kinds of contracts subject to this preapproval procedure so that it covers any agreement, whether written or oral, that might allow directors or executives to benefit at the company's detriment.¹⁴⁸

Under the approval procedure,¹⁴⁹ the "interested" director or officer must inform the board of directors about the conflict of interest, that is, the

141. See GIBIRILA, *supra* note 123, at 382.

142. *Id.*

143. See Loi N° 66-537, art. 437, C. soc., *supra* note 1, at 556-65, translated in COMMERCE CLEARING HOUSE, INC., FRENCH LAW ON COMMERCIAL COMPANIES 167-68 (1971).

The president, the administrators, or the general managers of a corporation who, acting in bad faith, use the corporation's property or credit in a manner which they know to be contrary to the interests of the corporation, for personal ends, or for the benefit of another company or enterprise in which they have a direct or indirect interest, will be punished by imprisonment from one to five years and/or receive a fine of 2,000 to 2,500,000 Francs.

Id.

144. See Loi N° 66-537, art. 102, C. soc., *supra* note 1, at 263-65.

145. Article 101 of the Loi N° 66-537 provides that:

Toute convention intervenant entre une société et l'un de ses administrateurs ou directeurs généraux doit être soumise à l'autorisation préalable du conseil d'administration.

Il en est de même des conventions auxquelles un administrateur ou directeur général est indirectement intéressé ou dans lesquelles il traite avec la société par personne interposée.

Sont également soumises à autorisation préalable, les conventions intervenant entre une société et une entreprise, si l'un des administrateurs ou directeurs généraux de la société est propriétaire, associé indéfiniment responsable, gérant, administrateur, directeur général ou membre du directoire ou du conseil de surveillance de l'entreprise.

Loi N° 66-537, art. 101, C. soc., *supra* note 1, at 259-63.

146. See Loi N° 66-537, art. 109, C. soc., *supra* note 1, at 272. The *jetons* are simply compensation paid to directors for their attendance at board meetings. See *id.* art. 108.

147. See *infra* notes 157-59 and accompanying text.

148. See generally GIBIRILA, *supra* note 123, at 389-90.

149. See Loi N° 66-537, art. 103, C. soc., *supra* note 1, at 265-66.

transaction, contract, or both in which he or she has a direct or indirect interest. The entire board (not a board committee), acting without the voting participation of any interested director (who neither counts toward the board quorum nor can vote), must authorize the transaction by a specific decision after receiving adequate information about the transaction and deliberating formally on its merits. Once the board approves the transaction, it can proceed.¹⁵⁰ The PDG must inform the company's statutory auditors (*les commissaires aux comptes*) about the transaction. Prior to the next annual shareholders' meeting, the auditors must prepare for the shareholders a report on this transaction, as well as on any other similar transactions, including those that the statutory auditors may have discovered and those that did not receive the board's disinterested pre-authorization. At the annual meeting, shareholders are asked to approve the transaction. Failure to obtain shareholder approval, however, does not render the contract void, but may lead to liability of the interested director, and possibly the board, for any damages suffered by the corporation because the contract was not approved (for example, if the contract or transaction were contingent upon shareholder approval).¹⁵¹

Fraud nullifies an "interested" contract. Even in the absence of fraud, the contract is void if the board of directors did not pre-approve it, provided that the corporation suffered damages as a result.¹⁵² A shareholder vote at a general meeting can ratify the contract if shareholders approve it after receiving a special report by the statutory auditors explaining why the board failed to follow the proper pre-approval procedures. As noted above, a violation of the duty of loyalty by a director or officer can also give rise to criminal liability.¹⁵³ Fraudulent use or appropriation of corporate assets can lead to such a penalty, as can the intentional use of corporate goods or credit for a director or executive's personal ends or for his or her other business, if detrimental to the corporation (the classic *abus de biens sociaux*).¹⁵⁴ Similarly, criminal liability attaches when directors or executives abuse their powers or positions for other self-interested purposes.¹⁵⁵

Having entrusted their funds to corporate managers, French shareholders receive the legal protection that the "duty of loyalty" provides. Managers realize that, if they do not follow the pre-approval process and their self-dealing is detected and determined to be unfair to the corporation, the transaction will be voided and they will suffer any losses arising from unwinding the transaction, as well as criminal liability. From a capital market perspective, these laws help ensure that shareholder funds are not diverted to management's personal uses and that shareholders need not impose a significant discount on a corporation's share price as com-

150. In certain cases, pre-approval by shareholders can substitute for board approval. See GIBIRILA, *supra* note 123, at 403.

151. See Loi N° 66-537, art. 104, C. soc., *supra* note 1, at 266-67.

152. See Loi N° 66-537, art. 105, C. soc., *supra* note 1, at 267-70.

153. See *supra* note 143 and accompanying text.

154. See Loi N° 66-537, art. 437, C. soc., *supra* note 1, at 556-65.

155. See *id.*

pensation for the risk of management self-dealing.¹⁵⁶

A potentially troubling kind of self-dealing arises in management compensation. By law, the French board of directors alone determines the compensation of its president and general director;¹⁵⁷ it cannot delegate this matter to a compensation committee, nor does this determination come within the above approval procedure for contracts or transactions involving a conflict of interest. Individual compensation of executives has generally been kept secret in French companies, while the aggregate compensation figures for all executives is customarily disclosed. Further, no detailed disclosure is required under French securities laws, even though other systems have concluded that complete disclosure deters serious compensation abuses. Given the considerable power of the PDG over other directors (and the likelihood that other directors, themselves often PDGs or former executives, would support generous PDG's compensation package) and the secrecy of compensation arrangements, the possibility for abuse still exists in French management compensation.

Yet, in France, executive compensation has not generally been debated or viewed as a corporate governance problem.¹⁵⁸ Since the State and family owners have for some time closely supervised managers, they may well have kept compensation within reasonable bounds. This lack of attention to executive compensation, however, is likely to change. As the State recedes from its influence in some large companies, the likelihood of management opportunism in compensation increases. Capital market investors (whether French or non-French) are likely to pay more attention to how French management compensation is determined and demand more information about individual executive compensation. Market forces alone may effect change in this area.¹⁵⁹ In addition, the board's legal obligation in setting compensation will likely come under increased scrutiny and French jurisprudence in this area will be developed.

Thus, French corporate law addresses management and director self-dealing in a detailed manner. Again, this is not surprising because the French corporate form rests upon a basic agency relationship and there is a need in any such relationship to find an economical way of guarding against overreaching by the agent. If anything, French corporate law may be too strict in discouraging contracts between management and the corporation, which might arguably be beneficial to both parties, and in penaliz-

156. The duty may thus be the most efficient (i.e., least costly) way for shareholders to monitor corporate agents. See EASTERBROOK & FISCHEL, *supra* note 132, at 90-108.

157. See Loi N° 66-537, art. 110, C. soc., *supra* note 1, at 272-80.

158. See Pastré, *supra* note 3, at 32.

159. Because of pressure from non-French shareholders, some French executives are "voluntarily" disclosing their compensation. In economic terms, this could be seen as an effort by agents to "bond" with their principals, which reduces the discount that investors would assign to a company's shares for the risk of management opportunism on compensation. See *France's Boardroom Revolution*, WALL ST. J., Oct. 17, 1995, at A20 (discussing executive compensation disclosure by management at Lyonnaise des Eaux).

ing management under criminal law for minor violations of the duty.¹⁶⁰ In fact, in his proposed reform to the French corporate law, Senator Marini suggests eliminating criminal penalties for conflict-of-interest transactions when the interested managers and directors involved do not personally benefit from a particular transaction.¹⁶¹

In the conflicts of interest area, French law is well-suited for closely-held corporations. Yet, in public companies, where capital market shareholders predominate, disclosure about management and directors and their dealings with the company is necessary to discourage self-dealing. Here, as exemplified by executive compensation, French law is not completely developed.¹⁶² Increased disclosure on management activity and its potential conflicts, which would deter self-dealing and act as a useful signal of management's loyalty to shareholders, would further capital market financing in France. If this disclosure is improved and other internal controls on management are instituted, then it will make sense to eliminate the criminal penalties for minor violations of the duty of loyalty.

C. Monitoring Through Accounting

Shareholders must rely on other parties inside the corporation to ensure that the corporation is being operated on their behalf.¹⁶³ One check on management behavior comes from an auditor or accountant. Depending upon the circumstances of his or her employment, the auditor or accountant may be either a corporate agent or an independent professional. A business operates for profit, and profit depends not only upon the product or services offered, but also to some extent upon control of, and information about, expenses and revenues. Particularly, because neither executives nor directors have the time, nor often the expertise, to do this work, and because they need financial information to make business decisions, the establishment of financial controls, the preparation of financial statements, and the accountants who perform this work are significant in corporate

160. Indeed, the prevalence of criminal sanctions for violations of a duty of loyalty goes hand in hand with the State's involvement in companies, for a violation of corporate law or a company's *statuts* (certificate of incorporation) implicates State interests. See *infra* Part VI, Section D.

161. See Marini Report, *supra* note 2, at 112-21. The French Court de Cassation has recently held that criminal sanctions for an *abus de biens sociaux* may not lie when a director or manager does not personally benefit from the transaction. Judgment of Feb. 6, 1997, Cass. Crim., 1997 Bull. Crim. (Fr.) at *20-21, available in LEXIS, Intlaw library, Frprcs file (holding that a bribe paid indirectly by a company president to a government official seeking to reduce the amount the company owed the government did not constitute, without any more showing, a payment for the president's personal interest).

162. Since statutory auditors report potential conflicts of interest to shareholders, who must vote to approve them at the annual meeting, and since these conflicts are then publicized by the financial press, deterrence may be accomplished without legal reform.

163. There are also forces outside the corporation that monitor agent behavior. These forces, such as product and capital market pressures, are not properly the subject of an analysis of legal corporate governance. See Jensen, *supra* note 5, at 850.

governance.¹⁶⁴

For any French company of significant size, French corporate law creates an official corporate governance role for accounting professionals.¹⁶⁵ These *commissaires aux comptes* are similar to U.S. external auditors. Elaborate rules, which govern eligibility for the position, ensure that *commissaires* cannot have, either directly or indirectly, any relations with management, owners, or affiliates of the company (or their relations). In addition, they cannot take positions in the company following the conclusion of their employment mandate. Other regulations require that *commissaires* be independent accounting professionals who are under the jurisdiction of regional and national commissions, and the *Cours d'Appel*.¹⁶⁶ Only a French court can remove the *commissaires* for cause.¹⁶⁷

The basic role of the *commissaires* is to audit a company's accounts. This is not a one-time effort provided at the end of the fiscal year, but rather the work extends throughout the year and involves reviewing any prepared accounts and continually monitoring a company's internal financial control systems.¹⁶⁸ Whether or not they "certify" a company's accounts, the *commissaires* must report on them to both the board of directors and the shareholders. The latter must vote to ratify the accounts and can do so only after receiving the report.¹⁶⁹ The *commissaires* must also verify any other company accounts, as well as any management reports on a company's financial situation. In accomplishing these tasks, they cannot participate in company management and must guard their independence from it.¹⁷⁰ The requirements that the *commissaires* notify the board and shareholders of any irregularities discovered in the company's accounts and that they alert the French public prosecutor to any serious problems therein exemplify this independence.¹⁷¹ Under French law, the accountants are liable to the company and to third parties for damages arising from their negligence.¹⁷²

164. See Louis Lowenstein, *Financial Transparency and Corporate Governance: You Manage What You Measure*, 96 COLUM. L. REV. 1335 (1996) (reaffirming the importance of accounting in corporate governance).

165. See Loi N° 84-148 du 1er mars 1984, [1984] JO 2 mars 751, arts. 218-35, C. soc., *supra* note 1, at 374-402 (Fr.) [hereinafter Loi N° 84-148]. See generally JEANTIN, *supra* note 77, at 144-56.

166. See Loi N° 84-148, arts. 219, 219-1, 219-2, 219-4, C. soc., *supra* note 1, at 375-77.

167. See Décret N° 67-236, art. 188, C. soc., *supra* note 1, at 662 (as amended by Décret N° 85-295 du 1er mars 1985); see also Loi N° 84-148, art. 227, C. soc., *supra* note 1, at 390.

168. See Loi N° 83-353 du 30 avril 1983, [1983] JO 3 mai 1356, C. soc., *supra* note 1, at 1386 (Fr.); Loi N° 85-11 du 3 janvier 1985, [1985] JO 4 janvier 101, C. soc., *supra* note 1, at 793-94 (Fr.); Loi N° 66-537, art. 228, C. soc., *supra* note 1, at 392-93.

169. See Loi N° 66-537, arts. 230, 233, C. soc., *supra* note 1, at 395, 398-99.

170. See Loi N° 66-537, art. 228, C. soc., *supra* note 1, at 392.

171. See *id.* For example, Article 233 provides that "they shall inform the state Prosecutor of any offenses of which they have knowledge, but they may not be held liable for such disclosure." *Id.* art. 233, translated in COMMERCE CLEARING HOUSE, INC., *supra* note 143, at 113.

172. See Loi N° 66-537, art. 234, C. soc., *supra* note 1, at 399-402. The *commissaires* also have a duty to notify the board, and ultimately the shareholders, of any information

The duties of the *commissaires aux comptes* are related to French law's requirements on publication of financial statements. At the end of each fiscal year, the board or managers of large French public companies must compile, among other things, an inventory, financial statements, and a written report. The report covers the management of the enterprise, information on current assets and liabilities, the value of shares held in the company's investment portfolio, financial results, and plans pertaining to financing.¹⁷³ Management makes this information available to the *commissaires* for verification prior to the shareholders' annual meeting.¹⁷⁴ At mid-fiscal year, a company's board or management gives a preliminary review of balance sheet information and pre-tax revenues, which is once again reviewed and certified by the *commissaires*.¹⁷⁵ Similarly, a company must prepare a statement of its net revenue every four months, categorized by activity and compared with preceding periods.¹⁷⁶ The end-of-year information is published in an official legal journal, as is the semi- and tri-annual information.¹⁷⁷

The corporate governance conclusions that can be drawn from French legal requirements on financial statement certification are similar to those discussed in the context of directors' duties. As one would expect given the importance of accounting in any evaluation of business results, verification of accounts by the *commissaires* has long been used in France as a way of detecting management abuse. Yet in recent years, the *commissaires* have become increasingly important as amendments to French corporate law in 1984 enhanced the position of the *commissaires* and as greater financial reporting obligations (subject to *commissaire* review) have been imposed upon large French companies.¹⁷⁸ Such developments point to French legal policy-makers' recognition of the increased importance of capital market investors in France. These investors, together with the market professionals acting on their behalf, need reliable information about companies that is "certified" by outsiders. The broad powers of continuous review given to the *commissaires* and their reporting (even to parties outside the corporation) represent an attempt by French law-makers to equalize the balance of power (if only in the information area) between management and shareholders and to push the board to take its oversight duties more seriously.¹⁷⁹ To improve further the internal controls on management of

coming to their attention indicating that the company is in financial difficulty. Loi N° 84-148, art. 29, C. soc., *supra* note 1, at 758. The *commissaires* are criminally liable for any serious dereliction of their duties.

173. See Loi N° 66-537, art. 340, 340-1, 341-1, C. soc., *supra* note 1, at 469-70, 472-73.

174. See Décret N° 67-236, arts. 243-44, C. soc., *supra* note 1, at 676-77.

175. See Décret N° 67-236, arts. 244-1, 297-1, C. soc., *supra* note 1, at 677, 700-01.

176. See Décret N° 67-236, art. 297, C. soc., *supra* note 1, at 700.

177. See Décret N° 67-236, arts. 295-96, C. soc., *supra* note 1, at 699-700.

178. Much of the preceding discussion about *commissaires* refers to provisions placed in French corporate law as a result of the 1984 amendments. See, e.g., *supra* notes 165-67 and accompanying text.

179. In addition to the *commissaires*, French law allows shareholders representing 10% of the capital of a corporation to petition a court to appoint an expert to review the

French companies, Senator Marini recommends increasing the responsibility of the *commissaires*.¹⁸⁰

While the *commissaires'* corporate governance role and their responsibility to detect serious management errors is important, it is ultimately limited by the restrictions on their participation in management. They simply cannot provide *all* of what dispersed capital market shareholders often need: adequate representation in the supervision of a corporation that can provide strategic advice to, and a strong check on, executives *before* serious problems develop. As their role is currently defined, the *commissaires* will not fully be able to address difficulties arising from a separation of ownership and control in a public corporation if such difficulties become acute in France with the increase in capital market investors. While it is important to understand the corporate governance contribution of the *commissaires* through accounting, they should not be seen as a substitute for an effective board of directors.¹⁸¹

IV. Governance Issues Related to the Elimination of Minorities

A major transformation of the corporation's business is an important event for both the corporation and its shareholders. Investors who have elected to fund a particular kind of venture may not want to be equity holders in a different enterprise. Several central legal corporate governance issues arise in such cases: whether corporate directors conduct themselves appropriately in deciding upon the transformation, whether shareholders should have any input in the decision, and whether shareholders who disapprove of the transformation can exit the corporation's capital without incurring "unfair" losses. These issues are important in a market-based system of corporate governance where dispersed capital market investors cannot easily oppose transformations proposed by management. The following discussion briefly explains the legal decision-making structure of the major forms of corporate transformations, such as a merger or significant asset sale, and its corporate governance import. It then discusses the availability of exit for a French shareholder objecting to a transaction and the absence of special obligations on directors relating to the elimination of minorities from a corporation's capital.

management of specific business operations. See Loi N° 66-537, art. 226, C. soc., *supra* note 1, at 382-389. Furthermore, under French law, representatives of employees (the *comité d'entreprise*) can demand considerable information from management. See JEANTIN, *supra* note 77, at 156-57. Associations of shareholders also have considerable power to address management abuses.

180. See Marini Report, *supra* note 2, at 99-104 (recommending, among other things, to improve the *commissaires'* audit of an enterprise and to give them additional powers to address problems in financial accounts).

181. Senator Marini misses this point when he worries that the use of independent directors in France may create a conflict with the *commissaires*. See Marini Report, *supra* note 2, at 42. There can be no such conflict, since the *commissaires* are not legally responsible for the direction of an enterprise.

A. Decision-Making in Corporate Transformations

A corporate transformation may involve a combination of a corporation with another (a "merger") or a sale of all, or substantially all, of the corporation's assets to the other corporation. In either event, the resulting business may look different, either because it combines previously separated enterprises or because it significantly expands or decreases current operations. Under French law, the legally-mandated decision-making structure applicable to some major corporate transformations is straightforward and helps correct the shareholders' informational disadvantage. Information is likely to be critical in this setting, for shareholders must decide whether to approve a major transaction and whether to exit a corporation. In a classic merger (where both companies, rather than their subsidiaries, are involved in the transaction), the board of each French company must establish a "*projet*" that describes, among other things, the transaction, the reasons for it, and the exchange ratio.¹⁸² The substance of this *projet* must be published in an official legal publication.¹⁸³ A corporation must make additional information regarding the transaction available to its shareholders at its corporate headquarters. The corporation must also provide recent financial statements of both companies and a report by special *commissaires à la fusion*, appointed by a commercial court, who examine whether, among other things, "*le rapport d'échange est équitable*."¹⁸⁴ Shareholders of each company must approve the transaction by a two-thirds vote of those present at a special shareholders' meeting.¹⁸⁵ The sale of a major part of a corporation's assets may follow a similar procedure, although, in practice, only shareholders of a company purchasing another's assets for its own shares are guaranteed the right to review the outlay of corporate funds.¹⁸⁶

Under French law, shareholders do not have a voice in all corporate decisions regarding major transactions. For example, an acquisition may be structured in such a way as to avoid the legal requirement of shareholder approval, as when a corporation conducts an acquisition or merger through a subsidiary organized for that purpose (known as a "triangular" merger or asset sale). The board of a large corporation may use this struc-

182. See Loi N° 66-537, art. 374, C. soc., *supra* note 1, at 519 (amended by Loi N° 88-17 du 5 janvier 1988); Décret N° 67-236, arts. 254-55, C. soc., *supra* note 1, at 688-89. In the context of a merger, the COB supervises the disclosure to shareholders. See Marie-Claude Robert, *The Internationalization of the Markets and the Experience of the French COB with Mergers and Acquisitions*, in EUROPEAN TAKEOVERS: LAW AND PRACTICE 403, 404 (Klaus J. Hopt & Eddy Wymeersch eds., 1992) [hereinafter EUROPEAN TAKEOVERS].

183. See Loi N° 66-537, art. 374, C. soc., *supra* note 1, at 519.

184. Décret N° 67-236, art. 258, C. soc., *supra* note 1, at 689-90; Loi N° 66-537, art. 377, C. soc., *supra* note 1, at 520-21.

185. See Loi N° 66-537, art. 376, C. soc., *supra* note 1, at 519-20.

186. See *id.* art. 387, C. soc., *supra* note 1, at 527-30. For shareholders of the selling company, a sale of all assets might amount to a liquidation under French law, which would trigger a shareholder vote. See COZIAN & VIANDIER, *supra* note 98, at 573. The Viénot Report recommends that a board should conduct a major sale or divestiture of a company's assets only after receiving shareholder approval, although this is not now required under French law. See Viénot Report, *supra* note 2, at 6.

ture in order to conduct an acquisition or sale without having to present it to the shareholders for their approval. The structure of a corporate group thus permits the group to conduct significant mergers and acquisitions at the subsidiary level without the approval of the parent corporation's shareholders. Finally, if, as is often the case, a controlling group or family dominates a public company, a minority shareholder vote to approve a merger is not particularly significant, even when shareholders receive the vote, because the dominant shareholder controls the outcome.

B. The Shareholders' Right of Exit

In some countries, such as the United States, corporate law grants shareholders the right, in certain major transactions, to demand that the corporation repurchase their shares at "fair value" if they disagree with the transaction. This right, known as the appraisal or dissenters' remedy, owes its origin to a former feature of corporate law, which mandated a unanimous shareholder approval of any major transaction. This unanimity requirement became impractical as the number of shareholders increased, for it allowed one shareholder to stand in the way of an economically favorable or necessary transaction, or alternatively created an unwieldy and unexpected corporate dissolution. Historians of the corporate form suggest that, in exchange for the loss of their veto right, shareholders received the right to walk away from an enterprise with the fair value of their share.¹⁸⁷

The appraisal remedy has a corporate governance purpose. With the rise of majority rule, the lack of veto authority subjects minority shareholders to potential abuses by a control group or person. Even when no such controlling entity exists, minority shareholders may nevertheless find themselves at the mercy of management, especially where the shareholders are too dispersed to form a united opposition. A dissenting shareholder's right to force a corporation to cash them out may thus check majoritarian and management overreaching and is yet another legal method of addressing the positional weakness of capital market investors.¹⁸⁸ The effectiveness of the appraisal remedy for corporate governance purposes depends, however, upon its facility of use. For example, in the United States, the remedy is not available in every transaction and its costs make it prohibitive to small shareholders.¹⁸⁹

187. 2 PRINCIPLES, *supra* note 110, at 291-314 (presenting the origins of the U.S. appraisal remedy and summarizing scholarly work on it).

188. *See id.* at 292-93.

189. Under a typical U.S. state corporate law, a shareholder does not receive the appraisal right in every major transaction. Nearly every state corporate law grants a shareholder an appraisal right when his or her corporation is merging into another (but not necessarily when another corporation is merging into his or her own). In certain states, shareholders receive this right when their corporation is selling all, or substantially all, of its assets. *See id.* at 358-79 (summarizing in a chart, as of 1994, state corporate laws on appraisal). Delaware corporate law, for example, does not give a shareholder an appraisal right upon the sale of all or substantially all of a corporation's assets. Nor does the right attach when a corporation conducts a major transaction through a subsidiary. In some cases, as under Delaware corporate law, a shareholder of

This kind of appraisal remedy (that is, a judicial determination of fair value) does not generally exist under French corporate law. A shareholder of a French corporation involved in a merger cannot request that the company purchase his or her shares at fair value. The absence of this right can have serious consequences in French corporate governance, for controlling shareholders can decide to conduct a merger and determine the terms of the transaction.¹⁹⁰ In certain cases, however, CMF regulations create a rough equivalent of appraisal for shareholders in French publicly-owned companies. If a person or group acquires more than one-third of the shares of the surviving company in a nonmerger context (for example, by purchasing a control block from a controlling shareholder), such person or group is required to make a buyout offer for all of the outstanding shares.¹⁹¹

In a merger where minority shareholders are offered cash or other nonshare consideration in return for their shares (in other words, they are "frozen out" of the enterprise), they have no immediate right to approach a court to ask for a determination of the "fair value" of their shares. Yet, at this point in time, if a party had become a dominant shareholder, owning more than one-third of the total shares, through a prior share acquisition, the above CMF rule may have already come into play to ensure that minority shareholders have some exit strategy. In this acquisition situation, the CMF demands that the offer include a justification for the price offered for the shares and it can hold up the offer if it finds that price unacceptable.¹⁹² An independent French agency, if not immediately a court, thus examines the substance of an offer in a transaction that may eventually lead to a merger.¹⁹³

a publicly-traded corporation (or a corporation with a certain number of shareholders) will not have an appraisal right, even in a "classic" merger, if he or she ends up holding shares of a publicly traded corporation as a result of the transaction, whether of his or her own company or of another firm. See DEL. CODE ANN. tit. 8, § 262(b)(2) (1996).

Appraisal is a potentially cumbersome and expensive process. As a typical statutory procedure indicates, a shareholder must elect the remedy prior to the shareholder vote on the transaction. Then, he or she must file a petition requesting a court to determine the "fair value" of the shares as of the date before the transaction and this determination demands a trial with all its pre-trial proceedings and costs, particularly on valuation issues. For an example of the procedural complexity of appraisal, see DEL. CODE ANN., tit. 8, § 262(d)-(k). See also 2 PRINCIPLES, *supra* note 110, at 293 (providing the standard criticisms of the appraisal remedy). During the appraisal proceeding, unless the shareholder withdraws, he or she receives no dividends nor has any other rights (e.g., voting) as to the shares. This procedural difficulty, which requires the involvement of lawyers, guarantees that the only shareholders electing appraisal are those with a significant stake in the enterprise, not small capital market investors.

190. See Eddy Wymeersch, *Problems of the Regulation of Takeover Bids in Western Europe: A Comparative Survey*, in EUROPEAN TAKEOVERS, *supra* note 182, at 95, 104.

191. See CMF Règlement Général, art. 5-4-1, C. soc., *supra* note 1, at 931-32. For further discussion, see *infra* Part V.B.

192. See *id.* arts. 5-2-5, 5-2-7, C. soc., *supra* note 1, at 928.

193. French shareholders can challenge CMF determinations in the French *Cour d'Appel*, thus involving French courts in valuation disputes. See Décret N° 88-603 du 7 mai 1988, [1988] JO 8 mai 6606, art. 3, C. soc. 836 (Paul Le Cannu ed., 13th ed. Petits Code Dalloz 1996) (Fr.).

There are several additional exit possibilities for minority shareholders when a supermajority shareholder (one who has 95% of the votes) exists, which may be the case following a tender offer or other significant transaction (such as where a few shareholders declined, or neglected to, tender their shares in the original offer). Either the minority can request the CMF to order the majority holder to make them an offer to purchase their shares, or the majority on its own initiative can propose the offer.¹⁹⁴ In either case, the CMF reviews the "fairness" of the offering price. Pursuant to a recent change in French law, and similar to a situation common in the United States,¹⁹⁵ the 95% supermajority shareholder can now compel the minority to take the offer and exit the corporation's capital (effect a "squeeze-out").¹⁹⁶ In this case, the law provides that the CMF evaluate the minority's shares using valuation methods accepted in the financial community.

Shareholders in a French public company also receive an official exit in certain cases involving a sale of all, or substantially all, of a company's assets (and in other major corporate events).¹⁹⁷ Under CMF regulations, if a controlling shareholder decides upon the sale, it must alert the CMF and begin a procedure to repurchase the minority's shares. Again, this procedure involves CMF review of the offering price.¹⁹⁸ Under French law, a shareholder is presumed to control a corporation if he or she holds 40% of the votes and no other shareholder holds more, or if facts suggests that he or she controls shareholder decisions albeit with a smaller holding.¹⁹⁹ Finally, French shareholders of public companies can always "exit" by selling their shares into the market, although sometimes at a discount.

Are capital market shareholders in France really worse off than their counterparts in countries with laws that provide for a judicial evaluation of a "fair" exit price when a major transaction is proposed? French law does not offer shareholders an exit in every situation where a typical state's corporate law would provide such relief. (For example, mergers fall in this category.) Where French law offers shareholders an exit, an independent market agency, not a court, initially reviews the terms of the offer, so that minority shareholders do not have to bear the expense of arguing with the company over the proper valuation of their shares.²⁰⁰ However, dissatisfied minority shareholders can proceed to the French *Cour d'Appel* to challenge a CMF determination, generally its approval of a company's valuation methods.²⁰¹ If the CMF and the COB take their substantive review of offer-

194. See CMF Règlement Général, arts. 5-5-1 to 5-5-6, C. soc., *supra* note 1, at 934-36.

195. See DEL. CODE ANN., tit. 8, § 253(a) (1996) (allowing a 90% shareholder to merge a corporation's subsidiary into it without any vote of subsidiary's shareholders).

196. See COZIAN & VIANDIER, *supra* note 98, at 409; see CMF Règlement Général, arts. 5-6-1, 5-6-2, C. soc., *supra* note 1, at 936-37.

197. For a list of these events, see Marini Report, *supra* note 2, at 71-72.

198. See CMF Règlement Général, art 5-5-5, C. soc., *supra* note 1, at 935.

199. See Loi N° 66-537, art. 355-1, C. soc., *supra* note 1, at 486-88.

200. See Marie-Noëlle Dompé, *Offres publiques: Réglementation et contestation*, PETITES AFFICHES, June 15, 1994, at 27, 28-30.

201. See *id.*

ing prices seriously in these situations, as a practical matter where French law provides these exit alternatives, they may be more useful to minority shareholders than a solely court-based appraisal remedy with all its litigation expenses.²⁰² This independent review of price is critical for capital market shareholders in France because market capitalization is smaller and market liquidity is less than that which exists in the United States. Therefore, the option of selling shares into the market may not always be the best way of realizing their "fair" value.

C. Additional Protection for Shareholders in Freeze-Outs

Because a freeze-out places capital market shareholders in a vulnerable position (in a situation where they are being "cashed out" of a company's capital by a controlling shareholder electing to merge the corporation with a special acquisition vehicle), they may need special legal protection. Generally in a weaker position than management, minority shareholders occupy an even more precarious position when facing a management and board which represent a major shareholder who may desire to eliminate them from a corporation's capital in pursuit of his or her own interests. This is not an uncommon situation in France, given the extent of family and controlling group capitalism. In this situation, managers and the board of directors may be inclined to offer a price to the minority shareholders that favors the dominant shareholder. At an informational disadvantage, the minority shareholders cannot be sure that they are receiving a "fair" price. Further, their minority position and the lack of public information about the controlling shareholder's plans for the corporation may cause the market itself to impose a "discount" on their shares.²⁰³ Given the controlling shareholder's dominance, the minority shareholders have few options but to accept the price offered in the merger.²⁰⁴ To protect shareholders in these circumstances, U.S. corporate law enhances directors' duties of good faith, care and loyalty. In addition, U.S. federal securities laws impose specific disclosure requirements upon the merging corporations and controlling shareholders.²⁰⁵

202. The evidence suggests that these market authorities take their review seriously. See Robert, *supra* note 182, at 414-16 (also noting that the COB reviews disclosure relating to such transactions).

203. See CLARK, *supra* note 75, at 508-09 (describing how majority shareholder may depress market price of stock to take advantage of minority shareholders).

204. There are often valid reasons to eliminate minority shareholders from a business, e.g., taking a company private and thereby saving the cost and trouble of a public company.

205. See, e.g., *Weinberger v. UOP, Inc.*, 457 A.2d 701 (Del. 1983) (Delaware cause of action for unfair treatment of shareholders in a freeze-out); 17 C.F.R. § 240.13E-3(d) (1995) (requiring any company or affiliate, including a controlling shareholder thereof, that, among other things, "goes private" (effects a "freeze-out" of minority shareholders resulting in the company becoming privately-held) to file with the SEC and to disclose to minority shareholders information about the transaction and its procedure as required by Schedule 13E-3). Small shareholders can easily find attorneys willing to take cases based on a violation of either of these laws for a contingency fee since there is an economic incentive to such counsel, i.e., numerous minority shareholders can be joined in a "class action," which means an increased potential recovery for the lawyer, who gener-

Although French corporate law does not afford comparable protections against freeze-out problems as does its American counterpart, oversight by market authorities may, nevertheless, be adequate to deal with abuses by controlling shareholders in certain situations. For example, French law mandates a buyout offer to the minority shareholders under the CMF's supervision, ultimately with court review. If the CMF provides adequate supervision of these offers and the offering price, it is questionable whether any additional check on the majority shareholder and its "controlled" directors is needed in such cases. Moreover, French directors are held by law to high standards of conduct so as to avoid conflicts of interest, and their misbehavior subjects them to civil and criminal penalties. In a freeze-out situation, a shareholder in a French company appears currently to have the legal basis to sue a director for failing to analyze adequately the transaction from the perspective of *all* the shareholders, when the director approved a merger involving a corporation's controlling party on the other side of the transaction and followed without question the controlling shareholder's demands.²⁰⁶

Whether more jurisprudence on directors' duties and more disclosure will develop in France in this kind of transaction depends upon future restructuring of French companies and any perception that current French law inadequately protects minorities. U.S. legal developments on minority treatment in these contexts can be traced to a period of restructuring in U.S. public companies that often resulted in the "going private" of formerly public companies and the elimination of minority shareholders. Because present French market policy is directed towards encouraging more public shareholders, not eliminating those who exist, French finance circumstances may not lead to similar legal developments. Yet, because of the likely continued existence of dominant shareholders in French public companies and their control over major transactions, it may become important to enhance the duties of directors towards *all* shareholders in such transactions to attract public investors into French capital markets.

V. French Legal Corporate Governance and the Market for Corporate Control

The market for corporate control, or the takeover market, characterizes market capitalism. Some Europeans view this kind of restructuring as hostile and wasteful.²⁰⁷ If managers do not produce immediate results, or even sometimes if they do and a financier wants to take advantage of their success, a potential buyer is always in the wings. Investors, eager for quick profits, are ready either to sell to this buyer (or some other bidder drawn into the contest by the lure of easy gains) or to professional traders ("arbi-

ally takes 1/3 of the damages awarded. For small shareholders, the suits thus offer a more practical form of redress than appraisal.

206. The difficulty of bringing and financing such a suit may undercut its usefulness. See *infra* Part VI.D.

207. See ALBERT, *supra* note 62, at 75-98.

trageurs”), who earn their living by purchasing shares in these circumstances, that is, by putting companies into “play.” Managers have no choice but to focus upon short-term results and defensive measures, at the expense of long-term projects and research and development. The restructuring generates enormous transaction costs and ultimately benefits only the financiers, investment bankers, and lawyers. It invariably destroys companies, which must be broken up and sold to pay down the debt that buyers incur to finance their purchases and injures creditors and employees to the benefit of shareholders and these parties, who principally capture the wealth gains.²⁰⁸

While some scholars agree with this portrayal of the market for corporate control, others, even if they do not absolutely condemn the hostile tender offer which characterizes this market, find it a blunt instrument for restructuring.²⁰⁹ Many economists, finance theorists, and business law professors, however, believe that the market for corporate control addresses the basic agency problem of disciplining management in a market capital situation and that its nefarious effects have been greatly exaggerated.²¹⁰ They view the threat of a tender offer as a way to keep in check powerful managers, who are always tempted to take advantage of shareholders by engaging in negative net present value investments, and as a way to force the managers to make the restructuring called for by economic circumstances.²¹¹ In the most vilified form of a tender offer — a leveraged buyout or “LBO” — a company is purchased by funds borrowed on the security of the company’s assets, often followed by a bust-up sale of the company. This makes perfect sense from a finance perspective, as shareholders can cash out and the excessive leverage keeps management within tight fiscal constraints. Many scholars, therefore, regret the declining use of the hostile offer in the United States, which they attribute to laws passed at the demands of managers and other interest groups, such as labor unions, who are unwilling to accept the needed restructuring which threatens their positions.²¹²

Given that the takeover has been, and continues to be, an important aspect of business restructuring in any market capitalism situation,²¹³ it is thus necessary to review how French law regulates this phenomenon. There have been many tender offers in France, but few have been hostile.²¹⁴ According to Professor Wymeersch, French tender offer regulation,

208. See generally MARGARET M. BLAIR, *OWNERSHIP AND CONTROL: RETHINKING CORPORATE GOVERNANCE FOR THE TWENTY-FIRST CENTURY* 61-68 (1995).

209. For a useful summary of positions both criticizing and supporting takeovers, see VICTOR BRUDNEY & WILLIAM W. BRATTON, *CASES AND MATERIALS ON CORPORATE FINANCE* 939-56 (4th ed. 1993).

210. See, e.g., Michael Jensen, *The Takeover Controversy: Analysis and Evidence*, reprinted in *THE NEW CORPORATE FINANCE: WHERE THEORY MEETS PRACTICE* 465-91 (Donald H. Chew, Jr., ed., 1993).

211. See, e.g., Jensen, *supra* note 5, at 850-52.

212. See ROE, *supra* note 27, at 226-30.

213. See Jensen, *supra* note 5, at 831-35. See also Pound, *supra* note 5, at 1011-17.

214. See OECD FRANCE, *supra* note 46, at 118 (observing that, although merger and acquisition activity in France is far below that of the U.K., it leads that in other European

like that in most other Continental countries, has been used to eliminate public shareholders after a controlling block of shares has been transferred between parties, such as groups or families. This form of regulation generally does not effect control changes.²¹⁵ Although French corporate law regulates tender offers in detail, the law and related court decisions are relatively recent products of the 1980s and 1990s.²¹⁶ The following summarizes some striking features of French regulation of tender offers from a market capital perspective and suggests that French regulation limits, but does not eliminate, the French market for corporate control.

A. French Legal Impediments to the Market for Corporate Control

Numerous provisions in French law give management (with the board's acquiescence) time to prepare its defenses and power to make a company an unfavorable candidate for a takeover. Management of French companies have an "early warning" system. French corporate law requires shareholders, acting alone or "*agissant de concert*," who own shares in excess of certain defined thresholds (i.e., 5%, 10%, 20%, 33 $\frac{1}{3}$ %, 50%, 66 $\frac{2}{3}$ %) of the company's capital or voting rights to declare their existence within five business days to the CMF and within fifteen calendar days to the company. If they fail to do so, they lose voting rights on those shares in excess of the thresholds for two years, or such longer period as imposed by the CMF.²¹⁷ Companies can also lower the thresholds to .5% and increments thereof. Since companies know the identity of shareholders having shares in registered form (*titre nominatif* or on the company's books), this law is useful where shareholders hold them in bearer form (*au porteur*) and where parties are acting "*de concert*."²¹⁸

countries). Times may be changing, however. See John Rossant, *Why Merger Mania Is Rocking the Continent*, Bus. Wk., Oct. 27, 1997, at 64 (describing hostile offers in France).

215. See Wymeersch, *supra* note 190, at 101-03.

216. A complete explanation of this law and of its corporate governance effects is beyond the scope of this Article. An excellent discussion of French tender offer regulation and its background (to which the following discussion owes a great deal) is found in SCHOEN, *supra* note 82, at 79-145. See also COZIAN & VIANDIER, *supra* note 98, at 600-15; André Tunc, *Les Prises de contrôle par l'intermédiaire du marché*, in CORPORATE TAKEOVERS THROUGH THE PUBLIC MARKETS 157 (Phaedon John Koziris ed., 1996).

217. See Loi N° 66-537, arts. 356, 356-1, 356-4, C. soc., *supra* note 1, at 488-90, 494-95.

218. Since all French shares are "dematerialized," this shareholding distinction has no physical meaning. Shares of French companies are "held" in the official French depositary, SICOVAM: registered shares are in a company account (or in the account of a bank acting as the company's agent) with this depositary, and bearer shares are held through financial intermediaries that also have SICOVAM accounts. French law permits a company's *statuts* to provide that the company can ask SICOVAM to require the intermediaries to identify the beneficial shareholders (the company's bearer shares are then known as *titres porteurs identifiâbles*). See Loi N° 66-537, art. 263-1, C. soc., *supra* note 1, at 423-24 (added by Loi N° 87-416 du 17 juin 1987). This cumbersome procedure does not always produce accurate information. In fact, with the growth of international, particularly Anglo-Saxon, investors in the capital of their companies, French managers are concerned that the law does not adequately permit them to identify non-resident shareholders. See generally Valuet, *supra* note 107, at 708 (noting a problem

These declarations of share ownership alert the management of a target company to the identity of new significant shareholders. COB regulation supplements this disclosure by requiring an acquiror of more than 20% of a company's voting rights to declare whether, in the next twelve months, it intends to continue to acquire shares, take control of the company or request a seat on the board.²¹⁹ Supporting both this regulation and the early warning law is the rule regarding acting *de concert*, which is broadly defined to include agreements to acquire or sell voting rights.²²⁰ This term, with its detailed jurisprudence,²²¹ covers an agreement by several persons to act jointly to take control of a company. Any agreement among shareholders dealing with a preferential purchase and sale of shares (for example, a right of first refusal) must also be disclosed to the CMF, which then makes it public.²²²

Under French law, management can also take defensive measures to ward off hostile bidders and avoid market discipline. A peculiar feature of French corporate law is that its charter or a special shareholder meeting may grant double voting rights to shares held in registered form for at least two years.²²³ From one corporate governance perspective prevalent in France, this provision rewards patient capital and thereby promotes long-term relationships between shareholders and management. From a market capital perspective, however, the device allows management to create a friendly shareholder group whose influence in the company grows while that of capital market investors declines, for the latter are likely to hold securities in bearer form, thus making them ineligible for double voting rights. In addition, under French corporate law, a company's charter may permit it to limit the total number of voting rights of any shareholder to a set percentage (the rule must apply to all shareholders), seriously obstructing a change of control.²²⁴ The COB disapproves of these limitations when they are not coupled with "outs" (the elimination of these limi-

and proposing a solution whereby financial intermediaries identify their non-French shareholders). Capital market investors' need for the "early warning" system thus remains.

219. See COB Règlement N° 88-02, reprinted in Loi N° 66-537, art. 356-1, notes, C. soc., *supra* note 1, at 489.

220. Loi N° 66-537, art. 356-1-3, C. soc., *supra* note 1, at 491-93 (providing "[s]ont considérées comme agissant de concert les personnes qui ont conclu un accord en vue d'acquérir ou de céder des droits de vote ou en vue d'exercer des droits de vote pour mettre en oeuvre une politique commune vis-à-vis de la société.").

221. COZIAN & VIANDIER, *supra* note 98, at 416-17.

222. See Loi N° 66-537, art. 356-1-4, C. soc., *supra* note 1, at 493 (providing that any agreement, made between shareholders of a company whose shares are listed on a regulated stock market, that includes special conditions of sale or acquisition of shares must be communicated to the CMF, which will publicize it).

223. See *id.* art. 175, C. soc., *supra* note 1, at 334-35. These double voting rights can be limited to French or EU shareholders.

224. See *id.* art. 177, C. soc., *supra* note 1, at 335. Apart from double voting rights, French corporate law does not permit the issuance of shares with supervoting rights (see art. 174 for the "one share, one vote" principle), which could have an anti-takeover effect. A French company can, however, issue nonvoting shares with dividend priority. See *id.* art. 177-1, C. soc., *supra* note 1, at 335-36.

tations upon acquisition of majority voting rights by a party),²²⁵ and Senator Marini recommends changing French law to this effect.²²⁶

The characteristic closeness of the French business world reinforces the effect of these limitations on voting rights. Although blatant abuses (such as secret agreements among companies and shareholders and secret holdings of shares) are now illegal,²²⁷ managers can create a friendly shareholder group (a *noyau dur*) of other companies, often bound together in elaborate cross-shareholdings with one another. The group's shareholders agree to hold their shares for a specified period of time, to limit the number of shares of the target any of them can acquire, and to give the others a right of first refusal if they dispose of their shares. They may also hold warrants exercisable for shares of the target in certain circumstances. While the corporate governance implications of this arrangement are subject to debate, it is clearly a defensive device for management in privatized companies that no longer have the State as a major shareholder.²²⁸

As the history of French takeovers has shown, these defenses are not impregnable. However, French tender offers generally occur as consensual, rather than hostile, transactions. French shareholders can remove board members without cause at a shareholders' meeting.²²⁹ In addition, French law strictly limits a company's share repurchase: it can only serve as a reduction of capital.²³⁰ The law has also removed much of the benefit

225. See SCHOEN, *supra* note 82, at 111.

226. See Marini Report, *supra* note 2, at 93-94. Marini recommends that the limitations become void once a shareholder has acquired over 50% of the voting rights so that they do not seriously impede changes in control. See *id.* This recommendation, however, does not address the situation where a significant shareholder (or shareholders) does not want control of a company, but wishes to express its displeasure with management through its vote.

227. See *supra* Part II.

228. See Fanto, *Transformation of French Corporate Governance*, *supra* note 2, at 59-67. See generally MORIN & DUPUY, *supra* note 67; Tunc, *supra* note 216, at 162. On the legality of these agreements, see generally JEAN-JACQUES DAIGRE & MONIQUE SENTILLES-DUPONT, *PACTES D'ACTIONNAIRES* (1995). While recognizing the pro-management effect of the *noyaux*, Senator Marini does not believe that legislation can address this phenomenon, because he attributes it to the small size of the French capital markets which encourages companies to look to other companies for capital. See Marini Report, *supra* note 2, at 44. He does recommend, however, that the French State not establish new cross-shareholdings in future privatizations, see *id.* at 50, and that existing ones be adequately disclosed to investors, see *id.* at 69. In some privatizations, moreover, the French government retains an absolute veto right (*l'action spécifique*) on major transactions, such as a change of control, which removes the company completely from the corporate control market. See generally Pezard, *supra* note 56.

229. See Loi N° 66-537, art. 160, C. soc., *supra* note 1, at 319-20.

230. See *id.* art. 217, C. soc., *supra* note 1, at 369-70. Unlike the case for U.S. companies, French companies cannot repurchase their shares as an alternative to paying dividends to return cash to shareholders or to change their capital structure when debt financing is cheaper than equity financing. See RICHARD A. BREALEY & STEWART C. MYERS, *PRINCIPLES OF CORPORATE FINANCE* 419-20 (5th ed. 1996) (discussing finance reasons for share repurchase). If the shareholders agree, a French company can repurchase its shares to "stabilize" its share price, see Loi N° 66-537, art. 217-2, C. soc., *supra* note 1, at 370-71, but it cannot hold more than 10% of its own capital, and such "treasury" shares have no voting or dividend rights, see *id.* art. 217-3, C. soc., *supra* note 1, at 371. Senator Marini and the CNPF, an organization of French company management, both

of having subsidiaries hold a company's shares (*auto-contrôle*) for defensive purposes,²³¹ although shares can still be sold to employees, who are usually favorable to management and hostile to outsiders threatening a restructuring. Generally, a company cannot grant defensive "lock-up" options on its assets, either directly or indirectly.²³² While friendly parties may acquire warrants and other special preferred shares, it is questionable whether French corporate law would permit the kinds of poison pills which allow a bargain purchase of a target or an acquiror's shares.²³³

B. French Procedural Regulation of a Tender Offer

French tender offer procedures demonstrate both the restrictions and flexibility of French law. If a person (or persons acting in concert), directly or indirectly, acquires more than 30% of the votes of a listed company, with some exceptions, he or she must make a public offer for the remaining shares.²³⁴ The rule (designed to comply with an earlier version of the European Union's proposed Thirteenth Directive²³⁵) protects minority shareholders when a person assumes control gradually through market purchases or all at once by the purchase of a control block.²³⁶ From the perspective of protecting capital market shareholders, the provision for an exit upon a change in control makes particular sense in French capitalism where these investors co-exist with, and are usually at the mercy of, controlling shareholders or organized groups of shareholders. In a similar vein, the CMF may authorize a person (or persons), who has obtained more than 50% of the voting rights or shares, to purchase the remaining shares by holding itself ready to acquire any shares tendered on the market during a set period of time.²³⁷ Both of these procedures, however, discourage changes in control and the monitoring of management promoted by such changes, as they make them more expensive for bidders than, for

recommend expanding the ability of French companies to repurchase shares. See Marini Report, *supra* note 2, at 62; CONSEIL NATIONAL DU PATRONAT FRANÇAIS, PROPOSITIONS DE MODIFICATIONS DU CADRE LÉGISLATIF ET RÉGLEMENTAIRE DU RACHAT PAR UNE SOCIÉTÉ DE SES PROPRES ACTIONS (fiche N° 1, Sept. 25, 1996). Yet neither Senator Marini nor the CNPF address the anti-takeover implications of their proposals, such as defensive use of the repurchase by company management to reduce the number of outstanding shares.

231. See SCHOEN, *supra* note 82, at 118.

232. See *id.* at 122.

233. See *id.* at 131-33. If shareholders have already delegated authority to a French board to issue new shares, the board may undertake such issuances (to a friendly party) as a takeover defense. See Tunc, *supra* note 216, at 181.

234. See CMF Règlement Général, art 5-4-1, C. soc., *supra* note 1, at 931-32. Under article 5-4-3, the acquiror of a company that holds more than one-third of a listed company's capital or votes must make a bid for the listed company, if such holding represents "une part essentielle" of the acquired company's assets. This mandatory bid procedure also applies to a greater than 1/3 shareholder that increases his or her holding by an additional 2% in less than a year. See *id.* art. 5-4-3.

235. Proposal for a 13th European Parliament and Council Directive on Company Law Concerning Takeover Bids, COM(95) 655 final (Feb. 7, 1996).

236. Before 1992, a bidder passing this threshold had to make an offer for only two-thirds of the company's shares. See SCHOEN, *supra* note 82, at 81-83.

237. See *id.* at 99-103.

example, a tender offer simply for majority control of a company.²³⁸

Under another French tender offer procedure, a party may launch a "voluntary" tender offer for *all* the shares of a company.²³⁹ Subject to the CMF's approval, the bidder can condition the offer upon receiving at least a set percentage of shares (enough to give it the majority of the votes). Although the French market and market authorities view a tender offer for less than all of the shares of a company as coercive of capital market shareholders, as a practical matter, the offeror may not care that it must bid for all the shares even if it does not expect to acquire all of them.²⁴⁰

French regulation also affects the tender offer price and may thereby benefit capital market shareholders because, when coupled with the rule regarding an all-shares offer, it deters low-priced, coercive bids. It is difficult, however, to see the need for an "official" substantive review of price, so long as the all-shares requirement exists, for a successful tender offer usually involves giving shareholders a premium to market price. Where a public tender offer follows a transfer of a controlling block — a potentially coercive "freeze-out" situation — the review may make sense because it ensures that some independent body evaluates whether capital market investors obtain the "fair price" for their shares.²⁴¹ The CMF reviews the price and obvious evaluative measures, such as premium to market price, asset price, and stock price to earnings ratio.²⁴² Whether this evaluation in fact hinders tender offers in France depends upon how restrictively the CMF applies the regulation.

Aside from price review, French tender offer regulation ensures that the capital market investor receives information about the bid and the bidder and has time to consider the offer. Through a bank or banks acting on its behalf, a bidder presents a *dossier* to the CMF that describes, among other things, its purpose in making the offer, its existing shareholding in

238. Cf. John C. Coffee, Jr., *Liquidity versus Control: The Institutional Investor as Corporate Monitor*, 91 COLUM. L. REV. 1277, 1316 (1991). Professor Wymeersch argues that such "mandatory bid" procedures are not as friendly to capital market shareholders as they seem. See Eddy Wymeersch, *The Mandatory Bid: A Critical View*, in EUROPEAN TAKEOVERS, *supra* note 182, at 351. According to Wymeersch, since they potentially increase the cost of a change of control for the bidder (who must acquire all the shares if he or she triggers the procedure), they actually encourage bidders to negotiate control transactions first with the existing controlling shareholder (who is generally present in French public companies). The bidder and such shareholder may structure the transaction in a way that eliminates the need for a mandatory bid or that benefits them at the expense of minority shareholders in the target. In other words, the mandatory bid requirement discourages hostile changes of control which occur through the market. See *id.* at 360-64.

239. See CMF Règlement Général, art 5-2-2, C. soc., *supra* note 1, at 923.

240. French regulations also require that a voluntary tender offer be for all "financial instruments giving access to capital or to voting rights" and thus includes preferred and convertible shares. See *id.*

241. In the "garantie de cours" (i.e., where a majority shareholder stands ready to purchase all shares tendered on the market), the bidder must generally offer the same price to public shareholders as it paid in purchasing a control block. See SCHOEN, *supra* note 82, at 101.

242. See CMF Règlement Général, art 5-2-7, C. soc., *supra* note 1, at 924. See also SCHOEN, *supra* note 82, at 83-84.

the target, any share minimum that must be tendered, and the price offered with a justification thereof.²⁴³ The CMF reviews the offer for five business days and can require modifications to it or refuse it altogether. At the same time that the CMF is conducting its review, a bank acting on behalf of the bidder must file a draft prospectus (*note d'information*) with the COB that includes the following information: (1) the bidder's identity; (2) its intentions as to the company's future operation and listing for the next twelve months; (3) the price offered; (4) financing for the offer; (5) any agreements between the bidder and others regarding the acquisition; and (6) financial information.²⁴⁴ The COB may demand supplemental information, disapprove of the prospectus altogether (which it rarely does), or even give its own views on the offer, which must be included in the prospectus.²⁴⁵ Once the prospectus is approved, the bidder sends it to the target company and publishes it in a financial paper (unless all the company's shareholders hold shares in registered form, in which case the prospectus is simply sent to all of them).²⁴⁶ Upon receiving the bidder's prospectus, the target must file its own prospectus with the COB describing, among other things, the shareholding structure of the company both at the time of filing and a year earlier, any agreements it has with respect to the offer, the board's views on the offer (as well as any minority views of the board), and financial statements.²⁴⁷ This prospectus must be made public in the same manner as the bidder's. The COB also requires that certain events occurring after the publication of the prospectus be publicized.²⁴⁸

Shareholders have twenty business days in which to decide whether to accept an offer and can withdraw their tenders at any time before the end of the offering period. If a competing bidder wants to make a tender offer, it must do so at least five business days before the close of the first offer.²⁴⁹ Upon this new bid, any tenders to the original offer become void, and shareholders have until the end of the second bid to decide whether to accept either offer, or reject both. In fact, the original bidder must respond to a competing offer by announcing its intention either to maintain, withdraw or increase its bid.²⁵⁰ More importantly, a competing bid must be at least 2% higher than the initial bid; and any response to it must involve an

243. See CMF Règlement Général, art. 5-2-5, C. soc., *supra* note 1, at 923-24.

244. See COB Règlement Général, art. 5-2-1, C. soc., *supra* note 1, at 922-23; COB Règlement N° 89-03, arts. 7-8, C. soc., *supra* note 1, at 948-49 (Fr.).

245. COB decisions are subject to the judicial review of the Paris *Cour d'Appel*. See Décret N° 90-263 du 23 mars 1990, [1990] JO 25 mars 3655, art. 6, C. soc., *supra* note 1, at 953-56 (Fr.).

246. See *id.* arts. 10, 12, C. soc., *supra* note 1, at 955-56.

247. See *id.* art. 11, C. soc., *supra* note 1, at 956. If the transaction is a friendly one, the bidder and the target can file a joint prospectus.

248. COB Règlement N° 89-03, art. 4, 12, C. soc., *supra* note 1, at 948, 950 (article 4 requires notification of agreements between a target's shareholders and third parties, such as a "white knight;" article 12 allows the COB to request the CMF to hold open the offer period so that information reaches shareholders).

249. See CMF Règlement Général, art. 5-2-14, C. soc., *supra* note 1, at 925.

250. See *id.* art. 5-2-15, C. soc., *supra* note 1, at 926.

additional 2% increase over its bid (and so on).²⁵¹

French market authorities generally take the view that bidders must have equal chances to compete and disfavor extreme management efforts either to favor one bidder at the expense of its shareholders or to block a tender offer completely.²⁵² French law strictly regulates a target's or bidder's purchase of securities outside the bid and requires disclosure of any such purchases, special defensive measures, or agreements.²⁵³ It appears that French law would not allow lock-up options on key assets or special share option arrangements.²⁵⁴ Management of a French company can resist a tender offer and, as noted above, has many ways of doing so. Once a bidder appears, however, management does not have the freedom to take a "scorched earth" approach.

C. Summary

The best sign that French regulation is not a significant impediment to tender offers is that they occur with some frequency in France, although again they do not necessarily have the same change-in-control effect as is typical of U.S. tender offers.²⁵⁵ In fact, if French companies attract more capital market shareholders and if the networks of company cross-shareholdings diminish in importance, then there could be a rise in this form of restructuring and its accompanying disciplinary effect on management. In such an event, current French law adequately protects shareholders, and, if abuses develop, the CMF and the COB have the power to increase their review of these transactions.

If, however, hostile tender offers increase in France, then management may increasingly choose to oppose them. Even without such an occurrence, management in companies without a dominant shareholder may take such action if its other defenses, such as the *noyaux durs* and continued State ownership, diminish. Recently, for example, the Conseil National du Patronat Français has proposed changes to French corporate law specifically designed to enhance management's ability to resist unwanted tender offers. It requested that the CMF prolong a tender offer up to 40 days to give managers the time to call an extraordinary shareholders' meeting, where shareholders could approve management strategy contrary to the offer (for example, an asset sale or a merger with a "white knight"). It also asked the CMF to lower the French company law declaration of share ownership and future intentions from the present 20% threshold to 10%.²⁵⁶ It will be interesting to see whether, with such legal efforts

251. See *id.* art. 5-2-24, C. soc., *supra* note 1, at 928. However, a new bidder need not offer more than the original offer price if it meets that price while suppressing any minimum share condition to acceptance.

252. See SCHOEN, *supra* note 82, at 131.

253. See *id.* at 89-90.

254. See *id.* at 128, 131-33.

255. See *id.* at 3-16 (describing the recent history of French securities markets, which in effect centers around tender offers).

256. See, e.g., CONSEIL NATIONAL DU PATRONAT FRANÇAIS, DÉROULEMENT DES OFFRES PUBLIQUES (le 10 octobre 1996; fiche N° 2, Sept. 25, 1996; fiche N° 3, Sept. 25, 1996)

to resist these transactions, there will be increased development in somewhat neglected areas of French law, such as a directors' duties in a tender offer, which could protect shareholders against this opportunistic management resistance.

VI. Corporate Governance and Shareholder Suits

Although imposing duties upon company directors has by itself a corporate governance impact, punishing those who fail to fulfill their duties helps ensure that directors take them seriously. Similarly, mandatory disclosure affects corporate governance by correcting the informational disadvantage of dispersed investors when there is an enforcement mechanism for the accuracy of such disclosure. Shareholder lawsuits against the board and managers enforce board duties and company disclosure. In the eyes of many Europeans, this monitoring characterizes market capitalism: litigation against companies and their agents has become so prevalent in the Anglo-Saxon world that board members and managers cannot take any business action or make any statement about company prospects without running the risk of incurring numerous suits that are costly and time-consuming to defend and that make company management overly cautious in the future. Nonetheless, shareholder suits against management are possible under French law.

A. The French "Derivative" Lawsuit

Directors owe duties directly to the corporation, which is a separate legal personality, and thus owe these duties indirectly to its shareholders. Any violation of these duties harms the corporation and, indirectly, the shareholders. In enforcing director obligations, therefore, shareholders are really acting on the corporation's behalf against its agents. Their lawsuit is derivative: it derives from the corporation's right to sue.²⁵⁷

From this basic concept of a derivative shareholder right of action arises the potential procedural complexity of the lawsuit, as well as difficult substantive issues which have corporate governance implications.²⁵⁸ Although the lawsuit "belongs" to the corporation, it often makes sense for

(discussing these proposals pertaining to law discussed *supra* at text accompanying note 217). See also Valuet, *supra* note 107, at 708 (discussing proposal to allow French companies to identify non-French shareholders as partially justified by takeover concerns). Politically-motivated resistance to tender offers in France also arises through the promulgation of laws, such as the privatization law allowing for the "golden share," which make it difficult for non-EU members to acquire French companies in politically "sensitive" businesses. Since many potential bidders for French companies may come from outside France, management may play upon nationalist feelings to push for the enactment of other laws impeding or preventing tender offers by foreigners.

257. When directors harm shareholders "directly" (e.g., by abusing minority shareholders), shareholders have a direct, not a derivative, lawsuit. The distinction is not always easy to draw. See 2 PRINCIPLES, *supra* note 110, at 18-20 (discussing distinction with examples of each). The following discussion focuses on the derivative suit, but direct lawsuits clearly have a corporate governance impact as well. See *infra* Part VI.B.

258. For a general discussion of these issues, see KLEIN & COFFEE, *supra* note 112, at 195-201; 2 PRINCIPLES, *supra* note 110, at 4-9.

shareholders to bring it. Since the corporation acts through its directors and managers, they are unlikely to want to sue themselves or one of their number. Some outside party is needed, and no one is better suited to pursue the directors than the residual owners of the corporation. However, because the suit is on behalf of the corporation, the corporation through its agents should have the right to decide the questions which arise in all litigation: whether the costs of a lawsuit justify its benefits; whether, if a suit is commenced, it should be pursued, and how far; and whether other corrective action is more appropriate. As with other "problem" situations, corporate solutions that are less costly than litigation could address the conflict of interest in the board's decision concerning a derivative lawsuit. Since any recovery from a lawsuit accrues to the corporation and since any individual shareholder generally receives (again indirectly) only a small part of such recovery, he or she has little economic incentive to bring the suit.²⁵⁹ Consequently, outsiders to the corporation, such as lawyers specializing in such actions, may be the driving force behind many of these suits.

The French "derivative" lawsuit exists without much procedural complexity and without any debate concerning its existence. French directors and officers owe their duties to the corporation as such, and, since any violation directly harms the corporation, its representatives (the directors) should bring the lawsuit. In fact, under French law, the lawsuit belongs to the directors.²⁶⁰ Yet French law allows a shareholder or group of shareholders to bring a suit in the company's name (*l'action sociale ut singuli*).²⁶¹ Only current shareholders can bring the lawsuit, but it will not be dismissed if the requisite group of shareholders loses the statutory minimum before the end of the litigation.²⁶² Some of the restrictions on this collective shareholder lawsuit, however, diminish its effectiveness for capital market shareholders. In general, for shareholders to act, they must represent at least 5% of the company's share capital, a percentage that is gradually reduced as the company's capital increases over FF 5 million.²⁶³ Moreover, it is not clear that a successful prosecution or settlement allows the prosecuting shareholder or shareholders to recover legal expenses.

French law does not give directors much control over a derivative suit, nor does it entitle their views to any special status before the court hearing the lawsuit. Shareholders must join the corporation as a necessary prosecuting party in the suit, but directors cannot refuse a shareholder request

259. A large shareholder would have more incentive to sue because he or she would capture more of the gains. It can also be argued that, if the derivative suit improves corporate governance in general because it puts directors in other firms on notice that the threat of a lawsuit is real, gains to shareholders cannot be limited to the recovery of damages for a specific violation in a firm, but rather extend to the improvement in corporate governance in all firms. See, e.g., KLEIN & COFFEE, *supra* note 112, at 200.

260. See COZIAN & VIANDIER, *supra* note 98, at 283.

261. See Loi N° 66-537, art. 245, C. soc., *supra* note 1, at 411-413.

262. See *id.*

263. See Décret N° 67-236, art. 200, C. soc., *supra* note 1, at 666.

that the company be a plaintiff.²⁶⁴ Directors cannot dismiss a derivative suit once it has begun. French law, in fact, declares invalid any clause in a company's articles of association that requires a prior shareholder resolution to bring a derivative action (or completely renounces their right ever to bring this kind of action) and further states that the shareholders cannot vote to extinguish a lawsuit.²⁶⁵

Under French law, moreover, there are no legal features such as "demand" and "demand excused," which in the United States give directors considerable power to dismiss derivative complaints that they disfavor.²⁶⁶ This may simply reflect the relatively infrequent use of the derivative lawsuit against French directors or officers so far. If, however, shareholders begin to use this instrument more vigorously to monitor and punish management, managers and directors might lobby for statutory or judicial relief against these suits. Such relief could take the form of giving them more control over the actions through such devices as the "demand" requirement.

B. The French "Direct" Shareholder Lawsuit

A French shareholder also has the right to bring a direct lawsuit, and shareholders can join together to prosecute this suit.²⁶⁷ In the direct action, a shareholder can file a complaint that he or she was individually harmed by the failure of board members (and others in the company) to provide the accurate disclosure of a company's financial position as mandated by French corporate law (a cause of action similar to a securities suit under section 10(b) of the U.S. Securities and Exchange Act of 1954).²⁶⁸ If numerous shareholders were similarly harmed, they could delegate the right (*mandat*) to act on their behalf in court, to one or more of them, provided that the "main plaintiff" receive authorization from each shareholder in writing. Such authorization must identify the mandating shareholder and the number of shares that he or she possessed.²⁶⁹ Again, the costly nature of such suits undermines their effectiveness.

C. Protection Against Lawsuits For Directors

The above picture is not complete without considering who pays the monetary award assessed against an offending manager or director. If directors

264. See *id.* art. 201, C. soc., *supra* note 1, at 666.

265. See Loi N° 66-537, art. 246, C. soc., *supra* note 1, at 413.

266. Generally, under U.S. corporate law, a shareholder must make "demand" on the board to determine whether the board wants to proceed with the lawsuit, unless demand can be "excused" (e.g., when the board is involved in the challenged transaction). If demand is excused and the shareholder proceeds with the suit, the board still may make a recommendation to the court concerning the suit, which, if the recommendation is done properly (through a committee of independent directors), is generally entitled to considerable deference. See 2 PRINCIPLES, *supra* note 110, at 55 (discussing the complexity of the demand requirements and jurisprudence thereunder).

267. Shareholders can also act collectively in prosecuting the French "derivative" suit.

268. See Loi N° 66-537, art. 245, C. soc., *supra* note 1, at 411-13 (noting the possibility of direct and derivative suits); see also SCHOEN, *supra* note 82, at 187.

269. See Décret N° 67-236, art. 199, C. soc., *supra* note 1, at 665-66.

and managers do not bear the financial burden of monetary penalties, the corporate governance impact of the legal duties imposed upon them is somewhat undermined. Yet a successful lawsuit against a director may, for example, carry a "reputational" penalty even if he or she suffers no financial loss. The issue involves balancing different corporate governance goals. If financial penalties against management are too draconian, capable persons may decline to accept positions as directors or officers, to take necessary business risks, or to make useful disclosure, all of which could hurt the operation and market evaluation of a business thereby producing *negative* corporate governance effects.

One possible outcome is for corporate law to allow a corporation to indemnify or purchase insurance for its directors and officers. Such insurance would cover honest mistakes of judgment, but not intentional misbehavior and self-serving transactions. Persons would not want to occupy corporate positions unless individual directors or officers were protected in situations where they had not gained personally and had simply committed errors of judgment, even if somewhat egregious ones. A judgment or large settlement to recover monies lost by a corporation could seriously impair or wipe out the assets of even a wealthy individual. With insurance, moreover, a corporation, and indirectly its shareholders, does not have to bear the entire cost of officer or director negligence, because the risk of misfeasance is spread among all corporations as a cost of doing business.

Directors and officers in France can obtain insurance policies for most civil penalties assessed against them, except for those arising from fraudulent conduct or from intentional misbehavior.²⁷⁰ Yet, there seem to be no provisions under French law that allow a company to indemnify directors for adverse judgments, lawsuit expenses, or settlements. This result is not surprising. There have been relatively few lawsuits in France from capital market shareholders, as there were few such shareholders and large controlling shareholders had other ways of disciplining management. Thus, management and directors had little need for protection against lawsuits and large judgment awards.

D. Summary

The existence of collective direct shareholder suits, the constraints on the board's ability to dismiss derivative suits, and the limited protection of directors from significant monetary penalties suggest that at least the letter of French law gives complaining shareholders some power to prosecute lawsuits against directors and management in France. Yet these lawsuits are infrequent and, as a result, have not had much corporate governance effect, positive or negative. This lack of utility may be partly due to both the requirement that 5% of shareholders join the suit and the uncertainty as to the recovery of plaintiffs' expenses. Moreover, it appears that there is no group of French lawyers who specialize in such lawsuits, and who would have an economic incentive to bring them and lobby for legal devel-

270. See GIBIRLA, *supra* note 123, at 433.

opments to make them easier and less costly to pursue. There is no clear explanation for this social phenomenon, although the "closed" nature of the French financial and legal communities along with the fear of social exclusion and ostracism from undertaking an activity not favored by the "group" may offer some justification.²⁷¹ Where a group shareholder action has emerged, it has been through associations of small shareholders that act on their own behalf and that have not developed a large "plaintiffs bar" to support them.²⁷²

However, the situation may be changing. There are a few lawyers in the French financial and legal community, generally with foreign training, who are beginning to experiment with the legal possibilities of French corporate law for collective action purposes.²⁷³ While creating an "industry" from which they benefit (much the same way that U.S. plaintiffs' lawyers do), they appear so far to have limited their representation to large minority shareholders, choosing not to stray from the accepted norms of appropriate behavior in the French business and legal community. It remains to be seen whether success and the entry into the French capital market of more non-French investors will cause these new lawyers/businessmen further to develop lawsuits and related legal techniques as an important corporate governance device.²⁷⁴

If, moreover, French corporate law is reformed in accordance with the suggestions of Senator Marini, there may well be more shareholder suits. Marini believes that the monitoring of directors and management through criminal sanctions (one of the main forms of oversight in France) must give way to direct shareholder action, including shareholder lawsuits.²⁷⁵ He even recommends that judges receive increased training in economics and finance because of the likelihood that (if the reform occurs) they will hear more cases involving shareholder and management disputes.²⁷⁶ In one respect, however, his reform proposal is hostile to collective shareholder

271. In the United States, it is probably fair to say that the plaintiffs' bar which specialized in such suits and many of the legislators and judges who favored their legal development first came from ethnic groups (e.g., Jews and Italians) that were traditionally excluded from other financial work. Cf., RONEN SHAMIR, *MANAGING LEGAL UNCERTAINTY: ELITE LAWYERS IN THE NEW DEAL* (1995). The absence of a similar bar in France may owe something to the absence of a clearly defined "outcast" group among the business bar that needs to find a source of livelihood.

272. Specifically notable are the *Association nationale des actionnaires français* and the *Association de défense des intérêts des actionnaires minoritaires*.

273. The most well-known of this small group would be Sophie L'Hélias of Franklin Global Investments, a bilingual lawyer with both French and U.S. legal and business school training. See *Fair Shares*, *ÉCONOMIST*, Feb. 15, 1997, at 65 (discussing her activity).

274. See generally Fanto, *Transformation of French Corporate Governance*, *supra* note 2, at 22-28.

275. See Marini Report, *supra* note 2, at 87.

276. See *id.* at 124. This Article has mentioned only in passing the French court system and its availability to hear commercial law disputes. Suffice it to say that basic shareholder disputes are heard by a *tribunal de commerce*, with the possibility of appeal to the *Cour d'appel* and ultimately to the *Cour de cassation*. See generally CHRISTIAN DADOMO & SUSAN FARRAN, *THE FRENCH LEGAL SYSTEM* 60-63, 82-89 (2d ed. 1996).

legal action because he opposes France's adoption of the "class action" mechanism, whereby an attorney can receive a contingency fee for representation of a large group of similarly situated shareholders in a successful lawsuit.²⁷⁷ One could criticize this opposition to collective shareholder action in lawsuits because capital market shareholders must join together in these actions for practical economic reasons.²⁷⁸ Nonetheless, the overall thrust of his proposal is to facilitate shareholder suits.

It is important to mention here the role of French criminal law in monitoring corporate agents. As Senator Marini has observed, French corporate law is extremely criminalized: a director's violations of duties may well subject him or her to criminal penalties.²⁷⁹ This made sense in the context of State ownership and control of enterprises, for violation of almost any corporate law could conceivably implicate State interests and justify a criminal penalty.²⁸⁰ In fact, criminal penalties are one of the major ways in which the State punishes violations by its agents who directed and managed its corporations. Yet, with privatization and the increased number of capital market shareholders in France, it is necessary to distinguish those obligations that a civil action by interested parties could appropriately enforce from the few that implicate societal interests in such a way as to demand criminal sanctions. This is a delicate reform in France as numerous management abuses in French companies might suggest a continuing need for criminal actions,²⁸¹ and the newly privatized companies are not yet prepared to control their corporate agents without the help of dominant shareholders (which might in fact explain these abuses). The Marini Report recommends limiting the scope of criminal sanctions to serious, intentional and fraudulent violations of corporate law, such as those involving misstating company accounts, abuses in stock issuance, serious hindrance of shareholders' information and voting rights, and self-interested transactions. It also suggests developing civil actions for the parties harmed through other failures by management and directors to fulfill their legal obligations.²⁸² If the reform becomes law, a new era may begin for French shareholder lawsuits.

277. See Marini Report, *supra* note 2, at 96. Marini does not recommend adoption of the contingency fee arrangement in France because of the problems that have appeared with it in the United States. *Id.*

278. Marini favors collective action in other contexts, such as voting.

279. For a brief summary of financial and corporate crimes, see Claude Ducouloux-Favard, *Délits financiers et boursiers*, DICTIONNAIRE PERMANENT ÉPARGNE ET PRODUITS FINANCIERS, Mar. 15, 1995, § 53.

280. See Bernard Bouloc, *Le droit pénal des sociétés*, in MODERNISATION DU DROIT, *supra* note 80, at 69-73 (describing the evolution of the criminalization of French corporate law largely as arising out of State responses to scandals concerning public companies).

281. See *France: Who's next?*, ECONOMIST, July 13, 1996, at 48 (discussing French company executives and politicians subject to criminal proceedings).

282. See Marini Report, *supra* note 2, at 106-10. Professor Bouloc cautions that the Marini Report's effort to decriminalize corporate law will be difficult since, even if statutory criminal violations are eliminated, common law criminal violations will remain. See Bouloc, *supra* note 280, at 73-78.

Conclusion

This Article has considered how well French legal policy-makers have adapted French corporate law to promote market capitalism. It generally concludes that, in many cases, French law provides protection for these shareholders, but that the law is often of recent origin or not yet adequately developed and rarely used. This state of affairs makes sense: market capitalism, while not new in France, has only recently become more important as the State abandons its role in the capitalization of major corporations. The growth of corporate governance within French law is most visible in the area of securities law where, for the past two decades, French legal policy-makers have been trying to provide French capital market investors with protections similar to those in traditional capital market systems to which investors are accustomed. As French capital-raising increasingly emphasizes stock market funding and as State monitoring of management decreases, French corporate and securities law will play a more critical role in French corporate governance than it has previously done. Even if family control, in the absence of State ownership, assumes a larger role in France, such firms will still need capital market investors for additional financing and thus have to ensure that the corporate governance system protects these investors.

One could hardly talk about legal reform in French corporate governance without discussing the Viénot Report, which this Article has occasionally cited. The Report shows that some important French business and legal practitioners believe that French corporate law must be targeted to counter the current weakness of capital market shareholders in the face of management power. Nearly all of its recommendations have this purpose.²⁸³ Although the Viénot Report does not suggest any concrete legal reforms to French law, it attempts to reinvigorate the board of directors through informal recommendations that would make board members take their duties more seriously. This orientation makes sense in a new finance situation where capital market investors must rely upon the board to protect their interests. The Viénot Report recommends the following: all boards have at least two independent members (without ties or other links to the company); special board committees should be created to deal with such critical subjects as audit, compensation, and board nomination (all of which go to the heart of supervising management activities and should thus include outside directors as members); and board members should not only take seriously their legal duties (to be informed about company matters and to avoid conflicts of interest), but they also should be in a better position to fulfill them (such as having enhanced rights of access to company information). The Report urges boards to provide shareholders with more information about their activities and the company's operations

283. For discussions and evaluations of the report, see, for example, Daniel Hurstel & Thomas Bieder, *Est-il urgent et indispensable de réformer le droit des sociétés au nom de la "corporate governance"?* 113 *REVUE DES SOCIÉTÉS* 633 (1995); Alice Pezard, *A propos du Rapport Viénot sur le gouvernement d'entreprise*, in *RAPPORT MORAL*, *supra* note 61, at 197.

in order to increase shareholder involvement in critical company decisions. Together, these recommendations are designed to improve the monitoring ability of capital market investors themselves.

Yet the Viénot Report is somewhat schizophrenic. From the perspective of market capitalism, improvements to board structure and behavior are designed to enhance the monitoring of managers by directors (the primary agents working for the shareholders) and thus to curb managers' power and prevent their inevitable domination of the board. Nowhere, however, does the Report specifically acknowledge this purpose and logic or explain that its reforms are based upon this agency framework. Rather, the Viénot Report emphasizes that French corporate law is founded upon a different theoretical basis — that the board serves company, not shareholder, interests.²⁸⁴ From an agency perspective which focuses on countering management power, this justification simply invites managers to "divide and conquer": rather than serving company interests, executives can pit various company constituents (such as creditors, employees and shareholders) against one another to maintain their own primacy. One is, therefore, left wondering about the purpose behind the "voluntary" reforms proposed by the Viénot Report if, as it appears, they do not rely on an agency justification.

The Viénot Report's recommendations are presented as clarifying the flexibility of French company law and its board structure for investors unfamiliar with them and as improving board behavior in a minor way.²⁸⁵ Taking a cynical view, the Report could be seen as acknowledging the power of international and primarily Anglo-Saxon institutional investors (it was released in French and in English) without recommending any fundamental changes to the French system.²⁸⁶ If, moreover, the State continues to influence significantly large firms or if many firms fall under family

284. See Viénot Report, *supra* note 2, at 2 ("This framework is rooted in a principle which the Committee considers essential, namely that *whatever a board's membership and procedures may be, its members collectively represent all shareholders and it must at all times put the company's interests first.*"). Professor Alain Couret explains well this intellectual foundation of French company law. See Alain Couret, *Chronique: Le gouvernement d'entreprise: la corporate governance*, 22 RECUEIL DALLOZ SIREY 163, 165 (1995).

285. See Viénot Report, *supra* note 2, at 1.

Privatization and the growing presence of non-resident investors on the Paris stock market has led to the rapid emergence of a new type of shareholder with little knowledge of the rules and practices applied by the boards of directors of listed companies in France. Such shareholders have naturally sought clarification.

Id.

286. A cynic might also suggest that, since U.S. scholars and practitioners produced their "Principles of Corporate Governance" and their U.K. counterparts their "Cadbury Report," the French felt obligated to do the same, without acknowledging that they were simply following an Anglo-Saxon model (thus, the briefness of the Viénot Report). Olivier Pastré observes that the drafters of the Viénot Report were responding to the concerns of non-French institutional investors. See Pastré, *supra* note 60, at 203.

The Commission des Opérations de Bourse has done much to publicize in France developments in U.S. and U.K. corporate governance. See, e.g., MARIE-NOËLLE DOMPÉ & ALAIN DORISON, FINDINGS OF THE COB: THE POWERS IN THE ENTREPRISE (1994); Bulletin COB, oct.-déc. (1994) (discussing ALI Principles and Cadbury Report). See also André

control, recommendations to enhance capital market investor power are likely to be muted. A more charitable view of the Viénot Report's approach is that it advocates informal corporate governance reforms because its drafters realized that change in this area (which could lead to serious restructuring of French industry) is likely to be a highly charged political subject. Furthermore, from an agency perspective, a complete U.S.-style system of corporate governance is not needed where counterweights to management, such as families and continued State influence, exist.

Any French legal reform promoting a corporate governance system protective of capital market investors requires serious reconsideration of the foundations of French corporate and securities law and of French corporate governance in general. This is not to say that French law is now inflexible or that it requires major changes to accommodate market capitalism, whose growth French law is clearly facilitating. Like the drafters of the Viénot Report, French corporate law scholars have shown that this law has little difficulty embracing many of the reforms (examples include use of independent directors and specialized board committees) proposed in Anglo-Saxon countries to improve the monitoring ability of directors.²⁸⁷ Yet without reconsidering and possibly reformulating the basis of the law, any reforms will work counter to other sections of the corporate code. If more French corporate governance disputes come to the courts, judges will also have considerable difficulty developing a jurisprudence out of statutory provisions that have no unified intellectual perspective.²⁸⁸

This Article has also referred to Senator Marini's proposal on the reform of French corporate law.²⁸⁹ More important than the Marini Report's specific proposals is the overall spirit of the proposed reform which clearly supports market capitalism. The Report observes that Anglo-Saxon and German legal traditions have influenced French corporate law (perhaps, as France turned to one or the other as a political ally).²⁹⁰ The German influence prevailed in the major 1966 reform of French corporate law, and this result adversely affected the law's utility to business under the

Tunc, *Le gouvernement des sociétés anonymes: le mouvement de réforme aux Etats-Unis et au Royaume-Uni*, 46 R.I.D.C. 59 (1994).

287. See, e.g., Paul Le Cannu, *Légitimité du pouvoir et efficacité du contrôle dans les sociétés par actions*, BULLETIN JOLY, juillet 1995, at 637; Nathalie Dion, *Corporate governance et sociétés françaises*, ÉDITION DU JURIS-CLASSEUR, DROIT DES SOCIÉTÉS, juillet-août 1995, at 8.

288. See Pastré, *supra* note 60, at 205 (noting the increased power of judges in French corporate governance and their need for a more sustained economic formation).

289. See Marini Report, *supra* note 2. Many of the reforms proposed by Senator Marini have been suggested by other commissions or groups studying French corporate law. See *id.* at 6 (listing previous reform suggestions). See also CONSEIL NATIONAL DU PATRONAT FRANÇAIS, *POUR UNE RÉFORME EN PROFONDEUR DU DROIT DES SOCIÉTÉS* (juillet 1996) (proposing many corporate law reforms that the Marini Report adopted). Such reforms are unlikely to proceed quickly, however, now that a Socialist majority has taken control of the French government.

290. This is a common observation in French business and legal circles. See, e.g., ALBERT, *supra* note 62, at 263-87 (discussing France as something of a battleground between the German and Anglo-Saxon approaches to company management).

current capital-driven economic circumstances.²⁹¹ That influence supported the "institutional" nature of the corporation (particularly the large corporation), which in turn promoted State ownership and control of large enterprises that typified the post-war years and which privileged social purposes and other constituencies in an enterprise over its shareholders. According to the Marini Report, this view of the corporation as an institution exemplifies the "Statist" character of, and thus rigidity in, legal obligations and relationships arising under French corporate law: it observes that this law "demeure contraignant, très fortement imprégné d'ordre public."²⁹²

The Marini Report argues that French corporate law must move away from this Statist approach and return to one that is compatible with the Anglo-Saxon perspective. It explains that enterprise adaptability to current economic circumstances demands this transformation. The institutional or Statist approach to corporate law no longer works; rather, it fails to contribute to such adaptability, as the State recedes from its position in the economy and the capital of large corporations. Because of the rigidity of Statist corporate law, not only do enterprises fail to adapt readily to changing economic circumstances, but managerial agents, no longer checked by State controls and increasingly operating in market capitalism, can now use the "*intérêt social*" strategically to pursue their own interests, generally at shareholders' expense.²⁹³ Such adverse effects of the Statist approach have serious consequences because French companies must compete for investors in the French and global product and capital markets and because law plays a role in this competition, particularly by encouraging capital market investing. If, therefore, corporate law handicaps French enterprises, especially in their capital raising, France and French enterprises will suffer in global competition.²⁹⁴

The main purposes of the Marini Report are, therefore, to simplify French corporate law (by eliminating its numerous rigidities and formalities that are costly to enterprises and that owe their origin to the Statist

291. See Marini Report, *supra* note 2, at 5.

292. See *id.* at 18 (noting that the law "remains constraining, very strongly marked by the public order") (translation by author).

293. See *id.* at 8-9.

294. See *id.* at 17.

Par ailleurs, on ne peut méconnaître que *la compétition économique met également en concurrence les systèmes juridiques*. De ce point de vue, la lourdeur et les rigidités du droit français des sociétés constituent un handicap. Parmi les éléments pris en considération dans le choix du pays d'accueil d'une société commerciale, nul doute que la faculté d'adaptation de l'instrument juridique aux besoins spécifiques de l'entreprise et aux modifications de l'environnement économique et social soit un facteur important.

Id. The author translates the previous passage to state: Moreover, one cannot fail to recognize that *economic competition also puts legal systems in competition*. From this perspective, the heaviness and rigidity of French corporate law is a handicap. Among the elements that a firm takes into consideration is its choice of a country in which to locate, as there is no doubt that the adaptability of a country's laws to the specific needs of business and to changes in the economic and social circumstances is an important factor.

approach), to give businesses more choice in their use of the corporate form, and to enhance shareholder rights. In other words, the shift to an Anglo-Saxon model means making French corporate law contractual, flexible, and friendly to capital market investors.²⁹⁵ Parties should find in corporate law legal mechanisms that they can adjust to their circumstances, which will in turn enable them to adapt their business relations (for example, shareholder/management relations) better to the economic situation facing them. This approach, well-known to U.S. business law scholars,²⁹⁶ considers corporate law as enabling, that is, as providing default rules for a contract (rules between shareholders and their agents), and as occasionally mandatory where needed to resolve certain structural abuses in contractual relationships.²⁹⁷ In its approach, the Marini Report looks to laws in other countries (particularly Anglo-Saxon ones), especially those concerning basic shareholder/management relations, which provide the substance of corporate governance. Because Anglo-Saxon investors are increasingly present in the capital of French companies, hold approximately one-third of this capital, and are familiar with this contractual focus, the potential use of these laws is not surprising.²⁹⁸

Much more than the Viénot Report, Senator Marini offers a reconceptualization of French corporate law that is sensitive to, and explicitly acknowledges, changing corporate governance in France and the evolving nature of agency problems in that country's large enterprises. Yet it is unlikely that any reformulation of French corporate law will result in a wholesale adoption of an Anglo-American style market capitalism. A reformulation and reconsideration of the foundations and function of French corporate law and governance may reveal that the historical "weight" accorded to some current French corporate governance practices will prevent them from being easily changed. As some have observed,²⁹⁹ strong management in French companies has historically served certain pur-

295. See *id.* at 17 ("Ces considérations militent en faveur de sa simplification et, plus encore, de sa contractualisation. Mais ce qui justifie fondamentalement cette démarche, c'est le constat de la très grande diversité des projets des créateurs d'entreprise et de leurs besoins."). The author translates the previous passage to state: These considerations argue in favor of [the law's] simplification and even more, of its contextualization. But what fundamentally justifies this effort is the observation that there is a very great diversity of projects and needs of entrepreneurs.

296. See generally EASTERBROOK & FISCHER, *supra* note 132, at 1-39.

297. See Marini Report, *supra* note 2, at 9.

En effet, la société est d'abord une technique d'organisation juridique des entreprises. Celles-ci doivent pouvoir trouver dans le droit non pas des entraves, mais les outils nécessaires à leur développement. La loi doit donc mettre à leur disposition des formes sociales aussi souples que possible tout en garantissant la sécurité juridique des salariés, des créanciers et des clients. Son rôle est moins d'interdire que de permettre.

Id. The author translates the previous passage to state: In effect, the corporation is first a legal way of organizing firms. They must be able to find in the law, not obstacles, but the tools necessary for their development. The law must therefore make available to them corporate forms as flexible as possible while guaranteeing the legal security of the employees, creditors and customers. [The law's] role is less to prohibit than to permit.

298. See *id.* at 6.

299. See PASTRÉ, *supra* note 60, at 204; Tunc, *supra* note 216, at 72.

poses, such as providing a necessary alternative to an ineffectual board or to one dominated by conflicting interests. The primary focus of a corporate board on company interests not only has a powerful intellectual foundation in the institutional theory of the corporation, but, since it also allows the board to consider interests beyond those of shareholders, it could be, and has been, used in particular economic circumstances to promote social harmony. As noted earlier,³⁰⁰ the French State has been very involved in large enterprises, and the *noyaux durs* organized around financial institutions may simply be an indirect continuation of this phenomena. Moreover, family capitalism, even on a large scale, has been, and remains, important (a phenomenon that Senator Marini does not directly address). A reaffirmation and the continued existence of capitalist systems other than market capitalism in French economic life may undermine or limit legal reforms useful for capital market shareholders.

Legal reforms of French corporate governance are therefore daunting, not only because French corporate governance is evolving, but also because few studies exist on the nature of this system and its evolution. In such circumstances, Olivier Pastré's admonition rings true: a thorough *national* analysis of French corporate governance is necessary and such analysis must involve different disciplines and approaches.³⁰¹ Only this kind of reflection can intelligently guide legal reform. The analysis will not be easy, not only because of its complexity, but also because it will bring to the forefront competing groups who stand to gain by the triumph of one or another form of corporate governance.³⁰² As in all human endeavors, whatever emerges from the analysis will be the result of compromise and the relative power, whether intellectual or other, French or non-French, of those involved in the debate. Yet without a sustained *French* public analysis and discussion, French corporate governance will be shaped largely away from the public's eyes, and valuable alternatives and solutions, which might have surfaced and even prevailed in an open debate, may never come to light.

300. See *supra* Part II.

301. See Pastré, *supra* note 60, at 201-03. This is not to suggest that none of this work has been done. One has only to think of the writings (many of which have been cited herein) by Bauer, Le Cannu, Morin, Pastré, Thiveaud and Tunc, to name just a few. There is simply more work needed. See also GÉRARD CHARREAUX, ÉD., *LE GOUVERNEMENT DES ENTREPRISES: CORPORATE GOVERNANCE THÉORIES ET FAITS* (1997) (finance articles on French corporate governance).

302. See generally YVES DEZALAY, *MARCHANDS DE DROIT: LA RESTRUCTURATION DE L'ORDRE JURIDIQUE INTERNATIONAL PAR LES MULTINATIONALES DU DROIT* (1992).

