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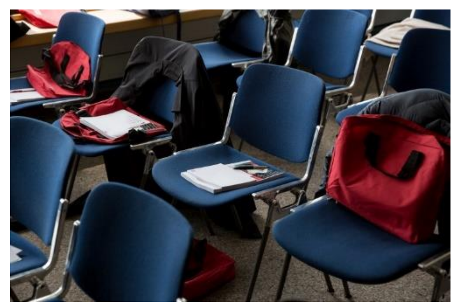
Editorial



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Dear Readers,

This special edition offers you an overview of the presentations given at the Institute's May event, "Fixing Societies by Fixing Business? Comparing Corporate Law Reforms". In view of the discussions on legal, economic, societal and ethical aspects of corporations' activities and corporate law in Switzerland and many other countries, the Institute organized this workshop on the laws of Switzerland, Belgium, and the United Kingdom.

We know that not all of you can make it to all of our events, but that many of you are also interested in the topics we investigate. Therefore, we have decided to create a new, special edition of our Newsletter, dedicated to presenting the information and ideas developed by the participants. We will present the contributions in the language in which they were originally given.

Your feedback on this new series is very welcome, as our wish is to continue publishing special editions on workshops held at the Institute.

We hope you will find this issue both useful and a pleasure to read!

The editors,

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Introduction

Krista Nadakavukaren, Vice-Director, Swiss Institute of Comparative Law, Switzerland

The topic of corporate law reform is one of great current interest among publics as well as among scholars and practitioners. The academic and practitioner interest in corporate reform is not particularly new – most would assume that scholars and practitioners are interested in legal reform in their area of work – but the strong interest of the public in these processes is striking. The colloquium hosted by the Swiss Institute for Comparative Law took on this topic in part to discover where the public interest was affecting the reforms being undertaken and where it might even be driving the reform efforts. We also wanted to know what corporate law experts thought about legislatures making corporate law such a visible tool to promote items on their social agendas that are only partly or only indirectly related to corporations.

Using the examples of Switzerland, Belgium, and the United Kingdom, the speakers described the current state of discussion of their respective corporate law codes and then focused on the social change aspects. These contributions, found in this newsletter, were followed by an open discussion on the "better societies through better companies" question.

To put these contributions in context, one must be aware of how international law's vigorous debates on what to do with multinational corporations has pushed national reform agendas. Numerous international law questions are being asked, answered, and those answers challenged: from the most basic issue of whether international law's traditional focus on states should yield to the practical realities of corporate power to affect populations and recognize corporations as subjects of international law; to the somewhat more technical question, which state should have the authority to regulate the conduct of corporate entities that are owned by foreign corporate entities; and the very practical related matter of determining how, even if corporations *should be* held responsible for the conduct of their subsidiaries abroad (itself by no means clear), the international community can make corporate liability a reality for individuals affected by their activities. The United Nations Guiding Principles on Business and Human Rights has pushed the conceptual discussions along, stimulating the thinking of academics about matters such as whether corporations have obligations to protect human rights (they do not) and what rights individuals have in terms of access to remedies. Very importantly, these international discussions have also spurred coordinated efforts of interested groups to push for more than just slight adjustments to corporate law at the national level.

In the jurisdictions we highlight, this push for corporate liability for actions taken abroad has been taken up in debates on corporate reform efforts. Other issues that are also concerns internationally and in other states are also being discussed: the continued discrimination against women and growing income inequality, among others.

When looking at the proposals emerging from this heavily social policy-oriented reform environment, it is important to distinguish the policy interests from the technical tools being used to achieve them. As corporate law expert Manning Bayless noted over forty years ago, corporate legal reform is *corporate* legal reform (Bayless Manning, Thinking Straight About Corporate Law Reform, 41:3 L. & Contemp. Prob. 3, 4 (1977)). That is, it is a change in the laws regulating a legal form called "the corporation". However, from the legal standpoint the corporation is not an economic entity – it is a legal form that can cover a variety of structures (Manning at 4-5). Yet publics generally do not view corporations in this way: rather, they see corporations as economic structures that should perform well to the benefit of society (Manning at 4). As a result, when there are repeated – even though isolated – incidents of bad behavior by managers and directors of corporations, publics see their predispositions as confirmed and therefore push for reform (Manning at 4).

The question we address today, however, is the same as from 1977: are the bad behaviors and the mistakes made by corporate executives best addressed by corporate law reform? Corporate law is a set of rules regulating the structure and powers of the corporate entity; not (usually) the behavior of its managers and directors, which may be socially undesirable regardless of their belonging to the legal entity (Manning at 6). Moreover, Manning writes:

> *Most commentators who polemicize against, and politicians who run against, "corporations" have in mind not corporations at all but a particular handful of large-scale commercial enterprises. It may be that the business conduct of some enterprises should be subjected to additional regulation, but it is not because they are corporations. Correspondingly, if one's purpose is to modify the conduct of those enterprises, amendment of state corporation laws, which are of general applicability to all commercial incorporated enterprises, will certainly be misdirected.* (Manning at 5)

At the same time, recent reports remind us of some very disturbing findings coming out of the corporate world:

1. The number of women in corporate positions of authority is dropping – think gender diversity.
2. CEO pay in Fortune 500 companies is higher than we might think and the differences to average wages egregious: a recent US study shows that some CEOs make in one year what the median worker in the company would make in over 20 professional lifetimes (defined as 45 years of work), and one even makes what his median employee would make in 111 lifetimes.
3. Labor and environmental abuses in the supply chain are rampant and serious, including in the foreign subsidies of corporations headquartered in the Global North.

The need to improve societies exists. Can we, in fact, improve societies by improving corporations? This is what the contributors to this project discuss.

Switzerland: Pending Corporate Law Reforms with a Special Focus on Socio-Political Objectives

Tizian Troxler, PostDoc and Lecturer, Universität Basel, Switzerland

The beginning of the ongoing Swiss corporate law reform dates back to the turn of the millennium. Now it seems that this winding and ambitious project is finally reaching the home straight. Against this backdrop, and in the light of the conference topic, this contribution summarises the key points of the current reform, including the development of milestones, before it turns to the rather socio-political goals, such as gender diversity, the prevention of excessive executive remuneration and transparency for commodity extracting firms. This contribution also aims to identify whether such objectives are drivers or obstacles of the ongoing reform and whether the proposed new regulations actually have – at least in theory – the potential to mitigate socio-political issues. It also includes the "Responsible Business Initiative", a pending popular initiative that might result in some rather radical changes in terms of global corporate social responsibility for Swiss-based businesses.

1. Overview of the Ongoing Corporate Law Reform

1.1. Remarks on the Development

In principle, and aside from some partial amendments, the current Swiss corporate law remains the same as implemented with the last major reform in 1991. Although modernisations have been discussed and proposed earlier, the actual starting point of the current corporate law reform dates back to the turn of the millennium. In 2007, after careful and extensive analysis and evaluation of the results of the public consultation process, the Federal Council submitted the first draft for a new corporate law to the federal parliament. The draft included the new accounting law, which has come into force separately in the meantime. The legislative procedure, however, could not be completed as planned. In 2008, the reform was completely interrupted by the federal popular "initiative against fat cat salaries" (also called the "anti-rip-off initiative"). The purpose of this initiative was to include a provision with compulsory guidelines for Swiss-listed corporations' executive remunerations in the Swiss Constitution and to grant a mandatory and binding "say on pay" right to shareholders. Parliament tried to include the claims of this initiative in the draft reform to cause the retraction of the initiative. However, these attempts failed and the anti-rip-off initiative had to be put to a vote. It was accepted by the superior majority of the Swiss electoral in 2013. As a consequence, the federal parliament sent the 2007 drafts back to the Federal Council with a mandate to include the anti-rip-off initiative in the new draft version of the modernised corporate law. In 2016, the Federal Council submitted the revised and amended drafts to the parliament and the ordinary legislative debate started all over again. Almost concurrently, the so-called "Responsible Business Initiative", a popular initative aimed at holding Swiss companies conducting business activities abroad responsible for violations of human rights and environmental standards, was initiated and submitted. Currently, the impact of this initiative on the ongoing reform is unclear. What can be said is that the Legal Affairs Committee of the National Council (the Parliamentary chamber of the people's representatives) submitted an indirect counterproposal that meanwhile was accepted by the National Council under the condition that the Responsible Business Imitative would be retracted. After the National Council's debate and the final vote, the reform package, including the Responsible Business Initiative and the counter-proposal, have been tabled for debate in the Council of States, the second chamber of the Swiss Federal Parliament.

1.2. The Cornerstones of the Ongoing Corporate Law Reform

In general, the revision will not change the basic characteristics of the Swiss corporation as a universal and capital-based legal entity that is available for all kinds of lawful businesses and that can be tailored to the enterprise's specific needs. The reform will maintain the vast and generally appreciated flexibility of the Swiss corporate form that can be used for publicly held or listed corporations as well as for closed corporations. Although the idea of creating separate legal forms for listed and non-listed corporations has been discarded, the draft contains more mandatory provisions applicable to listed and/or economically important corporations only. In addition to this, the "same business, same risk, same rule-approach" that has already been introduced with earlier reforms will be further implemented, should the proposed law come into force. Significantly, this would not only affect corporations, but also other types of business organisations, such as cooperatives. The idea behind this approach is that the law should contain identical or at least similar provisions for all legal forms if the underlying economic issues are comparable. Another key element of the ongoing reform is the reduction of administrative costs for the formation and maintenance of the corporation. As an example, under certain restrictive conditions, the draft proposes the formation, dissolution and removal of legal entities from the Commercial Register without public certification of the charter or other corporate documents. Furthermore, the reform proposes greater flexibility in the capital structure of the corporation and to allow the denomination of equity capital in foreign currency. As regards flexibility, the draft proposes the permissibility of all face values greater than zero and that the board of directors shall have the power to adapt the equity capital within a certain range upon prior approval of the shareholders' meeting that shall remain in force for up to 5 years. In principle, the proposed flexible range of equity capital expands the existing conditional capital increase, by introducing the possibility of "conditional capital reduction". Against the backdrop of traditional Swiss (and other European) corporate law theories, in which the determination of the equity capital structure is deemed to be a fundamental decision requiring the approval of the shareholders' meeting, the proposed flexible capital range is quite a substantial new feature. The revisions also include some modifications aimed at increasing the chances of a successful reorganisation of the corporation in case of financial distress. The draft foresees implementing incentives for preventive measures to avoid bankruptcy. These include liquidity requirements in general and the board's obligation to plan and monitor the corporation's liquidity. Finally, the reform contains a proposal to improve the position of shareholders as individual investors but also as a group that acts through the shareholders' meeting. This includes the expansion of shareholders' individual rights (e.g., regarding the possibility of putting a proposal to the vote of the shareholders' meeting or of obtaining access to information) and the transfer of competences from the board of directors to the shareholders' meeting (e.g., the binding and mandatory say on pay for executive compensations; however, this has already been stipulated in the federal ordinance against executive remunerations).

2. Socio-Political Goals of the Ongoing Swiss Corporate Law Reform

2.1. Implementation of the Anti-Rip-Off Initiative into the Formal Corporate Law

One of the main goals of the ongoing corporate law reform is to fully implement the above-mentioned anti-rip-off initiative into formal corporate law. At this point, the substantive requirements of this initiative are realised by an ordinance of the Federal Council, but they are not part of the formal Swiss corporate law. As regards the contents, the draft is basically identical with the current regulations stipulated in the Federal Council ordinance against excessive remunerations. Therefore, the proposed law would not alter the substance of the existing regulations, but the legal grounds would change. From a neo-classical corporate governance perspective, the design of executive remuneration is a crucial element to align the interests of managers and directors with those of the shareholders as a class so as to mitigate generic agency conflicts. Hence, it is typically not perceived as a socio-political topic, such as the protection of external constituencies. The developments in Switzerland regarding executive compensations are, however, only partially driven by such neo-classical corporate governance concerns. The real drivers behind the new regulations are socio-political in nature. The gap between salaries and the actual amounts of the executive compensation packages have had and still have the potential to disturb social peace. The movement against such allegedly excessive executive compensation packages has been fuelled in recent years and has caused public outrage due to the events of the last financial crisis and the fact that one of Switzerland's systemically important banks had to be saved from bankruptcy – at least partially – with taxpayers' money. Hence, the Swiss approach to regulating executive compensation is also aimed at achieving socio-political goals and, as a consequence, should not be analysed from a mere neo-classical corporate governance perspective. At this point, it is, however, unclear whether the current and proposed new regulations will actually lead to lower executive compensations, as they include no caps and the "say on pay" is – except for some prohibited forms of compensation – at the full discretion of the shareholders' meeting without any mandatory external control or approval, *e.g.* by a court or supervisory authority. Therefore, the relevant (although probably also the only) effects are that the boards and compensation committees will pay more attention to the possible socio-political impacts of the respective top executive remunerations.

2.2. Gender Guidelines at the Senior Executive Level in Economically Important Listed Corporations

An obvious socio-political topic is the proposed gender guidelines at the senior executive level of economically important listed corporations. Although in Switzerland the formal constitutional right and the goal of legal and factual equality between genders has existed for decades, factual shortcomings in terms of equal pay for equal work and of representation of genders in top management positions remain. Therefore, the draft proposes gender quotas as a "soft affirmative action" to ameliorate the factual, but not the legal situation. The quota topic caused controversial reactions in the public consultation process and in the public debate in general. Affirmative actions typically interfere with other constitutional rights, such as the economic freedom and the freedom of contract as a specific part of the former constitutional right. Therefore, they need to be evaluated thoroughly in terms of their constitutionality, including their compliance with the fundamental principle of proportionality. However, after taking a closer look, the proposed gender quotas for private corporations are more symbolic than affirmative in nature. First, the quota goals are set rather low: at least 30% of directors and 20% of top level executives should be represented by each gender. Second, they are based on a 'comply or explain' approach only, meaning that no strict legal sanctions apply in case of non-compliance. Furthermore, the rules will only apply after rather long interim periods and will only capture economically important listed corporations which, in most cases, have already included gender diversity in their agendas. Hence, from a purely socio-political point of view, the proposed new rules might be rather disappointing. Even from a corporate governance perspective the rules are rather sobering, as the diversity topic is restricted to the gender issue and does not include other diversity dimensions. However, the proposed gender quotas appear to be in line with the Swiss Constitution and, after all, have a realistic chance of passing the legislative procedure in the Parliament. In any case, the National Council has already voted in favour of the new quota provisions.

2.3. Increased Transparency for Commodity-Extracting Businesses
The draft proposes to improve transparency for commodity-extracting businesses. For such companies, the risks of corruption are considered to be higher than for businesses in other sectors. In order to prevent corruption and its negative effects on third parties, the draft includes special transparency duties for economically important commodity-extracting businesses. In principle, all payments to governmental bodies exceeding 100'000 Swiss francs must be disclosed and documented in order to comply with the proposed new standards. Apart from these rather socio-political goals, the proposal also intends to achieve transparency standards for commodity-extracting businesses that are fully equivalent with the pertinent regulations of the European Union.

3. The Responsible Business Initiative
3.1 Contents and Goals
The "Responsible Business Initiative" intends to implement the UN Human Rights Council Resolution 17/4 into the Swiss national law while it extends the scope of application to international environmental standards. International enterprises based in Switzerland would be obliged to respect human rights and environmental concerns irrespective of the actual place of their activities. In a group of companies, the diligence obligations are formally not restricted to the activities of the Swiss mother corporations, but rather include the actions of foreign subsidiaries and other businesses under at least factual control of the Swiss mother. Businesses coming within the scope of the initiative will have to carefully assess the risks involved. Under the new law, they would have to carry out adequate due diligence and would have to take all the necessary measurements to prevent the violations of the relevant rights and duties. The latter are, according to the initiative's committee, the rights and duties under the UN Covenant I and II, the eight core conventions of the International Labor Organization as well as the rights and duties under the broad understanding of environmental standards, which include not only international treaties but also international soft law standards. The initiative has two main goals, which can be summarised as (i) compensatory justice and (ii) prevention. The initiative wants to ensure that victims of violations of human rights and/or environmental standards have the right to seek redress in Switzerland. Therefore, according to the initiative, a special place of jurisdiction in Switzerland shall apply, irrespective of the applicable private international law or other conflict of laws regulations (compensatory justice goal). However, businesses will be exempted from liability if they carry out appropriate due diligence and take the necessary preventive measures. Hence, according to the terminology of tort law, the initiative proposes strict liability with the possibility of exemption in case of due care. It is not for the victim to prove negligence, and the enterprise needs to prove its due care. The goal is to enhance the preventive effects of the liability rule. Apart from the compensatory justice goal, the proposal is therefore clearly aimed at preventing violations of human rights and internationally recognised environmental standards in the first place. From legal and economical perspective, the initiative intends to foster the internalisation of negative externalities. Depending on the actual design of the relevant diligence standards, this internalisation of externalities will also promote efficiency, understood as an increase of total (global) social welfare (efficiency goal).

3.2. Critical Evaluation
While the underlying ethical and moral goals are indisputable and even from a pure social welfare perspective the initiative points in the right directions, some potential shortcomings still exist and need to be addressed briefly.

First, Switzerland would be one of the first nations pushing forward to implement the UN Human Rights Council Resolution 17/4. Of course, some other jurisdictions, such as France, have already implemented Resolution 17/4 or have put at least partially similar regulations in place. However, no strong international coordination exists in this regard. Moreover, in many aspects, the initiative reaches far beyond the UN Human Rights Council Resolution 17/4, by extending the scope of application to international environmental standards. Being in the role of the first mover always involves risks and chances that require comprehensive assessments. This, of course, cannot be done here. However, it is still possible to outline some of the core aspects, by analysing different hypothetical outcomes. In the worst case scenario, some or even all of the international businesses will leave Switzerland. In this case, people from abroad would not benefit from the proposed new regulations at all, and Switzerland would be worse off, too. In the best case scenario, the initiative improves the competitive advantages of Switzerland as a domicile for international businesses. In this case, additional international businesses might move to Switzerland, which will be favourable not only for people abroad, who would eventually benefit from the new regulations, but also for Switzerland. In which of these two possible general directions the real-world scenario actually will go, depends on whether the additional costs of compliance and damages can be outweighed by countermeasures, such as cost reductions or other advantages. The former could be achieved by further reducing administrative costs or by implementing an appropriate tax law reform; the latter depends largely on how market participants, especially consumers, perceive the fact that an enterprise has its domicile in Switzerland. This is to say that the reputation of Swiss firms could be improved by the new regulations and that the respective positive effects could actually outweigh the additional (compliance) costs.

Second, the outcome of the analysis outlined above obviously depends on the actual effectiveness of the proposed regulations. To start with the initiatives' compensatory goal, it is not clear at all if it can be achieved as intended. Litigation costs in Switzerland are high, the "loser pays all" rule applies, and it might be difficult for plaintiffs to win, since in most cases at least some of the relevant facts happen abroad and therefore will be difficult to prove before a Swiss civil court. Hence, the litigation risks for plaintiffs would in many cases be high and might deter many victims from actually seeking redress in Switzerland. This issue is amplified by the fact that, unlike in the United States, in Switzerland lawyers are not allowed to assume the litigation risks of their clients by working purely on the basis of the contingent fee, and therefore there is no "plaintiff bar" that could or would eventually reduce the potential deterrence effect. Of course, this issue could also be mitigated by national or international (humanitarian) organisations willing to finance litigation in Switzerland and to take the respective risks for the victims.

Third, tort law can only foster efficiency – in the sense of causing the internalisation of negative externalities into the relevant market mechanisms – under the condition of an optimum level of private law enforcement. The abovementioned litigation risks will likely result in under-enforcement of the proposed liability rules. Although various options other than contingent fees for lawyers exist to mitigate this well-known issue of under-enforcement, they are not generally implemented in Swiss tort law and Swiss civil procedure law. This can be explained by the fact that neither Swiss tort law nor Swiss civil procedure law is intended to promote efficiency in the described sense. Instead, they are designed to achieve compensatory justice in a two-party setting only. This could be best illustrated by the fact that, at least in principle, no punitive damages and no class actions are available in Switzerland, both of which would be effective private law instruments to deal with the notorious issue of under-enforcement of tort law. That issue is, of course, associated with tort law in general and not only with the initiative. However, the Swiss legal system often reinforces the desired preventive effect with parallel administrative or criminal sanctions and does not rely on tort law instruments only. The initiative, in contrast, relies on the latter instruments only in order to generate the desired preventive effects and might therefore miss one of its goals.

Despite these "technical shortcomings", the actual impacts of the initiative on the daily business of international enterprises should nevertheless not be underestimated. Although from an analytical point of view the actual (financial) risks might be considered low due to the under-enforcement issue mentioned above and also due to price differences and the lack of criminal sanctions, the reputational risks at stake for international businesses are undeniably substantial. Hence, international enterprises would most likely implement the proposed new due diligence obligations into their compliance and risk assessment standards and processes. This would improve the involved personnel's awareness of potential violations of human rights and international environmental standards and, as a consequence, might also alter 'global corporate behaviour". Hence, despite its technical shortcomings, the initiative might cause important impacts. It will, however, also create costs and thus the abovementioned worst-case scenario persists and deserves thorough analysis.

4. Fixing Societies by Fixing Business?

Although economic growth alone is rarely sufficient to fix social problems, it is in many cases a necessary precondition. Even from a socio-political point of view, it appears therefore reasonable to analyze the potential economic effects of the corporate law reform. This necessitates the application of a functional approach, which is based on the core functions of corporate *law*. In market-based economies these functions of corporate *law* include the facilitation of the financing, organization and operation of large businesses. Against this backdrop the core question then is: does the reform actually improve the possibility to procure equity capital from the public and does the reform reduce the costs of organising large businesses? Generally speaking, this appears to be the case, as the proposed rules are likely to reduce transaction costs by mitigating potential agency conflicts and reducing administrative costs in general. However, these findings do not clearly apply to the whole draft. Moreover, against the backdrop of the ongoing international and interdisciplinary corporate governance debate, some of the proposed new rules are controversial. For example, it is uncertain whether improving shareholders' rights is actually desirable since it reduces agency conflicts, or whether it is undesirable because it might foster short-termism. Reasonable arguments can be found on both sides of the debate and the empirical data fails to provide a clear-cut answer. Markets are, however, not free from failure. On the contrary, they often fail and cause inefficient and socio-politically undesirable or even harmful outcomes. One of the reasons for such market failures are external effects, meaning that not all costs of goods or services are reflected in the respective market prices and, hence, some of the actual cost are borne by third parties or even by "the environment". It should also be asked then, whether the proposed new rules promote the internalisation of such negative externalities. This certainly appears to be the case regarding the Responsible Business Initiative. From a socio-political perspective, however, efficiency is not the only important value, since aspects of distributive justice are also relevant. Of course, it is highly controversial whether and to what extent redistribution is socially desirable and if so, whether this should be done by tax law only or also with the help of other legal instruments, including corporate law. This question must be left open here. What can be said, though, is that the implementation of the anti-rip-off initiative – at least in theory – also addresses distributional concerns. However, it remains unclear whether or not the respective regulations will actually result in significantly lower compensation packages and who will eventually profit from such effects (only shareholders or also other constituencies). Finally, in the light of the leading question of this conference, it should also be analysed whether the reform is aimed at realising the socio-political goals of the Swiss Constitution. With the previously described guidelines for gender quotas in place, this is quite obviously the case.

5. Concluding Remarks

The historical dimension of the pending corporate law reform clearly shows that socio-political objectives are drivers of but also obstacles to corporate law reforms in Switzerland. The pending reforms include the realisation of socio-political goals, and eventually the proposed new rules have a limited potential to actually fix some specific socio-political issues.

Belgium: The Project for a New Companies & Associations Code, the Role of Stakeholders and the Place for Social Goals

Henri Culot, Professor, Université catholique de Louvain, Belgium

When he became Justice Minister in 2014, Koen Geens, a renowned corporate lawyer and professor of company law at KU Leuven, undertook to reform all "basis legislation". By this, he meant essentially all major Codes (*Code civil*, *Code pénal*, *Code judiciaire*, *Code d'instruction criminelle*, *Code de commerce*). Some still date from Napoleonic times, although many of their provisions have been revised since then. The Belgian Companies Code is much more recent. It was enacted in 1999, after preparation work by two professors amongst which is the current minister. But it was then a mere rearrangement of the existing rules – there was no major reform, let alone a complete rethinking of the principles of Belgian corporate law. The ideas for the new companies Code emerged from academic circles and were first put forward in a book published in 2014 (H. Braeckmans *et al.*, *La modernisation du droit des sociétés/De modernisering van het vennootschapsrecht*, Larcier, 2014). Several working groups composed of professors from all Belgian universities gathered during the following years to refine the proposals. The new Code was drafted in 2017 by a group of four professors and adopted by the Council of Ministers in July 2017. It was then submitted to the Council of State, which gave an opinion on the coherence of the text and on its conformity with higher rank norms (mainly the constitution and EU law). The draft was subsequently revised to implement the Council of State's observations and to consider the remarks of various interest groups which in the meantime had become aware of the project. The bill was introduced in Parliament in June 2018, but following the hearings held by the competent commission, it was decided to again submit the text to the Council of State. Its opinion is expected for September 2018, after which the legislative procedure will follow its course. It is hoped that the new Code will enter in force in January 2019. The following remarks are based on a draft text that may still be modified during the legislative procedure.

1. Contract vs Institution

One way to assess company law norms is to situate them on a continuum between a contractual pole and an institutional pole. Contractarians tend to view the company as an object created by and for the shareholders, pursuing their private interest through a freely negotiated contractual arrangement. Institutionalists consider the company as a legal creature, authorized by (public) law due to the contribution of this institution to the public interest, particularly in the economic sphere. The company is therefore not an object owned by its shareholders and used for their private interest. Rather, it is a (legal) being with its own independent interest. Its functioning is governed by mandatory rules which provide for the involvement of various stakeholders (amongst which the shareholders have obviously an important role to play). Either description should be more nuanced. Pure contractual or institutional forms do not exist because each law-maker strives to strike the right balance between the two extremes. What is considered an adequate equilibrium changes according to country, legal tradition and political opinion. Like fashion, it also changes over time, depending on the political or philosophical ideas *en vogue*. Viewed under this angle, the current Belgian reform clearly represents a move towards the contractual side of the continuum. Many mandatory rules are repealed or transformed into default rules; a general tendency against the extensive implementation of European Union (EU) directives beyond their scope of application can be observed; shareholders will enjoy more contractual freedom; and the role of other stakeholders in the functioning of the company will be reduced. This evolution should not come as a surprise under the current right-wing government of Belgium. But it is more surprising when viewed against other current evolutions, particularly in EU law. Recent developments have witnessed more attention being given to the stakeholders – for example in Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups and in the May 2017 version of the Corporate Governance Code for SMEs (known in Belgium as "Buysse Code"), which accords greater importance to corporate values, sustainability and attention to stakeholders and the local environment. The following sections will provide a short description of four examples of the contractual turn envisaged for Belgium's future company law.

2. Four Illustrations

2.1. Companies and Associations

Companies (business corporations) and associations used to be regulated under separate laws (*Code des sociétés* and *Code des associations*). The draft Code merges both into a single Code applicable to companies and associations alike, called the Companies and Associations Code. This emphasizes the technical nature of legal entities and clearly shows that the legal techniques are similar even though the ultimate goal may differ. Both under the previous and the coming laws, some rules are common to companies and associations while others differ. The new Code will contain more rules applicable to all legal entities, especially in its Book 2. The new Code also clarifies the criteria distinguishing companies and associations. Under the *Loi du 27 juin 1921 sur les associations sans but lucratif, les fondations, les partis politiques européens et les fondations politiques européennes*, still in force today, an *association* is characterized by the prohibitions on (1) conducting industrial or commercial operations as a main purpose (but such operations are authorized if they remain ancillary) and (2) distributing its profits to its members, directly or indirectly. These two conditions are cumulative. The purpose of *companies*, on the other hand, is to generate profits to distribute them to the shareholders. The new Code provides that only the second condition is maintained: an association may not distribute or procure, directly or indirectly, any economic benefit to its founders, members, directors or any other person except for the non-profit purpose determined by the articles of association. Unlike the present rule, however, associations will be allowed to operate as businesses (i.e. to engage in economic activities) as long as the profits are not distributed to the members. This development led to protests from the representatives of associations. From a symbolic point of view, they fear that the specificities of the non-profit sector will gradually disappear, and that they will be considered as enterprises like all others, which they precisely do not want to be. Above all, they do not want to lose the favorable tax regime reserved to non-profit associations and from which they were presumed to benefit due to the legal limitations to their authorized activities.

2.2. Corporate Interest

Corporate interest is the main standard to be used when judging the legality of decisions by the corporate organs. Judges may annul the decision if it runs against the corporate interest. This rule is, as such, generally accepted. How the corporate interest is defined, however, is subject to an intense debate. Not unrelated to the contractual vs institutional divide, contractarians tending to reduce the corporate interest to that of the shareholders, while for institutionalists the interests of a broad range of stakeholders should be considered. In its decision of 28 November 2013 (*Pasicrisie*, 2013, p. 2384-2386), the *Cour de cassation*, highest court of Belgium's judiciary order, declared that the corporate interest is determined by the collective profit-making goal of current and future shareholders. This decision revived the debate. Many commentators are not enthusiastic about this very contractarian statement. While they welcome the view that the corporate goal should be thought of in a forward-looking way, taking into account the long-term interest (represented by the future shareholders), they regret that only shareholders are mentioned, to the exclusion of any reference to the stakeholders. The new Companies and Associations Code would have been an occasion to rectify this omission, but its authors decided not to include a definition of the corporate interest. Thus, the text implicitly confirms the drafters' approval of the Court's definition, at best leaving it to further jurisprudence to initiate an evolution if deemed necessary.

2.3. Annulment of Board Decisions

The current Article 178 of the Companies Code provides that any interested party may apply to the commercial court for the annulment of a decision of the general meeting of shareholders. In such a case, the claimant will have to demonstrate that the decision is illegal (for example, because it was not taken in the corporate interest). The question of who is an "interested" party has been debated. Usually individual shareholders and board members are recognized as being interested in the legality of corporate decisions, especially if they are affected by the contested decision. Whether other stakeholders should be considered as interested is more controversial. This issue took on heightened interest with a 26 November 2013 judgement by the Commercial Court of Liège which granted the workers of a company the right to claim for the annulment of a decision taken in the general meeting. The context behind the judgement was that, despite warnings by the workers' representatives, the company had been mismanaged for a few years by its German mother company and was threateningly low on cash. Regardless of this, the general assembly, controlled by the mother company, decided to distribute a substantial dividend which, if and when paid, would lead the company to bankruptcy. The decision to include workers in the "interested" parties, rendered in a rather blatant case by an inferior court, was enough to prompt the reaction of the draft Code's authors. They proposed to amend the rule to allow a request for annulment by the legal entity or by any party who has an interest in the respect of the rule that was breached (Art. 2:43). This is intended to limit the request for annulment to shareholders (in the case of general assembly decisions) or board members (for board decisions). As always, much depends on the interpretation that courts will give to the new rule, which is linked to the definition of the corporate interest. If the corporate interest is interpreted to include also that of the employees and the creditors, then courts could recognize that they have an "interest in the respect of the rule that was breached". But to be clear, this is not the intention of the drafters.

2.4. Social Enterprise

The limitations to the operations of associations (described above) historically led the creation of the "company with a social purpose" (*société à finalité sociale*). This is a label attributed to any company whose by-laws respect nine conditions defined in Article 661 of the Companies Code. The three main conditions provide for the company seeking a limited profit only and distributing no or a limited dividend (currently 6% of the paid-up capital), a limitation of the shareholders' voting power in the general assembly (no individual shareholder may vote more than 10% of the total votes) and a mandatory participation of employees in the capital of the company. The initial intention of the new Code's drafters was to simply suppress this kind of company. The non-profit sector complained and remarked that many legal provisions in other domains (especially provisions granting subsidies to activities in the public interest) referred to the company with a social purpose in their scope of application. The drafters therefore decided to keep a "social" form of company: the social enterprise ("*entreprise sociale*"). This still operates as a label, but is reserved to the cooperative societies. Three conditions must be met to benefit from this label: the main purpose of the company should be to generate a positive societal impact for humankind, the environment or society; the yearly dividend should be limited (still at 6% of paid-up capital); and in case of liquidation of the company, its net assets should be contributed to a social goal. A simple comparison shows that the limitation of the shareholders' voting power and the involvement of employees do not appear in the new regime.

3. Conclusion

It would be unfair to reduce Belgium's current company law reform to the elements described above. To be sure, there are also many improvements to a regime which was to some extent outdated and poorly adapted to the current European context where corporate mobility has become the rule. But as far as social goals and stakeholders are concerned, the reform appears to go against the tide, by founding company law on more contractual and liberal principles, which were fashionable in the 1990's but now appears contrary to the wider European evolution.

United Kingdom: Corporate Governance that Works for Everyone

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Corporate governance has traditionally been viewed as a way to reduce agency costs between shareholders and managers in the context of private ordering. Laws and regulations pertaining to corporate governance have, therefore, typically aimed to enhance long-term wealth for shareholders. Governments have in recent years, however, discovered a new use for corporate governance: advancing the public interest. This has been done by promoting everything from environmental causes to gender diversity to humanitarian aid. In the United Kingdom (UK), the government has been explicit in advocating this view of corporate governance. Prime Minister Theresa May has expressly noted that corporate governance should be used to ensure that corporations work towards providing a "fairer economy" or an economy that "works for all." A review body working under the government has been even more forthcoming in describing corporate governance as a replacement for national regulation in employment issues. Yet the UK is not alone in its views. India is relying on corporate governance rules to hold corporations accountable to the public, China is using it to promote "social harmony," and in the United States (US), the Securities and Exchange Commission has used corporate governance rules to "promote peace and security" and "combat global corruption". While governments undoubtedly have broad discretion in using regulations to achieve public policy goals, we question whether corporate governance rules with a public focus is an appropriate and efficient means for doing so. This is because the practice suffers from two main shortcomings: requiring corporations to pursue public objectives at the expense of other goals and discouraging governments from using more effective forms of regulation.

1. Corporate Purpose

As to the first shortcoming, the starting point for our critique is the corporate purpose. Because we find that the corporate purpose lies somewhere between exclusive shareholder wealth maximisation and the pursuance of public interests, governmentally mandated corporate-governance rules may justifiably include public goals. Yet, we argue that such rules must reflect a balanced corporate purpose and promote governance that serves multi-faceted corporate aims. This is not to say that corporate governance rules must necessarily promote public and shareholder interests equally, but rather that the overall effects of a particular governance mechanism should be balanced and, insofar as possible, be directed at benefitting the full range of corporate stakeholders. This suggests that when corporate governance mechanisms address social issues they should not promote public over shareholder interests as the aim should remain to benefit the corporation in a holistic manner. Moreover, in some instances, public-oriented corporate governance has been designed primarily to further the interests of one set of stakeholders. This creates problems when it disadvantages the interests of other stakeholders. As an example, corporate governance rules designed to promote humanitarian aid may divert funds from corporate activities supporting employees or the local community. In these instances, the furthering of one stakeholder group's interest may impinge on competing stakeholder interests and risks hampering the long-term interests of the corporation.

2. Indirect Regulation

The second problem is that public-oriented corporate governance rules tend to focus only on indirectly regulating corporate conduct. For instance, the rules encourage corporations to disclose their executives' pay, the number of women on their boards, or their efforts to reduce greenhouse gas emissions rather than direct them to do so. Of course, direct and indirect regulation each has its benefits and costs and only by weighing them can a government determine the optimal combination. However, in the case of public-oriented corporate governance, there is a marked preference for indirect regulation. The entire model of corporate governance in the UK, for example, is premised on a "comply or explain" model, meaning that corporations can choose to comply with corporate governance practices or explain why they have chosen not to do so. Indirect regulation can be an appropriate compromise between those that view over-regulation as inefficient and those that view under-regulation as ineffective. Nevertheless, indirect regulation is only effective if reinforced by traditional forms of regulatory fiat where regulatory delegation fails. In the area of public-oriented corporate governance, failure of regulatory delegation is apparent in a number of areas. Most notably, a recent UK study found that, despite countless attempts by the government to indirectly regulate executive compensation through corporate governance, neither the pay gap between CEOs and employees has narrowed nor has the relationship between executive compensation and firm performance improved.

3. Conclusion

To address these shortcomings, we suggest several reforms. To avoid unduly privileging specific stakeholders, we argue that governments should try to balance the overall effects of public-oriented corporate governance rules and, insofar as possible, aim to benefit the full range of corporate stakeholders. Where this is not possible, it may well be that using corporate governance is the wrong approach to solving that specific public problem. Indeed, if governments are truly seeking to regulate and change corporate conduct towards public policy issues, they must complement current approaches with more direct ones. While we do not necessarily advocate an interventionist approach in all areas, we do find that it is both more effective and justifiable to address legitimate public goals directly rather than relying (exclusively) on the shaming and nudging techniques of indirect regulation often found in corporate governance mechanisms with public aims. Overall, we conclude that public-oriented corporate governance should not be used as a one-stop shop to fix the ills of society. Where appropriate, it should be used strategically and form part of a concerted, multifaceted effort to address the root of the public policy issue.

The Institute

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