December 2019

High Committee for Corporate Governance Annual Report

HCGE

Haut Comité de Gouvernement d'Entreprise

Contents

Preface

This sixth annual report of the High Committee on Corporate Governance covers the period from September 2018 to September 2019, the first full year of application of the version of the AFEP-MEDEF Code revised in June 2018. It follows on from the activity reports which the High Committee has published each year since October 2014, and reflects the profound changes in its work and the context in which this is carried out.

Over the past six years, the High Committee has gradually emerged as the guardian of large French listed corporations' compliance with the principles of good governance. The progress it has seen encourages it to remain rigorous and attentive to the implementation of the recommendations governing the main SBF 120 corporations.

The business environment has seen major changes. In its task of monitoring the code's implementation, the High Committee needs to take into account the significant changes which are happening now.

Shareholders and investors are demanding more active engagement in governance, while other *stakeholders* want to be more involved in defining corporate strategy. The increasingly widespread presence of directors representing employees requires company offers, the parties concerned and those who appointed them to adapt accordingly. Diversity within governing bodies which, according to the code's latest recommendations, is a key objective, must now become a reality. The issue of the gender balance on boards of directors has given rise to appropriate responses, and French boards now lead the world on this topic; however, much still remains to be done to increase diversity within executive committees. Attentive to this matter, the HCGE will not hesitate to investigate corporations whose policy in this area is inadequate. The HCGE's priorities also include strengthening the quality of the dialogue with shareholders. Such a dialogue is all the more essential given the surge in a certain kind of shareholder activism driven by funds with a somewhat short-termist view.

By giving weight to the kind of corporate interest which should take social and environmental aspects into account, the PACTE Law will inevitably lead to CSR policies being given a greater role in corporate governance. Corporations are already gradually taking up the "purpose" by involving *stakeholders* and increasingly opening up to civil society. As part of its Sustainable Finance Action Plan, the European Commission is deliberating on the advisability of requiring boards of directors to develop a sustainable growth strategy and clarify the rules of conduct for directors in the long-term interest of the undertaking. The revision of the Non-Financial Reporting Directive should further strengthen the need to take sustainable governance aspects into consideration.

Undertakings cannot stand by and watch this societal revolution: they have to be proactive players, engaged in sustainable development aspects reflected in their governance policy. The role of boards of directors and supervisory boards, which is central to the recommendations of the AFEP-MEDEF code, is expanded as a result.

The High Committee intends to make an active contribution to the implementation of these developments. It shall do so through its task of supporting undertakings and through its participation in the discussions set to continue in the coming months. French governance has acquired a respectable image internationally, and the High Committee has a duty to strengthen this.

Patricia Barbizet
Chair of the High Committee on Corporate Governance

The AFEP-MEDEF Code, the yardstick of good governance

The year just ended saw the installation of an expanded committee. Indeed, the High Committee grew from seven to nine members, allowing it to welcome a diverse range of profiles and skills. The chairmanship of the committee also changed during this year and is now held by Mrs Patricia Barbizet.

In terms of the deliberations undertaken during the year, the place of the AFEP-MEDEF Code within the regulatory framework and the practical organisation of listed companies prompts the High Committee to make three observations:

1) The code is continuing to establish itself as the frame of reference favoured by the largest corporations. Although its adoption is voluntary according to the terms of the law, almost all French SBF 120 corporations have chosen it, in other words 105 corporations, with the exception of foreign corporations and a few other corporations listed in Appendix 1 of this report. Stricter than most of the codes in force in other European countries, the implementation of the AFEP-MEDEF Code requires a certain level of diligence and appropriate resources, which is why certain smaller corporations, or those whose capital is not as widely open, favour the Middlenext Code. The latter, unlike the AFEP-MEDEF Code which makes recommendations, is essentially education oriented by being specifically directed at different players in governance. It points out the main questions to consider to ensure the sound functioning of governance, without the need to report the responses provided. Nevertheless, a number of corporations which do not have the capitalisation or trading volumes associated with the SBF 120 index have opted to refer to the AFEP-MEDEF Code, and some unlisted corporations use it as their model. It is ultimately up to shareholders and investors to decide whether the guarantees with which it provides them, notably in terms of proportion of independent directors, rules preventing conflicts of interest and compensation transparency, justify these constraints.

More widely, beyond the world of business itself, the debate continues between oversight by hard law or soft law, between the role of the law and that of professional regulation, focusing on the issue of compensation. The PACTE Law saw the legislator take the lead in overseeing compensation. In this context, it appears important to reaffirm the importance and relevance of professional regulation and of the HCGE in implementing soft law. The HCGE is not just an authority that polices behaviour that deviates from the recommendations of the code: it has now acquired real authority. The recommendations and requests it sends to undertakings are largely acted upon, leading in recent years to a notable improvement in governance by those corporations which apply the AFEP-MEDEF Code.

2) The second observation concerns the degree of compliance with the provisions of the code by the corporations which refer to it. The analyses reported in successive High Committee reports show that this has continued to increase, and the statistics presented in this report further attest to this.

3) Finally, the dialogue between the High Committee and the executive officers of corporations and other operators on the financial market facilitates implementation of the code adapted to the characteristics and actual circumstances of undertakings, and contributes to the development of the code.

1. Tasks

According to Article 27.2 of the AFEP-MEDEF Code, the High Committee is "*responsible for monitoring the implementation of the Corporate Governance Code for the listed corporations that refer to it and ensures the actual implementation of the fundamental corporate governance rule, which is the 'comply or explain' principle".*

The task assigned to the High Committee by this article of the code is twofold: to monitor its implementation and propose any changes needed to AFEP and MEDEF. The task of monitoring was felt to be essential to ensure the proper implementation of the "comply or explain" principle. Therein lies the very feature of soft law that the High Committee promotes in accordance with the AFEP-MEDEF Code. It involves encouragement without constraint, so that undertakings adopt virtuous practices corresponding to their requirements and circumstances. In this regard, good practices should take hold beyond the mandatory standards that are for the law to lay down to protect shareholders and other stakeholders. However, the varying situations of undertakings means that it is impossible to take a "*one size fits all*" approach to governance. Furthermore, in the event of non-compliance with the precepts of the code, the quality of the explanations must provide credible justification for the choices made by undertakings. Without this, corporate behaviour could not be understood and accepted by all those affected by their activities.

For this reason, the High Committee makes the interpretations and recommendations required in order to implement the code. It may, on the one hand, be consulted by the boards of directors or supervisory boards of the corporations that refer to it and, on the other, investigate in order to draw the attention of corporations to the points of the code which they have failed to apply without giving sufficient explanation. It does so whenever a non-compliance is brought to its attention, either by contacting the executive officers directly or, more formally, by sending boards detailed written requests. In exceptional cases, it is forced to publish its position when the situation justifies this, particularly when it triggers an immediate reaction from the financial market. More systematically, at the end of the "season" when annual reports are published and shareholders' meetings are held, the High Committee reviews the reports and reference documents and requests explanations.

Furthermore, the publication of its annual report contributes to the performance of the High Committee's tasks. The statistics it contains measure the rise in good practices among large undertakings. Similarly, the measured "*name and shame*" practice has an incentive effect. In accordance with the High Committee's now established policy, this concerns those corporations which, despite its calls, have persisted, on the one hand, in deviating from significant recommendations of the code and, on the other hand, have not acted on the opinions received, mentioned in their annual report why they may have decided not to act on them or undertaken to rectify this situation. Finally, themed comments contribute to the deliberation on changes to the regulatory framework in a constantly changing environment.

2. Activities of the High Committee

2.1. Meetings and external contacts

Eleven meetings of the HCGE took place between October 2018 and October 2019, based on a planned schedule. In addition, one ad hoc meeting was held by conference call to consider an urgent consultation by an undertaking. The rate of attendance of members during the year was 88%.

At the same time as adhering to the duties of confidentiality to which they are subject, the HCGE and the AMF discussed matters of common interest informally, in the context of their respective interventions. The AMF now regularly recommends that issuers should consult the HCGE and suggests areas of consideration to it in order to promote the complementarity of the two institutions. The HCGE commends this relationship, which contributes significantly to the effectiveness of the rules and precepts of good governance. The High Committee also had conversations with Euronext to address issues concerning the financial market.

As happens every year, a press conference was held in October 2018 to coincide with the publication of the annual report. Furthermore, the chair and the general secretary are regularly asked for interviews or clarifications by specialist press bodies, and to speak at seminars or conferences on matters such as the functioning of boards, the role of directors and shareholder democracy.

2.2. Consultations, investigations and review of the reference documents of the SBF 120

The High Committee intervenes both at its own initiative through investigations and in response to consultations by undertakings.

Investigations

The High Committee's interventions at its own initiative relate first and foremost to one-off events (mainly when executives leave). Of the responses to leaving conditions for executives, two related to corporations registered outside of France but listed on the Paris stock exchange. The High Committee pointed out that they were outside its jurisdiction since they do not refer to the AFEP-MEDEF Code. However, it was able to point out what the non-compliances would have been if this code had been applicable.

Secondly, its interventions relate to it sending out letters systematically after reviewing corporations' annual reports. This year, 33 requests were sent out: incidentally, this figure is not significant in itself, as it corresponds on each occasion to the scope of the topics on which the High Committee decides to focus, and not to a variation in the quality of undertakings' practices.

These requests are divided more or less evenly between actual governance matters and compensation matters. With regard to the former, this notably concerned provisions of the code relating to board meetings without the executive directors being present, the board's self-evaluation including the evaluation of the individual contribution of directors, a director representing employees taking part in the compensation committee, the profile of the lead director and succession planning. With regard to compensation, mention was notably made of the structure of directors' compensation, the description of the qualitative or extra-financial criteria for the variable compensation of executive directors, the terms of their non-competition agreements, their termination benefits and the share-based compensation plans from which they benefit (including the formal commitment not to engage in any hedging transactions). Each of these topics gave rise to a small number of letters, which means that none of them are of major concern to the financial market. The deficiencies observed appeared to be information deficits rather than deliberate deviations not explained or incorrectly explained. In most cases, the corporations undertook to communicate more comprehensively next year.

Broadly speaking, and despite the extremely diverse nature of the reference documents of SBF 120 corporations, systematically reviewing them each year shows the progress made in governance practices and the communication related thereto.

Beyond the dry figures included in the statistical part of this report, we see that compliance with the recommendations of the code is in fact increasing, and in particular that certain provisions which previously met with reticence are now being widely followed.

Consequently, we find that:

- holding concurrent directorships beyond the limits laid down by the code has disappeared: this practice, which was long considered characteristic of the governance of large French corporations and severely criticised, now appears to be a thing of the past;
- the position of lead director, greeted with scepticism only a few years ago, has demonstrated its value and is no longer considered a simple token given to shareholders hostile to the combination of the offices of chairman and chief executive officer: it is implemented by a number of corporations which practise separation, and indeed by corporations with a supervisory board;
- with regard to qualification as an independent director, boards how communicate more transparently about their analysis of the significant or non-significant nature of any business relationships between the director and the corporation: this is a point to which the High Committee has paid particular attention in recent years;
- the self-evaluation of boards is now standard practice: the account provided in the reference documents regarding this is necessarily concise because confidentiality is a condition of conducting the exercise, but it notably appears that it increasingly includes an analysis of each director's individual contribution, which is a sign of the maturity of the boards which implement it;
- the regular practice of holding board meetings in the absence of the chief executive officer has also become established: once again, the reticence with which it was met by those who considered it to be a practice clumsily imported from the Anglo-American culture has subsided.

However, some recommendations of the code still appear to be followed (or are the subject of satisfactory explanations in the event of deviating from them) by fewer than 90% of the corporations in the sample. These will therefore be reviewed by the High Committee with particular care in its future work.

As regards actual governance, this mainly concerns the proportion of independent members on audit committees and compensation committees, directors representing employees taking part in the latter, and succession planning.

As regards executive directors' compensation, this concerns:

- information about the extra-financial criteria used to set the variable compensation;
- the proportion of the compensation in securities (options and free shares) due to the executive officers, which has to be published and form a sub-ceiling in the shareholders' meeting resolutions authorising boards to award them;
- the formal commitment that executives must make not to engage in hedging transactions for the securities received;
- the period used to set the reference compensation used to calculate the defined benefit pension amount, which must be several years.

Consultation by undertakings

The HCGE is regularly given the opportunity to deliberate consultations referred to it on behalf of boards (by chairmen, chairmen of compensation committees, lead directors or general secretaries) in order to be given interpretations or recommendations in a given context.

These deliberations notably concerned:

- the effect of a potential or actual **conflict of interests**, not only on taking part in deliberations but also on the performance of the director's duties when the conflict of interests cannot be considered a one-off on account of its duration or scale;
- the consequences of a director being prevented, due to circumstances beyond his control causing him to be repeatedly absent for an unspecified period, from complying with his **attendance** obligations;
- whether the duties of chairman of the supervisory board are compatible with a **contract for the provision of services** to the same corporation, relating to tasks which clearly fall within the remit of the management (strategy, choosing investments);
- whether two directors appointed at the proposal of a shareholder which, in a passive manner, has exceeded the threshold of 10% of the corporation's capital (but not permanent representatives of this corporation as a legal entity director) should continue to qualify as **independent directors**.

2.3. "Six Chairs Group" European dialogue

In November 2018, the High Committee went to Rome for the now annual meeting of the chairmen of the committees responsible for drafting or monitoring corporate governance codes in six European countries (Germany, France, Italy, the Netherlands, the United Kingdom and Sweden). This meeting of the "*Six Chairs Group*" resulted in the publication of a press release. Despite the differing legal contexts, the different codes share a number of points in common. This informal forum allows views on governance developments to be shared and conditions conducive to improved effectiveness of codes to be discussed.

The meeting was devoted to the many regulatory initiatives aimed at encouraging investors and undertakings to develop a sustainable development strategy, and at guiding their risk analysis in this direction. The market is, quite rightly, increasing its focus on environmental, social and governance (ESG) issues. This warrants oversight of practices, which is reflected in the first instance by the European Commission's actions to implement and develop the non-financial reporting Directive, as part of its Sustainable Finance Action Plan. The group of chairmen emphasised the importance of undertakings earning the trust of the market and the need, for legislators and regulators, to take into consideration the decisive role played by corporate governance codes and their monitoring committees in guiding corporate policy.

3. Main topics addressed by the High Committee

The investigations and consultations gave the HCGE the opportunity to delve deeper into certain topics where difficulties in interpreting or applying the AFEP-MEDEF Code needed to be resolved.

Furthermore, as in previous years, the High Committee opted to devote its deliberations to certain topics outside of any consultation or investigation. The results of these analyses are reported below.

3.1. Implementation of the PACTE Law and deliberation on the purpose

In line with the recommendations of the so-called Notat-Senard report (*Business and the common good*, March 2018), the PACTE Law opened up the possibility for corporations to specify their

"*purpose*" in their articles of association, consisting of the "*principles which the corporation adopts and in accordance with which it intends to allocate resources in the performance of its business activity*" (C. civ., Art. 1835). As specified in the explanatory memorandum of the law, the notion "*aims to bring chief executive officers and undertakings closer to their long-term environment*" at the same time as encouraging "*corporations, in the form of a ripple effect, to no longer be guided solely by an interest, but also by a 'purpose', enabling a long-term approach to be adopted".* This new possibility is consistent with the wider objective, supported by section 2 of the PACTE Law, to "*rethink the place of undertakings in society*" by broadening the corporate interest to include the social and environmental issues (C. civ., Art. 1833) which boards of directors and management boards are also required to take into consideration (C. com., Art. L. 225-35 and L. 225-64).

To date, two corporations have adopted a purpose in their articles of association. Indeed, Atos stated in its articles of association in April that its mission was to "*help design the future of the information technology space*", and Carrefour said that its shareholders' meeting had approved the insertion of a stipulation specifying that the corporation's mission was "*to provide [its] customers with quality services, products and food accessible to all across all distribution channels*". A number of corporations also state – in their reference documents or on their website – that they have started to reflect on the subject, using different terms (purpose, objective, mission, aim, goal, motivation, mission statement, etc.). Veolia has led the way in this regard, after having adopted a three-page manifesto entitled "*Our purpose*" at its shareholders' meeting.

The introduction of this new non-binding mechanism raises several questions, on which the High Committee has focused its attention. While the first issue relates to the actual value of stipulating a purpose in the articles of association, a second series of questions will consist of determining, if the articles of association do mention a purpose, what the mechanisms might be for measuring its proper application in terms of corporate governance.

In this regard, the High Committee noted the conclusions of the Notat-Senard report, which considers that, in addition to the philosophical virtue of embarking on such a deliberation on the policy orientation – broadly speaking – of a corporation's action, including a purpose in the corporation's articles of association may provide "*most boards of directors with guidance on important decisions, a useful counterpoint to the financial criterion of the short term, which cannot serve as a compass* [but] *embodies the legal fiction that the undertaking represents*". However, the High Committee considered that the purpose did not necessarily have to be included in corporations' articles of association in order to guide their action. It is nevertheless clearly desirable for all corporations, including those which have already adopted a CSR approach, to begin thinking about this subject with all of their actors and stakeholders to affirm together the values guiding their action within the undertaking.

3.2. Applicability of the AFEP-MEDEF Code to foreign companies

The compensation that Mr Thierry Pilenko received when he left Technip highlighted the difficulty linked to the specific circumstance of foreign corporations listed on a French regulated market.

Indeed, while emphasising that the compensation at issue was not in line with the recommendations of the AFEP-MEDEF Code, the High Committee could only observe that it was not within its jurisdiction to decide, Technip having become a foreign corporation not subject to the code.

The benefits that Mr Thomas Enders received when he left Airbus again raised a comparable difficulty; although it is listed in France, Airbus is also listed in Germany and, as a Dutch company, it implements the Dutch code of governance and is not required to comply with the AFEP-MEDEF Code.

On both these occasions, the High Committee had the opportunity to review the relevance of the scope within the AFEP-MEDEF Code, and to observe that 11 SBF 120 corporations did not apply the AFEP-MEDEF Code due to being registered outside France.

The difficulty obviously stems from the dual role of governance codes. As well as being instruments for good corporate governance, they also serve the sound functioning of the market, such that both the *lex societatis* and the law of the country where the corporation's securities are admitted to trading on a regulated market can designate the governance code applicable to a corporation.

Within the European Union, the various Member States can choose either connecting criterion.

Consequently, in Germany, the governance code applicable is designated by the law. The corporate code requires certain categories of German corporation to comply with the Deutsche Corporate Governance Kodex or explain deviations from its recommendations. The nationality of the undertaking triggers the application of a code directly designated by the law. Things are different in the United Kingdom, where the *Financial Conduct Authority* makes admission to the London Stock Exchange dependent on compliance with the UK Corporate Governance Code. Compliance with the code is a condition of entry to the financial market. Listing on the UK market therefore triggers the application of a code directly designated by the market authority.

The French legislature has made yet another choice. Article L. 225-37-4 of the Commercial Code actually allows corporations to choose a code developed by business representative organisations. Although the requirement to refer to a governance code is imposed only on those corporations whose securities are admitted to trading on a regulated market, the requirement to comply with a governance code is a rule governing the functioning of corporations, and in this respect only concerns corporations governed by French law and not corporations listed in France.

Moreover, although the AFEP-MEDEF Code does not clearly specify whether it is aimed at French corporations alone or whether it can be applied to foreign corporations, the HCGE's various reports have always excluded foreign corporations from the scope of their analysis.

The High Committee has reviewed the advisability of changing the scope of the AFEP-MEDEF Code, to extend the supervision of good practices to all corporations listed in France, particularly when the French financial market is the main place where the corporation is listed. Besides the United Kingdom (see above), it seems that at least two other countries, Spain and Luxembourg, allow or require their governance code to be implemented by a foreign company listed on their market.

While there is nothing preventing a foreign corporation from applying the AFEP-MEDEF Code voluntarily – subject to recommendations not compatible with the law governing it – it does not, however, appear necessary at this stage to require foreign companies listed in France to refer to a French governance code. A measure of this kind might, in fact, limit the liquidity and attractiveness of the Paris financial market.

However, the High Committee can only call for the convergence of governance codes within the European Union, so that each one imposes an equally demanding standard of good practices and equivalent protection for investors regardless of the nationality of the listed corporation. Such convergence is already observed with regard to certain recommendations, such as the one relating to independent directors. The intention of the international dialogue in which the High Committee participates (see above) is to strengthen this.

3.3. Impediment to taking part in meetings of the board of directors for an unspecified period

a) The High Committee was consulted by the lead director of SCOR, who is also the chairman of the compensation and nominations committee of the BoD, with regard to the situation of one of the corporation's directors who is also the chairman of a corporation which has indicated its intention to merge with SCOR. Having indicated that he had decided to effect a “temporary withdrawal” from the board of directors due to a conflict of interests, this director had asked the corporation not to send him meeting information and documents relating to the meetings of the board of directors that would be held during the period of withdrawal, estimated to be approximately seven months (until the next annual shareholders’ meeting). The consultation of the High Committee concerned finding out whether effecting a “temporary withdrawal” was compliant with the rules and principles of good governance of the AFEP-MEDEF Code and, more specifically, whether it was compatible with the duties of diligence and regular attendance and to remain informed of members of the board of directors laid down in Articles 6.1, 11.3, 18.1 and 19 of the AFEP-MEDEF Code. The High Committee's response was no.

On this occasion, the High Committee pointed out the following:

- the AFEP-MEDEF Code does not make mention of any “temporary withdrawal” situation which would enable a director not to continue participating in the work of the board at the same time as retaining his or her corporate office;
- in legal terms, no article of the Commercial Code provides for a withdrawal situation;
- a director who finds himself or herself in a one-off potential or actual conflict of interests situation would, in accordance with Article 19 of the AFEP-MEDEF Code on ethical rules for directors, be required to report his or her conflict of interests situation to the board and should abstain from attending the debate and from taking part in voting on the related resolution.

  The High Committee is of the opinion that he or she could also, in this case, ask not to be furnished with the dossier relating to the agenda item causing the conflict of interests.

  However, even given the fairly specific circumstances of this case and the explanations provided, this withdrawal situation could only be limited to the matter constituting the conflict of interests;
- if the director considers that, generally speaking, he or she is no longer capable of holding his or her directorship, he or she should bear the consequences of this and give up his or her corporate office.

Otherwise, he or she is in fact running the risk of a serious breach of the rules of the AFEP-MEDEF Code relating in particular to regular participation in the work of the board and the committees on which he or she sits.

In legal terms, this situation could also lead to this director being held civilly liable due to his or her “abstention”, this being the exact term used by the case law of the Court of Cassation to give shareholders the right to reparation.

Following the HCGE’s intervention, the director who had asked to withdraw temporarily from the board of directors decided to resign from said board.

b) The High Court was also consulted by Renault's lawyer regarding a request for an opinion from the lead director and the chairman of Renault's nominations and governance committee regarding the compatibility between the recommendations of the AFEP-MEDEF Code concerning the presence and

regular attendance of directors and the situation of one director who was prevented from participating in the work of the board for an unspecified period.

Following an exchange of views, the High Committee decided that it was up to Renault's board of directors to assess the situation in a relevant way in the light of Article 19 of the AFEP-MEDEF Code, which states that "the director should be regular in his or her attendance and take part in all meetings of the Board and of any committees of which he or she is a member. He or she must also be present at the shareholders' meeting". It was consequently reiterated that regular attendance is a key condition of the position of director.

Insofar as a director is prevented from performing his or her duties for an unspecified period, the High Committee is therefore of the opinion that it would in fact be impossible to comply with the duties of presence and regular attendance and would run the risk of a serious breach of the rules of the AFEP-MEDEF Code.

3.4. Provision of services and corporate office

The High Committee received a request for an opinion from an investment company regarding the compatibility of an agreement for the provision of services with the office of chairman of the supervisory board with regard to the provisions of the AFEP-MEDEF Code.

First of all, it should be pointed out that this agreement for the provision of services concerned the provision of strategic, partnership and investment advice to the corporation's management.

While the code makes no specific provision regarding concurrently holding a contract for services and the office of chairman of the supervisory board of a partnership limited by shares, the High Committee made the following points:

- the members of the supervisory board are treated as directors, as appropriate. In fact, the preamble to the code, referring to the recommendations it contains, states that: "Finally, most of them have been written with reference to public limited companies (*sociétés anonymes*) with a Board of Directors. Public limited companies with a Management Board and a Supervisory Board, as well as partnerships limited by shares (*société en commandite par actions*) will therefore need to make the necessary adjustments";
- as a non-executive officer, the chairman of the supervisory board has an enhanced duty of independence, which requires him or her not to put himself or herself in a structural conflict of interests situation;
- the two-tier public limited company, with a management board and a supervisory board, stems from a desire to separate management bodies from supervisory bodies, which is incompatible with the chairman of the supervisory board taking part in the corporation's management.

Given these conditions, in the light of the provisions of the code, the High Committee considered that:

- the director bound by a contract for services could not be held to be independent in the light of Article 8.5.3 of the code, which states that the director is "not to be a customer, supplier, commercial banker, business banker or consultant:
  - that is significant to the corporation or its group;
  - or for which the corporation or its group represents a significant portion of its activities" as well as due to the existence of a capital link exceeding 10%.

This situation would therefore not be in line with the fact that the chairman of a supervisory board should not be in a situation such as to lose his or her independence due to a conflict of interests situation with the management.

- in terms of ethical rules for directors, Article 19 of the code on ethical rules for directors notably expresses the following obligations:
  - "the director is mandated by all the shareholders and should act in all circumstances in the best interests of the corporation;
  - the director is bound to report to the Board any conflict of interest, whether actual or potential, and abstain from attending the debate and taking part in voting on the related resolution".

The High Committee was of the opinion that the concurrent situation envisaged would constitute a structural conflict of interests situation *de facto* hindering the effective performance of the office of chairman of the supervisory board as well as compliance with Article 19.

Consequently, even though concurrently holding the office of chairman of the supervisory board and service provider appears to be technically possible in legal terms, the High Committee was of the opinion that the performance of a contract for the provision of services to the management, which would concern advice regarding the strategy and choice of investments so critical to the tasks of the management, could not be held concurrently with management supervision responsibilities regarding this same management through the supervisory board. This agreement would structurally expose the chairman of the board of directors to a conflict of interests preventing him from performing his duties as chairman of this body under satisfactory conditions. The High Committee considered the plan to be incompatible with the recommendations of the AFEP-MEDEF Code.

In more general terms, the matter of concurrent corporate office and provision of services is now the focus of specific attention by the High Committee.

3.5. Independence of the director representing a shareholder having exceeded the 10% threshold

It is essential first of all to highlight the unique procedural situation which prompted the High Committee to consider the matter raised. In the case in point, the difficulty came from the fact that one corporation (the Corporation) had considered two directors with links or previous links to one of its main shareholders (the Shareholder Corporation) as independent. The AMF thought that the explanations provided by the Corporation in its annual report should be referred to the HCGE. The High Committee was therefore consulted by a Corporation following a matter raised by the AMF and at the invitation of the AMF itself. The High Committee would like to commend the dialogue established with the AMF and the resulting strengthening of the rules of good governance.

Fundamentally, the matter raised by the AMF after reviewing the situation of two directors held to be independent related to the fact that the directors in question had or had previously had links with a shareholder of the Corporation that had exceeded the 10% threshold in February 2017 in a passive manner, as a result of the allocation of double voting rights. This prompted the High Committee to review the scope of Article 8.7 of the code, and specifically the wording "*in the light of the make-up of the capital*".

Article 8.7 of the AFEP-MEDEF Code states that "*directors representing major shareholders of the corporation or its parent company may be considered independent, provided these shareholders do not take part in the control of the corporation. Nevertheless, beyond a 10% threshold in capital or voting rights, the Board, upon a report from the nominations committee, should systematically review the*

qualification of a director as independent in the light of the make-up of the corporation's capital and the existence of a potential conflict of interest".

The High Committee considered that:

- directors representing a major shareholder cannot be held to be independent if this shareholder takes part in the control of the corporation;

  They may therefore be held to be so if this is not the case.

- above a 10% threshold (in capital or voting rights), the board must "*review*" whether to maintain this qualification as independent. There is an obligation to state reasons concerning the qualification given. It goes without saying that such an obligation to state reasons may only be considered to have been met if the arguments given to justify the director's independence are relevant;

- in this regard, the reasons stated must, according to Article 8.7, take into account "*the make-up of the corporation's capital and the existence of a potential conflict of interest*", which pertains, for both these aspects, to the specific future situation of the shareholder who exceeds the aforementioned threshold, in capital or voting rights.

The board of directors must therefore consider whether the director representing such a shareholder should no longer be considered independent, or in other words whether the situation means the loss of "*his or her freedom of judgement*", which is the criterion for independence laid down by Article 8.2 of the code.

On this basis, called upon to ensure compliance with Article 8.7 by the board of directors of the Corporation concerning the situation of the two directors whose links with the Shareholder Corporation are detailed in the consultation letter, the High Committee noted that:

- the Shareholder Corporation did not control the Corporation;

- the Shareholder Corporation exceeded the threshold of 10% of the voting rights, triggering the aforementioned obligation to state reasons;

- the Corporation explained its position in its Reference Document 2017/2018, page 47, in the following terms:

  "*Consequently, it was decided that the Shareholder Corporation does not take part in the control of the Corporation and is not planning to do so as indicated in the declaration relating to exceeding the threshold published by the AMF on 23 February 2017:*

  ● *the Shareholder Corporation has no links to any other shareholder nor to the R. family, the Corporation's reference shareholder;*

  ● *Messrs I. G. and G. S. do not chair any of the Board committees and are not members of the Nominations, Governance and CSR committee; and*

  ● *the Shareholder Corporation does not intend to request the appointment of other directors, as indicated in the aforementioned AMF declaration.*

  The Nominations, Governance and CSR committee and the Board of Directors have also noted that there is no conflict of interests:

  ● *exceeding the threshold of 10% of the voting rights is not liable to create a conflict of interests situation;*

● *there is no significant business relationship between the Shareholder Corporation and the Corporation or its Group liable to create a conflict of interests situation which may interfere with their freedom of judgement; and*

● *the Shareholder Corporation has a reputation as a diligent and demanding investor whose interests are in line with those of all the shareholders.*

Given the above, the Nominations, Governance and CSR committee and the Board of Directors considered that Messrs I. G. and G. S. fully met the 'specific' criteria for independence related to exceeding the threshold of 10% in capital or voting rights. "

The Corporation therefore satisfied its formal obligation to state reasons.

Various concrete elements enable such a justification to be considered well founded. In fact:

- the Shareholder Corporation exceeded the threshold of 10% in voting rights in a passive manner, due to the granting of double voting rights, a situation which is clearly different from a shareholder increasing his or her holding in an active manner in order to increase his or her influence over the corporation;
- the observation is not a new one, given that this threshold was exceeded in 2017 and nothing has happened since to change the Shareholder Corporation's situation;
- the Corporation's shareholding structure is characterised by the fact that the R. family holds 16.29% of the capital and 22.59% of the voting rights. Although it is a major shareholder, the Shareholder Corporation is not, in fact, in a position to determine decisions in shareholders' meetings (no de facto control) through the voting rights that may be exercised and, in more general terms, does not appear to have effective power over decision-making within the Corporation;
- the Shareholder Corporation has not entered into an agreement with the R. family that might alter the previous assessment;
- nor is the Shareholder Corporation in a situation of marked opposition to the decisions which might be taken by the corporation's management that would otherwise be characteristic of a lack of independence or a conflict of interests.

It does not therefore appear that the two directors with links to the Shareholder Corporation in question can be considered to have lost their freedom of judgement and therefore their independence within the meaning of the AFEP-MEDEF Code.

These various reasons enabled it to be considered that the board of the Corporation had indeed satisfied the requirements of Article 8.7 of the AFEP-MEDEF Code.

3.6. Balanced gender representation on governing bodies

The High Committee paid particular attention to balanced gender representation on governing bodies, in line with the AFEP-MEDEF Code, which recommends that boards should consider "*what the desirable balance of its membership and that of the Board committees should be, particularly in terms of diversity (gender representation, nationalities, age, qualifications, professional experience, etc.).*" (§ 6.2.).

The proportion of women on boards of directors and supervisory boards continued to rise. All of the corporations which apply the code adhere to the 40% lower limit for female members of boards of directors or supervisory boards, and 35 SBF 120 corporations exceed the 50% rate for female directors (see below).

However, the number of women is still too low within other governing bodies, and in particular executive/management committees. Despite the fact that Article 1.7 of the AFEP-MEDEF Code has recommended since 2018 that the board should ensure that "the executive officers implement a policy of non-discrimination and diversity, notably with regard to the balanced representation of men and women on the governing bodies", we currently find that women make up less than 20% on the executive/management committees of CAC 40 and SBF 120 corporations.

The quotas method may seem more difficult to implement in this case, given the constraints inherent in the functioning of executive/management committees, which are not company bodies but established based on the specific practices of each organisation, making it difficult for the legislator to intervene.

The reasoning of the Copé-Zimmermann Law appears difficult to transpose in this case. In fact:

- recruitments within BoDs are external recruitments, unlike executive/management committees where they are internal promotions most of the time, which demands attention to the gender balance considerably upstream, from the time when young employees are recruited;
- executive/management committees consist of operational staff, and groups are by nature diverse (different business areas and sectors, some attracting more women than others, but also diverse international operation, with countries where it may be difficult to recruit talents);
- unlike boards of directors, positions within executive bodies are not renewed at regular intervals, since their members are generally linked to the corporation by a permanent contract. The natural *turnover* within undertakings makes it physically impossible to replace men with women within the timeframes that would be required by the legislature.

However, the High Committee can only again urge boards to take into account the recommendation in Article 1.7 of the code. It also strongly urges the corporations in question to review applications from women for executive positions from the beginning to the end of the recruitment process, put in place support measures for female talents internally and set themselves ambitious target figures in this area by giving themselves the means to achieve them. We note, furthermore, that the Law of 22 May 2019, known as the PACTE Law, introduces "*a selection process which guarantees from beginning to end the presence of at least one person of each gender among the candidates*" for deputy chief executive officer positions (Art. L. 225-53 and 225-58 of the Commercial Code).

The High Committee will carefully monitor corporations' stance regarding this point in the coming years.

3.7. Assessment of the qualitative criteria for variable compensation

The High Committee would like to reiterate the importance of monitoring the qualitative criteria for variable compensation. During its meetings, it has taken the opportunity to discuss this monitoring and the assessment of these criteria, and is of the opinion that as well as applying the formulas for calculating variable compensation, it is important for the board to have some degree of discretion for setting the compensation of company officers.

Furthermore, the HCGE intends to draw attention to the difficulties raised by the variable compensation awarded to non-executive officers. It reiterates that the AFEP-MEDEF Code considers that it is not desirable to award variable compensation, stock options or performance shares to non-executive officers (§ 24.2), and that such an officer cannot be considered independent if he or she receives variable compensation (§ 8.6).

Furthermore, active vigilance regarding the specific situation of certain corporations has been implemented throughout the year.

Finally, throughout last year, the HCGE contributed to deliberations within the financial community through enhanced exchanges (changes to the AFEP-MEDEF Code, shareholder dialogue, changes to the law, etc.).

4. Topics of deliberation for the High Committee for the coming year

Furthermore, the High Committee intends to deliberate the following topics in the coming months:

4.1. Relations between undertakings and proxy advisors

Proxy advisors, whose consulting with respect to investors regarding their engagement and how to exercise voting rights is not subject to approval, have been the focus of growing attention. In October 2019, the Woerth report on shareholder activism (no. 2287) again highlighted that "it is unhealthy for an investor to relinquish their policy role (voting in the shareholders' meeting) to a third party, even when prompted by considerations relating to cost and capacity to process the information of listed corporations".

In both emerging countries and developed states, regulators have expressed their desire for stricter control over the influence of proxy advisors, which would go beyond the self-regulation promoted by operators in the sector – which recently decided to place themselves under the authority of an independent supervisory committee. In France, the PACTE Law, transposing the SRD2 Directive and mentioning the AMF's previous recommendation, has taken a step in this direction, by requiring proxy advisors to adopt a code of conduct, ensure that conflicts of interest are prevented and managed as well as assume an obligation to report annually on their activity and the methods used to prepare their analyses and recommendations (PACTE Law, Art. 198; C. mon. fin., Art. L. 544-4).

The High Committee considers it necessary to ensure that the analyses and recommendations of these proxy advisors do not have a disproportionate impact on the adoption of certain resolutions in shareholders' meetings. It intends to deliberate on relations between undertakings and proxy advisors and how any resulting conflicts of interest are managed, and draws attention to the role of the chairman of the board or the lead director in relations with proxy advisors.

4.2. Shareholder activism

The High Committee notes the recent development of shareholder activism beyond the traditional interventions of minority shareholders, either in order to react to the corporation's governance or make significant profits quickly. Several French corporations have recently been subject to sometimes virulent interventions from certain activist funds, which raise questions about the methods used and about the possibility of preserving calm shareholder dialogue – which the High Committee defined in its 2017 Annual Report (p. 22) – in the interests of the market.

Following the example of a number of financial market authorities, particularly the AMF, and as part of its constant and global deliberation on shareholder dialogue, it intends to endeavour to take into consideration the specific difficulties raised by shareholder activism.

4.3. Sustainable governance

In its Sustainable Finance Action Plan published on 8 March 2018, the European Commission set as its objective the emergence of a lower-carbon economy. Inspired by a report drafted by a High-Level Expert Group (HLEG) on sustainable finance, the action plan notably intends to emphasise the need to favour more sustainable corporate governance and, to achieve this, calls for changes in corporations' corporate governance practices. It notably recommends that boards should take environmental and social sustainability issues into greater account.

Under this influence, the tasks of governance bodies are set to change, and European governance codes are already mindful of these social and environmental responsibility issues, now identified as good governance practices.

In this context, the High Committee intends to deliberate in a more global way on the place of sustainable governance, not only within the tasks of governance bodies but also with regard to its potential role in monitoring the practices to be developed.

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