*Patrick Letourneur, Avocat au Barreau de Paris, Docteur en droit, Maître de conférences associé à l'Université Pascal PAOLI*

# «Legal Impact of Human Capital in Corporate Organization in France, a new legislation as a commitment for the Future» [1]

*A graduate of the University of Lyon III "Jean-Moulin" and a Doctor of Law, Patrick Letourneur is Associate Professor at Paoli Tech, the Engineers' College of the University of Corsica "Pasquale Paoli". Member of the Paris Bar since 2002, he formerly held various senior executive positions within the steel industry, having being appointed Vice President & General Counsel of UGINE and Vice President & General Counsel Operations of USINOR, both worldwide leading steel makers.*

1. As an integral component of the Labor Factor, the concept of "Human Capital" within corporate organization has received its main legal recognition by being incorporated into the corpus of French labor law both through general provisions regarding the legal status of employees and more specific provisions dealing with sharing of profits and corporate governance, both in the public and private sectors. The executive and legislative branches of the French government continue to produce new developments in the area [for example, the "Macron" Ordinances" promulgated by the government in September 2017 and the expected new "Pacte" law ("Pacte" is an acronym for *plan d'action pour la croissance et la transformation des entreprises*, i.e., "Action plan for growth and transformation of enterprises") likely to be enacted in the coming months].

2. In the context of discussions on the respective rights of employees and shareholders, it should be recalled that, in a market economy, the business conducted by a company is considered to be the property of the company itself and not that of its shareholders or directors, nor is it considered to be shared with "stakeholders" including the company's employees, clients, suppliers or other state and public entities, even though the outcome of the firm's activities is beneficial to all such stakeholders and employees are entitled to share partially profits and to play a role in corporate governance. Moreover, the case law concept of "*intérêt social*" (corporate benefit) creates limitations on the exercise by directors and employees of their respective rights and prerogatives and imposes liabilities on them when such exercise conflicts with the interests of the company itself.

3. Although there is no doubt that the proper interest of a company is private and different from the public interest and that the corporate purposes of a company as defined in its by-laws is based on the earning of profits to be shared by its shareholders (Art.1832 French Civil Code), some authors of learned legal commentary (*doctrine*) as well as the recent "*Notat-Sénard*" report to the Ministry of Finance of March 2018 have suggested that the concept of "corporate purpose" (*objet social*) should be redefined in the French Civil Code to refer more explicitly to the social and environmental dimensions of corporate activities and empower the Board of Directors (as a right –not an obligation) to specify the global objectives of their company (Art.1833 and 1835 French Civil Code would be consequentially modified).
As proposed, such changes would not be that compelling for companies, as it is not obvious and almost impracticable to define identical objectives for all, taking into account the heterogeneity of companies and abilities to confront their respective environment.

**Strong legal signs acknowledging the existence of Human Capital and revised limits**

4. Labor law provides for various individual rights protecting health, wages and employment and the rules are generally applied in their most favorable sense for employees (*principe de faveur*) and, together with corporate law, creates collective rights and prerogatives, such as the right to be consulted on almost all management issues, to be represented at meetings of the board of directors or even to elect members thereof, to share in profits (*participation & interessement*) and to obtain advantages by way of employee savings plans or attribution of shares, or more recently the right to make an offer to purchase their company under certain circumstances and conditions relating to threatened termination of business or sale of a majority of shares of companies of which they are employees.

5. There is no single legal concept of Human Capital and the term itself is not used in the official legal terminology:

- Under Corporate Accounting rules, Human Capital is dealt with exclusively as "personnel" and is considered to be a "cost" in the Profit and Loss Account rather than as a resource or an asset for the company
- Under Corporate Law, Human Capital is not recognized as a component of the capital or equivalent to shareholders status. However, there are specific provisions dealing with (i) the rights of the "*comité d'entreprise-CE*" (soon to be replaced by the "*comité social et économique-CSE*") to be informed of and consulted by management with respect to certain actions and for employees to be entitled in certain circumstances – regardless of levels of employee shareholding – to be represented at meetings of or to elect members of the Board of Directors and (ii) employee shareholding, the offering of which is mandatory under limited given conditions.
- Under Labor Law: Human Capital (the employees) is to be protected (labor conditions), fairly paid, collectively informed and consulted on all management issues and possibly a party to the acquisition of their company. Moreover, a significant part of applicable rules is a result of the extended scope of collective bargaining.

6. Although (or indeed perhaps because of the existence of) conflict of interests between employees and shareholders remains high (particularly due to the penchant of certain French trade unions to be driven by revolutionary socialist themes such as "class struggle" ("*lutte des classes*") questioning the legitimacy of corporate interests at all) and the constraints and economic shocks resulting from globalization and digitalization are growing, such labor law provisions (and incidentally the corporate law) have been regularly and continuously improved (even recently).

[1] This abstract relates to the article, titled in French « *Reconnaissance juridique du capital humain en entreprise, pari ou défi, remarques d'actualité* », and results from research works at University of Corsica «EMRJ- *Patrimoine et Entreprises* EA7311». It is presently released under the sole responsability of the author©.

With respect to Human Capital, it seems appropriate to concentrate on two main aspects: "governance rights" and "profit sharing" issues, both having been permanently enhanced but evidencing the social-liberal approach in France which, from the right to the left of the political spectrum, aims at developing, at the same time and moderately, "political rights" and "financial rights", emphasizing alternately one or the other option, from time to time, without a clear choice or expressed preference, while employers themselves are usually reluctant on both issues.

**Increased Governance rights and drawbacks**

7. The rationale is not (except for some of those companies which fall within the scope of the social economy (*économie sociale et solidaire – ESS*)) to change capitalism into socialism and provide for control of companies by their employees. It is, however, to share control over the management selected by the shareholders. As such, employees representatives (CE-CHSCT/CSE) benefit from expanded rights to be informed and consulted (including assistance by experts) on all (CE/CSE) or specific (CHSCT) management issues (especially in the areas of mergers with and acquisitions of other companies and changes in technology). Employees' rights may be strong enough to challenge and even supersede the shareholders' rights on the basis of mandatory permanent and direct exchange with the management and corresponding influence upon the governance. In addition –but only in companies having the form of "*société anonyme -(SA*)"- employees have the right (recently expanded to medium and large-sized companies – *ETI*) to have members of either the board of directors ( "*conseil d'administration*") or (in two-tiered management companies) the supervisory board ("*conseil de surveillance*") elected directly by the employees regardless of the level of (or even in the absence of) any shareholding and, as a separate matter, subject to the condition of having an employee shareholding of at least 3%, the right to have an employee shareholder or employee shareholders representative appointed as an employee shareholders' board member. Conversely, even in the absence of any veto right (CE/CSE's level) and the implied limitations resulting from the limited (if not symbolic) number of employees representatives at the board level, this structure of rights and prerogatives has for long be considered as a satisfactory equilibrium.

8. However, while not denying the positive contribution for years of the use of such employees' collective rights and prerogatives in considerably improving employees' status and work conditions and as a likely lateral effect of the economic crisis, it is often considered by employers as well as by experts and politicians that such employees' collective rights and prerogatives are complex and costly in terms of management of the firm and adversely affect its competitiveness. It is also said that collective bargaining suffers from an excessive influence of trade unions at the national level, while trade unions' and/or employers' representativeness is questionable at a local or individual company's level and where Human Capital is seen more as a macroeconomic item and a governmental policy stake or issue. Consequently, the result of collective bargaining at the branch or national level tends always to increase the employees' rights uniformly, meaning additional costs at the individual company's level and failing to take into account the feasibility thereof on each company's own financial situation. As a legal response, the Macron Ordinances have promulgated new rules to simplify and address the issues, including the unification of the former various employees' representatives bodies (IRP) into a single new one, the CSE, and the principle of primacy of collective bargaining at the individual company level over regional, branch or national collective agreement. Further, the upcoming loi Pacte is likely to enact provisions increasing the number of board members designated by employees (between 1/4 to 1/3) but far from allowing a parity between employees' and shareholder's board members, in the event that France try to implement the so-called German "co-determination" or "Mitbestimung" concept in French corporations. It would be fair, in order to attain this objective, to decide to expand it to companies which do not have the form of an SA and to make the necessary adaptations to corporate law extending the concept to other legal forms of share companies as well as to limited liability companies (SARL) (especially as to the requirement to have a management board) but excluding partnerships.

**Ambivalent features of Profit sharing and Employee shareholding schemes**

9. Profit sharing does exist considering the amount (generally 2/3) of the Added Value paid over by employers in terms of wages, benefits and all other mandatory or implied costs linked to employees including collective savings. The concept applies more specifically to amounts of remuneration linked to the profitability of a company (*participation & intéressement*). Profit sharing could also bridge categories of employees and shareholders and be used as a tool to recognize, financially speaking, human capital as a resource or a contributing factor equivalent to that of capital through, for instance, a payment to employees, in addition to the total amount of existing wages and other advantages or benefits, of an amount calculated proportionately to any extra dividend paid to shareholders and exceeding a pre-agreed level of return on capital (or ROCE) similar, for instance, to the one paid to shareholders in comparable companies (i.e. different from the concept of shareholder value). This was the purpose of the aborted dividend premium ("*prime dividendes*") put into place by former President Sarkozy through collective agreements and terminated by the socialist government in 2012. Besides the political issues entailed, there probably exist too many different mechanisms relating to profit sharing, with different legal and tax regimes, which would need to be simplified if the intention is to make profit sharing comprehensible for employees.

10. On the other hand and apart from the ESS sector (particularly companies set up as "*coopératives*"), Employee Shareholding has developed as a minority interest in the share capital of relevant SA, since the time of the privatizations of companies in 1983 and in furtherance of the modalities and incentives granted in relation to collective savings plans. Employee Shareholding is usually presented as a management tool to increase both the remuneration and the basic management knowledge shared with employees, which could assist in the management of a company. More incidentally it may provide additional political rights to employees depending on the adequate level of employees' shareholding, which must exceed relevant thresholds to benefit from various minority shareholders rights. This is far from the case at the current time, since such shareholding represented on an average in 2016 only 3.7% of the amount of share capital, with a few companies significantly above such amount and with the exception of two particularly militant companies, Bouygues and Eiffage, both having over 20%.

Moreover, employees' shareholding faces certain structural and cyclical issues such as: complexity of various legal and tax regimes, reluctance of employers regarding potential management rights, employees' fear of investment and the lack of funds to be invested on a long term basis and, last but not least, the financial crisis which has destroyed performance and share value. To the extent that Employee Shareholding would be a means of limiting risks of speculation and taking into greater account the social dimensions of management with respect to potential abuses by financial investors, new measures could be considered: (i) to increase the level of Employee Shareholding to a level providing it with sufficient influence and even veto right (resolution subject to a qualified majority), (ii) to extend it to companies other than those having the form of SA or which are not listed and (iii) to finance it in part through specific pension plans. It appears that most employers are not prepared to accept such changes.

**Functionalism**

11. In any event, absent any other major choice, development of the Human Capital in corporate organization in France would require both trade unions and employers to cease approaching social relations based on the overriding principles of either "*lutte de classes*" or "shareholders value", which mantras would have to be overridden by a new collective agreement reached at a corporate level approving common project and objectives of the firm –including in terms of profit sharing (and loss sharing, particularly in the case of employees shareholding) - superseding shareholders agreements and labor contracts which should then conform such a collective agreement. However, it has to be assumed that certain trade unions characterized as "reformists" and likely most of the employees would be prepared to share at a greater level the ups and downs of their company. The primacy of collective bargaining at the local level –even though limited by a number of matters reserved to the branch level (Ordinance Macron)- could be viewed as a step towards such major change, in line with the spirit of the recent punctual collective agreements entered into between employers and trade unions with the aim of strengthening jobs or even developing them in exchange for new flexible labor conditions (See: *Loi El-Khomry* 2016).

New legislation (which is unlikely to be part of the *Loi Pacte*) providing changes and necessary details to push forward on a progressive basis the level of management attributes of Human Capital in the corporate organization to a level up to parity with shareholders –while not imposing it - would be at least a positive signal that the scheme of social relations could attain a new mature yet constructive level in France in a manner which shares a common understanding of economics of the firm and mutual interest, and is more on a par with the standard of Germany and certain Scandinavian countries, and would certainly demonstrate a commitment for the future and an expectation that additional performance and value of the firm should be supportive of a possible success.