

# PRI RESPONSE TO THE AFEP-MEDEF CODE OF CORPORATE GOVERNANCE FOR LISTED COMPANIES

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## INTRODUCTION

The United Nations-supported Principles for Responsible Investment (PRI) is the world's leading initiative on responsible investment. The PRI has over 1900 signatories (pension funds, insurers, investment managers and service providers) globally with approximately US \$70 trillion in assets under management. 180 of these signatories are based in France.<sup>1</sup>

Responsible investment explicitly acknowledges the relevance to the investor of environmental, social and governance (ESG) factors in investment decision-making for the long-term health and stability of financial markets. The PRI welcomes the opportunity to contribute evidence on revisions to the Afep-Medef Corporate Governance Code for listed companies.

## ABOUT THE CONSULTATION

The Afep-Medef Code is a set of recommendations that listed companies may refer to in order to fulfil their obligations under Articles L.225-37 and L.225-68 of the French Commercial Code.<sup>2</sup> It has been adopted by most companies on the SBF120. The Code was updated in 2013 and more recently in November 2016, following the launch of a public consultation in May 2016. The current consultation has been launched to explore views on proposed amendments to the November 2016 version of the Code.<sup>3</sup>

## SUMMARY OF PRI'S CONSULTATION RESPONSE

The PRI strongly commends Afep-Medef for significant changes proposed in its revisions to the corporate governance code of listed corporations for the French market, and particularly those that place emphasis on the need for company boards consider ESG issues in long-term value creation. The PRI's overarching recommendation is that the incorporation of sustainability considerations is further developed and strengthened in the Afep-Medef Code. High quality Corporate Governance and boards that consider and manage a full breadth of sustainability issues are critical to the successful implementation of; the French Energy Transition Law (Article

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<sup>1</sup> See <https://www.unpri.org/signatory-directory/>

<sup>2</sup> <https://www.legifrance.gouv.fr/Traductions/en-English/Legifrance-translations>

<sup>3</sup> A full list of all eleven sections of the revised code that open for comment as part of this consultation is provided in appendix A.

173),<sup>4</sup> the Paris climate agreement,<sup>5</sup> commitments made at the One Planet Summit,<sup>6</sup> forthcoming changes from the European Commission Action Plan on Financing Sustainable Growth,<sup>7</sup> and ultimately, the preparedness of French companies to demonstrate leadership in sustainable business and finance. The PRI recommends greater clarity on sustainability within the Code.

We make two further overarching recommendations regarding this consultation process. Firstly, we recommend that investors are more comprehensively engaged by the Afep-Medef in drafting the Code. We welcome the public consultation as a forum for investors and other stakeholders to provide views, however, noting that the Afep<sup>8</sup> and Medef<sup>9</sup> are company representative bodies, and that investor capital and stewardship are core to companies' operation, we believe that it is important for investors to have a direct role in drafting and editing the final text of the Code. Secondly, we believe that the Afep-Medef should consider more broadly how it supports companies' understanding and implementation of the Code in order to enhance its effectiveness.

Our further answers below draw on specific expertise and evidence from the PRI's work.<sup>10</sup>

## PRI RESPONSES TO SECTIONS OF THE REVISED CODE OPEN FOR COMMENT

### Value creation and corporate purpose

#### Afep-Medef revised code section 1.4

We commend the introduction of an explicit statement that companies need to take into account ESG factors to improve long term value creation.

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<sup>4</sup> Article 173 of the French Energy Transition Law came into force on 1 January 2016. It strengthened mandatory carbon disclosure requirements for listed companies and introduced carbon reporting for institutional investors, defined as asset owners and investment managers. See [PRI's briefing on Article 173 of the French Energy Transition Law](#).

<sup>5</sup> The Paris Agreement entered into force on 4 November 2016. Parties to the agreement prepare, communicate and maintain successive nationally determined contributions (NDCs) to contribute to a worldwide effort reduce climate change. For more information see: <https://unfccc.int/process/the-paris-agreement/what-is-the-paris-agreement>

<sup>6</sup> See 12 international commitments here: <http://www.gouvernement.fr/en/one-planet-summit-new-tangible-initiatives-for-the-climate>

<sup>7</sup> One intervention proposed by Action 10 proposed by the [European Commission Action Plan: Financing Sustainable Growth](#) is that by Q2 2019, the Commission will carry out analytical and consultative work to assess: (i) the possible need to require corporate boards to develop and disclose a sustainability strategy, including appropriate due diligence throughout the supply chain, and measurable sustainability targets; and (ii) the possible need to clarify the rules according to which directors are expected to act in the company's long-term interest.

<sup>8</sup> <http://www.afep.com/en/>

<sup>9</sup> <http://www.medef.com/en/>

<sup>10</sup> See also the PRI publication [engaging on director nominations](#) specifically the section of the report which outlines [results from investors' engagement with French companies](#). Between November 2014 and June 2016, 17 investors with a collective US\$2.3bn in AUM commenced dialogue with 11 large cap listed companies in France. The report offers data on how CAC40 companies disclosed against multiple criteria, including; the percentage of women on boards, how they analyse board skills and diversity, and the proportion of companies that separated CEO and Chair roles and appointed Lead Independent directors, among other areas. It also presents' international investors' experience engaging with French boards on these issues.

We welcome the statement that it is the role of the board to propose ‘any statutory change to the corporate purpose that it deems appropriate’ in the context of companies’ consideration of ESG issues and long term value creation.<sup>11</sup>

## Tasks of the board and review of the opportunities and main risks

### Afep-Medef revised code section 1.6

We welcome the introduction of section 1.6 of the Code. We recommend clarified wording for section 1.6 of the Code, to reflect that the board should take ESG factors into account as opportunities as well as risks.<sup>12</sup>

## Non-discrimination and diversity

### Afep-Medef revised code section 1.7

We welcome the introduction of section 1.7 of the Code. We recommend that the scope of this diversity provision is expanded beyond ‘a balanced representation of men and women’ only, to also encourage diversity of skills and qualifications. We recommend that companies describe, in their public reporting, how incumbent board members and new candidates enhance board diversity.

## The board and communication with shareholders

### Afep-Medef revised code section 4.2

We welcome the introduction of section 4.2 regarding recommendations for how companies manage shareholders’ access to the board of directors. We recommend that it is further strengthened in three main ways, to:

- 1) Clarify wording from ‘may’ to ‘should’ to state that shareholders access to the board ‘should’ be entrusted to the Chair (or Lead Director). This is to remove any notion of optionality for the board to deal with shareholder’s requests for board access.
- 2) Expand shareholders access to engage the board on a range of issues that impact long term value creation of the company, not limited to matters of corporate governance only.
- 3) Clarify that other board members may engage with shareholders as appropriate. It should note that the Chair, Lead Director or other the initial contact point at the board may distribute meetings among board members as relevant to their expertise (for example, to the chairperson of a specific committee).

The PRI has recently produced ‘a practical guide to active ownership in listed equity’<sup>13</sup> which encourages PRI signatories to incorporate ESG issues into their ownership policies and practices, including engagement with companies and exercise of voting rights. It demonstrates how stewardship and focus on ESG issues is an effective tool to support long-term value creation in

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<sup>11</sup> We note that that the French government is currently considering the creation of a new legal status for companies with an extended social purpose (Société à Objet Social Étendu). This would make it possible for companies to state in their articles of association that, in addition to generating profit, its core objectives may include ESG considerations (e.g. positive impact for employment or the environment). This adaptation of the Code should not behave as a substitute for concurrent actions being led on behalf of the Government by Messieurs Nicole Notat and Jean-Dominique Senard. Their proposals will feed into the bill of the Action Plan for the Growth and Transformation of Enterprises (PACTE) to be presented in Cabinet on April 18, 2018. See further [here](#).

<sup>12</sup> See appendix B for the translation of the wording in full as it currently reads.

<sup>13</sup> See the PRI’s publication: [a practical guide to active ownership in listed equity](#)

listed equity investing, and provides examples of what may be considered as best practise disclosure. The PRI also provides guidance on how corporate bondholders may engage with companies on ESG issues.<sup>14</sup> These resources may serve as a useful reference for Afep-Medef to underline the importance of board access to enable investors to engage with companies on ESG issues for long-term value creation.

## Clarity and transparency of information

### Afep-Medef revised code section 10.1

We welcome section 10.1 that recommends companies disclose the number of meetings of the board of directors and any relevant information relating to directors' *individual* attendance at such meetings. It is important for investors to use this information as a proxy for whether individual directors are committing the requisite time and attention to their board duties.

### Afep-Medef revised code section 13.4

We welcome section 13.4 that recommends companies disclose reasons for the appointment of a new director to the general meeting of shareholders, in addition to their biographical information and curriculum vitae. We believe that the Afep-Medef should also recommend this disclosure for the renewal of incumbent board members, and that companies use board evaluation matrices to identify the qualifications, attributions, skills, and experience the company seeks to be represented on the board, and how new and incumbent board members fulfil these criteria.

## Executive officers' compensation

### Afep-Medef revised code 24.1.1

We welcome the addition to the Code that notes companies should consider social and environmental factors when determining compensation. We believe that executive pay should be aligned with performance and long-term strategy in order to protect and create value.

Specifically, the PRI recommends that the Code should support executive remuneration that drives long-term sustainable performance by encouraging companies to undertake the following steps:

1. Adopt a process to identify relevant ESG metrics and ensure these are a meaningful component of the overall remuneration framework.
2. Disclose information about the rationale, method and challenges faced when incorporating ESG metrics into executive pay.<sup>15</sup>

## Proposed procedure for revising the Code

In the interest of transparency we support the proposal for public consultation processes to be enshrined in the Code. In addition, we recommend that Afep-Medef publicly disclose how responses received to the consultation are analysed and considered in order to update the Code.

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<sup>14</sup>See the PRI's publication: [ESG engagement for fixed income investors](#)

<sup>15</sup> See PRI publication '[Integrating ESG issues into executive pay](#)'

## APPENDIX A

All eleven areas as presented for comment in the 2018 Afep-Medef Code consultation.

- **Value creation and corporate purpose (section 1.4)**

At a time when the government has launched a broad debate on the tasks of the company and on its corporate purpose, Afep and Medef wanted to highlight the theme of CSR in the corporate governance code of listed corporations due to the growing importance of non-financial issues in companies' strategies. Consequently, following the example of what appears in foreign codes, the role of the Board in improving the long-term value creation of the company is specified, taking into account the social, societal and environmental dimensions of its activities. The Board may also propose to the general meeting of shareholders any statutory change to the corporate purpose that it deems appropriate. Given its importance, the paragraph relating to the tasks of the Board is placed at the beginning of the code.

- **Tasks of the Board and review of the opportunities and main risks**

It is proposed to underline the necessity of a review of the opportunities and main risks by the Board of Directors. This risk review shall go hand in hand with closely monitoring the quality of the information delivered publicly.

- **Non-discrimination and diversity (section 1.7)**

It is proposed that the Board should carry out specific verifications regarding non-discrimination and diversity, ensuring that the executive officers implement a policy in these areas, notably with regard to the balanced representation of men and women on the leadership bodies beyond the Board of Directors.

- **Lead director (section 3.2)**

In the event of the combination of the offices of Chairman and Chief Executive Officer, it is indicated that the Board may appoint a Lead Director from among the independent directors.

- **The Board and communication with shareholders (section 4.2)**

To respond to demand from institutional investors, it is proposed that shareholders' access to the Board of Directors on corporate governance matters should be entrusted to the Chairman of the Board of Directors or, if applicable, the Lead Director, the latter having to report to the Board on this task.

- **Directors representing employees (section 1.7)**

To ensure the presence of directors representing employees precisely where the strategic decisions are made, it is proposed that they should be appointed within the company that applies the code. When several listed companies from the same group apply the provisions of the code, it is up to the Boards to determine the company or companies eligible for this recommendation.

- **Clarity and transparency of information (section 10.1 and 13.4)**

To enhance transparency with regard to shareholders and to respond to demand from the French Market Authority and institutional investors, it is proposed that the annual report should mention the attendance level of each director at meetings of the Board and at Board committees. Furthermore, to enable informed voting by shareholders when appointing a director, the company should state the reasons for proposing his or her appointment to the general meeting of shareholders.

- **Conflicts of interest (section 19)**

It is proposed to strengthen the recommendations regarding ethical rules for directors by adding that, in the event of a conflict of interests, the director, who must already abstain from voting on the related resolution, should abstain from attending the debate.

- **Executive officers' compensation (section 24.1.1)**

In order to take CSR considerations into account in determining executive compensation, § 24.1.1 is supplemented accordingly.

- **Composition and tasks of the High Committee on Corporate Governance**

It is proposed to specify and enhance the composition and tasks of the High Committee. Consequently, notably to enable a better balance between men and women on the HCGE, it is proposed that from now on the executive officers may be appointed from among individuals who either hold or have held directorships within companies that refer to the code, without requiring them to have held executive office. Furthermore, and to give greater prominence to the recommendations made in relation to matters addressed by or referred to it, the High Committee could propose amendments to the code in the light thereof.

- **Proposed procedure for revising the code**

Since the code was revised in November 2016, the consultation procedure has been public. It is proposed that this practice should be enshrined in the code.

## APPENDIX B

A table that demonstrates the comparison between the November 2016 Code and the proposed revisions can be seen [here](#).<sup>16</sup>

Below are excerpts from the proposed revised code where PRI has provided comment.

### **1. THE TASKS OF THE BOARD OF DIRECTORS**

*1.4 [The board] endeavours to improve the long-term value creation of the company, notably by taking into account the social, societal and environmental dimensions of its activities. It proposes any statutory change to the corporate purpose that it deems appropriate.*

*1.7 [The board] ensures 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 leadership bodies.*

### **10. MEETINGS OF THE BOARD AND OF THE COMMITTEES**

*10.1 The number of meetings of the Board of Directors and of the Board committees held during the past financial year is mentioned in the annual report, which also provides the shareholders with any relevant information relating to the directors' individual attendance at such meetings.*

### **13. DURATION OF DIRECTORS' TERMS OF OFFICE**

*13.4 When the general meeting of shareholders is asked to appoint a director or extend his or her term, the booklet or the notice calling the meeting of shareholders should, in addition to the items required by statute, contain biographical information outlining his or her curriculum vitae as well as, in the event of appointment, the reasons for proposing his or her appointment to the general meeting of shareholders.*

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<sup>16</sup> [http://consultation.codeafepmedef.fr/z\\_docs/tableau\\_comparatif\\_EN.pdf](http://consultation.codeafepmedef.fr/z_docs/tableau_comparatif_EN.pdf)

## **24. COMPENSATION OF COMPANY OFFICERS**

### **24.1 Principles for the determination of the compensation of executive Officers and the role of the Board of Directors**

#### **24.1.1 Role of the Board of Directors**

*The Board must debates the performances of the executive Officers in the absence of the interested parties. The Board of Directors which appoints the executive Officers is responsible for determining their compensation on the basis of proposals made by the compensation committee. The Board provides reasons for its decision in such matters. The compensation of these directors must be competitive, adapted to the company's strategy and context and must aim, in particular, to improve its long- term performance and competitiveness over the medium and long term, notably by integrating social, societal and environmental responsibility considerations. The compensation must make it possible to attract, retain and motivate high-quality directors.*