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Corporate officers have a duty of loyalty with respect to sales of shares

In a decision dated April 12, 2016[1], the Commercial Chamber of the *Cour de Cassation* (French Supreme Court) clarified the scope of a well-established case-law according to which corporate officers/members of company boards, who are bound by a duty of loyalty towards their shareholders, must disclose to the shareholders wishing to sell them their shares any and all information that is likely to influence their judgment.

The *Cour de Cassation* specified that corporate officers/members of company boards are merely required to disclose to such shareholders the information that is known only to them, thereby considering that the selling shareholders themselves must also inquire about the terms and conditions governing the sale of their shares.

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Relying on the principle of good faith[2] and US principles of corporate governance, the *Cour de Cassation* has been delineating in recent years the contours of the duty of loyalty imposed on a corporate officer/member of a company board towards the shareholders wherever he/she decides to acquire shares held by the latter.

This duty of loyalty translates into the obligation for the company manager/member of company boards to provide selling shareholders with any information that is likely to influence their judgment. By virtue of his/her duties, a company manager/member of a company board has access to information that is unknown to others, and must provide such information to the company's shareholders who intend to sell their shares.

Under this principle, French courts have ruled that a corporate officer/member of a company board breaches

his/her duty of loyalty whenever he/she merely provides the shareholders with accounting documentation and refrains from drawing their attention to the elements likely to affect the price of the to-be-transferred shares[3]. In another case, a corporate officer was convicted for having concealed the existence of on-going negotiations concerning the subsequent purchase of the shares by a third party, and resold such shares to such third-party at a much higher price[4].

Breach by the company manager/member of a company board of his/her duty of loyalty is sanctioned, as a fraudulent concealment, by the cancellation of the sale or by the award of damages to the aggrieved shareholders. The amount of damages is usually determined on the basis of the capital gains earned by the company manager/member of a company board from the resale of the shares to third-parties[5].

The April 12, 2016 decision is consistent with this line of decisions and provides clarification on the information that must be disclosed by a corporate officer/member of a company board who desires to acquire shares from the company's shareholders.

In that specific case, minority shareholders had sold their shares to the Chairman of the Supervisory Board of a French *société anonyme* (joint stock corporation) and to some members of such Board. Subsequent to the sale, all of the company shares were acquired by another corporation at a price per share that was substantially higher than that paid to the minority shareholders.

In these circumstances, the minority shareholders considered that the Board members had breached their duty of loyalty by concealing the contemplated resale of the shares – an information that was likely to influence their judgment. As such, they sued them and sought damages.

The trial judges upheld the minority shareholders' claim for damages, pointing out that the purchaser of the shares, in their respective capacity as Chairman and members of the Supervisory Board could not possibly be unaware of the contemplated subsequent acquisition of such shares by another corporation. Consequently, they considered that the board members who acquired the shares should have informed the selling shareholders of the conditions in which the offered price had been valued.

Yet, the *Cour de Cassation* quashed the judgment handed down by the trial judges.

It considered that, for corporate officers/members of a company board to be ordered to pay damages for fraudulent concealment, it must be established that they had in their possession information that could only be known to them and that was likely to affect the judgment of the selling shareholders. It also specified that, in that specific case, the negotiation for the subsequent acquisition of the company had not started at the time the board members acquired the shares of the selling shareholders.

In this context, there was no justification for ordering the board members to pay damages for fraudulent concealment.

Through this decision, the *Cour de Cassation* limits the cases where liability of corporate officers/members of company boards who acquire shares of shareholders can be sought for fraudulent concealment, and lays down the principle that the information to be disclosed is the information that no one else knows about.

This decision waters down the duty of loyalty imposed on corporate officers/members of company boards.

As such, the liability of a corporate officer/member of a company board may no longer be sought wherever it is established that the information he/she had in his/her possession in relation to the purchase of the shares of a shareholder was also available to the latter, or that the latter could himself/herself obtain such information.

It is hence up to the selling shareholders themselves to inquire on the terms and conditions surrounding the sale of his/her shares, in particular the market situation and the condition of the company.

[1] Commercial Chamber of the *Cour de Cassation*, April 12, 2016, n°14-19.200 14-20.529 14-20.844

[2] The principle of good faith is recalled in Article 1134 of the French Civil Code

[3] Commercial Chamber of the *Cour de Cassation*, May 6, 2008, n°07-13198

[4] Commercial Chamber of the *Cour de Cassation*, February 27, 1996, n°94-11.241; Commercial Chamber of the *Cour de Cassation*, May 12, 2004, n°00-15.618

[5] Commercial Chamber of the *Cour de Cassation*, March 12, 2013 n°12-11970