Universität Zürich[UZH]

Current Trends in Corporate Law

Principles of Corporate Law – Autumn Semester 2025
Lecture 12

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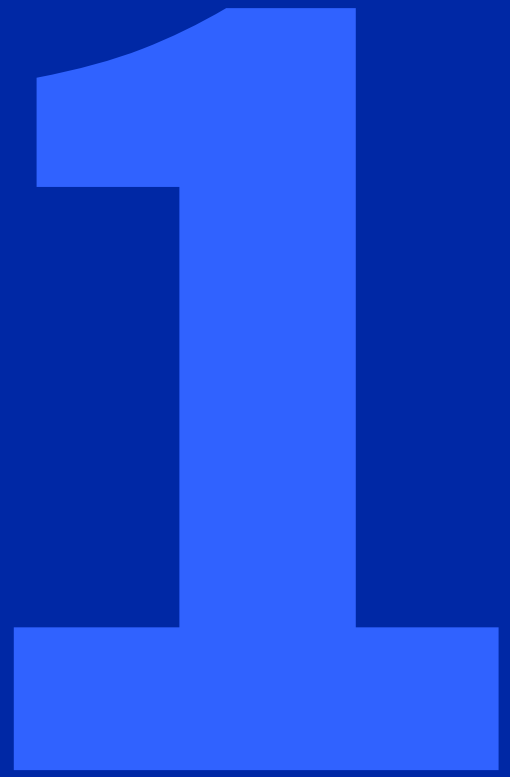
Corporate Governance - Repetition



What is Corporate Governance?

FSB: "*Corporate governance involves a set of relationships between a company's management, board, shareholders and stakeholders. Corporate governance also provides the structure and systems through which the company is directed and its objectives are set, and the means of attaining those objectives and monitoring performance are determined.*"

- Rules that:
  - govern how principals direct and monitor their agents;
  - how to operate a company.
- Concerns relationship among:
  - Management
  - Employees
  - Board of Directors
  - Controlling Shareholders
  - Minority Shareholders
  - Stakeholders
- Corporate Governance is a vast topic covering different internal and external aspects of how companies operate.

Corporate governance has been expanded to include more topics than the traditional understanding of the term

Traditionally, Corporate Governance addresses:

Divergence of interests	Incomplete contracts	Informational asymmetry	The expropriation problem (capital friction)
Principal-agent problem, Seperation of ownership & control Jensen & Meckling (1976), Berle & Means (1932	Impossibility to create contracts that account for every eventuality Grossman & Hart (1986)	The market for lemons (insider information), undervalued companies Akerlof (1970)	Why should an investor hand over cash to a manager? Shleifer & Vishny (1997)

In a nutshell:
Jensen & Meckling: The Manager doesn't own the money, so they are rationally tempted to waste it. Governance checks that impulse.
Oliver Hart: We can't write a perfect contract for the future. Governance fills the gaps when the rules run out.
Shleifer & Vishny: Investors are scared of being robbed. Governance is the set of rules that convinces them it's safe to write the check."

More recent additions include expansions of this basic idea, e.g.:

Stakeholder theory (not just one principal)	Redefining what value means (ESG, social aspects purpose of the firm)	Expanding on information (non-financial reporting)	Expanding on “capital” DEI and social trust to operate

Why Corporate Governance?

More concretely, in practice:

- Solving commitment problem:
  - high governance standards attract investments;
  - after capital has been raised, incentive to weaken governance to extract more benefits;
  - laws and regulations ensure that commitment to high governance standards are maintained.
- Value Creation:
  - good corporate governance enhances (long-term) performance of companies.
- Corporate Social Responsibility:
  - concerns about negative externalities caused by companies.
  - a company‘s purpose is not just to make profit but to have positive impact on society and environment.

Corporate governance can be understood to include five key topics, according to the Organisation for Economic Co-operation and Development (OECD)

Long-term Sustainability
CIntegrating environmental and social viability into core business strategy.

Accountability and Transparency
Ensuring accurate, timely disclosure to build systemic market trust

Protection of Stakeholder interests
Recognizing rights established by law to create sustainable long-term value..

Legal and Regulatory Compliance
Navigating the shift from voluntary codes to mandatory enforcement framework.

Risk Management
Aligning risk appetite with strategy to ensure organizational resilience.

Ongoing debates in Corporate Governance

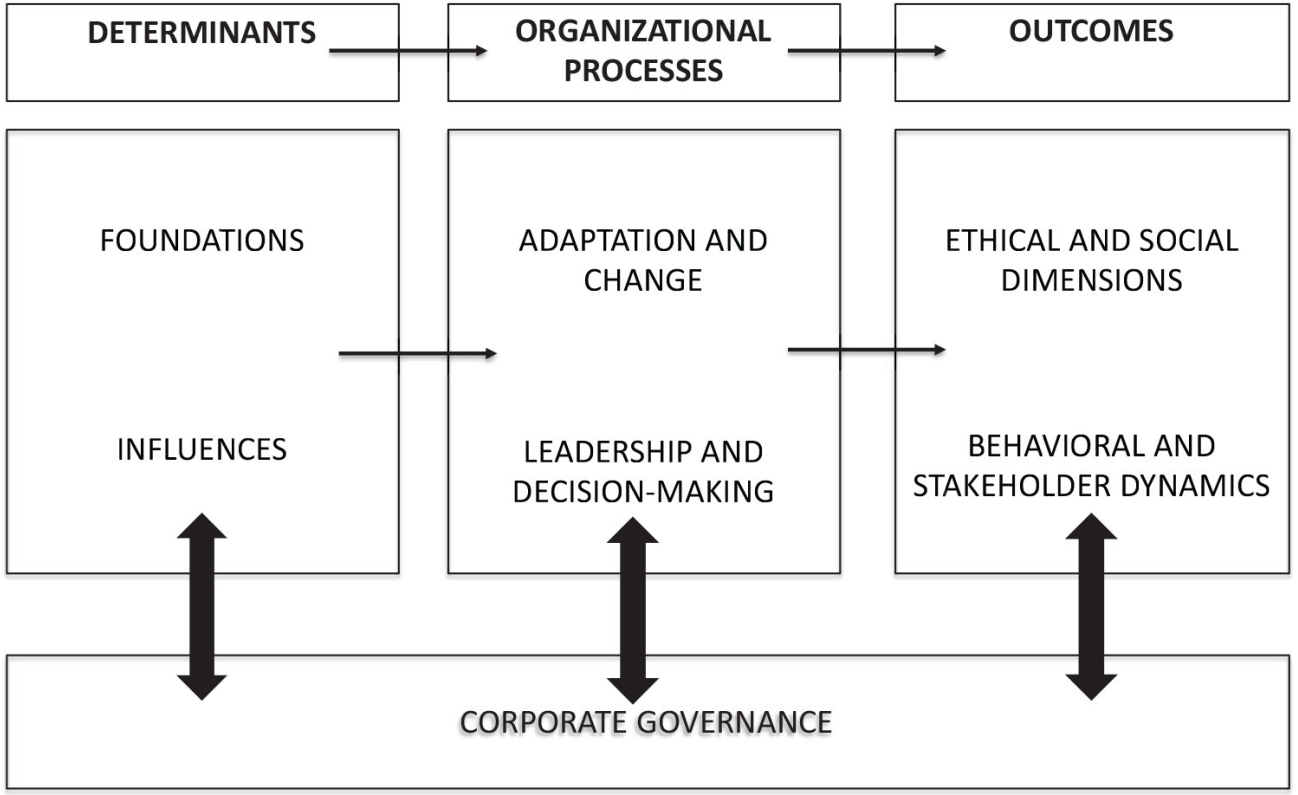
Shareholderism vs. Stakeholderism	Long-term vs. Short-term	Accountability
• In whose interest should company act?	• Focus on short-term profitability? • Focus on long-term sustainability?	• Accountability only towards shareholders? • Accountability towards all stakeholders?

→ ***Ongoing debates all link back to core question of company purpose***

Trends in Corporate Governance

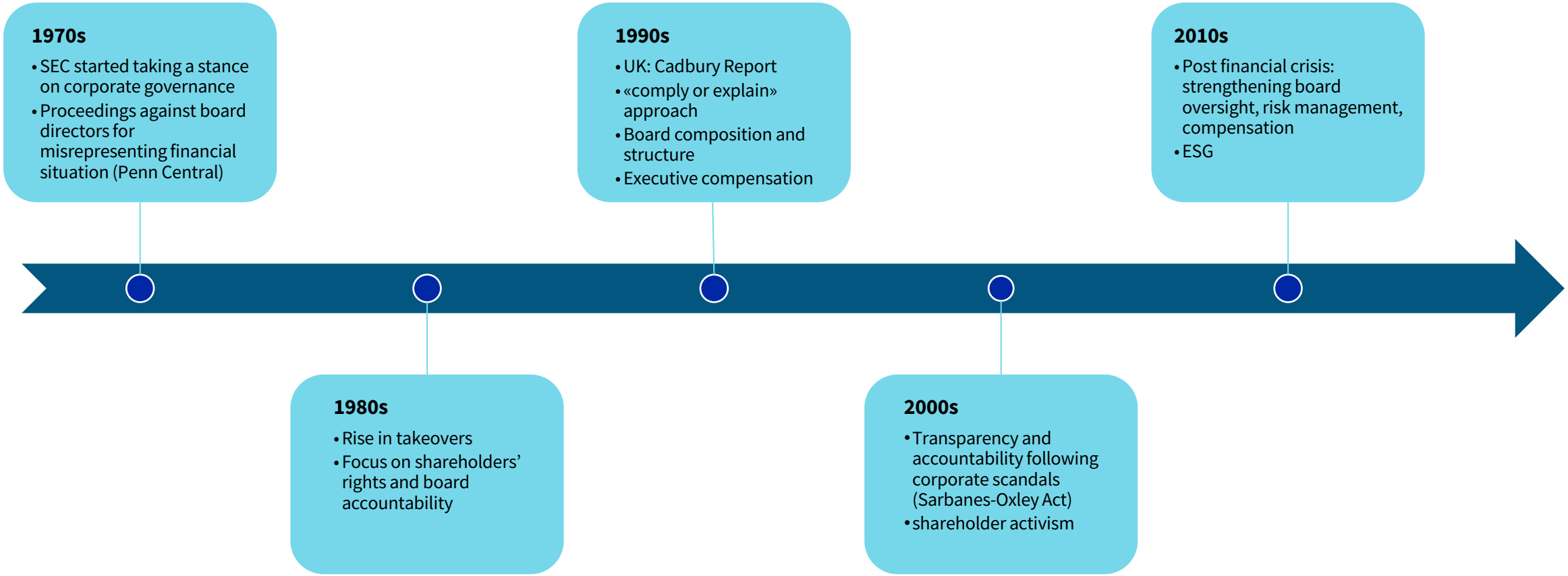
How are corporate governance trends shaped?

- Determinants
  - Factors influencing corporate governance structures and practices
- Organizational processes
  - The mechanisms and dynamics through which governance is enacted
- Outcomes
  - Results or consequences of corporate governance on organizational performance and stakeholder well-being



Source Figure: Toward an updated corporate governance framework: Fundamentals, disruptions, and future research - Ruth V Aguilera, Maria Ruiz Castillo, 2025

Past trends show an increasing focus on corporate governance and topics concerning social and environmental issues



Looking forward – new trends

- **The future of ESG**
  - ESG Backlash
- **Regulatory Arbitrage**
  - Corporate Governance as way to attract companies

Source: https://www.regcompliancewatch.com/esg-backlash-not-yet-weighing-on-ias-survey-finds/

Source: https://www.risk.net/our-take/7960519/thin-skinned-are-ccps-skimping-on-capital-cover

The Future of ESG in Corporate Governance

Rise of ESG

- ESG moved to forefront on corporate governance in the 2010s
  - Adoption of Paris Agreement
  - United Nations Sustainable Development Goals
- EU as leader
  - As part of EU Green New Deal new ESG Regulations and Directives introduced in EU
    - Sustainable Finance Disclosure Regulation
    - Corporate Sustainability Reporting Directive
    - Corporate Sustainability Due Diligence Directive
- Most major companies committed to sustainability strategies, net-zero goals and diversification programs

ESG Backlash

- Growing critique on ESG and ESG related governance
  - Inconsistent implementation / virtue signalling
  - Greenwashing
  - Unworkable concepts because politicize corporate decision-making
  - Focus always on maximizing shareholder value. If ESG aligned with this, it will be implemented, if not it will be ignored

Examples of anti-ESG efforts

- “anti-ESG” laws
  - over 100 bills opposing ESG introduced by US state legislators in 2025
    - Restricting investment standards for public funds
      - Prohibition to consider ESG or Diversity, Equity and Inclusion (DEI) in investment decision (e.g. Arkansas House Bill 1507)
    - Restring ESG consideration in private sector
      - Prohibition to use ESG criteria to determine whether services are granted (e.g. Georgia House Bill 1018)
      - Prohibition for proxy advisors to make judgments based on ESG and DEI (e.g. Texas’ Senate Bill 2337)
- Court Challenges
  - US Supreme Court overturns Chevron Deference (Loper Bright v. Raimondo) diminishing judicial deference toward federal agencies.
  - Appeals Court rejects Nasdaq SEC-approved listing rules requiring companies to disclose board diversity.

And in the rest of the world?

- EU
  - EU Parliament voted to scale back corporate sustainability laws
    - Higher thresholds for application of Corporate Sustainability Reporting Directive and Corporate Sustainability Due Diligence Directive
      - CSRD will now only apply to companies with more than 1,750 employees and 450 million euros (over $523 million) in revenue
      - CSDDD will only apply to even larger companies, with more than 5,000 employees and 1.5 billion euros (over $1.7 billion) in net revenue
    - Simplifying ESG laws and delay implementation until 2028
  - Switzerland
    - Asset Management Association published updated self-regulation on transparency and disclosure for sustainability-related collective assets on 18 September 2025.
      - Updated framework to strengthen sustainable finance in Switzerland.
      - Using ESG integration, exclusion or voting strategies alone no longer sufficient to qualify as sustainable fund. evidence based Sustainability Approach required (best in class/positive screen, impact investment, climatig-alignment etc.).

Old wine in new bottles?

- Critique of ESG corporate governance follows existing debates on effective corporate governance
  - e.g. Shareholderism vs. Stakeholderism or short-term vs. long term trade-offs.

- In shareholder-centric, short-term perspective of corporate governance, ESG does not seem to have a place.

- Is this correct?
  - Short-term profits with ESG investments?
  - Possible to be in shareholders' interest to incorporate ESG principles in corporate governance?

Consequences?

- More noise than action?
  - Most of anti-ESG bills in the US were either not passed or watered-down.

- Greenhushing?
  - Companies refrain from making public commitments to ESG but continue to implement ESG efforts in corporate governance

- Recalibration?
  - Focus ESG corporate governance away from branding towards strategic decision making on long-term resilience

Regulatory Arbitrage

Corporate Governance as tool to attract business

- Favourable corporate governance frameworks are being used by jurisdictions to become a more attractive place for incorporation.
- Longstanding debate on value of competition between corporate laws:

	Race to the Top (Advocates)	**Race to the Bottom (Critics)**
The Core Argument	Competition produces efficient laws that protect shareholders, increasing firm value.	Competition produces lax laws that protect managers, sacrificing shareholder value.
The Mechanism (How they win business)	**Strong Shareholder Rights** • Clear Fiduciary Duties • Efficient Courts (e.g., DE Chancery) • Easier to replace bad management	**Managerial Entrenchment** • Anti-Takeover Defenses (Poison Pills) • Liability Shields for Directors • Harder to fire the CEO
Outcome	High Shareholder Value	High Managerial Job Security
Key Literature	**Winter (1977)**; Easterbrook & Fischel	**Cary (1974)**; Bebchuk (1992)

What actually drives the decision?

Governance is powerful, but it doesn't happen in a vacuum. Companies optimize for a "Bundle" of factors.

Other reasons why corporations might choose a certain jurisdiction:

- Corporations treat jurisdiction as a strategic product to be selected rather than a fixed geographic constraint
- Firms increasingly decouple legal domicile from physical headquarters to optimize for distinct competitive advantages
- Strategic selection has evolved from simple tax minimization to a complex weighting of judicial predictability and socio-political alignment
- This competition compels states to differentiate their regulatory environments, effectively creating a marketplace for corporate charters and operational bases
- Modern site selection therefore prioritizes a holistic ecosystem approach, balancing immediate fiscal incentives against long-term operational resilience

Legal & Governance

- Specialized business courts mitigate judicial risk through consistent and expert adjudication
- Robust liability shields and indemnification provisions protect directors from personal exposure in litigation
- Legislative frameworks define the scope of fiduciary duties and the Board's ability to resist short-term activist pressure
- Statutory anti-takeover mechanisms serve to entrench management or enable long-term strategic pivoting

Finance

- Corporate tax regimes act as direct determinants of net profitability and capital allocation efficiency
- Personal income tax structures function as critical retention levers for C-suite executives and high-net-worth talent
- Regulatory efficiency lowers the opportunity cost of capital deployment by accelerating operational timelines
- Fiscal incentives such as tax holidays or grants act as immediate catalysts for relocation decisions

Operations

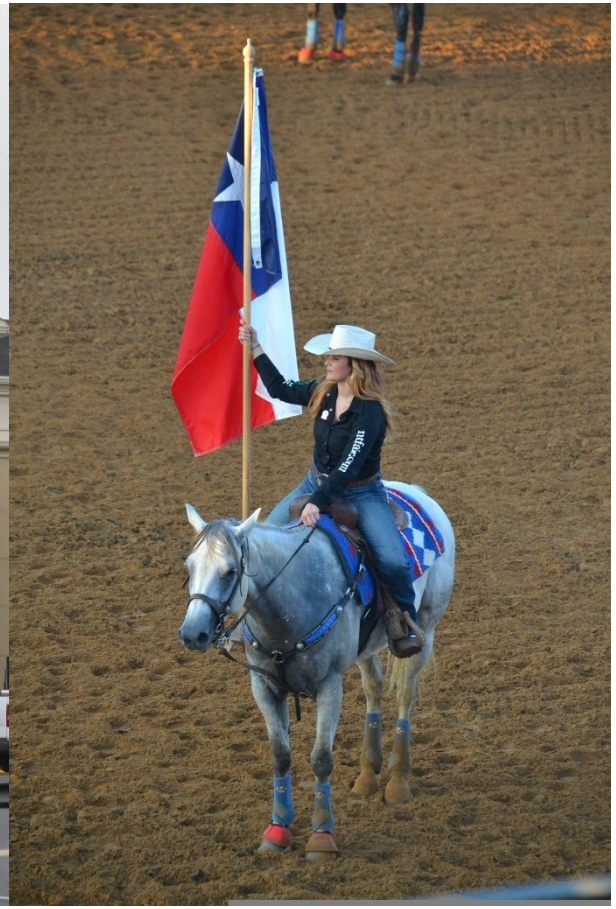
- Industrial agglomeration facilitates access to specialized labor pools and knowledge spillovers within clusters
- Labor market regulations regarding non-compete enforceability dictate the fluidity of talent acquisition
- Regional cost-of-living indices directly impact workforce purchasing power and wage inflation pressures
- Infrastructural resilience serves as a prerequisite for high-uptime manufacturing or data operations

Culture

- Alignment between legislative priorities and corporate strategy minimizes political friction with the host state
- Ideological congruence between state governance and executive leadership reinforces organizational ethos
- Social license to operate is secured through community receptivity rather than adversarial local activism
- Jurisdictional branding serves as a market signal regarding the firm’s innovative capacity or institutional stability

Case Study: Texas strive to take on Delaware

- Developments in Texan corporate laws aimed at challenging Delaware's supremacy.
- Successful?
  - Chevron
  - Coinbase
  - Space X
  - Tesla



Delaware vs Texas

	Delaware	Texas
Tax	Low corporate taxes	Low corporate taxes
Court System	Well established case law and specialized courts	Power to provide advisory opinions Only recently launched specialized court system (Texas Business Court)
Corporate Governance	Delaware General Corporation Law (DGCL)	Texas Business Organizations Code

Overview Delaware

Expertise (Judiciary)

- Home of the specialized Court of Chancery
- Decided by expert Chancellors without juries
- Rapid resolution of complex commercial disputes

Certainty (Precedent)

- Granular guidance on fiduciary obligations
- High predictability reducing litigation risk
- Consistent interpretation of corporate statutes

Cost (Premium)

- Annual franchise tax based on share capital
- Maximum tax bill capped at approximately 250k annually
- Recurring cost independent of corporate income

Trust (Signal)

- Universal investor familiarity lowers diligence costs
- Eliminates valuation discounts regarding legal risk
- Standardized rights attract institutional capital

Overview Texas

Expertise (Judiciary)

- New specialized Texas Business Court (2024)
- Appointed judges with corporate expertise
- Designed to rival Delaware's efficiency

Certainty (Precedent)

- Codified Business Judgment Rule in statute
- Lack of historical case law creates risk
- Outcomes are currently less predictable

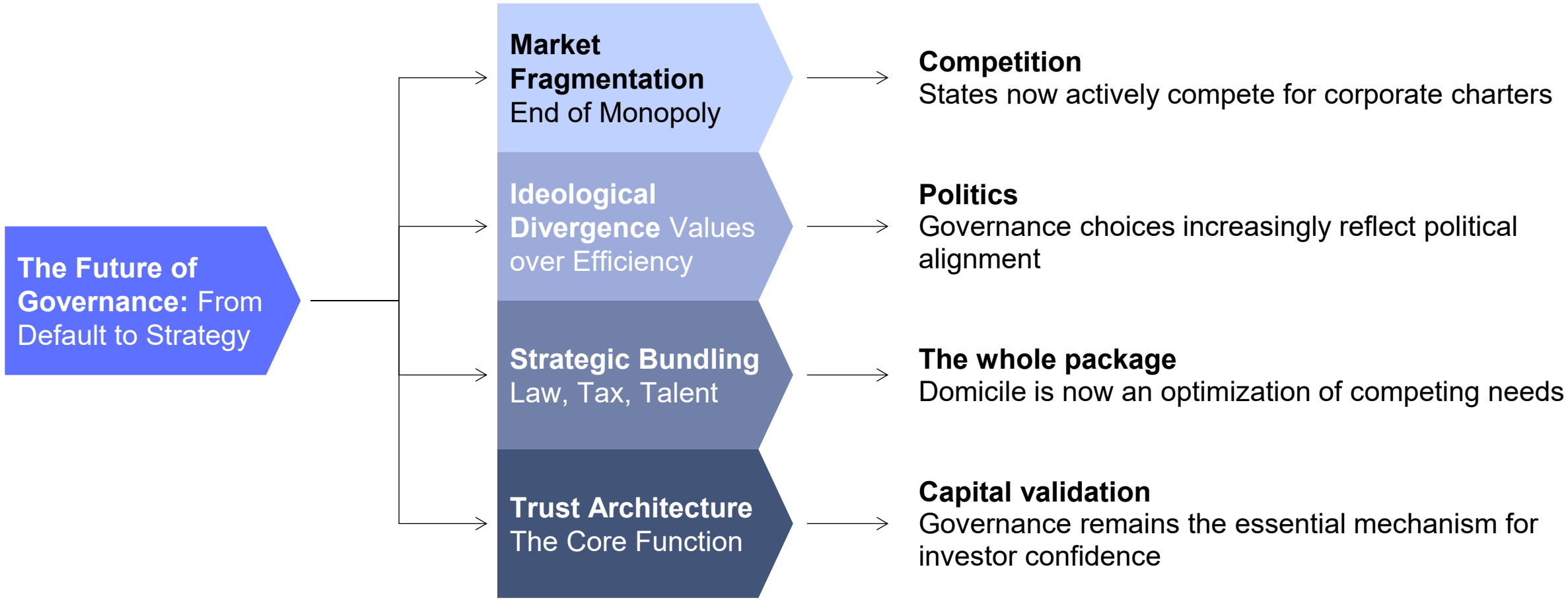
Cost (Premium)

- No state level corporate income tax on profits
- Margin Tax applied to gross receipts
- Avoids premium franchise fees for legal status

Trust (Signal)

- Signals alignment with founder control mechanisms
- Markets resistance to ESG driven judicial activism
- Aligns domicile with a broader deregulation ethos

Conclusion: Delaware vs Texas



Elon Musk’s compensation package: What happened?

Overview

- In 2018, Tesla offered Musk stock options worth up to $56 billion (see also Lecture 8).
- A shareholder filed a lawsuit against the compensation plan, arguing that
  - Musk had excessive influence behind the scenes over the approval process
  - Tesla failed to disclose that some of the people responsible for the decision at Tesla had close ties to Musk
- A Delaware judge has ruled in favor of the plaintiff, invalidating the pay package
- Move to Texas
  - Musk pushed to move Tesla to Texas
  - Tesla is now officially incorporated in Texas
  - A new Texas law strengthened corporate protections and helped revive Musk’s compensation plan after the Delaware ruling.

Key changes in Texas Business Code

Overview

- Texas has implemented significant changes to the Texas Business Organizations Code (TBOC)
- Objective: Make Texas more attractive to corporations by reducing litigation risks and providing clearer governance

Senate Bill 29 – Corporate Governance and Liability Changes

- Codification of the Business Judgement Rule (“BJR Statute”)
  - presumption that directors act in good faith and in the corporation’s best interests
- Protections for certain activities involving conflicts of interest
- Minimum ownership threshold for shareholders to bring derivative actions
  - Weakening of shareholder rights
- Allows for waiver of jury trials and exclusive venue provisions

Key changes

Senate Bill 1057 – Increased Thresholds for Shareholder Proposals

— Shareholders must reach a specific threshold to submit proposals

— Proposals must be supported by a majority of voting shareholders

Senate Bill 2411 – Officer Liability and Transaction Approvals

— Amendments addressing officer liability, merger approvals, and transaction administration

— Expanded exculpation to officers acting within the scope of their professional duties

— Provides procedural clarity for the approval of major transactions, such as mergers, without the need for final documents

Senate Bill 2337 – New Requirements for Proxy Advisors

— Proxy advisors must disclose when recommendations are based on non-financial factors (e.g. ESG)

Corporate Governance Trends in Texas

Context and implications of the new Texas Law

- Restrictions on shareholder lawsuits
  - Since almost no investor reaches this threshold, companies are effectively protected from shareholder lawsuits
  - Tesla immediately took advantage of this law
- Restrictions on shareholder proposals
  - This particularly affects activist investors
  - E.g. such as those pushing Exxon Mobil to take action on climate change
- Restrictions on proxy advisors
  - Proxy advisors must publicly declare that they have placed “non-financial factors” above shareholder interests when considering ESG aspects – effectively a means of pressure to prevent recommendations against management
  - ISS and Glass Lewis are taking legal action against this

Corporate Governance Trends in Texas

Context and implications of the new Texas Law

- Companies have more power and less control
- Strategic attempt to lure companies away from Delaware
- **“regulatory race to the bottom”**
  - significantly water down shareholder protections (and reduce shareholder rights)
  - strengthen management power
- Limiting shareholder proposals and lawsuits
  - weakened shareholder rights increase investment risk and make American companies less attractive
- Texas may be overstepping legal boundaries by applying governance rules to companies that only have their headquarters in Texas but are not incorporated there—which is likely to lead to lawsuits
- The combination of deregulation with culture war elements (e.g., anti-ESG) could ultimately make Texas less attractive than Nevada

Corporate Governance Trends in Texas

Has Texas gone too far?

- Texas may be overstepping legal boundaries by applying governance rules to companies that only have their headquarters in Texas but are not incorporated there—which is likely to lead to lawsuits
- The combination of deregulation with culture war elements (e.g., anti-ESG) could ultimately make Texas less attractive than Nevada
    - Texas may inadvertently end up scaring corporations who don't want their E.S.G. efforts to pose a legal risk

Legal questions:

- Glass Lewis and Institutional Shareholder Services, two leading proxy advisers, have sued Texas, claiming its law that regulates the advice of proxy advisers violates their First Amendment right to free speech
- Its regulation of proxy advisers and shareholder proposals applies to companies headquartered, but not incorporated, in Texas. That's a departure from the longstanding principle that a company's corporate governance falls under the laws of the state in which it incorporates, regardless of where it is physically based
- Applying a corporate governance law so broadly is an attempt by Texas to "trump" the corporate governance laws of other states
- The move is likely to be challenged in courts

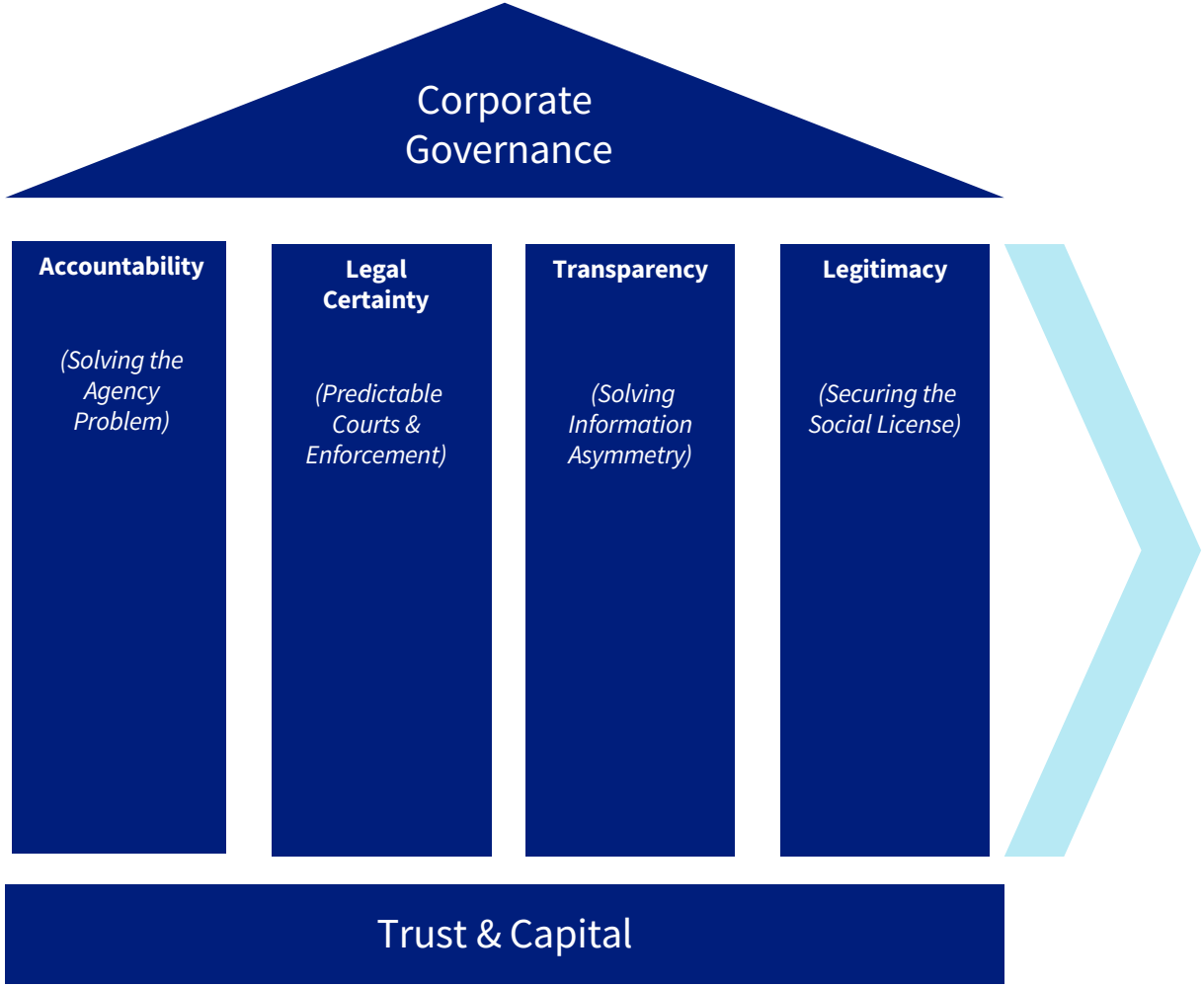
Discussion

Questions

- From a corporate governance perspective: What changes do these amendments bring?
  - 3%-Rule: Shareholder rights are weakened
  - E.g. at Tesla, there are only 3 investors who can clear this hurdle
- Does increased flexibility improve or weaken governance quality?
- Is the move from Delaware to Texas likely to reshape U.S. incorporation trends?
- Has Texas gone too far?

Conclusion

Key takeaways include the four most important aspects of corporate governance, but also how this information is crucial for your future careers



Why This Matters for Your Career

1. **Governance Drives Valuation:**
   It is a financial variable, not merely a compliance exercise. Companies with strong governance structures enjoy a lower cost of capital because investors price in lower risk.

2. **Jurisdiction is a Strategic Choice:**
   The "Default to Delaware" era is ending. You must now treat legal domicile as an active strategy, optimizing for either predictability (Delaware) or flexibility (Texas).

3. **The Risk Landscape has Expanded:**
   The definition of "Risk" has shifted from purely financial (theft/fraud) to reputational and ideological (ESG/Politics). You are now guarding the firm's social license to operate.

4. **The Lawyer's Role:**
   Your function is not just to enforce rules, but to engineer the "Trust Architecture." Without these mechanisms, strangers will not trust your client with their capital.

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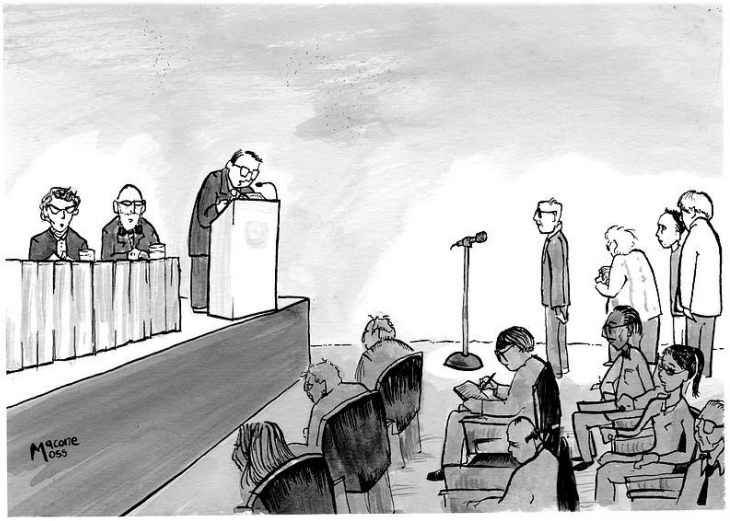
Q&A



"We'd now like to open the floor to shorter speeches disguised as questions."

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