

ecoDa

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European confederation of the Administrators' Associations
European confederation of Directors associations

ecoDa Position Paper

Consultation document on a simplified business environment for companies in the areas of company law, accounting and auditing

1. WHY SIMPLIFY EUROPEAN COMPANY LAW?

As central elements to achieve the common market, company law and accounting were among the first areas of legislation that were harmonised at European level. The field of auditing followed shortly afterwards (with the first version of the Eighth Directive on statutory audit dating from the early 80ies). Since then, the relevant directives and regulations have been updated several times in order to adapt them to new developments. A number of these revisions are recent and still need time before their effects can be measured and determined. However, none of these modernisation measures touched on the scope or the basic content of the directives concerned. They have remained fundamentally unchanged since their adoption.

In the last twenty to thirty years, the business environment of European companies has changed at high speed, with globalisation of economies and radical developments in technology. The legal environment too has evolved with the adoption of international standards in the field of accounting and the development of the jurisprudence of the Court of Justice of the European Communities. In recent years, this case law has helped to clarify the scope of the fundamental freedoms in the Treaty, paving the way for enhanced corporate mobility within the European Union.

There is a need to review existing EU directives in the light of these developments to assess their continued relevance. This assessment must also take account of the principles of better regulation together with subsidiarity and proportionality.

2. THE WAY FORWARD

There are essentially **two options** on how to proceed for certain company law directives that address mainly domestic situations:

- The **first option** is to address the question whether today all existing directives are still needed or whether the EU acquis in the area of company law should be reduced to those legal acts specifically dealing with cross-border problems.
- The **second, less far-reaching option** consists in focusing only on concrete, individual simplification measures in order to help EU companies.

With regard to the rest of the company law acquis that addresses specific cross-border problems as well as to the areas of accounting and auditing, individual simplification measures seem to be the right response. In accounting and auditing, the focus should be on reducing administrative costs for SMEs for which these costs are particularly heavy, whereas all companies should benefit from simplification measures in the field of company law.

With this communication, the Commission wants to present its first views on the subject and trigger a discussion involving Member States, the European Parliament and stakeholders in order to identify the measures in the areas of company law, accounting and auditing that are best suited not only to make European companies fit for the Internal Market but also to make them more competitive globally. The objective is to build a political consensus on the way forward so that appropriate legislative proposals can be submitted by early 2008.

Stakeholders are invited to comment on the questions raised and on the proposals put forward in this document and its annexes. In addition, stakeholders are also welcome to submit additional proposals for further simplification measures.

This exercise should be based on the understanding, underlined by the European Council on 8/9 March 2007, that any simplification measure at EU level can only be effective if the measures taken at EU level are fully endorsed by Member States at national level and if Member States make use of possibilities that already exist today under EU law to ease the burden on companies in the EU. Only a combined strategy will allow companies to benefit from clear improvements in the business environment.

The EU company law acquis has developed over the past 50 years. Over that time the business environment has inevitably changed and it is appropriate for the acquis to be reviewed as a whole. EcoDa believes that now is an appropriate time to conduct such a review, and that this should address both amendment to specific legal instruments and consideration of whether the acquis is appropriate to the present business environment or the environment in which EU businesses will be operating for the foreseeable future.

3. HOW MUCH REGULATION DOES EUROPE NEED IN THE FIELD OF COMPANY LAW?

3.1. The general approach to EU company law

In the field of company law, the increased mobility of companies today, not only at EU but also at international level, requires flexible responses to a constantly changing environment. These changes can only be addressed if Member States are able to react swiftly to these new developments. In this situation, a rigid, harmonised European framework might sometimes appear to be more of an impediment to innovation than a benefit for the Internal Market.

Furthermore, the competitiveness of companies also depends on the level of the administrative costs related directly or indirectly to their activity. Some of these costs derive from EU rules. It should be asked whether the benefits of these rules in all cases outweigh the costs related to them.

At the same time, harmonisation has also positive effects on the competitiveness of companies. Harmonisation is a strength for cross-border markets and can clarify the relation between two or more national legal systems involved. It also increases legal certainty. The same applies where minimum transparency standards are set up to protect third parties from

the dangers that increased mobility of companies can imply for them. In this case, common rules provide for the basis of trust that is needed for a functioning Internal Market.

However, the situation may be different for directives such as the Third, the Sixth, the Second and the Twelfth Company law Directives. These directives focus on mainly domestic situations and do not aim at solving specific cross-border problems.

The EU must, however, be considered in its approach to simplification. The acquis of EU company law has developed piecemeal over many years and represents the outcome of many compromises. Care has to be taken to ensure that any simplification does not lead to unintended consequences or the adoption of new instruments that are themselves detrimental to EU competitiveness.

3.1.1. Option 1: Placing the focus on cross-border problems

EcoDa believes that the general approach to EU company law should be that it should be used to address issues where a cross-border approach is necessary for the effective operation of the single market, but that it should not seek to intervene where differing national systems do not of themselves impede the internal market.

The **Third and the Sixth Company law Directives** regulate mergers and divisions of public limited companies in the same Member State. When these rules were adopted decades ago they played a role in opening up new possibilities for companies and promoting the internal market. Today, they guarantee a minimum level of protection for shareholders and creditors of public limited companies throughout the European Union.

However, given that these directives do not provide for full harmonisation, they do not create a level playing field; instead, some rules continue to differ between the Member States. At the same time, the existence of minimum requirements in EU law prevents Member States from adapting their national laws to changing needs. This leads to the question whether the advantages resulting from these directives justify the restrictions that they impose on businesses.

Similar considerations apply to the **Second Company law Directive** that deals with the capital of public limited companies. The capital maintenance system of the directive has been subject to discussions for a long time so that at least a review of that system should be considered in order to give companies more flexibility in the field of distributions to their shareholders. New national legal forms that fall outside the scope of the Second Company law Directive have been created in some Member States to offer the flexibility that the Directive lacks, notably with regard to minimum capital requirements.

The **Twelfth Directive** in principle is of an enabling nature as it allowed individuals to create private limited companies in Member States where, before the transposition of the directive, more than one member was required to form a company of that type.

However, at the same time, the directive sets a number of minimum requirements for the internal procedures of such a company. The question is whether such restrictions need to be determined at EU level.

In all these cases, the Commission considers that repealing the EU rules and increasing flexibility by leaving it to Member States to determine the conditions in the relevant areas would be a viable option. Indeed, the Commission considers that such an approach would fit best with better regulation principles and the need to equip the EU with a streamlined company law acquis for the 21st century.

With regard to the Second Company Law Directive, ecoDa would recommend that any proposals for repeal or amendment should await the outcome of the study being conducted by KPMG. EcoDa's initial view is that repeal would offer scope for considerable de-regulation for small and medium-sized enterprises. In any event, if complete repeal is not regarded as appropriate there should be radical reform to move to a principles-based approach that gives flexibility to individual member states. EcoDa would not favour the introduction of a different detailed regime, since that would likely to create different but as difficult problems as the existing regime. If complete repeal is considered unacceptable, there are areas that might be appropriate to be retained, such as the pre-emption provisions

With regard to the Twelfth Directive, while this does not have very much impact in all member states, the underlying principle of EU legislation dealing only with cross-border issues should be adhered to. On this basis it is appropriate to repeal the Twelfth Directive.

3.1.2. Option 2: More principle-based, less detailed regulation

The total repeal of the directives referred to above might seem to be too far reaching to some. In this case, at least parts of the Third, the Sixth and probably also the Second Company law Directives should be simplified. In their current form, these directives contain rules to a level of detail that leave Member States little flexibility to adapt their respective national systems to the evolving needs of businesses and stakeholders in general.

A first proposal for a simplification of the Third and the Sixth Directives was tabled by the Commission on 7 March 2007 as one of the measures contained in the Commission's Action programme for reducing administrative burdens and was endorsed by the European Council on 8/9 March 2007.

However, apart from this modification there are more substantial ones that should be tackled. In particular, a number of the reporting requirements contained in the Third and the Sixth Directive seem excessive from today's perspective.

3.2. Additional simplification measures in Company law

As explained above, further steps are needed, in addition to the measures envisaged in the previous section, in order to simplify other parts of the company law acquis.

This concerns first and foremost the First and the Eleventh Company law Directives. The ways of publishing information on companies that these directives provide for still do not exploit all possibilities that today's technology offers.

According to the rules of the **First Company law Directive**, certain information that has to be entered into the Member States' commercial registers, in addition has to be published in the national gazettes. In most cases, this publication entails unnecessary additional costs for the companies. These costs could, in the future, be avoided taking into account that nowadays all this information is available online through electronic company registers.

For branches, the **Eleventh Company law Directive** lays down special disclosure requirements. These requirements, too, imply considerable costs for many companies, due to national rules on translations and certifications related to the disclosure obligation. Efforts

are necessary to reduce these costs to a minimum by restricting the formal requirements that Member States may impose on companies in this context.

ecoDa supports the proposals for simplification to recognise that information systems and access have changed radically since the introduction of these measures, and that physical publication in national gazettes or commercial registers is no longer appropriate as a requirement where other systems are in place. ecoDa is in favour of the development of the BRITE project that will provide far more effective and appropriate information than does the present legislation and old-fashioned legislation that hampers its development and use should not be retained.

4. SIMPLIFYING BUSINESS FOR SMES IN THE AREAS OF ACCOUNTING AND AUDITING

In the field of accounting and auditing, small and medium-sized companies would benefit from further simplification of the Directives.

With the Fourth, the Seventh and the Eighth Directives, harmonised accounting and auditing requirements have significantly raised the quality of financial reporting and auditing in the EU. Whilst the overall goal pursued through these Directives to keep and improve accounting and auditing quality in the EU should be maintained, the existing requirements under those directives entail administrative work which companies, and notably small and medium-sized entities, criticise as being unnecessarily burdensome.

A successful reduction of the administrative burden for SMEs however needs to be addressed both at EU and national levels. It is of crucial importance to combine reporting for different purposes (such as tax, statistics, social security, employment reporting) at Member State level and thereby reduce the overall burden of keeping different accounting and reporting systems. This could also facilitate the use of electronic reporting formats such as XBRL.

The present simplification project for SMEs coincides with the publication of the International Accounting Standards Board (IASB) Exposure draft of a proposed IFRS for Small and Medium-sized Entities. After a first analysis, the Commission, however, does not believe that the current IASB work on SME accounting would provide sufficient elements to simplify the life of European SMEs.

The Commission has instead identified a number of other measures that could lead to tangible simplification for SMEs.

The first measure in this context is to exempt "micro entities" from the application of the accounting directives. For these smallest enterprises the burden related to the establishment of the annual accounts is particularly heavy. At the same time there is a lack of broad demand for their financial statements. With an exemption in the accounting directives, it would be left to Member States to determine which rules micro entities should be required to comply with. It should be noted in this context that a "micro entity" category has already been introduced in many Member States.

ecoDa supports the exemption of micro-entities from these requirements, and agree with the proposed definitions.

In addition, the following simplification measures in favour of SMEs are proposed:

- To extend the transition period for SME's crossing the thresholds from two to five years.

Companies in the start-up phase will particularly benefit from a longer transitory period before more detailed accounts have to be prepared;

– To exempt small entities from the requirement to publish their accounts;

– To make it possible for certain medium-sized entities to use exemptions currently available only for small entities. This measure would in particular concern companies where the structure of members is such that there are no particular external user needs and unlimited liability companies.

Further measures could be taken regarding the procedure for the regular adaptations of the SME thresholds, in the areas of consolidation requirements, regarding accounting for deferred taxes and to remove certain disclosure requirements.

ecoDa supports these requirements. At this level of organisation there is very rarely any cross-border element to the company's activities and EU intervention is inappropriate.

Notes for editors

The European Confederation of Directors' Associations (ecoDa) is representing the views of its ten members the *Association Belge des administrateurs* (AB), the *Institut Français des Administrateurs* (IFA), the *Institute of Directors* (IoD), the *Institut Luxembourgeois des Administrateurs* (ILA), the *Finnish Association of Professional Board Members* (Hallitusammattilaiset ry), the *Instituto de Consejeros – Administradores* (IC-A), the *Czech Institute of Directors* (CloD), the *Slovenian Association of Supervisory Board Members*, the *Polish Institute of Directors* (PID) and the *Croatian Association of Board Members* (HUCNO) on Corporate Governance and Company Law issues.

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Further information is also available on the following websites:

ecoDa : <http://www.ecoda.org>

IFA : <http://www.ifa-asso.com/>

AB: <http://www.administrateurs.be/>

IoD : <http://www.iod.com>

ILA : <http://www.ila.lu/>

Hallitusammattilaiset ry: www.hallitusammattilaiset.fi

IC-A : <http://www.iconsejeros.com>

CloD : www.ciod.cz

The Slovenian Association of Supervisory Board Members: www.zdruzenje-ns.si

PID : <http://www.pid.org.pl/>

HUCNO : <http://www.hucno.hr/index.php>

Contact:

Mana Livardjani
European Affairs Adviser
ecoDa

Tel: 0032 2 231 58 11 - Fax: 0032 2 231 58 31 - Email: mlivardjani@ecoda.org
www.ecoda.org