UNICE
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COMMISSION CONSULTATION ON ROLE OF (INDEPENDENT) NON-EXECUTIVE OR SUPERVISORY DIRECTORS[1]

UNICE RESPONSE

I. GENERAL COMMENTS

Before developing our views specifically on the substance of the above-mentioned consultation, UNICE would like to recall that the European Commission has repeatedly indicated that it is not appropriate to adopt a European corporate governance code[2]. According to the Commission, "*the adoption of such a code would not contribute significantly to the improvement of corporate governance in the EU*"[3]. UNICE shares this view.

When assessing the content of this consultation on non-executive directors (and other consultations on issues such as board responsibilities, corporate governance information, directors remuneration and Commission proposal for an 8th Company Law Directive on statutory audit which creates an obligation to create audit committees) we question the Commission's declared intention not to create a European Corporate Governance Code.

In the Company Law and Corporate Governance Action Plan, the Commission considered that[4] there would be no added value to developing a European corporate governance code as an additional layer between principles developed at the international level (particularly revision of the OECD corporate governance principles in which the Commission signaled it was particularly active) and national codes. The OECD principles have effectively been agreed on 22 April 2004, endorsed by Ministers on 14 May 2004. In that context, we fail to see the reasons behind the European Commission seeking to adopt a very detailed set of corporate governance rules, which will result in *de facto* a corporate governance code.

It is our considered opinion that corporate governance systems will develop and progress in a natural way under pressure from the financial markets. This is already happening and national rules or guidelines are constantly adapting to a global regulatory environment. Existing national corporate codes already address the subjects the Commission envisages to deal with in its intended Recommendation. Adding yet another layer of EU rules in this area would therefore be perceived as over-regulation and cannot be supported by European business.

Moreover, we feel that in that broader regulatory context due consideration should be given as well to the intended impact on restoring market confidence to be expected from the new disclosure requirements for listed companies under the IAS Regulation and the Directive on Continuous Disclosure and the disclosure requirement of art. 10 of the Directive on takeover bids. The Commission should rather concentrate its efforts on consolidating disclosure requirements for listed companies through IFRS.

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[1] Consultation document of the Services of the Internal Market Directorate General, "Recommendation on the role of (independent) non-executive or supervisory directors, 5.5.2004

[2] *Id*. section 1.2(1)

[3] See section 3.1 *in* "*Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward*" – COM (2003) 284, 21.5.2003

[4] *Id*., p. 12

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In this particular consultation, the Commission indicates that the envisaged Recommendation is not a corporate governance code due to the fact that the principles therein will not be designated for direct use by listed companies. Rather, Members States shall be invited to introduce the "*set of detailed principles*" into their national framework (with the possibility of adopting "binding provision" where appropriate).

We consider that, based on the very detailed rules outlined in the consultation document, the principles envisaged by the Commission go beyond a "*few essential rules*". The Commission's approach would result in a (detailed) rules-based rather than (broad) principles-based document. Hence, it tends more towards legislation than to non-binding principles for listed companies in the EU.

We consider that if the Commission proceeds with a Recommendation as outlined in this consultation document, it shall lead indirectly (via Member States) and *de facto* to the adoption of a European Corporate Governance Code albeit without the formal title.

II. SPECIFIC COMMENTS

Scope: Recommendation should apply to listed companies only

The Commission suggests that the requirements envisaged could also apply to companies that are not admitted to trading on a regulated market, i.e. non-listed companies. This is contrary to the approach taken in the Commission Action Plan: the requirements envisaged therein are done so with listed companies in mind. There is no reason for the requirements envisaged to be applied to non-listed companies. Extending the scope to subsidiaries of the listed company would be equally unreasonable.

We welcome recognition of the existence of both one-tier board and two-tier board structures. We, however, feel that the differences between these board structures should be given more emphasis. Other forms of governance should also be recognised.

Creation of board Committees

The Commission advocates the creation of three committees: Nomination, Remuneration and Audit Committees. While it is correct that the role of non-executive or supervisory directors is important in these three areas, advocating the mandatory creation of such committees together with detailed requirements[5] concerning their composition, role operation and transparency is overly prescriptive and does not properly take stock of the differences between one and two tier board structures.

Owing to the flexibility required to take account of the different needs and structures of a company in this area, UNICE considers that the details regulating the types of committees and their constitution should be left to the national corporate governance codes.

Concerning the Audit Committee, the Commission points out that the proposal for an 8th company law Directive on statutory audit (16.3.2004) already requires the setting up of an Audit Committee. Nevertheless we remain largely unconvinced by the arguments advanced to justify the Recommendation dealing further with this issue. First of all, the above-mentioned proposal for a Directive is subject to co-decision procedure and the adoption of a Recommendation would prejudge the legislative process and the prerogatives of the European Unions legislative bodies. Furthermore, we fail to see the need to complement the principles in the 8th company law Directive with "more detailed provisions": this runs contrary to the "*few essential rules*" as indicated in the Action Plan.

We appreciate the Commission acknowledging "*it is not considered desirable to include in the Recommendation a statement aimed at presenting the separation of these [i.e. Chairman – CEO] as best practice*". However, the Commission then proceeds to contradict this statement by

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[5] *See footnote 1, section 2.4 et s.*

setting as one of the minimum criteria to assess independence of non-executive directors, that a director should "*not be an executive or managing director of the company (…) for the previous five years*". This five-year "cooling off period" for former executive and managing directors to become non-executive directors would lead to a loss of substantial experience and management expertise. Clarification would be needed. In any case, this is an issue for national corporate governance codes.

Profile of (independent) non-executive or supervisory directors

In requiring that members of the Audit Committee should be able to read and understand financial statements, the Commission should not lose sight of the fact that the main role of the Audit Committee is not to check the sums but to probe at how the numbers are arrived at and their integrity. In this context, it is more important for members to have an understanding of how business in general, and the specific business in particular, operates.

A statement on the availability of a non-executive or supervisory directors should be dealt with in national corporate governance codes and not at European level.

In our view the proposed independence criteria[6] are overly formalistic and too detailed. The focus needs to remain on a general statement that describes what the objective of the independence requirement is. To be independent in mind is a qualification that is at least as important for an "independent" director than meeting certain formal "independence" criteria.

Throughout the Commission consultation document, we fail to see appropriate justification for the Commission choice of certain rules. For example, the Commission decides that non-executive directors or supervisory directors should be appointed and subject to re-election at intervals of "*no more than four years*". There is no indication as to why the Commission has chosen four years instead of three or five.

The intended Recommendation should restrict itself to a general definition of independence and leave the national codes which retain the necessary leeway for respective traditions to take responsibility for regulating further details and updates themselves without centralised stipulations lacking the afore-mentioned characteristics.

UNICE does not agree with a Commission Recommendation which would require that terms of reference of the committees be published in annual report. UNICE believes that the company should be free to decide on the most appropriate way to disclose such information (ex: available upon request or on the company website).

As a concluding remark, UNICE would like to call on the European Commission to urgently reconsider the orientations envisaged in this consultation and to respect its original intentions which was provide for a "*few essential rules*". This request is applicable *mutatis mutandis* to the other Commission initiatives in the area of company law and corporate governance.

To continue developing overly prescriptive chapters of a *de facto* European corporate governance code is running counter to the objective of the Company Law and Corporate Governance Action Plan, i.e. "*foster the global efficiency and competitiveness of businesses in the EU*".

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[6] *See footnote 1, section 2.3.3.*