

24 November 2005

THE FUTURE OF THE COMMISSION COMPANY LAW AND CORPORATE GOVERNANCE ACTION PLAN

UNICE'S REVIEW OF PRIORITIES IN THE AREA OF COMPANY LAW AND CORPORATE GOVERNANCE

Introduction

UNICE was supportive¹ of the European Commission Company Law and Corporate Governance Action Plan² released in 2003. (hereafter 'the Action Plan'). We welcomed in particular the declared objective of "*fostering efficiency and competitiveness of business*".

In this regard, UNICE agreed with the Commission's analysis that "*key to the achievement of this objective is the setting up of a proper balance between actions at EU level and actions at national level. Some company law rules are likely to be best dealt with, and updated, more efficiently at national level, and some competition between national rules may actually be healthy for the efficiency of the single market*"³.

The Commission Action Plan distinguishes actions to be carried out in three phases (short term – 2003-2005, medium term – 2006-2008, long term – from 2009 onwards).

As the short term phase comes to an end, UNICE appreciates that the EU Institutions will reflect on whether the actions foreseen in the medium are appropriate in light of what should be considered as priorities for EU action in the field of Company Law and Corporate Governance.

In our preliminary remarks, we would like to **(I.)** restate what European business considers as fundamental principles to serve as reference criteria for EU intervention or non-intervention in the areas of Company Law and Corporate Governance and point to what we consider as the **(II.)** right issues to address in this area in the years to come.

¹ See UNICE Comments, "*Commission Action Plan: Modernising Company Law and enhancing Corporate Governance in the European Union*", 6 August 2003 – available at www.unice.org

² See Commission Communication COM(2003)284, "*Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward*", 21.5.2003

³ See COM(2003)284, section 2.2, first paragraph, p. 9.

I. Principles for an EU approach to company law and corporate governance

Good and efficient company law and corporate governance are of utmost importance to companies and their stakeholders. Any action in these areas must pursue the objective of increasing competitiveness while respecting the legal environment in which they evolve. Excessive regulatory burdens may ultimately restrict the freedom of companies to do business, thereby holding them back from releasing their potential. This is detrimental to business, to company shareholders and more generally to the EU as a whole.

For this reason, UNICE would like to restate the principles⁴ set out below to serve as reference criteria for intervention or non-intervention in the areas of company law and corporate governance.

Subsidiarity – The EU should only intervene when it is proven that the foreseen objective cannot be reached by national action. EU action should not disrupt the delicate balance found at national level, which takes into account national traditions and cultures.

Principle-based approach – In light of the subsidiarity principle, in any EU intervention, a general principles-based approach should prevail over a rules-based approach. This would allow a degree of flexibility necessary for companies to develop the governance model best suited to them.

Market-driven approach - In UNICE's view corporate governance is better served by flexible self-regulatory initiatives as opposed to regulatory interventions. Over-regulating is a disincentive for companies to go beyond legislation and adopt corporate governance best practice.

Comply or Explain – When a corporate governance code is applicable, companies should either conform to the provisions of that code, or provide an explanation as to why the principles have not been followed. As stated in the 1992 Cadbury Report, the Comply or Explain route should enable companies to “*strike the right balance between meeting the standards of corporate governance expected of them and retaining the essential spirit of enterprise... Raising standards of corporate governance cannot be achieved by structures and rules alone (...)*”. This ‘Comply or Explain’ approach has been in operation for over 10 years and the flexibility it offers has been widely welcomed both by company boards and by investors. The spirit of the principles is important, not a mere formalistic ‘box ticking’ approach.

Transparency and disclosure - Transparency is an essential ingredient for any form of outside monitoring. It is very important for the shareholders and investors to see the manner in which a company follows the recommendations on corporate governance. Transparency enhances confidence in a company.

⁴ See UNICE Statement, “Principles for an EU approach to Company Law and Corporate Governance”, 27 July 2004, available at www.unice.org

Global orientation – EU policy should be oriented towards and take into account the global environment in which European companies inevitably evolve. Adding an additional and possibly contradictory EU layer of regulation would be a hindrance to achieving the goals of corporate governance.

Competition – should be encouraged between national systems so that society can benefit from an emulation effect. Competition in the field of legal systems stimulates legal innovation. In this context, the EU should ensure that Member States mutually recognise each other's legal systems.

Better regulation – Impact assessments and proper consultations⁵ are the basis of good regulation. Consultation remains one of the basic principles of participatory democracy but consultation needs to be carried out in the right conditions: sufficient time for considered responses and a weighted analysis of responses received are fundamental ingredients for successful consultations.

II. Future priorities in the area of Company Law and Corporate Governance

Regulatory fatigue

Since issuing the Action Plan the European Commission has carried out, or is in the process of carrying out, almost all the actions foreseen in the short term (2003 – 2005). This entailed significant activity of the EU Institutions and other interested parties, including European companies over a relatively short period of time.

We would like to draw the EU Institutions attention to the fact that European companies have not only to deal with company law and corporate governance issues but also intensive regulatory activity in other associated areas such as the adoption of International Accounting Standards and the implementation of the Financial Services Action Plan.

If Commissioner Mc Creevy recognises the existence of “*regulatory fatigue*”⁶ when referring to implementation of the Financial Services Action Plan (FSAP), we would like to extend this expression to “*regulatory exhaustion*” when taking into account FSAP at the same time company law, corporate governance, accounting standards and complying with the US Sarbanes-Oxley Act, in particular section 404 on internal controls.

In this context, UNICE sets out below what we consider priority actions to be carried out in the area of Company Law and Corporate Governance.

⁵ As highlighted by the High Level Group of Company Law Experts that largely inspired the afore-mentioned Commission Action Plan “for both primary legislation and any alternatives, proper consultation is necessary”. See “A modern regulatory framework for Company Law in Europe” presented on 4 November 2002, available at the following page of the Commission website: http://europa.eu.int/comm/internal_market/en/company/company/modern/, p. 4.

⁶ Speech by Charlie M^c CREEVY European Commissioner for Internal Market and Services on “Governance and Accountability in Financial Services”, Economic and Monetary Affairs Committee of European Parliament, 1.2.2005, [SPEECH/05/64](#)

1. Correct implementation of existing legislation

When evaluating the actions foreseen in the medium term by the Commission, we consider that efforts should concentrate on correct implementation at national level of the recently adopted or soon to be adopted Commission proposals rather than on new proposals.

2. Other priorities

We consider that EU initiatives should concentrate on initiatives that will provide optional means for companies to reap the benefits of the internal market and adapt their structures to suit their needs in a flexible manner as opposed to initiatives that would entail mandatory changes in company law and corporate governance.

a. The European Private Company Statute⁷

In this context, we consider that a proposal for a Statute for a European Private Company would be a Commission initiative that would provide small and medium-sized companies (hereafter “SMEs”) with a statute close to their needs and size. The existing European Company Statute or “*societas europaea*”, (hereafter “SE”) is ill-suited to SMEs because it was designed mainly for larger companies. It is inherently cumbersome, due in particular to the fact that this type of company may issue securities to the general public. One of the recitals of the SE regulation is very explicit in this sense in that it provides that the SE must be of a “reasonable size”. The minimum capital required is €120.000 euros which is too high for SME’s.

We fully appreciate that the feasibility study commissioned by the European Commission in accordance with the short term action foreseen in the Action Plan will officially deliver its results shortly and that a Commission initiative will have to take into account the results of this study. Nevertheless, we would like to reiterate that European business is keen to contribute to the assessment of the results and to fully cooperate with the EU institutions in any the ensuing action.

b. Providing the choice between monistic / dualistic board structures

The Action Plan endorses the views of the Winter Group of High Level Company Law Experts (the High Level Group) in proposing that listed companies across the EU should have the choice between a one-tier and two-tier board system and be able to adopt the structure which best suits their particular corporate governance needs and circumstances.

We welcome the Commission’s recognition of the importance of organisational freedom in board structure (freedom of choice between one-tier and two-tier structures).

⁷ The idea of creating a European Private Company Statute, suited to SMEs originated in 1998 in the work done by the Conseil National du Patronat Français – CNPF – now Mouvement des entreprises de France – MEDEF, the French business organisation – and the Paris Chamber of Trade and Commerce – CCIP (Chambre de Commerce et d’Industrie de Paris)

We stress the importance of adopting a principles based approach in this area. Any initiative should refrain from adopting a detailed list of requirements to be implemented when offering the choice. Indeed, there are different types of two tier boards in different countries and there is no evidence to suggest that one system is better than the other.

We recommend therefore a light-touch approach outlining a few essential principles recommending to Member States to enable their companies to choose between a monistic and a dualistic board structure which would be suited to their needs.

c. Study is foreseen on reform of the Second Directive (capital maintenance)

In the medium term of the Action Plan, a study is foreseen on reform of the Second Directive (capital maintenance). The High Level Group suggested that the interests of creditors and shareholders might be protected more effectively by the introduction of an alternative to the current regime based on the concept of legal capital. The Action Plan notes the need for further work, initially via a study to establish the feasibility of an alternative regime and identify the potential benefits. Any amending legislation would be subject to the outcome of this study.

UNICE believes that the case for legal capital regulation needs to be considered in relation to further issues, such as directors' duties, insolvency law, creditor protection and the regulatory context.

In this context, the SLIM exercise should be further pursued and we would welcome proposals in this direction.

In our response to the Action Plan as proposed in 2003, we UNICE urged the Commission to conduct a feasibility study in the short-term on an alternative to the capital maintenance regime as opposed the medium-term feasibility study foreseen in the Action Plan. In this context, we reiterate the necessity to conduct this study as soon as possible.

Remaining short-term measure: shareholder cross border voting

UNICE considers that the Commission has, through two consultations, taken a reasonable approach on this issue, but that there is need for clarification in light of UNICE's response to the consultations⁸.

Concerning the other actions foreseen, please see table at annex.

⁸ See UNICE response to "Second Commission consultation on fostering an appropriate regime for shareholders' rights", 28.7.2005, and Preliminary UNICE response to "Commission consultation on fostering an appropriate regime for shareholders' rights", 24.12.2004, both available at www.unice.org

Simplification of company law: codification and recast of existing legislation?

Recently, additional activities in the area of company law and not fully provided for in the Action Plan, are foreseen by the Commission in the context of its strategy to simplify the regulatory environment⁹. It is foreseen that the Commission would “codify or recast” several existing company law Directives¹⁰ in 2006.

The Commission does not specify which Directives would be subject to codification¹¹ (where no changes to the substance would be proposed) and which one(s) would be recast¹² (which would result in new legally binding act repealing the acts which it replaces, combining both the amendment of the substance of the legislation and the codification of the remainder which is intended to remain unchanged).

While we consider positive the Commission's declared intention to simplify existing legislation, it is still unclear how the concrete simplification proposals will look. It is thus important that simplification proposals really reduce burdens for business and that stakeholders are continuously consulted throughout the process of developing, determining and adopting simplification measures. This is particularly true in the case of recasting legislation. The ‘raison d'être’ of such proposals is simplification and if the process of recasting ends up running contrary to this objective, the proposal should be withdrawn. We would also like to reiterate that the first priority should be correct implementation of existing and recently adopted legislation.

Conclusion

In essence we urge the European Institutions to concentrate on correct implementation of the many Directives recently adopted or in the process of being adopted and take initiatives with a view to providing the optional means to companies to benefit of the internal market and adapt their structures to suit their needs in a flexible manner as opposed to initiatives that would entail mandatory changes in company law and corporate governance. Furthermore, objective, independent studies, impact assessments and proper consultations must precede any EU initiative.

⁹ See [COM\(2005\)535](#), 25.10.2005, Communication of the Commission "Implementing the Community Lisbon programme: A strategy for the simplification of the regulatory environment", pp. 16-17.

¹⁰ *Id.* **First Council Directive** 68/151/EEC of 9 March 1968 on co-ordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community.
Third Council Directive 78/855/EEC of 9 October 1978 based on Article 54 (3) (g) of the Treaty concerning mergers of public limited liability companies.

Sixth Council Directive 82/891/EEC of 17 December 1982 based on Article 54 (3) (g) of the Treaty, concerning the division of public limited liability companies.

Directive 2005/.../EC of the European parliament and the of the Council on cross-border mergers of limited liability companies [**Tenth CLD** – awaiting formal adoption]

Eleventh Council Directive 89/666/EEC of 21 December 1989 concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State

Twelfth Council Company Law Directive 89/667/EEC of 21 December 1989 on single-member private limited-liability companies

Directive 2003/58/EC of the European Parliament and of the Council of 15 July 2003 amending Council Directive 68/151/EEC, as regards disclosure requirements in respect of certain types of companies

¹¹ See definition of “codification”: *Id.*, footnote 18, p. 6

¹² See definition of “recasting”: *Id.*, footnote 21, p. 7

Annex - Specific Comments on medium term actions

Remaining short term action:

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
Restructuring	Proposal for a Fourteenth Directive on cross-border transfer of the seat	Directive	UNICE considers that the elimination of mobility constraints on companies within the single market is an important issue and a Directive to facilitate the transfer of seat would be significant. However, UNICE does not agree with a 14th Company Law Directive on cross-border transfer of seat that would mirror the worker participation arrangements as was the case for the 10th. Company Law Directive agreed early 2005.

Corporate Governance

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
Enhanced disclosure by institutional investors of their investment and voting policies	The Action Plan proposes that institutional investors should be obliged to disclose: <ul style="list-style-type: none"> • their investment policy and their policy with respect to the exercise of voting rights in 	Directive	In our view this topic should be left to corporate governance rules at national level rather than prescriptive rules at EU level. In any case we believe that a clear distinction should be made between holders

	<p>companies in which they invest;</p> <ul style="list-style-type: none"> to their beneficial holders at their request how these rights have been used in a particular case. <p>It notes that such requirements would not only improve the internal governance of institutional investors themselves, but would also enhance participation by institutional investors in the affairs of the companies in which they invest.</p>		<p>of a relevant percentage of share capital and institutional investors. Only the second category, in principle, owes fiduciary duties to the beneficial owners. Furthermore, the definition of institutional investor for the afore-mentioned purpose should be coherent with the one given by the European financial market regulation (ISD and linked regulations).</p>
<p>Choice for all listed companies between the two types (monistic/dualistic) of board structures</p>	<p>The Action Plan endorses the views of the Winter Group of High Level Company Law Experts (the High Level Group) in proposing that listed companies across the EU should have the choice between a one-tier and two-tier board system and be able to adopt the structure which best suits their particular corporate governance needs and circumstances.</p>	<p>Directive</p>	<p><i>See above position paper</i></p>
<p>Enhancing the responsibilities of board members (special investigation right, wrongful trading rule, director's disqualification)</p>	<p>The Action Plan endorses recommendations from the High Level Group designed to enhance directors' responsibilities:</p> <ul style="list-style-type: none"> the introduction of a special investigation right giving shareholders holding a certain percentage of the share capital the right to ask a court or administrative authority to authorise a special investigation into the affairs of the company development of a wrongful trading rule making directors to be held personally 	<p>Directive or Directive amending existing legislation</p>	<p><i>Directors' responsibilities: should be left to national laws or corporate governance codes.</i> These issues are deeply rooted in the political and cultural background of Member States' legal systems. Therefore, only an in-depth study on the subject matter would be able to assess whether in this field there is need for common EU rules. The liability of directors for misleading information and other negligent behaviour is a topic to be considered in a coherent and common framework and not to be split into</p>

	<p>accountable for the consequences of the company's failure, if it is foreseeable that the company cannot continue to pay its debt and they do not decide either to rescue the company and ensure payment or to put it into liquidation;</p> <ul style="list-style-type: none"> imposition of directors' disqualification across the EU as a sanction for misleading financial and non-financial statements and other forms of misconduct by directors. 		different regulatory actions.
<p>Examination of the consequences of aiming at achieving full shareholder democracy (one share / one vote), at least for listed companies</p>	<p>The Action Plan suggests that there is a strong case for establishing a real shareholder democracy based on the one share/ one vote principle. It believes any initiative in this direction would give further effect to the principle of proportionality between capital and control. As a first step in this direction it suggests a study to identify the consequences of such an approach.</p>	Study	<p>Any study commissioned by the European Commission on this issue should be conducted in a truly independent manner in order to get a neutral assessment of the topic and it should involve a sound economic corporate law analysis. If such a study is undertaken UNICE strongly advises it should not only deal with one share one vote but elucidate comprehensively the topic of shareholder democracy and treat also other to that related issues</p>

Capital Maintenance

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
Reform of the Second	The High Level Group suggested that the interests of	Study	<i>See above position paper</i>

Directive (capital maintenance).	creditors and shareholders might be protected more effectively by the introduction of an alternative to the current regime based on the concept of legal capital. The Action Plan notes the need for further work, initially via a study to establish the feasibility of an alternative regime and identify the potential benefits. Any amending legislation would be subject to the outcome of this study.	followed, if appropriate, by Directive amending existing legislation	
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Groups of companies

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
Framework rule for groups, allowing the adoption at subsidiary level of a coordinated group policy	The Action Plan recommends a framework rule for groups allowing those concerned with the management of a company belonging to a group to adopt and implement a co-ordinated group policy provided that the interests of creditors are effectively protected and that there is a fair balance of burdens and advantages for that company's shareholders.	Directive	<p>Large corporations and small medium companies are often structured as a group of companies. Groups of companies are a specific issue, and one which has been under discussion for a long time. A specific regulation concerning groups of companies is not necessary.</p> <p>Useful provisions concerning groups of companies have to recognise that groups are not an illness of companies, but an efficient means of organisation.</p> <p>As a consequence, it is necessary to collect information on the typical situations of groups of companies and, in particular, those concerning the powers of direction</p>

		<p>exercised by the parent company on its subsidiaries. When a company is part of a group, it is necessary to avoid considering intragroup transactions and the advantages and disadvantages of these transactions in a piecemeal way but taking account of the whole effects of belonging to a group.</p> <p>UNICE believes that if nonetheless the Commission pursues its intention to table any proposals related to groups, in-depth studies should be carried out beforehand.</p>
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Pyramids

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
<p>Prohibition of stock exchange listing for abusive pyramids, if appropriate, following further examination and expert input</p>	<p>The High Level Group recommended that, subject to certain exceptions, national authorities should be required not to admit to listing companies belonging to abusive pyramids – i.e. holding companies whose sole or main assets are shareholdings in other listed companies. The Action Plan notes the need for further examination of the issues involved and the need to avoid undue restrictions on companies' freedom to organise themselves efficiently.</p>	<p>possibly Directive amending existing legislation</p>	<p>Pyramids of companies ensure the control of large groups of companies by means of minority shareholdings. UNICE would like to stress the difficulty to define pyramids.</p> <p>It is necessary to avoid companies being managed just to secure personal benefits not connected with the creation of shareholder value. While strict provisions preventing company directors from mala gestio and specific measures beyond group transparency may be necessary, there may be cases where a Pyramid is useful tool. In</p>

			<p>any event, in the case of listed companies the power to regulate should be left to the competent market authority.</p> <p>This specific issue merits a special study in order to know the impact of different proposed rules in the different Member States' jurisdictions. The sole expert opinion of CESR could not be considered sufficient.</p>
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Restructuring

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
Simplification of the Third Directive (legal mergers) and Sixth Directive (legal divisions)	The Action Plan recommends the simplification of restructuring transactions pursued by the proposed relaxation of some of the requirements currently foreseen by the 3rd and 6th Directives in so far as the necessary safeguards are ensured. Simplification for example of the 3rd Directive would mainly concern requirements such as a special general meeting to be held in the acquiring company to authorise the transaction or at least special publicity and minority protection measures.	Directive amending existing legislation	<p>While UNICE supports the principle of simplification measures, we do not consider simplification of these Directives as a priority.</p> <p>For further comments on simplification (codification/recasting) see above position paper.</p>

European Private Company

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
Possible proposal for a Statute for a European Private Company (depending on the outcome of the feasibility study)	This is intended as an alternative to the Societas Europae and aimed at SMEs active in more than one Member State. Since views differ as to whether there is a real need for such a vehicle, the Action Plan suggests that action should be subject to the outcome of a feasibility study.	Study followed, if appropriate, by a Directive	See above position paper.

EU legal forms

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
Assess the need for the creation of other EU legal forms (e.g. European Foundation)	The Action Plan contains a recommendation to launch a feasibility study in order to assess whether there is a need for additional legal forms of enterprises such as for example a European Foundation.	Study	X

Transparency of national legal forms

MEASURE	CONTENT	PROPOSAL	UNICE VIEW
<p>Introduce basic disclosure rules for all legal entities with limited liability, subject to further examination</p>	<p>The Action Plan suggests that increased disclosure requirements for all legal entities with limited liability are needed to preserve fair competition and to prevent company law from being abused for fraud, terrorism or other criminal activity. But notes the need for further consideration of what might be involved.</p>	<p>Directive or Directive amending existing legislation</p>	<p style="text-align: center;">X</p>

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