

**PROPOSAL FOR A DIRECTIVE ON TRANSPARENCY REQUIREMENTS FOR ISSUERS WHOSE  
SECURITIES ARE ADMITTED TO TRADING ON A REGULATED MARKET**

COM(2003)138

**COMMENTS**

**I. GENERAL COMMENTS**

UNICE has taken note of the European Commission's proposal for a Directive on the harmonisation of transparency requirements with regard to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC.

UNICE had the opportunity to comment on this issue during the consultation phase which preceded the publication of the afore-mentioned proposal (comments dated 16 October 2001 and 15 July 2002 are available on [www.unice.org](http://www.unice.org) ).

Although UNICE welcomes many of the proposal's provisions, UNICE would like to state, and to a certain extent reiterate, certain concerns which it regrets, have not been adequately taken into account, notably the requirement for the disclosure of quarterly financial information.

UNICE supports EU efforts to build an integrated EU capital market by enhancing the quality and the comparability of financial statements by publicly traded companies and the intention of improving market transparency is commendable.

Nevertheless, whilst pursuing the aim of improving transparency, the right balance must be found to avoid imposing unrealistic obligations and administrative burdens on European companies.

More specifically, UNICE is opposed to legislation which would entail mandatory quarterly financial information requirements. The solution which seems to drive the above-mentioned proposal according to which increased transparency calls for increased legal disclosure obligations is in UNICE's view flawed. Indeed, the mass of information released on investors and the public already partly exceeds their capacity of processing and understanding it. Imposing such requirements could have a reverse effect and lead to a lack of transparency rather than increased transparency.

Such obligations deny the reality of the diversity of companies. For example, a less investor-dependent family SME with a long-term business strategy should not see its business decision to refrain from producing quarterly financial information pre-empted by legal regulations.

Furthermore, in UNICE's view the time limit that the proposal prescribes for the disclosure of annual financial reports and half year financial reports is too short, in particular if the reports are audited.

The proposal's aim of reaping the benefits of modern information and communication technology is welcomed by UNICE. In this context, publication of information in electronic form is an important step, provided that this is, at least during an initial period, an optional, and not mandatory, means of publishing information; furthermore, in case of publication in electronic form, no other requirement should be requested.

UNICE is in favour of leaving implementing regulations to committees (comitology procedure) but this should be restricted to technical details in a narrow sense. It appears that the comitology procedure mentioned in Article 23(2) is referred to in no less than eleven articles<sup>1</sup> of the proposal, some of which, in UNICE's view, inappropriately. As argued in previous UNICE comments<sup>2</sup>, transparency, consultation and involvement of relevant stakeholders must be ensured when resorting to such procedure.

## II. SPECIFIC COMMENTS

### ***Annual financial reports (Article 4)***

The proposal requires annual financial reports to be disclosed to the public within a maximum period of three months after the end of each financial year.

In previous consultations UNICE questioned the exact meaning of "annual financial report": whether it referred to the report approved by the shareholders' general meeting or the draft approved by the board of directors to be submitted for approval of shareholders.

The Commission indicates in a set of 'Frequently Asked Questions' (hereafter FAQ's) issued at the same time as the proposal: "that report would have to be audited, though not necessarily yet approved by the shareholders in their general meeting".

UNICE appreciates the Commission's effort to clarify this point but is of the opinion that such clarification should be included in the proposed Article 4 itself. Such clarification should not be left to the comitology procedure referred to in Article 4 paragraph 6.

Notwithstanding this clarification, the time limit of three months for the disclosure of the relevant audit report is not, in UNICE's view, appropriate. Auditors usually certify the annual report after the approval of the board of directors and before the general meeting of shareholders. Thus the second sentence Article 4.4 should be amended as follows:

*"The audit report (...), shall be disclosed in full to the public not later than 30 days after the approval by the board of directors and in any case 15 days before the general meeting of shareholders ~~together with the annual report~~".*

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<sup>1</sup> Articles 2.3, 4.6, 5.5, 6.4, 11.5, 13.4, 14.5, 15.4, 17.4, 18.2 and 19.3.

<sup>2</sup> See "A Modern Regulatory Framework for Company Law in Europe – Consultative Document of the High Level Group of Company Law Experts: UNICE Comments", 17 June 2002. Available at [www.unice.org](http://www.unice.org)

Otherwise, the deadline would be impossible to achieve. Furthermore the time limit appears to be too short especially for companies with widespread activities all over the world. This is particularly true considering that the annual report should be audited. For a parent company to issue an audited report, it must receive reports from the local auditors of its subsidiaries based in different countries which is a lengthy process, difficult to achieve within the prescribed three month period.

#### ***Half-yearly financial reports (Article 5)***

The proposal prescribes disclosure within a maximum of two months of the end of the relevant period of a half-yearly condensed financial report based on international accounting standards on interim financial reporting (IAS-34) and an update of the last management report.

In UNICE's view, the time limit of two months, even if based on IAS-34, is short, in particular if the report is audited. A longer period (at least three months) should be allowed for the disclosure of audited half yearly report.

Although the Commission does not provide for mandatory audit review of the proposed half-yearly report, it nevertheless indicates in the "Explanatory Memorandum" accompanying the proposal<sup>3</sup> that home Member States may impose it according to the proposed Article 3.2. In addition, the Commission in Article 5.5(c) allows for using comitology procedure with a view to imposing a mandatory auditors' review.

In UNICE's view, such an important issue should not be left to comitology but should be dealt with by primary legislation and in any case mandatory auditing of interim reports should be rejected in view of the costs and ensuing liability claims.

Furthermore, Article 5(4) requires the issuer who's half-yearly report has not been audited, to make a statement to this effect in the report. UNICE fails to see the logic behind requiring issuers to make a negative statement. It stands to reason that if such a statement is not made, that no auditing took place. Given that auditing is not foreseen in primary legislation, one would presume that it is the legislator's intention to provide for a principle according to which no auditing could be reasonably expected. Only if by exception such an audit takes place, this exceptional event is worth underlining in the report.

#### ***Quarterly financial information (Article 6)***

The proposal foresees the disclosure no later than two months after the relevant three-month period of mandatory quarterly financial information covering the first and third quarter of the financial year. This quarterly information shall indicate the net turnover and the profit or loss before or after tax for the concerned period and an explanatory statement relating to the issuers' activities and profits and losses during this same period. The proposal foresees optional provision of information on trends for the company's future developments.

As indicated in the above general comments, UNICE is opposed to the proposed mandatory quarterly financial information.

As stated in previous comments, UNICE is of the opinion that interim reporting between half-year and full-year figures should be a voluntary matter for companies, not necessarily on a quarterly basis, but on such occasions when it is appropriate to inform the market

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<sup>3</sup> See COM(2003)138, section 5.3.2, p. 23.

about information available to the company and to prevent a false market occurring in its traded securities, i.e. a trading update rather than formal quarterly reporting.

A trading update is often provided voluntarily prior to a closed period before the publication of full or half-year figures.

In UNICE's view, the Commission does not prove sufficiently the added value of quarterly financial information to justify the additional burdens such mandatory requirements will have on European business.

UNICE remains unconvinced by the tentative justification for mandatory quarterly financial information provided in the 'Explanatory Memorandum' and the afore-mentioned FAQs<sup>4</sup>. Moreover, contrary to what the Commission states, UNICE is of the opinion that mandatory quarterly financial information shall increase short-term earnings pressure on companies with a detrimental influence on governance and favours short term strategy at the expense of a long term vision of company's management.

Furthermore, UNICE is worried about the content of the quarterly report as described in Article 6 which requires "*the net turnover and the profit or loss before or after tax*". UNICE believes that the content of quarterly reports must be determined by reference to the information needs they are intended to satisfy, i.e. timely and continuous disclosure of key accounting data. Disclosing information like profit or loss, even after tax, may result in supplying the market with data based on uncertain assumptions, thus increasing volatility. On the contrary, if quarterly financial information reports were to become, mandatory UNICE believes that they should contain only the information that is important to the market like debt, net financial position, gross operating profit, turnover, etc.

UNICE would welcome specific mention of the fact that the issuer is exempted from publishing quarterly financial information for the last quarter of a financial year where the annual financial report has been published.

### ***Additional Information (Article 7)***

The proposal requires issuers to inform the public of additional information "without delay". Article 15 contains reference to a similar timeframe.

UNICE considers that the terms "without delay" are too vague and companies need clarification for reasons of legal certainty and to participate in the harmonisation effort pursued by the proposal.

### ***Company and director responsibilities and liabilities (Articles 4, 5, 6 and 7)***

Articles 4.2(c) and 5.2(c) concerning respectively annual and half-yearly reports, foresee that these reports shall contain statements made by the persons responsible within the issuer to the effect that these reports are, to the best of their knowledge, in accordance with the facts and that the report makes no omission likely to affect its import.

UNICE believes that these articles although unclear, may create further liabilities and responsibilities for directors. It appears that Article 4.6, which empowers the Commission to adopt implementing measures, aims provide for clarification. In the meantime, this lack of legal certainty is detrimental to legal security that must prevail.

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<sup>4</sup> See respectively COM(2003)138, p. 16 and section 5.3.3 p.23 and the FAQs available at the following link: [http://www.europa.eu.int/rapid/start/cgi/questen.ksh?p\\_action.gettxt=qt&doc=MEMO/03/68/01RAPID&lg=EN](http://www.europa.eu.int/rapid/start/cgi/questen.ksh?p_action.gettxt=qt&doc=MEMO/03/68/01RAPID&lg=EN)

In addition to urging for further clarification of these provisions, UNICE states that directors' responsibilities and liabilities is essentially an area which should be dealt with by national legislation.

Articles 4.1, 5.1, 6.1 each require the issuer to draw up and "*disclose to the public*" certain financial information (annual report, half-yearly report and quarterly financial information). Article 7 requires Member States to "*ensure that responsibility for the information (...) lies with the issuer (...)*".

UNICE urges for clarification of "disclose to the public".

If the phrase "*disclose to the public*" refers to disclosing information to the public at large, this could lead to an unacceptable extension of the ensuing responsibility and liability for companies and possibly directors. Indeed, it is our understanding that in certain member states, companies have obligations to their shareholders, securities holders and to regulators for obligations under regulatory and market rules when disclosing such financial information and not to the public at large.

The same reasoning applies to the management report disclosed "*to the public*" (Articles 4.2(b), 4.5 and 5.2(b)).

#### ***Timely access to regulated information (Article 17)***

It is unclear in Article 17.1 what the meaning of "effective dissemination" is, as opposed to disclosure, and when it extends to "the public" both throughout its territory and "abroad."

The requirement in Article 17.2(b) to "*alert any interested person*" is too far-reaching and uncertain, to be acceptable. UNICE also questions the appropriateness of Article 17.2(a) and the requirement for the host member state to keep the public informed as regards the Internet sites of issuers.

With regard to Article 17.4, we also question whether it is appropriate for the Commission to reserve powers to take implementing measures on the dissemination of information, which should be limited to shareholders, not the public. Public registries and the voluntary dissemination of information serve the public. This also seems an area where Member States and the regulators of markets in Member States should set the requirements.

The general principle should be, as discussed in connection with Articles 4 – 7, that companies owe their duties and responsibilities to their shareholders and not the public, with separate obligations to comply with applicable regulatory rules as a regulatory matter.

#### ***Electronic network between national securities regulators (Article 18)***

UNICE welcomes the proposed efforts to setting up an electronic network between national securities regulators within the European Union and strongly encourages the relevant authorities to draw up and implement the guidelines as soon as possible.

#### ***Transitional Provisions (Article 26)***

UNICE is concerned about the effects on companies having to adapt to international accounting standards in 2005 and applying this proposed Directive at the same time.

Article 26 contains an option for Member States to exempt issuers from applying Article 5(3) (the requirement to use IAS 34) in the half-yearly report for the 2005 half-year.

If this option is exercised, companies would be allowed to report their 2005 half-year in accordance with their pre-IAS accounting policies. Given that the annual report will be prepared in accordance with IAS, it will be misleading to the market for the half-yearly report to be prepared in accordance with current accounting practices.

UNICE strongly supports transitional provisions for 2005, but has doubts regarding the exact wording of the provisions in Article 26.

UNICE believes that a sensible transitional provision would be to delay the application of the Directive until at least 2007. This will allow the use of international accounting standards to become accepted before further burdens are placed on the markets as a whole in terms of shorter reporting deadlines and specific requirements for quarterly reporting. We are strongly of the view that this should be a specific transitional requirement, rather than being a member state option.

The amount of change that companies, auditors and users of financial statements will have to cope with to make the transition to IAS work should not be under-estimated. Nor should the requirements for additional communication with the markets of the impact of the conversion to IAS in 2005 be ignored. We are of the opinion that there will not actually be sufficient time in the first half of 2005 for companies to effectively communicate the impact of their conversion to IAS as well as producing quarterly financial information. Companies are likely to wish to have a separate market communication that explains how their opening IAS balance sheet has been produced and how their 2004 results have been restated to an IAS basis before they produce their first IAS 2005 results. If their first IAS 2005 results relate to the first quarter of 2005, there will not be time for thousands of companies with December year ends to present their 2004 annual report according to current accounting practices, their 2004 restatement to IAS and then their 2005 IAS quarterly results by August 2005.

Delaying the application of the Directive throughout all of the EU until 2007 can best mitigate these risks.

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