



European Economic and Social Committee

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Company law/Corporate
governance

Brussels, 10 December 2003

OPINION

of the European Economic and Social Committee

on the

Communication from the Commission to the Council and the European Parliament
Modernising company law and enhancing corporate governance in the European Union –

A plan to move forward

COM(2003) 284 final

On 22 May 2003 the European Commission decided to consult the European Economic and Social Committee, under Article 262 of the Treaty establishing the European Community, on the:

*Communication from the Commission to the Council and the European Parliament
Modernising company law and enhancing corporate governance in the European
Union - A plan to move forward
(COM(2003) 284 final).*

The Section for the Single Market, Production and Consumption, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 12 November 2003. The rapporteur was **Mr Ravoet**.

At its 404th plenary session of 10 and 11 December 2003 (meeting of 10 December) the European Economic and Social Committee adopted the following opinion unanimously.

1. Introduction

1.1 The European Commission has just submitted a Communication to the Council and the European Parliament entitled Modernising company law and enhancing corporate governance in the European Union - a plan to move forward (COM(2003) 284 final).

1.2 This communication is the Commission's response to the final report of the High Level Group of Company Law Experts appointed by **Commissioner Bolkestein** entitled A modern regulatory framework for company law in Europe.

1.3 The communication defines the key policy objectives which should inspire any future action to be taken at EU level with regard to the modernisation of company law and the reinforcement of corporate governance. In this connection the Commission is proposing an action plan, prioritised, over the short, medium and long term. For each priority it indicates which type of regulatory instrument should be used, and by when.

1.4 The action plan has two objectives: 1) strengthening shareholders' rights and the protection of third parties and 2) fostering efficiency and competitiveness of business.

1.4.1 With regard to the first objective, the Commission argues that an effective regime for the protection of shareholders and their rights, protecting the savings and pensions of millions of people and strengthening the foundations of capital markets for the long term in a context of diversified shareholding within the EU, is essential if companies are to raise capital at the lowest cost.

1.4.2 Maintaining efficient protection of members and third parties will be even more important in the future, in view of the increasing mobility of companies within the EU.

1.4.3 With regard to the second objective, business efficiency and competitiveness depend on many factors, particularly a sound framework of company law. and a proper balance between actions at EU level and actions at national level.

2. **Gist of the communication**

2.1 The action plan divides into seven main parts: corporate governance, capital maintenance and alteration, groups and pyramids, corporate restructuring and mobility, the European private company, the European co-operative society and other EU legal forms of enterprise and enhancing the transparency of national legal forms of enterprise.

The Commission concentrates mainly on corporate governance.

2.2 With regard to corporate governance, the Commission proposes that the EU should not develop a European code but rather follow a common approach with respect to a few essential rules and adequate co-ordination of corporate governance codes.

These rules include:

– *Enhancing corporate governance disclosure*

On this point of the Commission proposes that listed companies should be required to include in their annual report and accounts a statement of corporate governance.

The Commission also intends that information should be provided about the role played by institutional investors.

– *Strengthening shareholders' rights*

The action plan proposes, inter alia, that shareholders of listed companies should be provided with electronic facilities to access the relevant information in advance of general meetings.

Moreover, in order to establish a shareholder democracy based on the one share/one vote principle, the Commission is proposing that a study be carried out in the short or medium term on the consequences of such an approach.

– *Modernising the board of directors of listed companies*

The action plan proposes that where there is the risk of a conflict of interest for directors of listed companies, decisions should be made exclusively by non-executive or supervisory directors who are in the majority independent. The setting up of nomination, remuneration and audit committees should also be encouraged.

With regard to the remuneration of the directors of listed companies, the EU's objective is to promote a regulatory regime composed of four key items: disclosure of remuneration policy in the annual accounts, disclosure of details of remuneration of individual directors in the annual accounts, prior approval by the shareholder meeting of share and share option schemes in which directors participate, proper recognition in the annual accounts of the costs of such schemes for the company.

– *Directors' responsibilities*

The aim is, inter alia, to make provision for the collective responsibility of all board members for financial and key non-financial statements.

– *Co-ordinating corporate governance efforts of Member States*

The aim is to encourage the convergence of national codes by the establishment of a European Corporate Governance Forum.

2.3 The second part of the communication deals with *capital maintenance and alteration*.

The aim is, inter alia, to simplify the Second Directive in order to promote business competitiveness without reducing the protection offered to shareholders and creditors.

2.4 The third part of the communication deals with *groups and pyramids*.

The Commission does not intend to revive the draft Ninth Directive on group relations but rather to adopt specific provisions in a number of areas, e.g. the possible exclusion from listing of companies belonging to abusive pyramids.

2.5 The fourth part deals with *corporate restructuring and mobility*.

In the short term the Commission intends, inter alia, to adopt proposals for directives on cross-border mergers and the transfer of the seat from one Member State to another.

2.6 The fifth part deals with the *European Private Company*.

This optional form of company would serve the needs of SMEs which are active in more than one Member State.

2.7 The sixth part deals with the *European Co-operative Society and other EU legal forms of enterprises* (e.g. foundations, mutual societies).

The Commission intends to actively support the ongoing legislative process engaged on these statutes and to give significant attention to the development of new European legal forms of enterprises.

2.8 The seventh part deals with *enhancing the transparency of national legal forms of enterprises*.

The Commission argues that it is necessary in the medium term to increase disclosure requirements for all legal entities with limited liability.

3. General comments

3.1 The Committee welcomes the outlines of the Commission communication laying down the action plan modernising company law and enhancing corporate governance.

3.2 The Committee endorses the Commission's two objectives, strengthening shareholders' rights and protecting third parties, and fostering efficiency and competitiveness of business which are crucial components of economic growth and job creation. Moreover, as the Commission points out, this initiative is one of a number of European initiatives geared to these two objectives, taking account of workers, as stipulated in the communication on corporate social responsibility.

3.3 The Committee therefore supports the Commission when it proposes to make a proper distinction between categories of companies, with a more stringent framework for listed companies and companies which have publicly raised capital (point 2.1 of the communication). These distinctions make it possible to take account of the specific features and needs of each category of company.

3.4 The Committee notes that the European Commission communication contains a number of very general principles. It remains to be seen how these will be fleshed out. This is true, for example, of the measures which the Commission intends to adopt in connection with strengthening shareholders' rights and modernising the board of directors of listed companies.

3.5 The Committee also points out that certain concepts used in the communication are vague and should be clarified. Thus, in connection with the annual corporate governance statement, what exactly is meant by "any material transactions with other related parties" (point 3.1.1(e) of the communication)?

3.6 Finally, the Committee generally approves the Commission's timetable of priorities. It stresses the importance of resolving, as rapidly as possible and taking account of the actual situation of companies, a certain number of problems, including those of a cross-border nature, such as cross-border mergers or the transfer of a company's head office from one Member State to another, as well as cross-border obstacles to the exercise of shareholders' rights.

4. Specific comments

Corporate governance

4.1 The Committee is pleased that the EU has no plans to establish a *European code of corporate governance*. As a 2002 study commissioned by the European Commission shows¹, the main divergences between the Member States result from the differing national law and not from corporate governance codes, which generally show a high degree of convergence. The existence of a variety of codes in the EU is not generally seen as a problem for investors.

4.1.1 However, in the context of globalisation and EU enlargement, the Committee considers that it is in the interests of companies and investors to have the certainty that foreign companies are complying with a minimum number of essential and internationally recognised good management principles. These principles complement or clarify the regulatory provisions already adopted by the Member States. Other rules should come within the domain of self-regulation, e.g. corporate governance codes drawn up directly or with the close cooperation of issuers. The flexibility of this generally successful approach makes it possible to take greater account of the development of markets and the specific features of companies. The Committee points out that failure to comply with recommendations is punished by investors, who will not invest in companies which do not observe corporate governance standards.

4.1.2 Although the Committee generally endorses the corporate governance principles adopted by the Commission, it remains to be seen how they will be fleshed out in practice.

4.1.3 The Committee feels that the EU should lay down essential internationally recognised principles rather than becoming involved in too much detail. The latter approach would not meet the need for flexibility which is a precondition for the effective operation of companies.

4.2 With regard to *enhancing corporate governance disclosure*, the Committee endorses the principle of an annual corporate governance statement, which in a number of countries is already drawn up at the request of shareholders. The Committee feels that listed companies must be transparent and that they must provide investors with information on their mode of operation.

4.2.1 However, the Committee considers that the planned inclusion of an annual declaration in the accounts of listed companies should not place the Commissioner under an obligation to carry out a detailed examination of the content of the declaration. His role should, rather, be to check that the declaration has been made.

¹ Comparative Study of Corporate Governance Codes relevant to the European Union and its Member States
http://europa.eu.int/comm/internal_market/en/company/company/news/corp-gov-codes-rpt_en.htm

4.2.2 Moreover, with regard to information on the role played by institutional investors, the Committee stresses that a clear distinction should be made between institutional investors and shareholders holding a certain percentage of shares. To this end, the Committee feels that the concept of "institutional investor" should be defined in line with the definition set out in the rules on financial markets, and in particular those concerning investment services.

4.3 With regard to *strengthening shareholders' rights*, the Committee considers that companies should be given the opportunity to use new information technologies and that the current rules should be adapted accordingly. This should be an option rather than an obligation.

4.3.1 The Committee generally approves the measures envisaged by the Commission to make it easier for shareholders to exercise their voting rights. Companies should be able to make it easier for shareholders to vote, e.g. without their having to be present at the general meeting.

4.3.2 The Committee also notes the Commission's intention of carrying out a study on introduction of the one share / one vote principle. This study should clearly be part of the more general examination of the financing of companies and corporate governance.

4.4 With regard to *modernising the board of directors*, the Committee favours the drawing-up of a recommendation setting out a number of minimum criteria for the establishment, membership and role of the nomination, remuneration and audit committees. However, the Committee feels that these should be minimum criteria and that the Commission should not enter too much into detail with the risk of compromising the flexibility which is essential for the effective operation of a company.

4.4.1 Moreover, the Committee points out that the concept of "conflict of interest" should be defined. It also considers that the principle of collective decision-making by the board of directors should not be called into question. Even if it should be considered desirable for the preparatory work for decisions of the board of directors to be done by committees, these committees should under no circumstances take the decision.

4.4.2 With regard to the remuneration of directors of listed companies, the Committee endorses the Commission's objective: greater transparency of remuneration for directors of listed companies is what investors want. The Committee feels, however, that the EU should not intervene here. At the time of enlargement it should be ensured that the question is dealt with by national rules or recommendations which take account of specific national situations and of the culture of each state.

4.5 With regard to *directors' responsibilities*, the Committee considers that the question should, in keeping with the subsidiarity principle, be dealt with by each individual Member State. If the Commission is to intervene, it is essential that a detailed study first be carried out on the various aspects of directors' civil and criminal-law responsibilities and that the question of responsibility be dealt with as a whole rather than in piecemeal.

4.6 With regard to *co-ordinating corporate governance efforts of Member States*, the Committee notes the plan to establish a European Corporate Governance Forum. The objective of the Forum should be, as the Commission envisages, to promote the convergence of national codes and not to lay down new obligatory rules on corporate governance. The Forum should include representatives of the players concerned, including issuers and financial intermediaries.

Capital maintenance and alteration

4.7 The Committee endorses the Commission's policy in this area. The examination of the recommendations of the SLIM Group on Company Law should be continued.

Groups and pyramids

4.8 The Committee is glad that the Commission does not intend to revive the draft Ninth Directive on group relations.

4.8.1 The existence of groups of companies is a useful and legitimate feature of economic life. Any Commission initiatives on groups of companies or pyramids should be based on a prior study of the usefulness and impact of the planned measures. The Commission should not indirectly establish law on groups of companies and thus prevent them from operating.

4.8.2 The scope of certain terms should be clarified. Thus, it appears that the Commission is planning the exclusion from listing of companies belonging to *abusive pyramids*, if such action appears appropriate on the basis of a detailed study and in the opinion of experts, and not only that of the European Securities Committee. What is meant by "abusive pyramids"? The difference between "normal" and "abusive" pyramids should be clarified.

Corporate restructuring and mobility

4.9 In the process of establishing a truly integrated market, the Committee considers it essential that obstacles to companies' mobility be eliminated. In this context, the Committee points out that the Commission is intending in the short-term to adopt two proposals for a directive, one on cross-border mergers and the other on the transfer of a company's head office from one Member State to another.

4.9.1 However, the Committee considers it necessary to look into the question of the involvement of workers in the context of these cross-border operations. Provisions should preserve the rights of workers, e.g. their right to information and consultation, in accordance with the rules of social dialogue, and more generally in the framework of governance.

4.9.2 Finally, the Committee approves the objective of simplifying the Third and Sixth Directives on mergers and divisions of companies and the principle of introducing provisions on

squeeze-out and sell-out rights. It remains to be seen how these objectives will be fleshed out in practice.

European private company

4.10 The Committee has already in the past given its wholehearted support to the development of an optional statute² in this area. The Committee therefore endorses the Commission's initiative to launch in the short term a "feasibility study in order to clearly identify the practical benefits of – and problems related to – the introduction of an EPC statute". The Committee would like to see the early introduction of a statute which responds to the needs of SMEs.

The European Co-operative Society and other EU legal forms of enterprises

4.11 The Committee points out that in July 2003 the Council adopted the Regulation on the Statute for a European Cooperative Society and the Directive supplementing the Statute for a European Cooperative Society with regard to the involvement of employees³.

4.11.1 The Committee also supports the initiatives for the optional adoption of new legal forms of European enterprise. The cooperative and mutual sectors must have instruments enabling them to participate fully in the advantages of an integrated European market.

Enhancing the transparency of national legal forms of enterprises

4.12 The Committee shares the Commission's concern and agrees that there is a need in the medium-term to examine the scope and nature of the directive which may be adopted.

5. Conclusion

5.1 The Committee endorses the European Commission's initiative. It is part of a new phase in the harmonisation of company law and the strengthening of corporate governance. The action plan takes account of the cross-border dimension of commercial relations. In particular, with regard to corporate governance, the Committee calls for basic, internationally recognised principles of good management to be drawn up at the earliest opportunity.

² OJ C125, 27.5.2002

³ OJ C129, 27.4.1998

5.2 The action plan is concerned mainly with relations between shareholders, investors and companies with a view to optimising their management. The Committee points out that the Commission's action must be part of a more general policy for companies which takes account of the protection of workers.

Brussels, 10 December 2003.

The President
of the
European Economic and Social Committee

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Roger Briesch

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