Synthesis of the responses to the Communication of 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 of 21 May 2003

A Working Document of DG Internal Market

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NOTE TO THE READER

This report provides an objective presentation of the comments received by the Commission services in response to the Commission Action Plan "Modernisation of company law and enhancing corporate governance in the European Union – a plan to move forward", adopted in May 2003.

This presentation does not reflect any judgement on the part of the Commission services as regards the different comments made in the consultation. This document seeks to provide a synthesis of the basic positions advanced by respondents in respect of the recurrent themes in the feedback to the consultation.

In drawing up this synthesis, the Commission services have been guided not only by the number of proponents expressing a particular point of view, but also by qualitative considerations such as the extent to which the respondents are representative and the arguments advanced by respondents in support of their views. For this reason, the report will not present a systematic statistical/quantitative analysis of the responses provided on each point. It will endeavour to present a qualitative assessment of the responses received and of the main arguments underpinning these responses. What follows should therefore be regarded as a summary of statements volunteered by respondents regarding their perceived priorities in relation to the Action Plan.

Where relevant, the report will include histograms indicating the general feeling of respondents towards some individual initiatives of the Action Plan. These should be treated and considered with due care since they are inevitably the result of subjective interpretation.

Few respondents answered systematically to all the points mentioned in the Commission Action Plan. Instead, responses tended to deal extensively with the issues of greatest concern to them, especially the issues linked to corporate governance.

The report will broadly follow the structure of the Action Plan. It will start with a general presentation of all the replies received. It will then outline the general comments received on the process proposed, the objectives of the Action Plan and the scope of action and timeframe proposed. The core of the synthesis report will then be the responses to the list of initiatives contained in the Action Plan.

1. INTRODUCTION

The document summarises the responses to the Commission Action Plan "Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward", adopted by the Commission on 21 May 2003. The consultation of interested parties and the provision of a synthesis report fully comply with the Commission's commitment to greater transparency and public consultation.

Box: Core elements of the Commission Action Plan

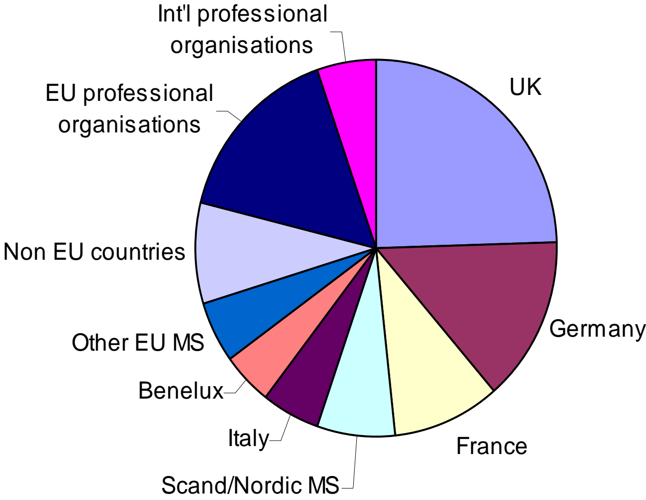
The Action Plan defines the key policy objectives which should inspire future actions to be taken at European Union level in the areas of corporate governance and company law. It prioritises over the short, medium and long term, the various actions which appear necessary to achieve a modern European regulatory framework. It indicates which type of regulatory instrument should be used, and outlines appropriate timeframe. In developing the Action Plan, the Commission has paid particular attention to the need for any regulatory response at European Union level to respect a number of guiding criteria: the subsidiarity and proportionality principles; the need to be flexible in application, but firm in the principles; and the need to help shape international regulatory developments.

The main objectives pursued by the Action Plan are to strengthen shareholder rights and third party protection, with a proper distinction between categories of companies, and to foster efficiency and competitiveness of business, with special attention to some specific cross-border issues.

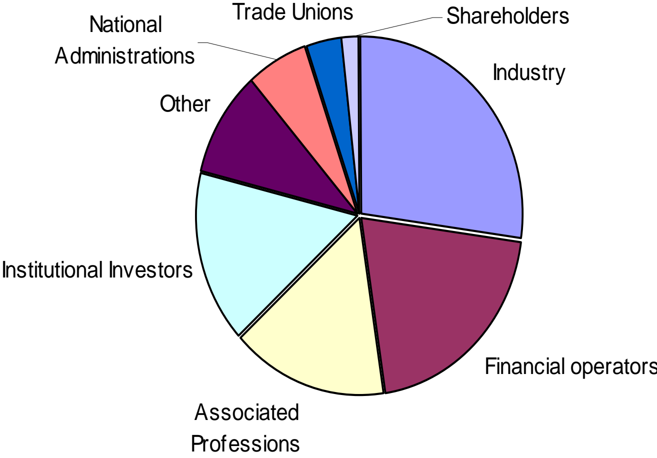
The Action Plan is based on a comprehensive set of proposals, grouped under six important chapters: corporate governance, capital maintenance and alteration, groups and pyramids, corporate restructuring and mobility, the European Private Company, cooperatives and other forms of enterprises.

114 contributions were received in response to this Action Plan. Reponses were received from a full cross-section of industry representatives, institutional investors, financial services providers and professional service providers (auditors, accountants or lawyers). Some national administrations also replied to the consultation. There was a wide geographic coverage with respondents from 17 countries including 14 EU Member States and 1 acceding country. A significant number of replies were received from representative organisations at EU level.

Responses to the consultation - Breakdown by countries



Responses to the consultation - Breakdown by category of respondents



The following broad-brush presentation highlights the main themes which were the object of extensive comments. In addition to some general and recurring messages outlined below, many other valuable insights were gleaned from the submissions. It has proved impossible to document all these in a text of a general nature, but the Commission will ensure that they will be taken into account in its preparatory work on the various initiatives of the Action Plan.

2. GENERAL REMARKS

2.1. The process

Widespread support was expressed in favour of the Commission initiative to modernize company law and enhance corporate governance. The vast majority of respondents considered this as an essential step to restore confidence in capital markets and the EU economy. The possibility for all interested parties to comment on the content of the Action Plan was also very much welcomed by respondents.

Some respondents highlighted the difficulty to comment on individual measures proposed in the Action Plan given the general wording of the Communication. They therefore considered their contribution as provisional and reserved specific observations to future consultations Some also highlighted the need for further clarification of a significant amount of detail and terminology used in the Plan

2.2. The objectives

The very large majority of respondents welcomed the Action Plan as a major contribution to capital market efficiency and enhanced confidence in the market. The focus recently placed on company law and corporate governance by the Commission was seen as crucial both for restoring trust in capital markets and enhancing the competitiveness of business in the EU.

A few respondents, however, not fully share this view. The following arguments were put forward:

- The objective of simplification and reduction of rules and regulations is not really taken into account in the Action Plan. The latter is likely to lead to considerable addition of rules and recommendations to those already in force. This could be largely detrimental to business confidence;
- Some respondents were of the opinion that the Action Plan should have paid more attention to the interests of other stakeholders in the corporate governance debate. The framework proposed by the Action Plan was viewed by some as considering business only accountable to its shareholders with stakeholders and wider society in general being a secondary consideration. Some also felt that corporate governance could not be separated from corporate social responsibility.
- The Action Plan does not contain enough measures aimed at regulating the activities of the professionals from the financial sector.

Some respondents focused more on the international dimension of the Action Plan. Some highlighted the need for the EU not fall behind in the increasingly globalised business community. A high-level approach, based on framework principles, would be the most effective way to make sure that companies from third countries or accession countries complied with the EU approach on corporate governance, and more generally company law.

2.3. The scope of EU action

To achieve the objectives pursued (fostering efficiency and competitiveness of business, and strengthening shareholders rights and third parties' protection), the large majority of respondents considered that a fully integrated approach combing self-regulatory market solutions, adequate co-ordination of corporate governance codes and legislation where necessary, was viewed as absolutely necessary. A small number of respondents however stressed that this integrated approach would inevitably be at odds with the prevailing international view, shared by the High Level Group, that a "one size fits all" approach is not appropriate.

Several respondents, however, expressed concerns about the apparent contradiction between the explanatory memorandum which notes the need to avoid over-regulation and the establishment through the Action Plan of an extensive legislative programme, in particular the use of directives in the field of corporate governance. While the need for directives in important company law areas is acknowledged, it was generally recognised that directives are not an appropriate instrument in the corporate governance area because of the lack of flexibility and the risk that these directives could be followed by further overly prescriptive and detailed implementing measures.

Those measures deemed necessary should furthermore be given the appropriate form to ensure effective fulfilment of their respective purpose. A great number of respondents favoured a more extensive use of recommendations, allowing for adjustments to different national legal frameworks, traditions and other special circumstances.

While there was also a wider support for clarifying the rules of governance for listed companies in the first instance, some respondents stressed that applying the same rules to unlisted companies should be carefully considered so that their implementation does not have an adverse impact on competitiveness and freedom of establishment.

Most respondents also agreed with the Commission on the timing envisaged for the realisation of the Action Plan and the degree of priority attached to individual measures. The more detailed comments that follow will, however, highlight some initiatives for which a number of respondents considered that the timing envisaged by the Commission should either be brought forward or postponed. Among the comments made on this point, one can mention the following:

- the timing envisaged was perhaps too ambitious and would not leave enough time for proper consultation of all interested parties;

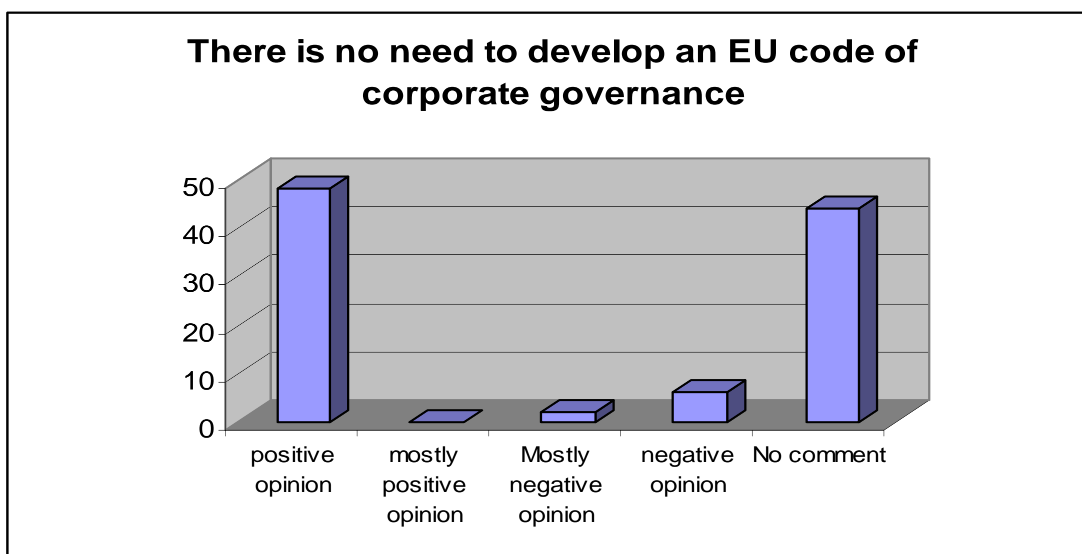
- the Commission should launch systematic consultation on all the individual proposals of the Action Plan. This consultation should include all those concerned, and not only experts from the business and academic sectors and Member States;

- the main measures of the Plan should be subject to detailed impact analysis as well as an analysis of their inter-dependencies and their relationship to the national legislation. The need to ensure subsidiarity and proportionality of the measures was also mentioned by some respondents.

3. CORPORATE GOVERNANCE

The Commission does not believe that a European Corporate Governance Code would offer significant added value but would simply add an additional layer between international principles and national codes.

The very large majority of respondents agreed with the Commission's assessment that there is no need for an EU corporate governance code. The view was generally expressed that corporate governance systems would develop and progress in a natural way under market pressure. The co-existence of different national codes was not perceived by issuers and investors as presenting any major difficulty. The arguments presented by the Commission in the Action Plan were considered as cogent and reasonable and the Commission was invited to follow this line of thinking in its future approach on corporate governance.



A very small number of respondents however disagreed with the Commission's assessment. The arguments put forward were as follows:

- If there is enough convergence between national codes, it should not be difficult to move towards a single code at EU level. An EU code could be particularly helpful for multinationals for which reference to a national code is not appropriate;

- The absence of an EU code could lead to regulatory arbitrage and delocalisation toward Member States with the least constraining code;

- An EU code could be used as a "reference code" where some broad principles and notions could be defined at EU level and applied homogeneously at EU level. This, together with the EU co-ordinating role and use of regulations, would stimulate a further convergence.

3.1. Enhancing corporate governance disclosure

3.1.1. Annual Corporate Governance Statement

The Action Plan proposed that the Commission should prepare in the short term a proposal for a Directive setting up the main principles applicable to an annual corporate governance statement which should appear prominently in the annual documents published for listed companies.

General agreement was expressed on the principle of enhanced corporate governance disclosure. This is considered as an essential element to improve the transparency of companies and to ensure companies provide investors with better information on the key elements of their governance structure and practices. However, concerns have been expressed about the form that an EU initiative should take. Half of those who commented on this precise aspect expressed their preference for an EU recommendation as an instrument for introducing some disclosure requirements, rather than a Directive. The main reason expressed was that a directive would inevitably result in a high level of prescription which would prevent disclosure evolving through market developments. It was also argued that the process for adopting such a Directive would be too complex and time-consuming, which would not fit with the urgent need to improve company disclosure.

As far as the content of the proposal is concerned, the comments (and sometimes concerns) expressed by the majority of respondents related to three key aspects of the proposal:

– Concern about **duplication of existing requirements** under national legislation, national codes or stock exchange regulations. Some responded that a number of items to be disclosed in the corporate governance statement were already regulated by mandatory requirement in Member States (such as the operation of the shareholders' meeting and its key powers and the description of shareholders' rights). Others also stressed that some of these requirements were already covered by the financial reporting instruments and that the Commission should take account of disclosure requirements set out in International Accounting Standards (IAS). This is especially the case for the direct and indirect relationship between major shareholders and the company.

– Concerns about **the scope of the Corporate Governance Statement**. On the one hand, a number of respondents considered that the non exhaustive list of items proposed by the Commission was already too demanding and related more to matters dealt with under company law (or governed by accounting rules). The statement should therefore focus on pure corporate governance information such as the composition and operation of the board and committees or the reference to a code. On the other hand, a smaller number of respondents suggested additional items to be included in the statement. They concerned, inter alia, details about the directors' nomination process, information of the holdings owned by shareholders exceeding the disclosure threshold, or details on external auditors. Moreover, some of the data proposed for inclusion in the corporate governance statement are received from third persons and can hardly be verified by the company (e.g. information on major holdings which is very difficult to check due to involvement of intermediaries/custodians and information about relationships between shareholders). Therefore asking a company to certify such data might be

inappropriate. Finally, a number of respondents nevertheless felt that it was difficult to comment on the scope given the very general and sometimes unclear nature of the items mentioned in the disclosure list.

– Concerns about the **inclusion of the Corporate Governance Statement in the annual accounts/reports.** A number of respondents did not support such inclusion as this would make it subject to statutory audit requirement and lead to additional costs for listed companies without generating much added value. It was argued that statutory auditors could only express an opinion on whether the corporate governance statement complied with the respective reporting standards while assessing the adequacy of management was the primary task of those in charge of governance.

But the initiative proposed by the Commission was generally favourably received by the majority of respondents on this point.

3.1.2. Information about the role played by institutional investors

> The Commission announced its intention to put forward, in the medium term, a proposal for a directive to oblige institutional investors to disclose their investment policy and their policy with respect to the exercise of voting rights in companies in which they invest, and to disclose to their beneficial holders at their request how these rights have been used in a particular case.

The general feeling was that there is a strong case for institutional investors to play a full and proper role in the companies they invest in and to ensure greater accountability of the institutional investors. But the legislative initiative as proposed in the Action Plan was received much more cautiously by a majority of respondents, not only institutional investors' representatives, but also industry at large.

The request for disclosure of investment policy was received positively by a majority of respondents, since it is already current practice in a number of Member States. However, the comment was made that this should not involve the disclosure of information of a confidential nature.

But a minority of respondents were critical about the two other proposals - to request institutional investors to disclose to their beneficial holders their voting policy and, on request, how voting rights have been used in a particular case. The main arguments put forward can be summarised as follows:

- Some respondents questioned the extent to which such a requirement would enhance institutional investors' participation in the companies in which they invest. They considered the existing rules imposing an obligation on shareholders to deposit their own financial instruments and barriers to cross-border voting as being the main impediments to more active participation by institutional shareholders;

- Some respondents insisted that the policy concerning the exercise of voting rights could not be determined in advance using predetermined or theoretical methods. The policy of voting rights is by its nature very dynamic as it must be able to change very rapidly according to current circumstances;

- Some respondents expressed fears that this could constitute a distortion of competition vis-à-vis non-EU institutional investors;

- Some respondents also highlighted the difficulties in reconciling such obligations with the principle of equal treatment of shareholders. They considered that institutional investors should not have different rights or obligations compared to other shareholders.

On the other hand, there was a very wide support for the position expressed in the Action Plan that institutional investors should not be required to systematically exercise their voting rights.

Diverging comments were made on both the timing and the form of the legal instrument:

- While the majority of respondents did not express an opinion on the issue of **timing**, some considered the matter as urgent and asked for action in the short term while some felt it deserved more analysis and should be transferred to the list of long-term initiatives. The main reasons behind the latter view are that it is better to wait until an effective system which facilitates cross-border voting and solves problems linked to clearing and settlement is in place before requiring institutional investors to disclose information about voting policy and rights.

- Concerning the **choice of a directive** as the legislative instrument, a number of respondents argued that this area was mainly a matter for national codes and should therefore not be regulated by means of a prescriptive directive. A number considered this should be a matter of recommended good practice rather than of compulsion.

A few respondents (especially from the asset management industry) highlighted the need, when elaborating such a proposal, to take account of the relationship between beneficiaries, institutional shareholders and asset managers and of the role of investment managers to whom decisions on voting are delegated by institutional investors. They also highlighted the need to ensure that there is effective transparency at reasonable cost.

Finally a significant number of respondents noted that the terms "institutional investors" and "beneficial holders" were rather broad and could be easily misinterpreted.

3.2. Strengthening shareholders' rights

3.2.1. Access to information – use of electronic facilities to access relevant information in advance of General Meetings

The Commission considers that the provisions existing in the proposal for a Transparency Directive are a significant and proportionate first step towards ensuring that shareholders are provided with the electronic means to access the relevant information in advance of General Meetings.

Broad support was expressed for encouraging the use of electronic facilities for the receipt and dissemination of information, provided this remained voluntary and best practice, and was not made mandatory. The prevailing feeling was that technological progress could not yet allow the use of electronic means to be made compulsory and that listed companies should be encouraged to offer investors the opportunity to receive communications electronically. At the same time, traditional methods should nevertheless be retained and made freely available.

Any legislation should therefore be enabling in nature and not compulsory as is set out in the proposal for a Directive on Transparency requirements. However, a number of

participants strongly criticised the approach contained in this proposal whereby a decision by a general meeting to allow use of electronic means has to be supplemented by the individual consent of the shareholder concerned.

The Commission announced its intention to propose further measures in the medium term, if desirable, in the light of the implementation of the Transparency Directive. This was generally welcomed by the small number of respondents that provided feedback on it.

3.2.2. Enhancing other shareholders' rights and solving specific problems linked to cross-border voting

The Commission proposed to come forward, in the short term, with a proposal for a directive setting up a legislative framework aimed at helping shareholders to exercise various rights (for example asking questions, tabling resolutions, voting in absentia and participating in general meetings via electronic means). These facilities should be offered to shareholders across the EU and specific problems relating to cross-border voting should be solved.

A very large majority of respondents on this point supported the proposal of the Action Plan to develop a regulatory framework to encourage the exercise of various shareholders' rights in listed companies and to solve problems related to cross-border voting. This is the legislative proposal that was received most positively by a broad range of respondents. Only a very small number of respondents felt that the European Union should not legislate on the issue of shareholders' rights.

The Commission's attention was nevertheless also focused on the need to draw up balanced implementing measures. As far as voting by proxy is concerned, the company should not be expected to bear the entire administrative burden. Rather; the investor should also be asked to take the necessary steps to vote in absentia or by proxy. Some respondents also noted that the proposal should endeavour to place certain limits on shareholders' rights in order to prevent abuse. This could be done by setting out some conditions, such as on the exercise of the right to table resolutions and to ask questions.

Some concerns were expressed about the proposal to make it compulsory for companies to allow the use of electronic voting, and some felt that the decisions to implement such a means should be left to the discretion of individual companies. Some also highlighted the need for a generalisation of the use of electronic facilities for participation in the general meetings to be abuse-free and to be guaranteed a high standard of security. Some respondents also suggested that such rights, once developed for listed companies, could be introduced as optional for unlisted companies as well.

On cross-border voting, the recommendations made by the "expert group on cross-border voting in Europe" were mentioned as being a good basis for any further EU initiative in this field. A key task in this regard would be to monitor and boost the efficiency of custodians and make sure that each intermediary looked to its accountholder for valid voting instructions. Many respondents felt this was a matter of urgency and supported the Commission proposal to deal with this in the short run.

3.2.3. Establishing shareholder democracy over the medium to long term

The Commission announced its intention to launch, in the medium term, a study on the consequences of an approach aiming at achieving a full shareholder democracy, at least for listed companies.

The responses on this point did not comment to any significant extent on the proposal to launch a study but focused more on the eventual establishment of a "one share = one vote" principle throughout the European Union. Very diverging views were expressed on the issue. A small majority of respondents on the subject supported the generalisation of the "one share = one vote" principle and urged the Commission to launch its study as a matter of urgency.

A significant minority, however, expressed sometimes serious concerns about the idea and contested the view expressed in the Action Plan that shareholder democracy should be interpreted as "one share = one vote". Some argued that such a principle would run counter to the principle of freedom of organisation and management of companies and would be detrimental to the shareholders' loyalty. While not contesting the idea of launching a study on the consequences of a "one share = one vote" approach, they argued such a study should be launched with a broader perspective and elaborate comprehensively on the question of shareholder democracy. It should also address the issues regarding pyramidal groups, cross shareholdings, golden shares etc..

One respondent representing pan-European views considered it appropriate for the EU to set as a target the enforcement of the "one share = one vote" principle for all newly listed corporations from a certain date (2006 was suggested) and to decide a workable solution for existing listed companies where the principle is currently not enforced.

There was, however, a broad recognition of the difficulties experienced with the issue in the Takeover Bid Directive and the current uncertainty as to whether these would be resolved.

3.3. Modernising the board of directors

3.3.1. Strengthening the role of independent non-executive and supervisory directors

The Commission proposes to adopt in the short term a recommendation aimed at promoting the role of (independent) non-executive or supervisory directors. Minimum standards on the creation, composition and role of the nomination, remuneration and audit committees should be defined at EU level and enforced by Member States, at least on a "comply or explain" basis.

A significant majority of the respondents to this point welcomed the Commission initiative to prepare a recommendation aiming to strengthen the role of independent non-executive and supervisory directors. The presence of independent representatives on the board, capable of challenging the decisions of management was considered by many as a means of protecting the interests of shareholders and, where appropriate, other stakeholders. A small number of respondents however criticised the Commission's intention to adopt a recommendation in this field. They considered board composition to be a corporate governance code issue where "comply or explain" must apply, and expressed reservations about strengthening the role of independent directors any further.

Many respondents however stressed the difficulty in defining what independence really means, and that in a rapidly evolving global economy, it is impractical to comprehensively list all possible threats to independence. Defining a lengthy set of rules would not necessarily be a solution, since the spirit of these rules could easily be circumvented. A principle based approach was therefore advocated to assess threats and safeguards to independence, as is the case in national law or codes requiring certain directors to be independent.

Many respondents also stressed that while it was indeed important to ensure independence, the involvement of high quality individuals, able to exercise objective judgement, was of greater importance than satisfying detailed rules on independence. Independence requirements should not prevent companies from enrolling non-executive directors of appropriate calibre, and "comply or explain" should be an available solution to any potential impairment of a non-executive director's independence.

The suggestion was also made by some that the supervisory board should publish its reasons for considering a director to be independent in the Corporate Governance Statement in those cases where there is any doubt as to the independence of the individual concerned.

Concerning the proposal to provide non-executive or supervisory directors with the exclusive rights to take decisions in areas where executive directors clearly have a conflict of interest, some respondents highlighted that it was important not to call into question the principle of collective responsibility of decisions taken by the board of directors that exists in some Member States.

A large number of responses also commented on the following issues:

(1) Nomination Committee: A very large majority of respondents suggested that the responsibility for identifying candidates to fill board vacancies should in principle be entrusted to a group composed mainly of independent non-executive directors, as proposed in the recommendation of the High level Group. To do otherwise would undermine the effectiveness of the independent challenge in the boardroom and, as was emphasised by some respondents, would allow executive directive directors to select 'tame' or 'friend of the friend' non-executive directors who would be unlikely to provide the necessary challenge to the executive management. This would have a serious impact on capital market confidence in the business community. The involvement of an independent, objective perspective in board appointments is an integral part of the overall governance "checks and balance" in the company.

(2) Number of mandates that may be held concurrently. Many of the respondents who commented on this point requested that a flexible approach be adopted and that any decision or recommendation should not necessarily stem from a pure numerical reasoning. A one-size-fits-all approach would take little account of the complexity of individual companies and the amount of work required to be undertaken. Some suggested that it would be more practical to introduce the necessary safeguards by requiring directors to disclose the nature and extent of their other commitments and confirm that they will have enough time to perform their duties. As far as the issue of interlocking directorships and the impact on their independence are concerned, some considered that this matter could only be

dealt with effectively in the framework of national codes, given the large diversity of situations.

(3) Choice between two types of board structures: With regard to the initiative to prepare a proposal for a directive allowing all listed companies to choose between the two types of board structures (monistic/dualistic), a majority of respondents supported the Commission's approach and highlighted the importance of ensuring flexibility for companies in their choice of board structure. Given the significant differences in some cases between Member States' legal regimes, particularly in the area of employee participation, some respondents however argued that it should be left to national legislators to decide whether or not to open national company law to both systems.

A minority of respondents expressed great scepticism as to the benefits such a choice would bring. They argued there was no real demand from companies for such flexibility and that it could result in lengthy and complex company law in each Member State. The point was also made that such a proposal would not pass the subsidiarity test and would complicate and "freeze" the traditional organisational structures in EU Member States.

3.3.2. Directors' remuneration – Adoption of a Commission recommendation

The Commission proposed the adoption, in the short term, of a recommendation fostering an appropriate regime for Directors' remuneration.

While emphasizing that directors' remuneration in the final analysis should be the prerogative of a company and its shareholders, and not government, a large majority of respondents on the issue welcomed the Commission announcement to issue a recommendation in the short term. They consider it as an important principle of shareholder protection that there should be proper recognition in annual accounts of any dilution of share capital. Some considered that this should only be the case for directors of listed companies.

A small number of respondents, however, felt that the remuneration of board members should remain a matter for national laws or corporate governance codes and questioned the need for any intervention at EU level. Some also strongly contested the need for details of remuneration of individual directors to be disclosed, since, they argued, investors need to know the global cost rather than individual remuneration.

With regard to the recognition in the annual accounts of the cost of share options schemes, some highlighted this as a controversial issue on which the International Accounting Standards Board was in the course of developing a new international financial reporting standard.

3.3.3. Enhancing Directors' responsibilities: Confirmation of the collective responsibility of all board members

The Commission proposed to confirm by law at EU level the collective responsibility of board members for financial and key non-financial statements in the short term.

Comments on the need for the EU to develop a regulatory framework in this field were fairly evenly split.

A majority of respondents supported the principle of the collective responsibility of all board members for financial statements. The comment was made, however, that the responsibility of the supervisory board should not be extended beyond the audited financial statements (and should therefore not apply for instance to quarterly reports). But the divergence in views was more subtle on whether collective responsibility should also apply for key non-financial statements, failing a proper definition of what sort of key non-financial statements this would entail. Some argued it might be impossible to discuss all this information among all members of a board prior to publication. All the information cannot be approved at the same time by all the members of the managing and of the supervisory board, so such proposal was seen as unrealistic and unworkable. But any initiative at EU level should not weaken the responsibility arrangements in individual member States. Minimum standards would therefore be appropriate.

A minority of respondents felt such matters were deeply rooted in the political and cultural background of Member States' legal systems and should therefore be left to national laws or corporate governance codes. Many Member States have equivalent mechanisms in place and it would be difficult to fit an EU concept into Member States legal systems without being able to take each system into account in its entirety. The same respondents argued this was the approach of the proposal for Directive on Transparency requirements which was deemed by a number of them to address the issue of collective responsibility in an appropriate manner. They therefore argued in favour of an in-depth study to assess whether there was a strong case for common EU rules.

Other questions that were put forward included to whom board members should be responsible (any extension of responsibility beyond shareholders was considered unacceptable by some), who would raise respective claims or to whom they would have to be addressed.

3.3.4. Enhancing Directors' responsibilities: introduction of special investigation rights, development of a wrongful trading rule and imposition of directors' disqualification

The Commission announced its intention to come forward in the medium-term with a proposal for a Directive to enhance the responsibilities of Directors.

This initiative was supported by a small majority of respondents but it was made clear that any directive on this matter should give flexibility to Member States as to how such provisions were implemented. An important minority however criticised all these proposals as going much further than the framework rules envisaged by the High Level Group. Although decision-makers in companies should indeed be held liable for their misconduct, company management involves taking risk, which should be allowed for in legislation. The comment was made that such initiatives would belong more to the sphere of insolvency or criminal law and would not fall under company law.

A recurrent comment was that the rules that would eventually be established should be set up in a constructive manner and that all necessary safeguards should be built into the rules in order to prevent disappointed shareholders abusing such rules. It was mentioned that becoming shareholder indeed implies a certain amount of risks and that an investment in a company may suffer from poor performance without any misconduct on the part of directors.

- As far as the introduction of a special investigation right is concerned, abuses should be avoided by fixing a relatively high percentage of minimum capital and defining strict conditions to exercise this right. Some highlighted that these rights were rarely exercised by shareholders but could still prove a useful safeguard for all those having dealings with companies. It was imperative, however, that these powers should not become a substitute for alternative remedies and that the investigating authority should have the power to decline a request for investigation where sufficient reasons for the investigation were not demonstrated by the applicants. The issue of costs and who should bear them also needed to be addressed in order to avoid abuse.

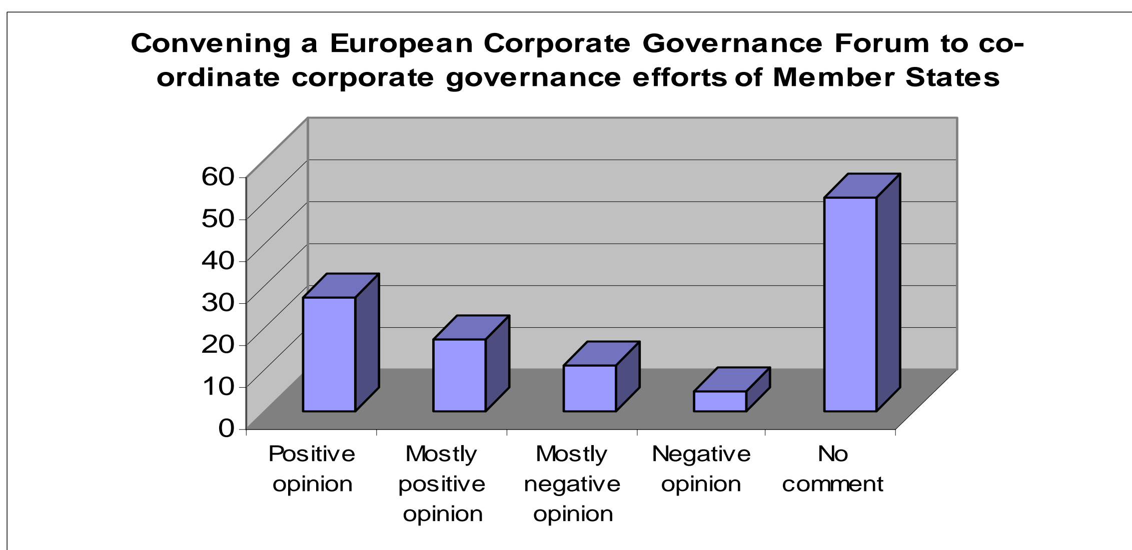
- With regard to the development of a wrongful trading rule, many considered this was an extremely sensitive issue which should remain a matter for Member States' legal systems. Moreover, some felt that this was not a matter of company law but rather of insolvency law or criminal law. It was also stressed that it is extremely difficult to specify when it is foreseeable that the company is insolvent and cannot continue to pay its debt. Finally, some argued that introduction of a wrongful trading rule might result in some sort of risk aversion for Directors.

- As far as the imposition of directors' disqualifications, it was also met with some scepticism, especially with the competence the European Union might have in this area. Some thought that this would be desirable but might be difficult to apply in practice. The imposition of directors disqualifications is an extremely grave sanction and should therefore be temporary; pronounced by the Judiciary of a Member State; and depend on the commission of a criminal act.

3.4. Co-ordinating corporate governance efforts by setting up a European Corporate Governance Forum

> The Commission's proposed to encourage the co-ordination and convergence of national codes through regular high level meetings of a European Corporate Governance Forum which should be set up in the short term. Participants to such a Forum will comprise representatives from Member States, European regulators, issuers and investors, other market participants and academics.

The idea of setting up a Forum was generally welcomed but great concerns were expressed over its mandate and objective. A general request was made to clarify the terms of reference of this Forum further. In this respect, a majority of respondents on this issue commented that if existing EU codes already showed a remarkable degree of convergence, this was mainly due to market pressure. The main task of this Forum should therefore not be to substitute to market forces in fostering further convergence and coordination of national codes but rather to disseminate best practices. Nor should it have any regulatory role or objective to institutionalise convergence of corporate governance.



A certain number of respondents also stressed that the Forum should be driven by issuers and investors, not by governments and regulators. Request was also made that all interested parties should be duly represented in the Forum, including all the legal professions involved in Corporate Governance and Company law issues.

The danger of duplication with the large number of bodies and high level Forum that discuss these matters was also mentioned. Ensuring a high level of coordination with these bodies, including the OECD, was therefore requested.

Some respondents, however, considered the establishment of the Forum as a priority since this could prove to be a source of advice for the Commission. The Forum could also play a useful role in assisting new Member States to meet suitable standards in a timely way. The proposal was also made to extend the Forum's mandate to company law issues.

Finally, a number of respondents were concerned by the heavy workload for Commission services and feared this could be detrimental to other priorities. Given the large number of parties involved, the Forum should be given sufficient resources to ensure its capacity to add value.

4. CAPITAL MAINTENANCE AND ALTERATION

4.1. Simplification of the Second Company Law Directive in respect of the formation of public limited liability companies and the maintenance and alteration of their capital.

The Commission intends to adopt in the short term a proposal aiming at simplifying the Second Directive on the basis of the recommendations of the SLIM Group and the proposals of the High Level group.

A very large majority of respondents supported the Commission in considering a rapid modernisation of the Second Company law Directive. Even if particular comments were expressed on some specific points, there was a general agreement that this should be done in line with the SLIM proposals and the recommendations made by the High level Group. However, comments were made on some specific points:

- Pre-emption rights: a few respondents expressed doubts about the proposal to restrict or withdraw pre-emption rights any further than currently permissible. Pre-emption rights are an asset belonging to shareholders, providing them with the means to protect the value of the capital they provide to business. Disapplying pre-emption rights without safeguards would represent a significant transfer of value away from existing shareholders and would weaken their position. While these respondents agreed it was in the interests of all parties for there to be some limited disapplication of pre-emption rights, there should not be any weakening beyond the current position.

- Financial assistance: some respondents questioned the proposal to relax the prohibition on companies using distributable reserves to provide financial assistance since it was considered that it might disadvantage shareholders.

- Burden of proof : only a few respondents felt that the proposal that creditors should bear the burden of proving that their interests are prejudiced by a capital restructure, results in a failure in the protection of their interests since in their opinion, good governance requires that the obligation to show that the creditors' position is secured should stay with the directors. Failure to protect the interests of creditors would weaken their position, increase risk and thereby raise the cost of borrowing and the cost of capital for companies. On the other hand, there was an opinion that requiring in all cases an enquiry as to creditors' position and creditor objection rights was not appropriate. The court should be able to dispense with an enquiry as to creditors' position (and the consequent publicity requirements and waiting period) if the company seeking to reduce its capital could demonstrate to the court that the creditors are adequately secured. Requiring an enquiry as to creditors' position and creditor objection rights to apply in all cases might lead to creditor hold-ups.

- Acquisition of own shares: some respondents considered that amendments to the present regime on the acquisition of own shares could be of little benefit compared to their disadvantages and should therefore be treated with much care. It was noted that any change in this area should be compatible with the Market Abuse Directive.

- Abandoning an expert valuation for the contributions in kind Some respondents argued that the use of a weighted average market price was subject to certain risks due to narrowness of the market or a limited trade volume, or existing distortions of value both in bull and bear markets. Additionally, it has to be taken into account that in many cases the Stock Exchange price of the stocks invested can be below their real value, which would result in immediate write-offs. Therefore additional protective measures might be necessary through burden of proof rules or enabling the minority shareholders to introduce a motion for an expert valuation.

- Accepting services as contributions in kind: Some respondents stressed that valuation problems had to be solved first. Setting a fixed price might be very difficult, especially for the services provided at the establishment stage when no transparent market exists. A couple of respondents felt that the respective proposal undermined the principle of capital formation and that services provided were "fugitive" and did not represent a part of liability "mass".

4.2. Alternative system:

The Commission announced the launch in the medium-term of a study into the feasibility of an alternative regime to the capital maintenance regime.

A large number of respondents welcomed the Commission's intention to launch a study into the feasibility of an alternative to the capital maintenance regime. Some respondents, however, urged the Commission to carry out this study in the short term taking into account that companies listed on the EU markets will be required to use IAS in their consolidated financial statements from January 2005. The accounting prescribed for pensions, deferred tax, the cost of share based payments and the impact of fair value measurement for financial instruments would affect the profits available for distribution. The possible result could be to reduce, or even eliminate, dividends being paid by some companies. This unfortunate situation and its possible repercussions on international competitiveness could be avoided if the calculations were based on whether the company had sufficient cash flow to enable it to pay a dividend, whilst maintaining the requisite amount of protection for its creditors.

The principle of launching a study may not have been subject to much criticism, but any idea about the possible introduction of an alternative regime in the second company law directive was forcefully criticised by close to half the respondents on the issue. Some questioned the usefulness of an alternative regime mainly inspired by non-EU jurisdictions. They considered that such a radical change of system regarding statutory capital was not advisable even at a later stage, since it would entail a loss of transparency and a loss of protection for third parties. The alternative introduction of a completely different kind of concept (alongside the existing capital formation and capital maintenance rules) would partly cancel out the harmonisation achieved and replace it with an unwelcome fragmentation of law. A certain level of harmonisation was felt essential.

5. GROUPS AND PYRAMIDS

5.1. Increased disclosure of groups financial and non financial information

The Commission intends to adopt in the short term legislative measures to improve the disclosure of financial and non financial information by groups.

A small majority of respondents on this point agreed with the Commission on the need for additional measures at EU level to improve the financial and non-financial information disclosed by groups when the parent company is not listed. This was seen as an essential part of the strategy to improve disclosure and transparency. The Commission's attention was however drawn to the need to assess carefully the trade-off between the cost and burden for reporting companies and the benefits for the users of such financial statements. Some also highlighted the risk that some additional disclosure could be provided in a very basic form and therefore provide little extra information.

A minority of respondents was much more critical of the Commission's proposal and asked for the issue to be better explained and deeply considered. A first argument advanced by some is that the matter should be left to Member States, since IAS regulations left this issue to Member States' competence in line with the subsidiarity principle. It was mentioned that the financial situation of various parts of the reporting group is already provided by segment reporting under IAS 14 which should be applied by listed entities from 2005. IFRS regulation leaves it to Member States to decide whether to apply the relevant accounting standard also to non-listed companies. A second argument put forward is that the task of consolidated accounts is to present the net assets, financial position and results of the parent enterprise and its consolidated subsidiaries as if they were a single entity. Requiring the disclosure of the effects of

intra-group transactions on individual enterprises would be inconsistent with that approach. If such information was nevertheless deemed necessary, it would be preferable considering such disclosure in individual financial statements. That would then be an issue for the Fourth Directive

5.2. Implementation of a Group Policy

The Commission intends to come forward in the medium term with a proposal for directive providing for a framework rule for groups allowing the adoption of of a co-ordinated group policy.

A small majority of respondents considered that it would indeed be beneficial to investors and markets as well as to business competitiveness to induce groups to adopt and implement a co-ordinated group policy. The focus of current company legislation was not ideally suited to groups, especially where subsidiaries wee wholly owned and operated as a division of the group rather than as separate companies in their own right. A framework should therefore be developed for groups to allow those responsible for managing a company within the group to implement a co-ordinated group policy, provided that the interests of the company's creditors were protected.

However, a significant minority of respondents criticised the Commission proposal. They felt that a more serious consideration of the need to undertake such an initiative was required. Some proposed that the Commission should undertake a feasibility study as is proposed for the alternative regime to capital maintenance. The main concern expressed was that the introduction of a group policy would be in clear contradiction with the basic principle that every company is, even when belonging to a group, a separate legal entity with its own rights and duties. There is therefore no need to define a rigid and uniform framework for the way enterprises want to organise themselves. This would be in contradiction with the dynamic, flexible framework which companies need.

5.3. Pyramids – Prohibition of stock exchange listing for abusive pyramids

The Commission intends in the medium term to give further consideration to the risk inherent in abusive pyramids and, if necessary, make a legislative proposal to prohibit them from stock exchange listings

A great variety of comments were expressed on the Commission's potential plan to refuse to admit to listing companies belonging to abusive pyramids, after consultation of the Committee of European Securities Regulators.

Quite a number of respondents on this point acknowledged the need for further reflection on the issue of the risk inherent in abusive pyramids for minority shareholder protection. While a number of respondents welcomed the consultation of the CESR, others felt that the opinion of CESR on its own was not sufficient and called for a more in-depth study.

The attention of the Commission was drawn by quite a few respondents to the difficulty of agreeing a clear definition of an abusive pyramid. The definition of abusive pyramids proposed by the High Level Group appeared very broad and might in fact capture perfectly innocent holding companies. It was also noted that pyramids not only improve transparency for financial services group but were sometimes necessary for supervisory reasons for instance for insurance companies. They were therefore necessary and not necessarily abusive.

Some respondents were more critical and claimed that imposing restrictions on companies' freedom to choose their appropriate structure by denying them access to listed stock exchanges could prove harmful. Since the main problems with pyramid groups seemed to come from a lack of transparency, the investors' risk concerning pyramidal groups could be effectively met by the corresponding transparency requirements in the documents to be published for stock exchange listing.

6. CORPORATE RESTRUCTURING AND MOBILITY

The Commission intends to present in the short term a new proposal for a tenth Company Law Directive on cross-border mergers and a proposal for a Fourteenth Company Law directive on the transfer of seat from one Member State to another. The Commission also considers that the simplification of restructuring transactions pursued by the relaxation of some of the requirements in the Third Directive and the Sixth Directive is desirable in the medium term.

The Commission's intention to present in the short term a new proposal for a tenth Company Law Directive and a proposal for a fourteenth Company Law Directive was supported by a very large majority of respondents. Many highlighted the urgency of coming forward with this long-awaited proposal. In drawing up these proposals, careful consideration would need to be given to the need to ensure there were comprehensive protection rights for members and creditors and to the interaction of the directives with domestic tax law. It should also recognise that rights to shift the seat/place of incorporation of a company can lead to fundamental changes to the rights and obligations on which a range of stakeholders may to date have relied.

A very small number of respondents were more critical about the Commission's intention. Some said that the time was not ripe for such a proposal and that more time was needed to draw the first conclusions from the European Company Statute. Others insisted that more progress needed to be achieved towards taxation and company law harmonisation.

A majority of industry representatives, however, criticised the approach proposed in the Action Plan for solving difficulties relating to employee participation. They opposed the idea that the regime agreed for the European Company Statute should be applied in a somewhat compulsory way in cases of cross-border mergers or transfer of seat, as well as rules that could lead to the import of different systems of employee participation in countries where such a system did not exist. They argued this could act as a disincentive to cross-border mergers and could undermine European companies' competitiveness. As a solution, some respondent recommended that the law of the country in which the merged company was incorporated or to which the seat was transferred should apply.

The request was also made to include investment funds in the scope of the directive so that it could enable fund managers to rationalise their fund rangers and approximate the economies of scale enjoyed by their peers in the US. The difficulty of merging on a cross-border basis was one of the main barriers to a single market for investment funds.

Very few comments were expressed on the proposal to amend the Third and Sixth Company Law Directives. There was a general support for the objective of simplification. Some nevertheless expressed their opposition to the abrogation of the

provision submitting the merger to the shareholders of the acquiring company for agreement, as it was legitimate that the shareholders were properly informed.

7. THE EUROPEAN PRIVATE COMPANY

The Commission will launch a feasibility study in the short term with a view to presenting a proposal for an EPC statute in the medium term if the feasibility study confirms the need for such an initiative.

The proposal to launch a feasibility study to evaluate the advantages and problems generated by a possible European legal statute for small and medium-sized enterprises received a very broad support from the respondents. The most important advantage of an EPC was considered to be the incorporation of subsidiaries in different EU Member States under the same conditions, which would create a greater legal certainty for SMEs.

Among the objectives such a study should pursue, the following were mentioned:

– focus on questions concerning the access to this form of company, on the definition of its statute, on the requirement of creditor and employee's protections and on the integration of this form of company law into national legal systems;

– explore the practical problems that could be addressed by the creation of the EPC and alternative means by which these practical issues might be resolved;

– consider any disadvantages that might arise from the creation of a new pan-European vehicle of this nature.

It was felt that issues related to taxation should not be an important part of the study and should remain a matter for national experts. It was highlighted that the study, once completed, should be publicly available.

Some, however, expressed the view that the priority was the adoption of the 10th directive and that the study should only be conducted after its adoption.

8. THE EUROPEAN CO-OPERATIVE SOCIETY AND OTHER EU LEGAL FORMS OF ENTERPRISES

The Commission intends to actively support the ongoing legislative process engaged on the legislative proposals for these forms of Enterprises. The Commission also intends to launch in the medium term a study aiming at assessing the feasibility of a Statute for European Foundation

Very few respondents commented on the Commission's intention to actively support the ongoing legislative process engaged on the proposed legislation on the statutes of the European Association and European Mutual Society. Some Member States expressed their concerns about these proposed legislation and reserved their comments for the ongoing negotiations on these proposals: they considered this should not be a matter of priority for the Commission. But a majority of the other respondents stressed the importance of finalising these proposals, especially on the Mutual Society. The comment was made that there was an urgent need for work on the Statute of the European Mutual, which stopped in 1996, to resume as soon as possible. Whereas public

limited companies could develop their activities by choosing the legal form of the European Company, no such option was available for mutual companies, leading to unfair competition between companies of different legal forms.

With regard to the possible development of a proposal on the European Foundation, a few respondents on this point saw no need for further supranational legal forms alongside the European Company. But a majority of respondents considered it appropriate to continue to assess whether the available corporate forms within the EU genuinely meet all the needs of business and other users. It was argued that a European legal form of a foundation would improve the cross-border operations of foundations and their founders, and would provide a new voluntary instrument for cooperation among other types of funders and foundations. It was felt that there was a growing need for a European instrument as the practice of co-funding and transnational activities is beginning to translate into transnational collaborative projects within the EU. The idea of a feasibility study was therefore generally welcomed.

9. ENHANCING THE TRANSPARENCY OF NATIONAL LEGAL FORMS OF ENTERPRISES –

The Commission intends to propose in the medium term a legislative instrument introducing disclosure rules for all legal entities with limited liability, subject to further examination

A very limited number of respondents commented on this point. Globally speaking, the Commission's intention to increase disclosure requirements for all legal entities with limited liability was welcomed. It was considered that some existing legislation in the company law area had a negative impact on the transparency of some enterprises. It was argued, however, that detailed consideration needed to be given to all specific types of limited liability companies across the EU upon which disclosure requirements were not presently imposed, as well as the benefits that might accrue through the imposition of disclosure requirements. Any new disclosure requirement would need to be proportionate.

Three respondents also felt that while subscribing to the objective of enhanced transparency, this should not be used to shift the attention of corporate laws towards fraud or anti-terrorism issues.

10. CONCLUSIONS

DG MARKT services wish to thank all respondents for their valuable and high quality contributions, the details of which may not have been correctly translated in this synthesis document. As announced in the Action, the Commission will give adequate consideration to all contributions when implementing the Action Plan.