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**“Reform of the fourth and seventh Company Law
Directive – state of play”**

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Title: “Reform of the Fourth and Seventh Company Law Directive – state of play”

Good morning, Chairman,

Ladies and Gentlemen,

Thank you for inviting me to this major Forum on Risk Management and Internal Control.

You are giving me the opportunity to present an important piece of our Company Law Action Plan: the proposal for amending the Accounting Directives. The Commission presented this proposal one year ago – after a broad public consultation early 2004. The Council agreed on a so-called general approach in June this year. In close cooperation with the UK Presidency we are now engaged in constructive discussions with the European Parliament, in particular with the Rapporteur Mr. Lehne to strike a deal before the end of the year.

Our proposal deals with three issues which I intend to address. **Firstly** more transparency about off balance sheet arrangements and related party transactions. **Secondly**, it introduces a corporate governance statement. **Thirdly**, the proposal confirms the collective duty for board members to consider financial statements.

Finally I would like to address a new issue that was not part of our proposal: accounting rules for SMEs.

1. *Related party transactions and off balance sheet arrangements*

The proposal firstly aims at improving information about off balance sheet arrangements and related party transactions. Such transactions or arrangements can make it difficult for investors to assess the real risk of investing in a company.

Therefore disclosure about material off balance sheet arrangements should be improved. The use of special purpose vehicles (SPVs) is a prominent example. SPVs can be organised to evade accounting rules to the detriment of investors.

Moreover, companies' transactions with their managers, the latter's family members or other so-called related parties are often not carried out under normal commercial conditions. While satisfactory disclosure exists for listed companies under IAS, requirements for non-listed companies should be improved.

I do not think that the principle based proposals are too burdensome for companies. Member States can exempt all small companies – which amount to around 90% of all companies as defined under the Accounting Directives – from these requirements according to our initial proposal. Discussions in Council and the European Parliament focus on whether these exemptions should be broader. I am confident that we can find a balanced solution.

2. *Corporate governance statement*

We also propose a corporate governance statement for all listed European companies. This statement would invite companies to explain their internal governance practices. This does however not represent a move towards a European corporate governance code.

The corporate governance statement should – amongst other things - include a description of the main features of internal control. This and risk management systems with regard to financial reporting. To put it simply, listed companies could even declare “we have no internal controls”. This would be within the boundaries of the law but I am sure that the markets would react. We have therefore opted for an approach allowing for flexibility and a demand driven process. Investors should drive the demand for better internal control not regulators.

Let me complete the picture on internal controls. The 8th Company Law Directive – recently agreed – also matters in this area. Listed companies will have to have in place an audit committee or a body that at least performs equivalent functions. One of which is to monitor the effectiveness of the company’s internal controls. However, this relates to the internal functioning of a company and does not entail any requirement to disclose all this to the public or even to certify the effectiveness of internal controls.

3. *Collective duties of board members for financial reporting*

Let me turn to the third element of our proposal. In the EU, board members should have collective responsibility – or better a collective duty - to prepare

and publish financial statements. They should collectively follow the requirements of the EU Accounting Directives and the IAS-Regulation. Our proposal confirms at EU level what are already established traditions in Member States. But it will be up to the Member States to decide under which conditions board members could be liable. However, each board will continue to act under the competencies assigned to it by national law. We do not put into question whether a Member State prefers a one tier or a two tier board structure. We all have an interest to strengthen the system of checks and balances each board offers as a whole. Individual board members should not have the final say.

4. *New issues: Accounting for SMEs*

As you know, small and medium sized companies can be exempted from certain requirements under the Accounting Directives – if a Member State considers this appropriate. Shortly after we had put forward our proposal to amend the Accounting Directives, namely in November 2004, the Competitiveness Council invited the Commission to consider changing the thresholds for defining small and medium sized companies¹. The Council considers this as a matter of priority in order to reduce regulatory burdens on companies. Along the same lines the Rapporteur in the European Parliament – Mr Lehne – suggests an increase of these thresholds by 25%.

The Council is carefully examining Mr Lehne's suggestion. We are also reflecting on our position in the light of our priority to reduce regulatory

¹ Article 11 companies are “small” companies, which for two consecutive years, do not exceed the limits of two of the three following criteria: balance sheet total: EUR 3 650 000, net turnover: EUR 7 300 000, and an average number of employees during the financial year: 50. Article 27 companies are “medium-sized” companies, which for two consecutive years, do not exceed the limits of two of the three following criteria: balance sheet total: EUR 14 600 000, net turnover: EUR 29 200 000, and an average number of employees during the financial year: 250.

burdens. I would like to underline that what we are discussing here is the possibility of broadening already existing national options.

Extending national options should however not lead to a situation where the EU Accounting Directives become an empty shell. That does not preclude further simplification and updating of the EU accounting rules for small and medium sized companies. We should look into this issue in the future - not least because the IASB is considering simplifying international financial reporting standards for SMEs.

Conclusion

Let me conclude.

Our discussions on financial reporting should not only focus on pros and cons of fair value accounting under IFRS. We must not forget the overall picture: good financial reporting and good corporate governance go hand in hand and are essential to restore and maintain investors confidence.. I hope therefore this proposal, which brings more transparency and clarity, can still be agreed upon this year.

Thank you for your attention.
