



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 10.7.2007  
COM(2007) 394 final

**COMMUNICATION FROM THE COMMISSION**

**on a simplified business environment for companies in the areas of company law,  
accounting and auditing**

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The European Council of 8/9 March 2007 underlined that reducing administrative burdens is important in boosting Europe's economy, especially given the potential benefits this can bring for SMEs. It stressed that a strong joint effort of the European Union and the Member States is necessary to reduce administrative burdens within the EU.<sup>1</sup>

The Commission has outlined the way for achieving this by adopting, on 14 November 2006, an updated simplification programme<sup>2</sup> and the main elements for measuring administrative costs and reducing administrative burdens<sup>3</sup>. These documents were complemented by an Action Programme adopted on 24 January 2007<sup>4</sup>. Both programmes emphasise the need to generate tangible economic benefits.

European company law, accounting and auditing have been identified as priority areas within this initiative. First analyses carried out by a number of Member States have shown that administrative costs caused by EU rules in these areas are particularly high.<sup>5</sup> In parallel, the Commission has started to measure the administrative burdens in company law and accounting throughout the European Union, as announced in November 2006<sup>6,7</sup>. A broad review of the EU acquis in these areas is indispensable to allow European businesses to compete more effectively and to be more successful in a highly competitive global environment.

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<sup>1</sup> Presidency Conclusions of the Brussels European Council - doc. 7224/07 Concl 1

<sup>2</sup> Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions - "A strategic review of Better Regulation in the European Union" (COM(2006)689 final, OJ C 78, 11.4.2007, p. 9)

<sup>3</sup> Commission working document of 14/11/2006 – "Measuring administrative costs and reducing administrative burdens in the European Union" (COM(2006)691 final)

<sup>4</sup> Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions on "Action programme for reducing administrative burdens in the EU", (COM(2007)23 final, not yet published in the Official Journal)

<sup>5</sup> See COM(2006)689

<sup>6</sup> See Commission Working Document of 14 November 2006 – "First progress report on the strategy for the simplification of the regulatory environment", COM(2006)690 final, page 12: "*Concerning company law, the Commission has planned to launch before end of this year a comprehensive initiative to measure the administrative costs originating from the company law directives with the view to identifying together with Member States and stakeholders the scope for reduction of these costs. The outcome of this exercise will be presented in a Communication in the second half of 2007.*"

<sup>7</sup> This measurement is currently carried out with the help of external consultants. The results of this exercise will feed into the impact assessments that will accompany any future legislative proposal on the subject.

The exercise will contribute to the on-going review of the single market initiated by the Commission as part of the citizens' agenda in May 2006<sup>8</sup>. In particular, it will support work towards a well regulated Europe, which involves a critical assessment of how existing laws can be improved and administrative burdens can be reduced.

## 1. WHY SIMPLIFY EUROPEAN COMPANY LAW?

As central elements to achieve the common market, company law and accounting were among the first areas of legislation that were harmonised at European level. The field of auditing followed shortly afterwards (with the first version of the Eighth Directive on statutory audit dating from the early 80ies).<sup>9</sup> Since then, the relevant directives and regulations have been updated several times in order to adapt them to new developments.<sup>10</sup> A number of these revisions are recent and still need time before their effects can be measured and determined. However, none of these modernisation measures touched on the scope or the basic content of the directives concerned. They have remained fundamentally unchanged since their adoption.

In the last twenty to thirty years, the business environment of European companies has changed at high speed, with globalisation of economies and radical developments in technology. The legal environment too has evolved with the adoption of international standards in the field of accounting and the development of the jurisprudence of the Court of Justice of the European Communities. In recent years, this case law has helped to clarify the scope of the fundamental freedoms in the Treaty, paving the way for enhanced corporate mobility within the European Union.

There is a need to review existing EU directives in the light of these developments to assess their continued relevance. This assessment must also take account of the principles of better regulation together with subsidiarity and proportionality.

## 2. THE WAY FORWARD

There are essentially **two options** on how to proceed for certain company law directives that address mainly domestic situations:

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<sup>8</sup> A first interim report was presented to the European Council in March 2007 (Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions - A single market for citizens - Interim Report to the 2007 Spring European Council (COM(2007)60 final, not yet published in the Official Journal))

<sup>9</sup> A list of the main measures in the areas of company law, accounting and auditing is contained in **Annex 1**.

<sup>10</sup> In the context of the fourth phase of the Simplification of the Legislation on the Internal Market Process (SLIM), the First and Second Company law Directives were modernised; furthermore, the Fourth and the Seventh Directives were updated, the Tenth Company law Directive on cross border mergers and the Directive on the exercise of shareholders' voting rights were adopted. In the field of accounting and auditing, the level of international harmonisation achieved has contributed to the acceptance of new standards which allow for transparency and increase the credibility of annual financial statements. For listed companies, the IAS regulation therefore requires the use of International Financial Reporting Standards (IFRS) for consolidated accounts. In addition, a new directive on statutory audit was adopted in 2006.

- The **first option** is to address the question whether today all existing directives are still needed or whether the EU acquis in the area of company law should be reduced to those legal acts specifically dealing with cross-border problems.
- The **second, less far-reaching option** consists in focusing only on concrete, individual simplification measures in order to help EU companies.

With regard to the rest of the company law acquis that addresses specific cross-border problems as well as to the areas of accounting and auditing, individual simplification measures seem to be the right response. In accounting and auditing, the focus should be on reducing administrative costs for SMEs for which these costs are particularly heavy, whereas all companies should benefit from simplification measures in the field of company law.

With this communication, the Commission wants to present its first views on the subject and trigger a discussion involving Member States, the European Parliament and stakeholders in order to identify the measures in the areas of company law, accounting and auditing that are best suited not only to make European companies fit for the Internal Market but also to make them more competitive globally. The objective is to build a political consensus on the way forward so that appropriate legislative proposals can be submitted by early 2008.

Stakeholders are invited to comment on the questions raised and on the proposals put forward in this document and its annexes. In addition, stakeholders are also welcome to submit additional proposals for further simplification measures.

This exercise should be based on the understanding, underlined by the European Council on 8/9 March 2007, that any simplification measure at EU level can only be effective if the measures taken at EU level are fully endorsed by Member States at national level and if Member States make use of possibilities that already exist today under EU law to ease the burden on companies in the EU. Only a combined strategy will allow companies to benefit from clear improvements in the business environment.

### **3. HOW MUCH REGULATION DOES EUROPE NEED IN THE FIELD OF COMPANY LAW?**

#### **3.1. The general approach to EU company law**

In the field of company law, the increased mobility of companies today, not only at EU but also at international level, requires flexible responses to a constantly changing environment. These changes can only be addressed if Member States are able to react swiftly to these new developments. In this situation, a rigid, harmonised European framework might sometimes appear to be more of an impediment to innovation than a benefit for the Internal Market. Furthermore, the competitiveness of companies also depends on the level of the administrative costs related directly or indirectly to their activity. Some of these costs derive from EU rules. It should be asked whether the benefits of these rules in all cases outweigh the costs related to them.

At the same time, harmonisation has also positive effects on the competitiveness of companies. Harmonisation is a strength for cross-border markets and can clarify the relation between two or more national legal systems involved. It also increases legal certainty. The same applies where minimum transparency standards are set up to protect third parties from

the dangers that increased mobility of companies can imply for them. In this case, common rules provide for the basis of trust that is needed for a functioning Internal Market.

However, the situation may be different for directives such as the Third, the Sixth, the Second and the Twelfth Company law Directives. These directives focus on mainly domestic situations and do not aim at solving specific cross-border problems.

### *3.1.1. Option 1: Placing the focus on cross-border problems*

The **Third and the Sixth Company law Directives** regulate mergers and divisions of public limited companies in the same Member State. When these rules were adopted decades ago they played a role in opening up new possibilities for companies and promoting the internal market. Today, they guarantee a minimum level of protection for shareholders and creditors of public limited companies throughout the European Union.

However, given that these directives do not provide for full harmonisation, they do not create a level playing field; instead, some rules continue to differ between the Member States. At the same time, the existence of minimum requirements in EU law prevents Member States from adapting their national laws to changing needs. This leads to the question whether the advantages resulting from these directives justify the restrictions that they impose on businesses.

Similar considerations apply to the **Second Company law Directive** that deals with the capital of public limited companies. The capital maintenance system of the directive has been subject to discussions for a long time so that at least a review of that system should be considered in order to give companies more flexibility in the field of distributions to their shareholders.<sup>11</sup> New national legal forms that fall outside the scope of the Second Company law Directive have been created in some Member States to offer the flexibility that the Directive lacks, notably with regard to minimum capital requirements.

The **Twelfth Directive** in principle is of an enabling nature as it allowed individuals to create private limited companies in Member States where, before the transposition of the directive, more than one member was required to form a company of that type.

However, at the same time, the directive sets a number of minimum requirements for the internal procedures of such a company. The question is whether such restrictions need to be determined at EU level.

In all these cases, the Commission considers that repealing the EU rules and increasing flexibility by leaving it to Member States to determine the conditions in the relevant areas would be a viable option. Indeed, the Commission considers that such an approach would fit best with better regulation principles and the need to equip the EU with a streamlined company law acquis for the 21<sup>st</sup> century.

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<sup>11</sup> The forthcoming study on an alternative to the capital maintenance system of the Second Company Law Directive that was launched by the Commission in September 2006 will provide additional information that should facilitate the assessment in this case.

Stakeholders are therefore invited to give their views on whether

- the rules on domestic mergers and divisions contained in the Third and the Sixth Directive;
- the rules on the capital of public limited companies or at least the capital maintenance system of the Second Directive; and/or
- the rules on single-member private limited liability companies of the Twelfth Directive

should be repealed entirely or in parts.

If such repeal is not considered appropriate it should be explained what the benefits are of having these rules at EU level and why these benefits outweigh the costs related to them.

### 3.1.2. *Option 2: More principle-based, less detailed regulation*

The total repeal of the directives referred to above might seem to be too far reaching to some. In this case, at least parts of the Third, the Sixth and probably also the Second Company law Directives should be simplified. In their current form, these directives contain rules to a level of detail that leave Member States little flexibility to adapt their respective national systems to the evolving needs of businesses and stakeholders in general.

A first proposal for a simplification of the Third and the Sixth Directives was tabled by the Commission on 7 March 2007<sup>12</sup> as one of the measures contained in the Commission's Action programme for reducing administrative burdens and was endorsed by the European Council on 8/9 March 2007<sup>13</sup>.

However, apart from this modification there are more substantial ones that should be tackled. In particular, a number of the reporting requirements contained in the Third and the Sixth Directive seem excessive from today's perspective.

Detailed proposals that address these problems under this option are contained in **Annex 2**. In addition, measures to simplify the Second Directive further could also be proposed once the study that currently<sup>14</sup> is being carried out on behalf of the Commission has been assessed.

Stakeholders are invited to give their views on the proposals presented in **Annex 2**.

If any of the proposed measures are not considered appropriate, the benefits of keeping the rules unchanged should be explained.

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<sup>12</sup> Proposal for a Directive of the European Parliament and of the Council amending Council Directive 78/855/EEC concerning mergers of public limited liability companies and Council Directive 82/891/EEC concerning the division of public limited liability companies as regards the requirement for an independent expert's report on the occasion of a merger or a division (COM(2007)91, not yet published in the Official Journal)

<sup>13</sup> Presidency Conclusions of the Brussels European Council - doc. 7224/07 Concl 1

<sup>14</sup> See footnote 11.

### 3.2. Additional simplification measures in Company law

As explained above, further steps are needed, in addition to the measures envisaged in the previous section, in order to simplify other parts of the company law acquis.

This concerns first and foremost the First and the Eleventh Company law Directives. The ways of publishing information on companies that these directives provide for still do not exploit all possibilities that today's technology offers.

According to the rules of the **First Company law Directive**, certain information that has to be entered into the Member States' commercial registers, in addition has to be published in the national gazettes. In most cases, this publication entails unnecessary additional costs for the companies. These costs could, in the future, be avoided taking into account that nowadays all this information is available online through electronic company registers.

For branches, the **Eleventh Company law Directive** lays down special disclosure requirements. These requirements, too, imply considerable costs for many companies, due to national rules on translations and certifications related to the disclosure obligation. Efforts are necessary to reduce these costs to a minimum by restricting the formal requirements that Member States may impose on companies in this context.

Proposals to this end are contained in **Annex 3**. The annex, furthermore, contains a proposal for an adaptation of the European Company Statute to the recent jurisprudence of the European Court of Justice that could be carried out at the occasion of the modernisation and simplification measures proposed in this Communication.

Stakeholders are invited to give their views on the proposals presented in **Annex 3**.

If any of the proposed measures are not considered appropriate, the benefits of keeping the rules unchanged should be explained.

## 4. SIMPLIFYING BUSINESS FOR SMES IN THE AREAS OF ACCOUNTING AND AUDITING

In the field of accounting and auditing, small and medium-sized companies would benefit from further simplification of the Directives.

With the Fourth, the Seventh and the Eighth Directives, harmonised accounting and auditing requirements have significantly raised the quality of financial reporting and auditing in the EU. Whilst the overall goal pursued through these Directives to keep and improve accounting and auditing quality in the EU should be maintained, the existing requirements under those directives entail administrative work which companies, and notably small and medium-sized entities, criticise as being unnecessarily burdensome.

A successful reduction of the administrative burden for SMEs however needs to be addressed both at EU and national levels. It is of crucial importance to combine reporting for different purposes (such as tax, statistics, social security, employment reporting) at Member State level and thereby reduce the overall burden of keeping different accounting and reporting systems. This could also facilitate the use of electronic reporting formats such as XBRL.

The present simplification project for SMEs coincides with the publication of the International Accounting Standards Board (IASB) Exposure draft of a proposed IFRS for Small and Medium-sized Entities. After a first analysis, the Commission, however, does not believe that the current IASB work on SME accounting would provide sufficient elements to simplify the life of European SMEs.

The Commission has instead identified a number of other measures that could lead to tangible simplification for SMEs.

The first measure in this context is to exempt "micro entities" from the application of the accounting directives. For these smallest enterprises the burden related to the establishment of the annual accounts is particularly heavy. At the same time there is a lack of broad demand for their financial statements. With an exemption in the accounting directives, it would be left to Member States to determine which rules micro entities should be required to comply with. It should be noted in this context that a "micro entity" category has already been introduced in many Member States.

Stakeholders are therefore invited to give their views on whether they agree with an exemption of micro entities from the scope of the Fourth Directive and on the following possible definition for these micro entities:

- less than ten employees,
- balance sheet total below 500,000 EUR, and
- turnover below 1,000,000 EUR.

In addition, the following simplification measures in favour of SMEs are proposed:

- To extend the transition period for SME's crossing the thresholds from two to five years. Companies in the start-up phase will particularly benefit from a longer transitory period before more detailed accounts have to be prepared;
- To exempt small entities from the requirement to publish their accounts;
- To make it possible for certain medium-sized entities to use exemptions currently available only for small entities. This measure would in particular concern companies where the structure of members is such that there are no particular external user needs and unlimited liability companies.

Further measures could be taken regarding the procedure for the regular adaptations of the SME thresholds, in the areas of consolidation requirements, regarding accounting for deferred taxes and to remove certain disclosure requirements.

Details on the measures proposed in this section can be found in **Annex 4**.

Stakeholders are therefore invited to give their views on the proposals presented in **Annex 4**.

If any of the proposed measures are not considered appropriate, the benefits of keeping the rules unchanged should be explained.

## 5. NEXT STEPS

Member States, the European Parliament and other stakeholders are invited to submit their views on the proposals contained in this communication<sup>15</sup> with a view to establishing a broad consensus on the changes that should be envisaged. Considering the timeframe for the simplification exercise, contributions are invited **by mid-October 2007**.

In the follow-up to this communication and on the basis of the responses received, the Commission will prepare full and comprehensive impact assessments that will also take into account the results of the measurement of administrative costs currently under way. Subject to the outcome of these impact assessments, the Commission intends to submit legislative proposals in the areas covered by this communication early in 2008.

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<sup>15</sup> This communication is also available under  
[http://ec.europa.eu/internal\\_market/company/simplification/index\\_en.htm](http://ec.europa.eu/internal_market/company/simplification/index_en.htm)

## ANNEX 1

**First Directive:** Directive 68/151/EEC of 9 March 1968 on co-ordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community (*OJ L 65, 14.3.1968, p. 8*; last amended by Directive 2003/58/EC of the European Parliament and of the Council of 15 July 2003 (*OJ L 221, 4.9.2003, p. 13*))

**Second Directive:** Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent (*OJ L 26, 31.1.1977, p. 1*, last amended by Directive 2006/68/CE of 6 September 2006 (*OJ L 264, 25.9.2006, p. 32*))

**Third Directive:** Third Council Directive 78/855/EEC of 9 October 1978 on mergers of public limited liability companies (*OJ L 295, 20.10.1978, p. 36*)

**Fourth Directive:** Fourth Council Directive 78/660/EEC of 25 July 1978 on the annual accounts of certain types of companies (*OJ L 222, 14.8.1978, p. 11*; last amended by Directive 2006/46/EC of the European Parliament and of the Council of 14 June 2006, *OJ L 224, 16.8.2006, p. 1*)

**Sixth Directive:** Sixth Council Directive 82/891/EEC of 17 December 1982 on the division of public limited liability companies (*OJ L 378, 31.12.1982, p. 47*)

**Seventh Directive:** Seventh Council Directive 83/349/EEC of 13 June 1983 on consolidated accounts (*OJ L 193, 18.7.1983*; last amended by Directive 2006/46/EC of the European Parliament and of the Council of 14 June 2006, (*OJ L 224, 16.8.2006, p. 1*))

**Eighth Directive:** Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC (*OJ L 157, 09.06.2006, p. 87*)

**Tenth Directive:** Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies (*OJ L 310, 25.11.2005, p. 1*)

**Eleventh Directive:** Eleventh Council Directive 89/666/EEC of 21 December 1989 concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State (*OJ L 395, 30.12.1989, p. 36*)

**Twelfth Directive:** Twelfth Council Company Law Directive 89/667/EEC of 21 December 1989 on single-member private limited-liability companies (*OJ L 395, 30.12.1989, p. 40*)

**Takeover bids Directive:** Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids (*OJ L 142, 30.4.2004, p. 12*)

**Statute of the European Company:** Regulation (EC) 2001/2157 of 8 October 2001 on the Statute for a European company (SE) (*OJ L 294, 10.11.2001, p. 1*)

**IAS Regulation:** Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards (*OJ L 243, 11.9.2002, p. 1*)

## ANNEX 2

### **Individual simplification measures concerning the Third and the Sixth Company law Directives (section 3.1.2. of the Communication)**

#### **1. REPORTING REQUIREMENTS UNDER THE THIRD AND THE SIXTH COMPANY LAW DIRECTIVES**

Under the Third and the Sixth Company Law Directives, companies, in the context of the preparation of a merger or a division, are subject to a number of reporting requirements. Thus, the management or administrative bodies of the companies involved have to draw up a **detailed written report** explaining the draft terms of the operation and setting out the legal and economic grounds for them<sup>16</sup>. Furthermore, the **report of an independent expert** is needed in order to assess in particular whether the proposed share exchange ratio is fair and reasonable<sup>17</sup>. In addition, an **accounting statement** has to be drawn up if the latest annual accounts relate to a financial year that ended more than 6 months before the date of the draft terms of merger or division<sup>18</sup>. Finally, where in the case of a division both an expert report under the Second Company law Directive and a report on the draft terms of division have to be set up, the rules of the Sixth Directive only allow Member States to provide that both reports can be established by the same expert<sup>19</sup>; an **exemption** from one of the reporting requirements cannot be granted.

The latter requirement appears to be a typical example of an administrative burden. In a modern business environment, double reporting should be avoided to the extent possible as it creates additional costs for companies without providing real added value to shareholders and creditors. But also the other three requirements appear to be very burdensome and leave little room for flexibility when established at EU level. In order to render the process of mergers and divisions less cumbersome it seems appropriate to leave it to Member States to decide whether they wish to leave more room to directors' liability, possibly on the basis of a specific decision by the general meeting, or require the provision of the relevant financial data on each occasion. There seems to be no reason for giving, at EU level, a clear preference to either of these two solutions. Furthermore, in order to reap the full benefits of the recent modernisation measures, the mechanisms concerning the assessment of the share exchange ratio should take account of the flexibility that has been introduced in 2006 into the Second Company law Directive with a view to the related case of the valuation of a contribution in kind<sup>20</sup>.

#### **2. PROTECTION OF SHAREHOLDERS AND CREDITORS UNDER THE THIRD AND THE SIXTH COMPANY LAW DIRECTIVES**

Directive 2006/68/EC modifying the Second Directive modernised the creditor protection rule applicable in case of a reduction in capital<sup>21</sup>. The procedure for protecting creditors whose

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<sup>16</sup> Article 9 of Directive 78/855/EEC, Article 7 of Directive 82/891/EEC

<sup>17</sup> Article 10 of Directive 78/855/EEC, Article 8 of Directive 82/891/EEC

<sup>18</sup> Article 11(1)(c) of Directive 78/855/EEC, Article 9(1)(c) of Directive 82/891/EEC

<sup>19</sup> Article 8(3) of Directive 82/891/EEC

<sup>20</sup> See Art. 10a of Directive 77/91/EC, introduced by Art. 1(2) of Directive 2006/68/EC

<sup>21</sup> Article 32 of Directive 77/91/EC as modified by Art. 1(9) of Directive 2006/68/EC

claim antedate the publication of the decision on the reduction was specified more in detail. It was also clarified that these creditors have to show credibly that their claims are being jeopardised by the capital reduction if they want to obtain security. The first step in modernising the creditor protection rules under the Third and the Sixth Directives should be to align the relevant provisions of these directives<sup>22</sup> with this new system.

However, the question is whether it is appropriate to subject the acquiring company, in general, to the same procedure as the company being acquired although there are cases where the effect of a merger on the shareholders and creditors of the acquiring company does not differ from normal trading transactions.

In this context, it should be noted that the rules of the Second Directive, too, protect the interests of the shareholders. Mergers often necessitate capital increases that via Article 29 paragraph 1 of the Second Directive lead to granting pre-emption rights to pre-existing shareholders. At the same time, Article 19 of the Second Directive limits the scope for mergers by acquisition without a capital increase. Creditors are protected by other rules, as explained above.

Under the condition that shareholders and creditors continue to be entitled to inspect the relevant documents at least one month before the general meeting of the acquired companies, one could therefore consider leaving it to the Member States to determine whether and in which cases the approval of the general meeting of the acquiring company should be required. However, this flexibility should at least exist in the cases of the transfer of the assets of a wholly owned subsidiary and of the acquisition of a subsidiary whose parent company holds 90% of the shares, which are already today subject to specific rules (Articles 24 and 25 of the Third Directive).

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<sup>22</sup> Article 13 of Directive 78/855/EEC and Article 12 of Directive 82/891/EEC

## ANNEX 3

### **Additional simplification measures in company law (section 3.2 of the Communication)**

#### **1. PUBLICATION OBLIGATIONS UNDER THE FIRST AND THE ELEVENTH COMPANY LAW DIRECTIVES**

In particular the **First Company law Directive** requires companies to publish certain information that has to be entered into the Member States' commercial register in addition in the **national gazettes**. In most cases, this publication entails additional costs for the companies.

Since January 2007, the Member States have to give companies the possibility to file their documents and particulars by electronic means (First Directive, Art. 3 paragraph 2). This information, through the electronic registers, is accessible to third parties in all Member States, and the European Business Register facilitates the access to national registers further. The obligation to publish registered data in the national gazette has therefore become superfluous, all the more so as the gazettes often do not reproduce the full information but only contain a reference to the register. This function of the gazettes can therefore easily be replaced by a simple service of the register that provides information on the register's latest changes.

In order to allow companies to save costs, the requirement of a publication in the national gazette in Article 3 paragraph 4 of the First Directive should consequently be repealed. Furthermore, Member States should not be allowed to require, in addition to the publication pursuant to Article 3 paragraph 2, a publication in the national gazette to the extent that such a publication would entail additional costs for the companies.

Specifically for **branches**, the **Eleventh Company law Directive** lays down special disclosure requirements.

These rules imply a double cost for companies: they have to ensure the translation of certain documents relating to the company into the local language of the Member State where the branch is situated and they have to register these documents and their particulars, together with the particulars referring to the branch, at the register of the branch. The national rules of the Member States that determine the details around the certified translation, furthermore, often entail excessive requirements (notarisation etc.) that raise the costs further.

In order to reduce these costs to an acceptable level, it is essential that the Member State of the branch accept the certified translation prepared in another Member State. This obligation should at least apply where the certificate that has been issued is accepted by the judicial or administrative authorities of that other Member State. Article 4 of the Eleventh Directive should therefore be adapted accordingly.

However, there is further scope for simplification with a view to the establishment of branches. The existence of electronic registers all over Europe makes it possible for registers to communicate with each other. The so-called **BRITE project** that provides a common multi-language interface to access the registers in form of the **European Business Register (EBR)** aims at allowing European citizens and companies to reap the full benefits of this

technology. The Commission will continue to encourage this work in order to pave the way for a future review of the Eleventh Directive that would allow reducing the administrative burdens related to the establishment of a branch in another Member State, in particular by giving the possibility to file the particulars of the branch in the Member State where the parent company is registered.<sup>23</sup>

## 2. REGISTERED OFFICE OF THE EUROPEAN COMPANY

In 2009 at the latest the Commission will submit a report on the European Company Statute, in accordance with Article 69 of the Statute<sup>24</sup>. A general overhaul of the Statute and in particular of the issues listed in Article 69 does only seem realistic on the basis of that report.

However, Article 7 of the SE statute provides inter alia for that the registered office of an SE shall be located in the same Member State as its head office and allows Member State to provide in addition that SEs registered in their territory have the obligation of locating their head office and their registered office in the same place.

In light of case law of the European Court of Justice, e.g. the judgment in the case C-208/00 ("Überseering", judgment of 5 November 2002) a modification of Article 7 of the SE-Statute may be considered.

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<sup>23</sup> The same principles should then apply to the registration of a **grouping establishment of a European Economic Interest Group (EEIG)** situated in a Member State other than that in which the official address of the EEIG is situated (Article 10 of the Council Regulation on the EEIG (Council Regulation (EEC) No 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG) (OJ L 124, 15.5.1990, p. 52)

<sup>24</sup> Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE) (OJ L 294, 10.11.2001, p. 1)

## ANNEX 4

### **Simplification measures for SMEs in accounting and auditing (section 4 of the Communication)**

The purpose of this annex is to further outline and describe what the individual measures are and how small and medium-sized companies can benefit from them. The measures will be explained in the following order:

1. Introduction of "micro entities"
2. Thresholds for SMEs
3. Relieve from publication requirements for small entities
4. Extension of exemptions for medium sized entities without particular external user
5. Simplification for all companies

#### **1. INTRODUCTION OF "MICRO ENTITIES"**

In order to facilitate significant simplification for the smallest limited liability companies, the Commission considers that a category of "micro entity" should be introduced into the Fourth Directive. Such a category has already been introduced in many Member States.

Inspiration could be taken from the definition in the 2003 Commission Recommendation<sup>25</sup> which defined micro entities as companies with less than ten employees, two million Euro turnover and a balance sheet total below two million Euro. Earlier consultations with Member States have, however, indicated that the thresholds in the Commission Recommendation of 2003 may be too high for accounting and auditing purposes. The thresholds defined in the recommendation for small and medium-sized enterprises are much higher than those in the Fourth Directive, and a full use of these exemptions could therefore nearly lead to a repeal of this Directive for small companies. This result does not seem desirable as harmonised accounting requirements are needed for cross-border investments and company operations also for many small companies.

The definition of micro entities in the Fourth Directive should therefore be based on lower thresholds than those contained in the 2003 Recommendation. The Commission would like to consult on the following tentative definition for micro entities:

- less than ten employees,
- balance sheet total below 500,000 EUR, and
- turnover below 1,000,000 EUR.

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<sup>25</sup> Commission Recommendation C(2003)1422 of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (OJ L 124, 20.5.2003, p. 36)

The Member States would be allowed to exclude such micro entities entirely from the accounting directives, and there would be an exemption for micro entities from the directives' requirements concerning statutory audits. As a consequence, national authorities can allow micro entities to use a simpler accounting framework at national level (normally national requirements require accounting for tax reporting) so that the amendment to the Fourth Directive could lead to a substantial decrease in administrative burdens for micro entities.

## 2. TRESPASSING THRESHOLDS FOR SMEs

At present, a small entity must already apply accounting and auditing requirements of a medium sized company if it trespasses the threshold for two consecutive years. The two-year period in Article 12 of the Fourth Directive is however ill adapted to actual economic cycles of SMEs. It often takes more than two years for a small entity to consolidate growth of its business. The chances that a successful company permanently exceeds the thresholds are much higher after five years. Yet, should a company cross the thresholds and for any reason (e.g. economic difficulties, higher thresholds implemented by law, etc.) fall below the thresholds again, the Directive requires the (now again small) company to apply for at least two years the provisions of a medium sized company. More flexibility whereby a five-year period for companies exceeding the thresholds, and a one year period for those ceasing to exceed the thresholds would certainly reduce the potential for administrative burden introduced by the current two years rule.

The accounting directives define “small” and “medium-sized” companies where a company meets two of the following three criteria (thresholds after amendments by Directive 2006/46/EC):

	<b>“Small” (Article 11 companies)</b>	<b>“Medium-sized” (Article 27 companies)</b>
Turnover	8 800 000 EUR	35 000 000 EUR
Balance sheet total (i.e. gross assets)	4 400 000 EUR	17 500 000 EUR
Number of employees	50	250

The thresholds were recently increased by around 20% by the above mentioned Directive. This will allow the Member States to offer by no later than mid 2008 the possibility for small and medium-sized entities to benefit from further simplification via exemptions.

However, the procedure for adapting thresholds should be simplified. At present, Article 53 provides that it is the Council that adapts the thresholds upon proposal from the Commission; the European Parliament is not involved in the procedure. In addition, a contact committee is established under Article 52. For the future, it could be considered to leave the adaptation of the thresholds to the Commission which would be assisted by the Accounting Regulatory Committee set up under the IAS Regulation within the framework of the new regulatory procedure, with scrutiny rights for the Council and the European Parliament. Such a new procedure would also allow smoother and faster adaptations of thresholds compared to the somewhat cumbersome adoption by the Council itself.

### **3. RELIEVE FROM PUBLICATION REQUIREMENTS FOR SMALL ENTITIES**

The publication requirements for small companies create major administrative burdens. The Commission therefore suggests abolishing these requirements for this category. It is less important for small companies to publish financial statements because they are used by a limited number of stakeholders, such as credit institutions and suppliers that have the possibility to require financial information directly from the company. Therefore a full exemption for small companies from publication requirements would benefit those companies considerably without having a significant negative impact.

### **4. EXTENSION OF EXEMPTIONS FOR COMPANIES WITHOUT PARTICULAR EXTERNAL USER**

There should be fewer requirements for those companies which do not have a wide range of external users of financial statements. Consequently, in order to reduce the administrative burden for those companies, the Commission proposes adopting a risk-based approach. It would allow the following medium-sized companies to use the regime applicable for small companies:

- Companies where the managers are also the owners: for instance, a managing director being the main shareholder or member (provided that no other member has more than 5%).
- Unlimited liability companies falling under the scope of the second subparagraph of Article 1 and under Article 47 paragraph 1a of the Fourth Directive.

### **5. SIMPLIFICATION FOR ALL COMPANIES**

#### *Consolidation*

Article 57 of the Fourth Directive allows Member States to use the option of not submitting audited financial statements for certain subsidiaries of groups, subject to certain conditions. Full use of Article 57 should be encouraged, in particular, when these subsidiaries are either small or medium-sized. The exemption would be mandatory for small companies. A further option offered to the Member States to exempt medium-sized companies in this situation from statutory audit should be examined. The main reason is that Article 27, point a, of the directive on statutory audit will introduce the responsibility of the group auditor.

Further simplification could be achieved through a clarification of the relationship between the IAS Regulation 1606/2002 and the Seventh Directive. It needs to be clarified whether parent companies that have subsidiaries of no material significance (Article 13 of the Seventh Directive) would fall under the IAS Regulation and would therefore, be required to prepare IFRS financial statements. Elimination of consolidation requirements or requirements to provide IFRS financial statements in cases where there are only such subsidiaries could be seen as a substantial simplification. In addition, requirements to provide consolidated accounts for personal holdings (where the main holder of the group is a natural person) are burdensome and could be abolished.

### *Accounting for deferred taxes*

Feedback from preparers confirms that accounting for deferred taxes (Article 43 paragraph 1, number 11, of the Fourth Directive) is very burdensome for companies in general. In addition it has been confirmed by preparers and users, e.g. credit institutions and rating agencies, that deferred tax information (whether recognised in the balance sheet or provided in the notes) often is not considered a relevant input for the decisions to be taken. If preparers and users agree on the irrelevance of this information, the Commission suggests decreasing the administrative burdens for SMEs significantly by abolishing this requirement.

### *Disclosures*

The accounting directives contain a large number of disclosure requirements. The number of requirements has increased each time the directives were amended. The accumulation of these disclosure requirements could be seen as burdensome particularly for SMEs although they have to be weighed up against the relevance for users of financial statements. Significant exemptions already exist for small entities to provide abridged disclosures.

The Commission therefore has been encouraged to explore further possibilities of abolishing requirements. A first analysis indicates that the deletion of the following disclosures could be considered:

- Disclosure of an explanation of formation expenses (Article 34 paragraph 2),
- Disclosure of the breakdown of net turnover into categories of activity and geographical markets (Article 43 paragraph 1, number 8).