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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 26.2.2009  
COM(2009) 83 final

2009/0035 (COD)

Proposal for a

**DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**

**amending Council Directive 78/660/EEC on the annual accounts of certain types of  
companies as regards micro-entities**

**(Text with EEA relevance)**

{SEC(2009) 206}  
{SEC(2009) 207}

## EXPLANATORY MEMORANDUM

### 1. CONTEXT OF THE PROPOSAL

#### 1.1. Objectives of the proposal

The objective of this proposal of an amendment to the Directive 78/660/EEC on the annual accounts of certain types of companies (4<sup>th</sup> Company Law Directive)<sup>1</sup> is to simplify the business environment and particularly the financial reporting requirements for micro-entities in order to enhance their competitiveness and release their growth potential. The changes should lead to reduced administrative burden while safeguarding adequate protection and information to stakeholders and enable alignment of the micro-entities' reporting requirements with the real needs of users and preparers.

#### 1.2. General context

The European Council of 8 - 9 March 2007 underlined that reducing administrative burden is important for boosting the European economy, especially considering 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 burden within the EU.<sup>2</sup> At its meeting in March 2008, the European Council called on the Commission to identify new "fast track" legislative proposals in order to reduce administrative burdens<sup>3</sup>. Accounting and auditing have been identified as key areas for reducing administrative burden for European companies.

In the aftermath of the financial crisis, the Commission issued "A European Economic Recovery Plan" to restore consumer and business confidence. The European Economic Recovery Plan pledges to reduce the burden on small and medium sized enterprises (SMEs) and micro-entities by among others "removing the requirement on micro-enterprises to prepare annual accounts"<sup>4</sup>.

Furthermore the European Parliament encourages "the Commission to continue its activities with regard to the simplification of company law, accounting and

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<sup>1</sup> OJ L 222, 14.8.1978, p. 11.

<sup>2</sup> Presidency Conclusions of the Brussels European Council - doc. 7224/07, point 24.

<sup>3</sup> Presidency Conclusions of the Brussels European Council – doc. 7652/08, point 9.

<sup>4</sup> Communication from the Commission to the European Council, A European Economic Recovery Plan - COM(2008) 800, 26.11.2008, point 4, Available on the Commission website: [http://ec.europa.eu/commission\\_barroso/president/pdf/Comm\\_20081126.pdf](http://ec.europa.eu/commission_barroso/president/pdf/Comm_20081126.pdf)

auditing..., in particular the 4<sup>th</sup> and 7<sup>th</sup> Company Law Directives”<sup>5</sup> and explicitly calls on the Commission to come forward with a legislative proposal that allows Member States to exempt local and regional undertakings from the scope of the Accounting Directives<sup>6</sup>.

The 4<sup>th</sup> Company Law Directive was adopted in 1978 in order to create a harmonised set of requirements for the external reporting of all limited liability companies in the EU. In 1983, the 7<sup>th</sup> Company Law Directive was adopted and added a common set of requirements for consolidated financial statements. The 4<sup>th</sup> and 7<sup>th</sup> Company Law Directives (Accounting Directives) create together the core of the accounting acquis. During the past 30 years the Accounting Directives were modified several times. Through the adoption of the Regulation (EC) No 1606/2002 on the application of international accounting standards (IAS Regulation)<sup>7</sup> listed companies (and those with listed debt) have to present IFRS accounts, and are consequently relieved from most of the requirements in the 4<sup>th</sup> and 7<sup>th</sup> Company Law Directives. These Directives however still forms the basis for SME accounting in the EU<sup>8</sup>.

The Accounting Directives have led to improved financial reporting environment in the EU. Every subsequent addition to the Accounting Directives has however created new requirements, and whilst every added requirement may have been justified in its own right, it is now important to reconsider whether less useful requirements should be removed or replaced.

Commission Recommendation 2003/361/EC<sup>9</sup> defines micro, small and medium-sized enterprises. However, consultations with Member States have indicated that the thresholds for micro-enterprises in that Recommendation may be too high for accounting purposes. The presented proposal suggests that a category of micro entities as the smallest enterprises could be introduced into the EU legislative framework<sup>10</sup>. Companies which on their balance sheet date do not exceed the limits of two of the following criteria: balance sheet total 500 000 EUR, net turnover 1 000 000 EUR and/or average number of employees during the financial year of 10 persons are considered to be micro-entities. Micro-entities are currently subject to the same rules as larger companies, but over time it has been found that the extensive reporting rules applied to them are not in proportion with the their specific accounting needs and create a cost burden and can hinder efficient use of capital for productive purposes.

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<sup>5</sup> Report on International Financial Reporting Standards (IFRS) and the Governance of the International Accounting Standards Board (IASB) (2006/2248(INI)), EP, Committee on Economic and Monetary Affairs, Rapporteur: Alexander Radwan, A6-0032/2008, 5.2.2008, p. 10.

<sup>6</sup> European Parliament's resolution of 18 December 2008 on accounting requirements as regards small and medium-sized companies, particularly micro-entities, P6\_TA(2008)0635.

<sup>7</sup> 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).

<sup>8</sup> A separate directive lays down the requirements for the audit of the annual accounts (Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts - OJ L 157, 9.6.2006, p. 87).

<sup>9</sup> OJ L 124, 20.5.2003, p. 36.

<sup>10</sup> This new entity group originates in the Commission Communication of July 2007 (Communication from the Commission on a simplified business environment for companies in the areas of company law, accounting and auditing - COM(2007) 394, 10.7.2007. Available on the Commission website: [http://ec.europa.eu/internal\\_market/company/simplification/index\\_en.htm](http://ec.europa.eu/internal_market/company/simplification/index_en.htm))

The proposed amendment represents a targeted change of the 4<sup>th</sup> Company Law Directive<sup>11</sup> that should lead to significant simplification of legislation in the short-term perspective. This proposal is part of the Simplification Rolling Programme of the Commission which is a key priority of the Better Regulation agenda.

Furthermore, this proposal shall be also seen as a part of a broader overhaul of the 4<sup>th</sup> and 7<sup>th</sup> Company Law Directives which is envisaged in the Commission Legislative Work Programme for the third quarter of 2009. In the context of this planned modernisation/change of the EU accounting framework, a public consultation is going to be launched shortly.

## **2. RESULTS OF CONSULTATIONS OF INTERESTED PARTIES AND IMPACT ASSESSMENT**

### **2.1. Consultation of interested parties**

The Commission Services conducted research in order to identify the potentially most burdensome requirements of the Accounting Directives<sup>12</sup>. The initial findings indicated that several amendments could be made in order to simplify them.

These initial ideas and suggestions were discussed with Member States in the Accounting Regulatory Committee (ARC) at several meetings from December 2006 onwards. Following these discussions, the Commission published a Communication in July 2007<sup>13</sup> identifying potential amendments/changes to the Accounting Directives. The Commission Services identified policy options to be considered and i.a. proposed to introduce a new category of so-called "micro-entities" in the 4<sup>th</sup> Company Law Directive, which could be optionally exempted by Member State from its scope. The majority of stakeholders who responded to the public consultation was in favour of exempting micro-entities from the requirements of the Accounting Directives as it would constitute a major reduction of administrative burden for those entities and encourage new start-ups.

The High Level Group of Independent Stakeholders on Administrative Burdens (High Level Group)<sup>14</sup> discussed the ways to reduce the burden in the area of company law and accounting, with the conclusion that several of the accounting obligations stemming from the Accounting Directives are not necessary. Therefore in

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<sup>11</sup> The 7<sup>th</sup> Company Law Directive does not need to be amended, as already the present text of this Directive gives the Member States an option to exclude from the obligation to draw up consolidated financial statements companies to be consolidated which together do not exceed the limits of medium-sized company as defined in the 4<sup>th</sup> Company Law Directive (Art. 6(1) of the 7<sup>th</sup> Company Law Directive).

<sup>12</sup> Including the study conducted by Ramboll Management, commissioned by the Commission: Study on Administrative Costs of the EU Company Law Acquis, July 2007, available on the Commission website:  
[http://ec.europa.eu/internal\\_market/company/docs/simplification/final\\_report\\_company\\_law\\_administrative\\_costs\\_en.pdf](http://ec.europa.eu/internal_market/company/docs/simplification/final_report_company_law_administrative_costs_en.pdf)

<sup>13</sup> Communication from the Commission on a simplified business environment for companies in the areas of company law, accounting and auditing - COM(2007) 394, 10.7.2007. Available on the Commission website: [http://ec.europa.eu/internal\\_market/company/simplification/index\\_en.htm](http://ec.europa.eu/internal_market/company/simplification/index_en.htm)

<sup>14</sup> For details on the High Level Group of Independent Stakeholders see the Commission website: [http://ec.europa.eu/enterprise/regulation/better\\_regulation/high\\_level\\_group\\_is\\_en\\_version.htm](http://ec.europa.eu/enterprise/regulation/better_regulation/high_level_group_is_en_version.htm)

their report<sup>15</sup> the High Level Group calls for rapid enactment of Member State option to exempt micro-entities.

## 2.2. Impact assessment

The Commission Services presented an impact assessment of this proposal to the Impact Assessment Board which approved it on 28 January 2009. The comments provided by the Board were taken into account.

This impact assessment concludes that the proposed removal of micro-entities from the scope of the 4<sup>th</sup> Company Law Directive is expected to have a positive impact on reduction of administrative reporting burden for micro-entities, creating opportunities for the provision of more relevant and understandable information to main users, creditors and management while having no significant negative impact on the information to the external stakeholders and creditor protection and for cross-border trade. It will have an impact on availability of statistical data in some Member States leading to changes in the collection of statistical data. This could, for instance, be overcome by additional statistical surveys. The proposal will also lead to some reduction of publicly available information. However, the role of published financial statements as regards micro entities is limited, as for example the employees of such companies have usually direct contact with the management and owner(s). As regards general public, the interest for information on micro entities is generally very low<sup>16</sup>.

## 2.3. Monitoring and evaluation

This proposal should be seen in connection with other simplification measures regarding the 4<sup>th</sup> and 7<sup>th</sup> Company Law Directives and their impact and evaluation shall be carried out together. The Commission will monitor the implementation together with the Member States and will organise implementation workshops. The evaluation of effects and functioning of the exemption for micro-entities will include an assessment as regards the key objectives of better alignment of the accounting rules with the needs of the users and preparers of the financial reports and overall reduction of administrative burden.

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<sup>15</sup> High Level Group Report:

[http://ec.europa.eu/enterprise/admin-burdens-reduction/docs/080710\\_hlg\\_op\\_comp\\_law\\_final.pdf](http://ec.europa.eu/enterprise/admin-burdens-reduction/docs/080710_hlg_op_comp_law_final.pdf)

<sup>16</sup> The Impact Assessment describes several policy options which the Commission Services reflected upon: Option 0 consists in making no changes to the 4<sup>th</sup> Company Law Directive, Option 1 in encouraging Member States to a full use of the currently in the 4<sup>th</sup> Company Law Directive existing options, Option 2 foresees an obligatory exemption of micro-entities from the scope of the 4<sup>th</sup> Company Law Directive, Option 3 establishes a Member State option to exempt micro entities from the scope of the 4<sup>th</sup> Company Law Directive, Option 4 would constitute a simplified mandatory accounting regime for micro-entities and Option 5 provides for amendments to the 4<sup>th</sup> Company Law Directive without introducing the new category of micro-entities.

Following the comparison of all the above-mentioned options, the Impact Assessment comes to the conclusion that establishing an option for Member States to exempt micro-entities from the scope of the 4<sup>th</sup> Company Law Directive (Option 3 above) provides the biggest burden reduction and can be also implemented within the shortest timeframe and is therefore the most appropriate alternative in order to significantly reduce the administrative burden of the small businesses and align the reporting requirements with the needs of the users and preparers.

A general overhaul of the 4<sup>th</sup> and 7<sup>th</sup> Company Law Directive envisaged in the Commission Legislative Work Programme for the third quarter of 2009 shall develop the issue of monitoring more precisely.

### **3. LEGAL ELEMENTS OF THE PROPOSAL**

#### **3.1. Legal basis**

Article 44 (1) of the Treaty establishing European Community<sup>17</sup>.

#### **3.2. Subsidiarity and proportionality principles**

This proposal does not fall under the exclusive competence of the Community. Action at EU level is necessary as obligations for financial reporting for micro-entities derive from EU directive. In order to allow Member States to exempt micro-entities from these requirements, the 4<sup>th</sup> Company Law Directive needs to be changed; action at EU level is therefore justified. The proposed modifications are proportionate to the objective of removing the unnecessary administrative burden for micro-entities.

The proposal continues the Community's principle based approach to EU-Accounting regulation. Also, the Accounting Directives represent "minimum harmonisation"<sup>18</sup>. This ensures proportionality and leaves flexibility to Member States on how to fulfil the objectives while minimising the financial and administrative burden of the micro-entities. Therefore, when implementing this Directive, Member States should also analyse and take into account the national legislation and further simplification measures at national level might be recommendable. It has to be also noted in this context, that the Commission is aware of the fact that it remains up to the Member States to check and monitor whether the micro-entities criteria by companies excluded from the scope of the 4<sup>th</sup> Company Law Directive continue or cease to be met. The Member States shall have relevant necessary information at their disposal (statistical, social data etc.). In the spirit of subsidiarity, the Commission has deliberately chosen this option.

#### **3.3. Choice of instrument**

The proposed instrument amends existing directives and is therefore a directive.

### **4. SIMPLIFICATION**

In October 2005, following the Commission communication "Better Regulation for Growth and Jobs in the EU"<sup>19</sup>, the Commission launched a new phase for the simplification of existing EU law by setting out a rolling programme<sup>20</sup>, initially covering the years 2005-2008. In January 2009, the Commission presented its Third

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<sup>17</sup> OJ C 325, 24.12.2002, p. 35.

<sup>18</sup> Member States can put in place more extensive requirements nationally. The Directives already contain numerous options for SMEs, but many of those have not been taken up by Member States.

<sup>19</sup> COM(2005) 97, 16.3.2005.

<sup>20</sup> COM(2005) 535, 25.10.2005.

Strategic Review on Better Regulation and updated its Simplification Rolling Programme<sup>21</sup>. The presented proposal is foreseen in this Simplification Rolling Programme for adoption by the Commission in 2009<sup>22</sup> as part of the review of the Accounting Directives to take account of the interests of small businesses and to reduce administrative burdens. This more general proposal requires more time for its preparation. The Commission therefore considers that in line with the European Economic Recovery Plan measures are needed in the short term to reduce the burden on micro-entities. Significant simplification benefits are proposed.

According to the estimations available to the Commission there are around 5.3m micro-entities in the EU that meet at least two of the definition criteria<sup>23</sup>. It costs each company €1558 on average to meet the reporting obligations of the Accounting Directives. It was assessed that without any legal obligations companies would still spend around 25% of that amount to meet their managerial and external information needs. Therefore the remaining 75% or €1169 is an approximation of the accounting burden these companies face. This amounts to accounting burden of €6.3bn. Thus, in the maximum scenario where all Member States exempt micro companies and do not impose additional requirements the best estimation of the potential savings stemming from the proposal is €6.3bn (with range of €5.9bn to €6.9bn).

## **5. EXPLANATION OF THE PROPOSAL**

The Commission suggests establishing an option for Member States of removing the micro-entities from the scope of the 4<sup>th</sup> Company Law and Directive and, by doing so, relieving them from the requirement to draw up annual accounts. Accordingly, the Commission proposes to add a new Article 1a to the 4<sup>th</sup> Company Law Directive extending the discretion of Member States to relieve the micro-entities from the scope of the 4<sup>th</sup> Company Law Directive.

However, it needs to be recalled, that companies, including micro entities, keep records of sales and transactions for their own management purposes and for tax reporting. The Directive will enable Member States to align the financial reporting to such other reporting needs to avoid unnecessary administrative burden. Micro entities can on a voluntary basis still draw up annual accounts, have them audited and send them to the national register.

## **6. BUDGET IMPLICATIONS**

There are none for the Community budget.

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<sup>21</sup> COM(2009) 17, 28.1.2009.

<sup>22</sup> and is also referenced in the Commission Agenda Planning as 2009/MARKT/051.

<sup>23</sup> balance sheet total 500 000 EUR, net turnover 1 000 000 and/or average number of employees during the financial year of 10 persons.

Proposal for a

**DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**

**amending Council Directive 78/660/EEC on the annual accounts of certain types of companies as regards micro-entities**

**(Text with EEA relevance)**

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 44(1) thereof,

Having regard to the proposal from the Commission<sup>24</sup>,

Having regard to the opinion of the European Economic and Social Committee<sup>25</sup>,

Acting in accordance with the procedure laid down in Article 251 of the Treaty,

Whereas:

- (1) The European Council of 8 and 9 March 2007 underlined in its conclusions that reducing administrative burden is important for boosting the European economy and that a strong joint effort to reduce administrative burden within the EU is necessary.
- (2) Accounting has been identified as one of the key areas for reducing administrative burdens for companies within the Community.
- (3) In its Communication on a simplified business environment for companies in the areas of company law, accounting and auditing<sup>26</sup> the Commission identified possible amendments to the Fourth Council Directive 78/660/EEC of 25 July 1978 based on Article 54(3)(g) of the Treaty on the annual accounts of certain types of companies<sup>27</sup>, including an option for Member States to exempt micro-entities from the obligation to draw up annual accounts according to that Directive.
- (4) Commission Recommendation 2003/361/EC<sup>28</sup> defines micro, small and medium-sized enterprises. However, consultations with Member States have indicated that the thresholds for micro-enterprises in that Recommendation may be too high for accounting purposes. Therefore, a sub-group of micro-enterprises, so called micro-

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<sup>24</sup> OJ C [...] [...], p.[...].

<sup>25</sup> OJ C [...] [...], p.[...].

<sup>26</sup> COM(2007) 394.

<sup>27</sup> OJ L 222, 14.8.1978, p. 11.

<sup>28</sup> OJ L 124, 20.5.2003, p. 36.

entities, should be introduced to cover companies with lower thresholds for balance sheet total and net turnover than the thresholds set up for the micro-enterprises.

- (5) Micro-entities are in most cases engaged in business at local or regional level with no or limited cross-border activity and have limited resources to comply with demanding regulatory requirements. In addition, micro-entities are important for creating new jobs, fostering research and development and creating new economic activities.
- (6) Micro-entities are however often subject to the same reporting rules as larger companies. Those rules put a burden on them which is not in proportion to their size and is therefore disproportionate for the smallest enterprises as compared to the larger enterprises. Therefore it should be possible to exempt micro-entities from the obligation to draw up annual accounts, even if such accounts provide an input for statistical information.
- (7) The High Level Group of Independent Stakeholders on Administrative Burdens called in its opinion of 10 July 2008 for rapid enactment of an option for Member States to exempt micro-entities from the obligation to draw up annual accounts according to Directive 78/660/EEC.
- (8) In its resolution of 18 December 2008 on accounting requirements as regards small and medium-sized companies, particularly micro-entities<sup>29</sup>, the European Parliament called on the Commission to present a legislative proposal that would allow Member States to exempt micro-entities from the scope of Directive 78/660/EEC.
- (9) Since the objective of this Directive, namely to reduce the administrative burden for micro-entities, cannot be sufficiently achieved by the Member States, and can therefore by reason of its effect be better achieved at Community level, the Community may adopt measures in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty. In accordance with the principle of proportionality, as set out in that Article, this Directive does not go beyond what is necessary in order to achieve those objectives.
- (10) Directive 78/660/EEC should therefore be amended accordingly,

HAVE ADOPTED THIS DIRECTIVE:

*Article 1*  
*Amendment to Directive 78/660/EEC*

In Directive 78/660/EEC the following Article 1a is inserted:

*“Article 1a*

1. Member States may provide for an exemption from the obligations under this Directive for companies which on their balance sheet dates do not exceed the limits of two of the three following criteria:

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<sup>29</sup> OJ C [...] [...], p. [...].

- (a) balance sheet total: EUR 500 000;
  - (b) net turnover: EUR 1 000 000;
  - (c) average number of employees during the financial year: 10.
2. Where on its balance sheet date, a company exceeds the limits of two of the three criteria set out in paragraph 1 in two consecutive financial years that company may no longer benefit from the exemption referred to in that paragraph.
- Where on its balance sheet date, a company has ceased to exceed the limits of two of the three criteria set out in paragraph 1, it may benefit from the exemption referred to in that paragraph, provided that it has not exceeded those limits in two consecutive financial years.
3. In the case of those Member States which have not adopted the euro, the amount in national currency equivalent to the amounts specified in paragraph 1 shall be that obtained by applying the exchange rate published in the *Official Journal of the European Union* on the date of the entry into force of any Directive setting those amounts.
4. The balance sheet total referred to in paragraph 1(a) shall consist either of the assets referred to in points A to E under 'Assets' in Article 9 or the assets referred to in points A to E in Article 10.

#### *Article 2* *Transposition*

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive if and when they decide to make use of the option provided for in Article 1a of Directive 78/660/EEC. They shall forthwith communicate to the Commission the text of those provisions and a correlation table between those provisions and this Directive.
- When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.
2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

#### *Article 3* *Entry into force*

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

*Article 4*  
*Addressees*

This Directive is addressed to the Member States.

Done at Brussels,

*For the European Parliament*  
*The President*

*For the Council*  
*The President*