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The European Accounting Directives

- Status of the Fourth and the Seventh Company Directives after implementation of Directive 2009/49/EC

Bachelor's thesis within European Company Law

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Abstract

This thesis examines the effects from Directive 2009/49/EC. This directive amend the Fourth and Seventh Company Directives, the Accounting Directives, regarding the information that Small and Medium-sized Enterprises (SME) have to present in notes connected to both the annual reports and notes to the consolidated accounts, in situations with subsidiaries when its necessary to draw up consolidated accounts.

The Accounting Directives does not affect all companies, almost only private limited liability companies, is this type of companies the only one discussed. Directive 2009/49/EC is not affecting all sizes of private limited liability companies within the European Union, since the most important reason for implementing it is to give SMEs less administrative burden by lower requirements regarding the information presented in notes attached to the reports.

The implementation of Directive 2009/49EC is a positive change since it is in line with the idea of an Internal Market with equal rights and obligations to all sized of limited liability companies, private or public. The lower obligations in the annual reports in the Fourth Directive are for SMEs to the better because of the less administrative burden and the loss of information for interested is not more important, but of course, for some it is crucial. Amending the Seventh Directive may have larger effect to some companies, most likely medium-sized SMEs, since the obligation to draw consolidated accounts will for some companies not be necessary.

Abbreviations

Art.	Article
EC	European Community
EEC	European Economic Community
E.g.	Exemplie gratia, for example
EU	European Union
IASB	International Accounting Standards Board
Ibid.	Ibidem
IFRS	International Financial Report Standards
P	Page
Para	Paragraph
SME	Small and Medium-sized Enterprises

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1 Introduction

1.1 Background

That the legal work from the European Union has great impact on all Member States it is no doubt about and this is the fact on the company law area that has affects a lot because of the work in the European Union.¹ Within the European Union, it is possible to harmonize the national legislations in different ways, in for example regulations, directives and recommendations.² For the company law area, the EU has chosen to use directives. The reasons for this can be many, but the most important is that it gives Member States the opportunities to choose how to implement the rules into the national legislation. Either can a directive be adopted as presented by the Parliament or be taken up as a national law with the same rules as the directive.³ This gives Member States an opportunity to adopt the directive in the best way for the Member State in difference from regulations that have direct effect in all Member States,⁴ which not is the case with directives.⁵ The uses of regulations are more common in more abstract areas than company law,⁶ like the area of companies as whole or for all listed companies. This is the reason for the use of directives on company law.⁷

The European Union has adopted several directives⁸ that affect different parts of the company law, like annual reports, mergers, consolidated accounts, disclosure, and capital requirements. In addition to this, there have also been amending to these directives.⁹

¹ Saenger, Ingo, *Recent Developments in European Company and Business Law*, Deakin Law Review, 2005, volume 10 No 1. p 297.

² Craig Paul, De Búrca Gráinne, *EU LAW, text, cases and materials*, fourth edition, Oxford Univeristy press, 2008, p 83-86.

³ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 42-43.

⁴ Ibid, p 44.

⁵ Steiner, Josephine, Woods, Lorna, Twigg-Flesner, Christian, *EU Law*, 9 th edition, Oxford University Press, 2006, p 57.

⁶ Ibid. p 57.

⁷ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 42

⁸ http://ec.europa.eu/internal_market/company/official/index_en.htm, accessed 10 May, 2010.

The cross-border business within the European Union has expanded and all sizes of limited liability companies, companies with an own legal body, no matter if they are private or public, possible to buy on a stock market or not, are part of the European Market. This is a positive start for the idea of an Internal Market because without the SMEs the Internal Market can be never establish in the European Union since these companies are the majority of companies within the European Union.¹⁰ Because of this is it still necessary to give SMEs better opportunities, like giving them financial support and less administrative burden, to be part of this cross-border market since these companies are an important group that includes approximately 99,8 %¹¹ of all companies in the European Union and thereby is the foundation for the European economy.¹²

To give the SME this possibility is the European Union trying to support SMEs in different ways and the most important part is to give SMEs less administrative burden in the annual reports, a report over the financial status of the company during the last year. The European Union is constantly working for an Internal Market with equal rights and obligations for limited liability companies, no matter the size of the company or if it is public or not. In 2009, the European Union therefore adopted Directive 2009/49/EC¹³ that gives less of an administrative burden to SMEs. This directive is still under implementation, thereby meant that the Member States still have time to adopt the directive into their national legislation. Therefore, to this it is still unknown how large the changes will be for the affected SMEs.

⁹ Ibid.

¹⁰ Audretsch, David, Van der Horst, Rob, Kwaak, Ton, Thurik, Ron, *First section of the Annual Report on EU Small and Medium-sized Enterprises*, Zoetermeer, January 12, 2009.

¹¹ Neville, Mette, Sørensen, Engsig, Karsten, *Company Law and SMEs*, Thomson Reuters Professional A/S, 2010, p 17.

¹² Ibid. p 17.

¹³ Directive 2009/49/EC of the European Parliament and the council of June 2009 amending Council Directives 78/660/EEC and 83/349/EEC as regards certain disclosure requirements for medium-sized companies and the obligation to draw up consolidated accounts, OJ L 164 26.6.2009 p 42.

Directive 2009/49/EC¹⁴ has one more amending that does not connect to the Fourth¹⁵ and Seventh¹⁶ Directives. The amending is that Article 27 of the Fourth Council Directive also will include the medium-sized companies in the group that will not need to present all information that is general obligated according to the Fourth directive¹⁷.

1.2 Purpose

The purpose of this thesis is to examine what effect Directive 2009/49/EC will have to the Fourth¹⁸ and Seventh¹⁹ Council Directives. Thereby is the purpose to analyze the effects of Directive 2009/49/EC on the disclosure requirements in Article 45 (2) of the Fourth Directive and to analyze the effects that Directive 2009/49/EC will have on SME and the obligation to draw up consolidated accounts in Article 13 (2a) in the Seventh Directive.

1.3 Method and materials

The methods used for this thesis is a descriptive method as well as a problem-oriented method. Chapter two is based on the descriptive method to clarify what kind of companies that will be affected by the implementation of Directive 2009/49/EC. The material used in this chapter is the Fourth²⁰ and Seventh²¹ Directive, Directive 2009/49/EC, as well as a recommendation²² about the definition of SME and literature.

¹⁴ Ibid.

¹⁵ 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. OJ L 222 14.08.1978. p 11-31.

¹⁶ Seventh Council Directive 83/349/EEC of June 13 1983 based on the article 54 (3) (g) of the Treaty on consolidated accounts. OJ L 193, 18.07.1983, p 1-17.

¹⁷ Fourth Council Directive 78/660/EEC, Art, 27.

¹⁸ Ibid.

¹⁹ Seventh Council directive 83/349/EEC.

²⁰ Fourth Council Directive 78/660/EEC.

²¹ Seventh Council Directive 83/349/EEC.

²² Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/361/EC). OJ L 124, 20.5.2003, p 36-41.

Chapter three has also the descriptive method as base to explain and describe the amendments Directive 200C/49/EC will have on the Accounting directives²³. To this chapter are the Accounting directives, Directive 2009/49/EC and literature used.

In chapter four and five where the larger discussion and analyze is, the chapters are based on the problem-oriented method to try analyzing the effects of Directive 2009/49/EC. Here is the used material, once again the Fourth and Seventh Directives together with Directive 2009/49/EC and literature.

1.4 Delimitations

Since the purpose of this thesis is to analyze the effects through Directive 2009/49 /EC will not all companies be discussed, only the affected companies, the SMEs. Since the purpose of this thesis focus on the judicial effects from the implementation of Directive 2009/49/EC is the economical aspects of the implementation not dealt.

Companies listed on a stock market are instead of using the European directives required to use IFRS-standards from IASB to the reports.²⁴ In other words, a limited liability company that is public and thereby possible to buy on a stock market in a Member State do not need to report according to the European Accounting Directives. Because of this are companies required to report according to the IFRS-standards not analyzed in this thesis.

Since Directive 2009/49/EC only affects the Fourth²⁵ and Seventh²⁶ directive are these the only directives together with Directive 2009/49/EC that will be discussed since the other directives from European Union not effects the annual reports or consolidated accounts. Even if there is a third Accounting directive²⁷ about auditors, is this not affected by Directive 2009/49/EC and will thereby also be excluded from this thesis.

²³ Fourth Council Directive 78/660/EEC and Seventh Council Directive 83/349/EEC.

²⁴ Regulation (EC) No 1606/2002 of the European Parliament and of the Council of July 19 2002 on the application of international accounting standards, OJ L 243, 11.9.2002, Art. 3.

²⁵ Fourth Council Directive 78/660/EEC.

²⁶ Seventh Council Directive 83/349/EEC.

²⁷ Eight Council Directive 84/253/EEC of 10 April 1984 based on Article 54 (3) of the Treaty on the approval of persons responsible for carrying out the statutory audits of accounting documents, OJ L 126, 12/05/1984. p 20-26.

1.5 Outline

This thesis is divided into five chapters including this introduction chapter and is split into two different parts. The first part is a descriptive part giving the important information necessary for the following part with the discussion and analyze of Directive 2009/49/EC.

The descriptive part starts with chapter two that describes the different types of companies that will analyzed and discussed in this thesis. The third chapter is describing Directive 2009/49/EC and the Fourth and Seventh Council Directives that affects by the implementation of Directive 2009/49/EC.

The discussion part with the analyze starts in the fourth chapter where the amendments will be discussed in detail for the affected companies, SMEs. In the last chapter, chapter five is a conclusion for the whole thesis as well for each size of the SMEs.

2 Concluded companies

2.1 Introduction

This chapter defines, the requirements that companies have to fulfil to classify as a SME according to the Fourth and Seventh directives. The requirements are similar between the three categories of SMEs, Micro, Small and medium-sized, but there are still some differences discussed in connection to each category of SME. It is important to know the definition of a SME because if a limited liability company exceed the definition of a medium-sized company it is considered to be a large company and then has to fulfil all requirements in the Fourth²⁸ and Seventh²⁹ directives. This means that they are not allowed to exclude information that SMEs can leave outside their reports.

The European Union has through a recommendation³⁰ from 2003 tried to find a definition of these companies that all Member States in the European Union can use. Before the recommendation from 2003³¹ entered into use, Member States did have their own definition, which was a problem since Member States could treat companies different only because their definition of a SME were not equal. This is not in line with the European Union idea of one Internal Market with same requirements and opportunities to take part on the European market, no matter the size of the limited liability companies or if it is private or public. The recommendation³² contains three things that companies have to fulfil to be classified as a SME under this recommendation. However, the Commission holds that it is only necessary that the company fulfil one of the two financial requirements.³³ The two optional financial requirements are the turnover and balance sheet total.³⁴ The reason why SMEs have the possibility to exceed one of these requirements is because different markets have different level of turnover, manufacturing

²⁸ Fourth Council Directive 78/660/EEC.

²⁹ Seventh Council Directive 83/349/EEC.

³⁰ Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/364/EC).

³¹ Ibid.

³² Ibid. para (4).

³³ Ibid. para (4).

³⁴ Ibid. para (4).

companies have in general a lower level of turnover than those in distribution and trade markets.³⁵ One more thing to keep in mind when talking about SMEs in general is that they are typical of having only a few shareholders. The reason for this is that most of SMEs are family companies or at least are the shareholders closely related to each other.³⁶

2.2 Micro companies

The smallest version of limited liability companies in the European Union is called “Micro companies” and cannot have more than up to nine employees. That companies of this category are small is also displayed by the requirements that have to be fulfilled. The most important requirement is according to the recommendation from the Commission that the company is not allow to have an average of employees over nine people during the same year.³⁷ The requirements stated in Article 2 of the annex of the Recommendation³⁸ are:

- 1) As said, the most important requirement is that the average of employees in the company during two years is not above nine. If that is the case, the company would instead end up under the definition of a Small company³⁹.

The requirement of employees is the most important, since that must be fulfilled before considering 2) and 3). It is only necessary that one of them is in the range of the criterion. The company will still be a Micro SME if one of 2) and 3) exceeded.

- 2) The second criterion is that the annual turnover is within 2 million Euros, but this can still be allowed if the annual balance sheet in the third requirement is below 2 million Euros. Because, as the Commission said in the recommenda-

³⁵ Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/364/EC). para (4).

³⁶ Neville, Mette, Sørensen, Engsig, Karsten, *Company Law and SMEs*, Thomson Reuters Professional A/S 2010 p 17.

³⁷ Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/364/EC) para (4).

³⁸ Ibid. Annex, Art. 2, point. 3.

³⁹ See chapter 2.3.

tion, it is only necessary that one of the financial requirements fulfils the criterion.⁴⁰

- 3) Thirdly, the annual balance sheet of the company must be within 2 million Euros.⁴¹ But once again, if this criterion is exceeded but the second criterion about the turnover is fulfilled is the company still defined as a Micro limited liability company in the Fourth⁴² and Seventh⁴³ directives according to the recommendation⁴⁴.

2.3 Small companies

For a company in the European Union to classify as a Small limited liability company there are almost the same requirements as for the Micro limited liability companies. The difference is that the maximum level is higher for Small companies. The requirements stated in the referred recommendation⁴⁵ are for Small companies:

- 1) Once again is the average of employees in the company the most important requirement according to the commission.⁴⁶ A Small limited liability company can have an average of employees up to 50 during two years.

For Small SMEs, there is a maximum employee requirement, 1). It is not necessary to consider 2) and 3) if the employees exceed the requirement of maximum 50 people, since the company then it is a medium-sized SME. If the employee requirement is fulfilled it is necessary that one of number 2) and 3) is within the range of the requirement. If one of them and the number of employees is under 50, the company defines as a Small SME.

⁴⁰ Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/364/EC) para (4).

⁴¹ Ibid. Annex, Art. 2 point 2.

⁴² Fourth Council Directive 78/660/EEC.

⁴³ Seventh Council Directive 83/349/EEC.

⁴⁴ Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/364/EC) para (4).

⁴⁵ Ibid, annex, Art. 2 point 2.

⁴⁶ Ibid. Para (4).

- 2) Instead of 2 million Euros that is the maximum for the Micro limited liability companies, is the Small limited liability company allowed to have an annual turnover for the company up to 10 million Euros.
- 3) Thirdly is the company allowed to have an annual balance sheet up to the maximum of 10 million Euros.⁴⁷ Also with the Small companies, it is only necessary that one of the turnover and balance sheet requirements is fulfilled. If one of these should exceed 10 million Euros, would the company still be defined as a Small company. In the case where both exceed 10 million Euros is the company to consider as a medium-sized company.

2.4 Medium-sized companies

This is the largest category of SMEs in the recommendation, if a company exceed these requirements it is seen as a large company and has to report according to all the requirements in the Fourth⁴⁸ and Seventh⁴⁹ directive. The requirements are in general the same as for the Small limited liability companies but for the medium-sized companies is the maximum level higher. The requirements according to Article 2 of the annex to the Recommendation are as follows:⁵⁰

- 1) This category of limited liability companies can have up to 250 as an average of employees during two years. If this requirement is exceeded, it does not matter if the company have fulfilled requirement 2 or 3, the company is still defined as a large limited liability company.

The requirement about employees is like for the Micro and Small SME the most important. The Commission states that it is not necessary that 2) and 3) are within 10 million Euros.⁵¹ If one of them, together with the employee requirement, is within 10 million

⁴⁷ Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/364/EC), annex, Art 2. point 2.

⁴⁸ Fourth Council Directive 78/660/EEC.

⁴⁹ Seventh Council Directive 83/349/EEC.

⁵⁰ Commission recommendation of 6 of May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/364/EC), annex, Art. 2 point 1.

⁵¹ Ibid. para (4).

Euros is the company considered a medium-sized SME company and can enjoy the lower disclosure obligation in the Fourth Directive and maybe does the company not need to draw up a consolidated account in accordance with the Seventh Directive.

- 2) The maximum amount of the annual turnover is for medium-sized companies allowed to be as high as 50 million Euros instead of the EUR 10 million for the Small companies.
- 3) Finally is the medium-sized companies allowed to have an annual balance sheet up to a maximum of EUR 43 million instead of the EUR 10 million for Small companies.

2.5 Limited Liability Companies

2.5.1 Limited liability companies in general

The meaning that a company is a limited liability company is very important since there is a difference between this category of companies and other types, like partnership, unlimited liability companies etc. The importance of this can be describe as, if the company is not a limited liability company then does the scope of the Fourth and Seventh directive does not cover them. The Fourth and Seventh directives is only applicable on limited liability companies. All limited liability companies are required to disclose financial information, thereby are all limited liability companies obligated to draw annual report⁵²s. This chapter includes a clarification about what is meant by a limited liability company.

The first thing to know about limited liability companies is that they, as the concept says, have a limited liability for its shareholders.⁵³ This means that the shareholders cannot be responsible for the actions done by the company, at least in the ordinary work. This leads to the point that the company has it owns legal body⁵⁴, a judicial body that gives the company the possibility to take actions against others but also be accused

⁵² Van Hulle, K, *Harmonization of accounting standards, A view from the European community*, European Accounting review, May 92, volume 1, Issue 1 p. 165.

⁵³ Dorresteyn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European corporate law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 25.

⁵⁴ Ibid. p 11.

and sued in the same ways as natural persons.⁵⁵ The company can in difference from partnership and other forms of businesses hold its own property.⁵⁶

2.5.2 Public and private companies

The Fourth and the Seventh Directives do not apply on all kind of limited liability companies. The category of limited liability companies is divided into private and public limited liability companies with some differences. It is hereby important to have this information to understand the discussion in chapter four and five. The Seventh directive does not apply on public companies because they, according to a regulation⁵⁷, shall present their annual and consolidated accounts in accordance with the IFRS-standards from IFSB.⁵⁸

The definition of a private limited liability company is in literature described as a company that is not public.⁵⁹ This category is in general for the Small and medium-sized concerns and companies (SME) because the companies have their own legal bodies as well as limited liability for its shareholders. This means that the SME has the same requirements as a public without the access of public founding to the company. The SME is still obligated to have an annual report and present notes connected to this and obey the true and fair principle, that the report shall give a correct view over the company. The private limited liability company gets its money from shareholders or by any kind of financial institution as a bank.⁶⁰ The right to transfer shares is often limited in SMEs since they in many cases are family businesses and that family members make their living in the company. The public limited liability company is defined as a company in

⁵⁵ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European corporate law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 11.

⁵⁶ Hicks, Andrew & Goo, S.H. *Cases and Materials on Company law*, Oxford University Press, 6 th edition, 2008, p 95.

⁵⁷ Regulation (EC) No 1606/2002 of the European Parliament and the Council of 19 July 2002 on the application of international accounting standards. Official Journal L 243 11/09/2002.

⁵⁸ Ibid, Art. 4.

⁵⁹ Hicks, Andrew & Goo, S.H. *Cases and Materials on Company law*, Oxford University Press, 6 edition, 2008, p 79 and Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009 p25-26.

⁶⁰ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 27.

which it is possible to buy shares on a public stock market.⁶¹ Because of this, it is possible to call public limited liability companies, Stock companies.⁶² Stock market companies are part of the market in all Member States in the European Union and the public status are mostly for the larger limited liability companies that need the possibility to use all types of external finances, like banks, shareholders etc. Of course can smaller companies as well be public, but it more common that larger companies are public because of the bigger need of external financial support. The most important difference from the private limited liability company is that the transfer of shares in Stock market companies is free and the requirements of disclosure and reports are higher.⁶³

2.6 Subsidiary companies

Since one of the Accounting directives, the Seventh Directive⁶⁴ is focusing on the situation of subsidiaries, it is necessary to have an idea of the meaning of a subsidiary. This means that a company have such great impact, through shares, in another company that it controls management of the bought company. At this point it is necessary to show interested people this ownership since that might help them to decide if it is worth investing or not. As well as, if this is not shown, it is difficult for a company that have several subsidiaries to show a true and fair view since its assets and liabilities are not correct. It is also difficult for people outside companies to see the connections. Since Directive 2009/49 /EC affect the Seventh directive, it is necessary to explain what a subsidiary company is.

When a parent company, the buyer, has reached the level prescribed in the complicated Article 1 of the Seventh Directive, it is obligated to draw consolidated accounts for the group of companies. It is common that a company has a number of subsidiaries. The idea is that all subsidiaries shall be included in the consolidated accounts but there are possibilities to not presenting all the subsidiaries. If the subsidiary not affects the parent company, it is not necessary to present it according to the Seventh Directive.

⁶¹ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 26-27.

⁶² Ibid. P 26.

⁶³ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 26-27.

⁶⁴ Seventh Council Directive 83/349/EEC.

3 The Company Directives

3.1 In general

Within the European Union, there are several directives⁶⁵ concerning company law for private limited liability companies. These directives will probably be amended or replaced by new directives as the market change. Further, the work for an Internal market with equal right no matter the size or version of limited liability companies in the European Union goes on. Since the purpose of this thesis is to analyze the effects that amending of Directive 2009/49/EC has to the Accounting directives, the Fourth⁶⁶ and Seventh⁶⁷ and Eight directive on auditors⁶⁸, not affected by the directive. These three directives contain very detailed rules for the national legislation of the Member States.⁶⁹ This is one reason why Directive 2009/49/EC only affects such small part of the Fourth and Seventh directives. Only the Fourth and Seventh directive is discussed in this chapter.

3.2 Directive 2009/49/EC

During 2009, the parliament adopted Directive 2009/49/EC that amends the disclosure requirements and obligations in two of the *Accounting Directives*, the Fourth⁷⁰ and Seventh⁷¹ directive. The Directive 2009/49/EC entered into force in 2009 and still are under implementation, meaning that Member States shall make this directive a national law with the same status and ruling as the directive, or adopt it as presented by the European Parliament. Member States of the European Union have until January 1th, 2011 to implement Directive 2009/49/EC,⁷² and because of this deadline is there many Member

⁶⁵ http://ec.europa.eu/internal_market/company/official/index_en.htm, accessed 10 May 2010.

⁶⁶ Fourth Council Directive 78/660/EEC.

⁶⁷ Seventh Council Directive 83/349/EEC.

⁶⁸ Eight Council Directive 84/253/EEC.

⁶⁹ Saenger, Ingo, *Recent Developments in European Company and Business Law*, Deakin Law Review, 2005, volume 10 No 1. p 306.

⁷⁰ Fourth Council Directive 78/660/EEC.

⁷¹ Seventh Council Directive 83/349/EEC.

⁷² Directive 2009/49/EC Art. 3.1.

States that still not have incorporate Directive 2009/49/EC into national legislation.⁷³ A larger discussion about the possibilities and probable effects based on the implementation of Directive 2009/49/EC is in chapter 5 and 6.

The implementation will not affect the Accounting Directives as a whole. Directive 2009/49/EC will only affect the information that private limited liability companies, have to present in notes to their annual reports according to the Fourth directive and the obligation to draw and present subsidiaries according to the rules in the Seventh directive. The effect is mostly concentrated to the SMEs⁷⁴. SMEs, companies that are private and have limited liability. This is because larger limited liability companies have the obligation to either follow the ordinary rules in the Fourth and Seventh Directive or present the annual reports according to the rules in IFRS-standards, if the companies are listed on a stock market in The European Union and because of this is obligated to follow the IFRS-standards.

Directive 2009/49/EC has actually one article that will affect the disclosure requirements in the Accounting Directives, Article 2. This article will be discussed in details in the following chapters.⁷⁵ The reason for the implementation of Directive 2009/49/EC is according to the Economic and Social Committee to give SMEs less administrative burden as well as to loosen up the obligation to draw consolidated accounts according to the Seventh directive.⁷⁶

3.3 Fourth Company Directive, 78/660/EEC

The Fourth Directive⁷⁷, also known as *the Account Directive* is originally from 1978. In general the directive concerns the principles used in the company's annual reports, e.g. do not deal with groups of companies, this is the scope of the Seventh Directive. The rules stated in the Fourth directive are such as the display of the balance sheet, a report

⁷³ Directive 2009/49/EC, Art 3.

⁷⁴ Chapter 2.2 – 2.4 above.

⁷⁵ Chapter 3.3-3.4 and 4.

⁷⁶ Opinion of the European Economic and Social Committee on the “Proposal for a Directive of the European Parliament and of the Council amending Council Directives 78/660/EEC and 83/349/EEC as regards certain disclosure requirement for medium-sized companies and obligation to draw up consolidated accounts” OJ C 77, 31.3.2009, p 37-40. para 1.4.

⁷⁷ Fourth Council Directive 78/660/EEC.

over the profit and loss accounts as well as rules about how additional information to these accounts shall be presented in notes.⁷⁸ This additional information shall be clear and precise.⁷⁹

The principle of “true and fair” used through the whole European Union has been established in the Fourth directive.⁸⁰ The meaning of this principle is that all information presented by the company has to show a correct view over the company’s assets, liabilities, financial position and the company profit or loss during the year.⁸¹ This principle is overriding,⁸² the reports must follow the principle.

Directive 2009/49/EC will only amend a small part of the Fourth directive⁸³, this is to say the disclosure requirements regarding additional information found in the Fourth directive and especially Article 45 (2)⁸⁴. Before Directive 2009/49 /EC is implemented, the second subparagraph of Article 45 (2) in the Fourth company directive the meaning:

‘The Member States may permit the companies referred to in Article 27 to omit the disclosures prescribed by Article 43 (1) (8). Article 12 shall apply.’⁸⁵

At the latest of first of January 2011, the sub paragraph in Article 45 (2) of the Fourth directive has the meaning instead:

‘The Member states may permit the companies referred to in Article 27 to omit disclosure of the information specified in Articles 34 (2) and 43 (1) (8).’⁸⁶

⁷⁸ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p 267.

⁷⁹ Fourth Council Directive 78/660/EEC, Art. 2.2.

⁸⁰ Ibid. Art 2.3.

⁸¹ Ibid. Art 2.3.

⁸² Van Hulle, Karel, *The true and fair view override in the European Accounting Directives*, The European Accounting Review, 1997, volume 6 issue 4, p 713.

⁸³ Fourth Council Directive 78/660/EEC, Art 45 (2).

⁸⁴ Directive 2009/49/EC, Art 1.

⁸⁵ Fourth Council Directive 78/660/EEC Art. 45 (2).

⁸⁶ Directive 2009/49/EC Art 1.

The major difference that this amending will do is that companies referred in Article 27 of the Fourth directive also can chose whether or not they want to obey the requirements found in Article 34 (2) in the Fourth directive. The companies affected by this amending are the companies explained in chapter two above, in other words the SMEs, which are limited liability companies.

Knowing the affected companies, it is easier to investigate and analyze the requirements that have been amended. According to Article 45 (2) in the Fourth directive, two articles are amended by directive 2009/49/EC. Both Article 34 (2) and Article 43 (1) (8). These articles are analyzed in detail, starting with the Article 34 (2) that states:

‘The amounts entered under “formation expenses” must be explained in the notes on the accounts’⁸⁷

The value of this article will first be clear knowing the meaning of “Formation expenses”. This is the costs for the company to take form before the day it starts the business, in many cases is it possible to say that “Formation expenses” is the start up expenses. This account can differ a lot between different limited liability companies. Some limited liability companies have huge amounts upon this account since the company can put up for example, employee training, advertising and similar activities that happens before the company starts up its business while other companies only have small account. The burden of this account, are for some limited liability companies a burden, because companies present a huge amount of information that has to be explained in notes.

To be able to analyse the effects that Directive 2009/49/EC have on the Fourth Directive it is also necessary to see what further information that the referred companies from Article 27, the SMEs, do not need to present in their annual accounts. These are found in Article 43 (1) (8) of the Fourth Directive, which provides:

‘The net turnover within the meaning of Article 28, broken down by categories of activity and into geographical markets in so far as, taking account of the manner in which the sale of products and the provision of services falling within the company’s ordinary activities are organ-

⁸⁷ Fourth Council Directive 78/660/EEC Art. 34 (2).

ized, these categories and markets differ substantially from one another.’⁸⁸

In general, the company has an obligation to present the sales of products as well as provisions of services and other things falling within the ordinary activities of the company. The company shall present this information in notes for each activity and geographical market for the company in the case that it differs substantially from how the activities are normally organized.⁸⁹ For SMEs, will Directive 2009/49/EC amend so it will not be necessary to present this information, still have SMEs the opportunity to present the information in notes if they want because companies are allowed to provide more information than the directive require since the requirements in the directives generally are a minimum.⁹⁰

3.4 Seventh Company Directive, 83/349/EEC

From the first of January 2005 may Member States permit or require that companies in that Member State shall present their consolidated in accordance with IAS regulation⁹¹ so that the consolidated accounts are in conformity to the IAS instead of the Seventh directive.⁹² The Seventh directive⁹³, also known as *The Consolidated accounts directive* entered into force 1983. This directive concerns companies that have subsidiary companies. This means that a company have a great influence of the management and control of another company, a subsidiary company. Because of this has the company that controls the management of the other present consolidated accounts for all the companies that are included in this group of companies. The company that have the possibility to manage the other have the obligation to present accounts that show a true and fair view for the group of companies as if they were one, similar to the obligations in the Fourth

⁸⁸ Fourth Council Directive 78/660/EEC, Art. 43(1) (8).

⁸⁹ Fourth Council Directive 78/660/EC, Art 43 (1) (8) and 28.

⁹⁰ Edwards, Vanessa, *EC Company Law*, Oxford University Press, Oxford EC Law Library, 2003, p 144.

⁹¹ Regulation (EC) No 1606/2002 of the European Parliament and the Council of 19 July 2002 on the application of international accounting standards.

⁹² Ibid. Art. 2.

⁹³ Seventh Council Directive 83/349/EEC.

directive⁹⁴ but for all companies in the group. The Seventh directive was from the beginning supposed to be part of the Fourth Directive but since there was a debate concerning the scope of the Seventh directive it instead became a separate directive.⁹⁵

One of the reasons for the adoption of the Seventh Directive is to create an Internal Market with equal opportunities and obligations for limited liability companies. It is also necessary that it is possible to compare groups of companies from different Member States in an easy way. Through the Seventh directive, the Council has managed to find a way that gives limited liability companies the possibility to have equal requirements and burden across the European Union. Thereby interested people have the opportunity to compare this category of companies from different Member States without doing many adjustments in the reports.

Directive 2009/49EC will, since the Seventh and Fourth Company Directives are connected to each other also affects the Seventh directive. Until Directive 2009/49/EC has been implemented, there is no subparagraph 2a in Article 13 in the Seventh directive. After the implementation will Article 13 (2a) state:

‘Without prejudice to Article 4 (2) and Articles 5 and 6, any parent undertaking governed by the national law of a Member State which only has subsidiary undertakings which are not material for the purposes of Article 16 (3), both individually and as a whole shall be exempted from the obligation imposed in Article 1 (1).’⁹⁶

To analyze the effects through Directive 2009/49/EC it is once again important to see the articles that will be indirectly affected by the implementation. Article 16 (3) of the Seventh Directive states that:

⁹⁴ Fourth Council Directive 78/660/EEC.

⁹⁵ Dorresteijn, Adriaan, Monteiro, Tiago, Teichmann, Christoph, Werlauff, Erik, *European Corporate Law*, second edition, Kluwer Law International BV, The Netherlands, 2009, p274.

⁹⁶ Directive 2009/49/EC, Art 2.

‘Consolidated accounts shall give a true and fair view of the assets, liabilities, financial position and profit or loss of the undertakings included therein taken as a whole.’⁹⁷

In general it is necessary for limited liability companies to present all subsidiaries in accordance with the True and Fair principle in the Fourth directive.⁹⁸ This is not necessary in cases where the subsidiaries have small or none effect on the parent company. In this case, is the subsidiary not part of the purpose of Article 16 (3) of the Seventh directive. If the subsidiaries have this small effect on the parent company it is not necessary to present consolidated accounts for the group since it is not in the scope of the Seventh directive to present consolidated accounts if they do not differ from the reports from the parent company in the group. This is the situation even in cases where the group as such is part of the scope and requirements founded in Article 1 (1) of Seventh directive.

⁹⁷ Seventh Council Directive 83/349/EEC Art. 16 (3).

⁹⁸ Fourth Council Directive 78/660/EEC, Art. 2. point 3.

4 Effects on the Fourth and Seventh Accounting Directives by Directive 2009/49/EC

As mentioned in chapter 3.1, Directive 2009/49/EC is only affecting the Accounting Directives, the Fourth⁹⁹ and Seventh¹⁰⁰ company directive. How much impact will it really have on these? Since Directive 2009/49/EC only affect one article in each directive directly, Article 45 (2) in the Fourth directive and Article 13 (2a) in the Seventh directive, it is difficult to see that the impact of Directive 2009/49/EC is that large in general for the directives. If focusing on the SMEs, the group of companies that is most affected through Directive 2009/49/EC is change, to both the better and worse, even if it is difficult to see the concrete effects. This is because Directive 2009/49/EC still is under implementation. It has to be incorporated into national legislation by the national authorities, before January 2011, so it is still not many Member States that has incorporated Directive 2009/49/EC.¹⁰¹

One of the more important amendment Directive 2009/49/EC have according to the Economic and social Committee (The committee) is the change of administrative burden for the SMEs.¹⁰² The Committee discusses the administrative approach but also the economic approach is of interest. Even the economic part may affects, even though the economic effect will be smaller than the effect on the administrative burden. If the amending gives less administrative burden, as supposed, it will also give an economic change since a less administrative burden for SMEs will give them more equal rights to compete with larger companies. In this case most seen as limited liability companies but as well as other kinds of businesses like partnerships and unlimited liability companies. The economic aspect is important because if the economy for SMEs is approved will this also stimulate the European economy since SMEs is the largest category of compa-

⁹⁹ Fourth Council Directive 78/660/EEC.

¹⁰⁰ Seventh Council Directive 83/349/EEC.

¹⁰¹ Directive 2009/49/EC Art. 3 (1).

¹⁰² Opinion of the European Economic and Social Committee on the "Proposal for a Directive of the European Parliament and of the Council amending Council Directives 78/660/EEC and 83/349/EEC as regards certain disclosure requirement for medium-sized companies and obligation to draw up consolidated accounts" 2.1.

nies in the European Union.¹⁰³ If this happen will it also be an improvement to the idea of an Internal Market since without the impact of SMEs the Internal Market can never be reality.

It is important to keep in mind that it is hard to make a general conclusion about the effect that less administrative burden will have on all SMEs. The amount of presented information differs between their annual reports, through both different national legislations as well as the spectra of opportunities of different reporting methods within one Member State. For those SMEs that try to have large amount of information in the notes attached to the annual reports will the implementation of Directive 2009/49/EC not be of such much interest since these companies already have a gap down to the minimum requirements in the Fourth and Seventh directives¹⁰⁴.

Many of these companies, probably often Medium-sized SMEs, since this group of SMEs more often have a larger interest in potential external investors. Because they more likely have larger contracts and affairs that may need external finance, from example financial institutes, banks of private investors, which may require more information about the company. Even the aspects that larger SMEs often have larger market for the business and thereby more people that see the company. Of course can the aspect of financial support be the reason for why even smaller SMEs have larger amount of information in notes attached to the annual reports, since it easier to present a good view over the company. In general, is the need of information is still lower in smaller SMEs since the group of interested in these companies is smaller.

The effect that less administrative burden will have will probably be different between different types of companies, because different types of businesses need different kind as well as different amount of information. Generally, the amendments have a positive effect to SMEs since the administrative burden is one of the most discussed parts of the Company law area. It has also been an important part for the Internal Market with equal rights and obligations for companies.¹⁰⁵ Still is the argument of less administrative bur-

¹⁰³ Neville, Mette, Sørensen, Engsig, Karsten, *Company Law and SMEs*, Thomson Reuters Professional A/S 2010 p 17.

¹⁰⁴ Fourth Council Directive 78/660/EEC and Seventh Council Directive 83/349/EEC.

¹⁰⁵ Opinion of the European Economic and Social Committee on the “Proposal for a Directive of the European Parliament and of the Council amending Council Directives 78/660/EEC and 83/349/EEC as

den for SMEs in general a good reason for implementing Directive 2009/49/EC since it will probably be a positive effect to both the European economy as well as the European Union.

Another important aspect due to the implementation of Directive 2009/49/EC is the loss of information. The Committee argue that it will not be of any substantial loss for interested. This is probably right in many cases. The loss may even be to the better because the presented information will be more concise and accurate and thereby more useful for the interested. Even though, it may also be the other way around since some interested can be in need of the information that will not be presented. The Committee seems to have considered only one side of the coin in this question. Have they really thought about the differences between Member States and the different groups of interested? Since the SMEs, as discussed in this discussion, in general do not have that many interests may the loss of information still be to the better. Even though it feels like The Committee only have seen part of the question, their opinion in general is correct and accurate and the amending is good for all the sizes of SMEs. Still it is not possible to ignore the fact that there will be SMEs that can be negative affected due to this aspect of the implementation of Directive 2009/49/EC.

Directive 2009/49/EC not only affect the information necessary to present by SMEs. The directive also expand the scope of affected companies, from only being Micro and Small SMEs, to also effect limited liability companies defined as medium-sized¹⁰⁶, so all kinds of SMEs will be affected by the amending.¹⁰⁷ Is it a good change of the scope? Of course it is possible to argue in both ways, the amending may be to the worse in branches where the companies are capital effective and have a smaller group of employees since even a company that is defined as small can be as strong as one defined as medium-sized on that kind of market. This will probably not be such a problem because

regards certain disclosure requirement for medium-sized companies and obligation to draw up consolidated accounts” 1.6.

¹⁰⁶ Chapter 2.4 above.

¹⁰⁷ Opinion of the European Economic and Social Committee on the “Proposal for a Directive of the European Parliament and of the Council amending Council Directives 78/660/EEC and 83/349/EEC as regards certain disclosure requirement for medium-sized companies and obligation to draw up consolidated accounts” 1.1.

the risk is that the actual company then will exceed the definition of a SME, described in chapter 2.2-2.4 above. Thereby is the company anyway not allowed to present the annual reports, or consolidated accounts, without following the general rules in the Fourth respectively Seventh directive. The amending of giving all SMEs the same requirements is an amendment that is positive for the whole European Union since it one small step towards an Internal Market.

The obligation to draw up consolidated accounts because of the ownership of shares in subsidiaries in the Seventh Directive¹⁰⁸ is also affected by Directive 2009/49/EC. Connected with this is the question about potential information loss for interested. If the SMEs do not need to draw these consolidated accounts there can be difficulties to find information about subsidiaries to the SME. This amending is probably positive for the SMEs as such, since it once again gives less administrative burden, but even more important is the expected positive change for interested since it in most cases is the parent company that is the interesting one to invest in. Of course, it is possible to argue that it is important to have a correct view over all assets and liabilities of the company and that ownership of larger shares in other companies, subsidiaries, is important and without the consolidated accounts is it difficult. Still is the loss of this information not of greater interest than the opportunity for affected SMEs not to be obligated to draw consolidated accounts to present the information. For some interested may the loss of information be of interest but in the general aspect is this amending in the Seventh directive positive and it is a smart and effective amending that really will give SMEs less administrative burden when they only have to present a report following the requirements in the Fourth directive¹⁰⁹.

¹⁰⁸ Seventh Council Directive 83/349/EEC.

¹⁰⁹ Fourth Council Directive 78/660/EEC.

5 Conclusions

For the Micro SMEs, the smallest ones described in chapter 2.2, is Directive 2009/49/EC mostly effecting their obligations in the Fourth Directive¹¹⁰ since they are not likely to have subsidiaries necessary to present because of the Seventh Directive¹¹¹. The effect to Micro SMEs annual reports will probably differ between different types of businesses since the need for information may differ between markets. Since the group of interested is small for Micro SMEs is the possible loss of information not important. Because the interested are in general few and since many Micro SMEs are family businesses it is easy to ask for information. The general conclusion for Micro SMEs is that Directive 2009/49/EC is positive for Micro SMEs since their administrative burden as well as the loss of information is to the better.

The Small SMEs, described in chapter 2.3, will probably get similar effects, as the Micro SMEs, since the requirements not differ much between the two groups. Even if Small SMEs generally have more interest from other, like banks and external financiers, and thereby have a larger interest in presenting information in the notes, the amending area of Directive 2009/49/EC. The amending in the Seventh directive¹¹², about the obligation of drawing up consolidated accounts, is in general affecting Small SMEs more than Micros. Because the differences between these two categories are small will the amending of the Seventh directive not be that great for Small SMEs either.

The largest SMEs, medium-sized, described in chapter 2.4, are the ones that in general is less affected by Directive 2009/49/EC amendments to the Fourth directive. Because in many cases have Medium-sized SMEs already a gap down to the minimum requirements and thereby will the changes not be that significant since they have the largest number of interested and thereby have most interest in presenting information in notes both in the annual reports and possible consolidated accounts. The biggest effect for Medium-sized SMEs is that in some cases is it not necessary to draw consolidated accounts. It may be a loss of information to interested people but in general, this loss is to the better.

¹¹⁰ Fourth Council Directive 78/660/EEC.

¹¹¹ Seventh Council Directive 83/349/EEC.

¹¹² Ibid.

The general conclusion drawn by the implementation of Directive 2009/49/EC is that it is a positive amending of the Accounting Directives, the Fourth and Seventh directive.¹¹³ The quality of financial reports has as well as the comparability between companies, increased since the Fourth directive was implemented in 1978,¹¹⁴ and Directive 2009/49/EC is probably a new step in the right way for better comparability between companies within the European Union.

Even if there may be some losses of information, the positive changes are still larger because the effects on SMEs in European Union, especially less administrative burden, are to the better. The change of the scope to include the medium-sized SMEs is also a amending to the better since there are only smaller differences between the sizes of the affected companies. Even if it is difficult to analyze what the exact effects will be, it is so that the effects from the new directive seem to be for the better and give the SMEs better opportunities.

¹¹³ Fourth Council Directive 78/660/EEC & Seventh Council Directive 83/349/EEC.

¹¹⁴ Van Hulle, Karel, *Harmonization of accounting standards, A view from the European community*, European Accounting review, May 92, volume 1, Issue 1 p. 167.

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