The European Community as an Investment Area

I. The Economic Situation

On occasions like this excellent lunch, I have been frequently asked to explain what the European Community is. Let me state from the very beginning that it is very difficult to give a short definition. By the way, this is just like an elephant; everybody knows what it is but it is difficult to define it.

I may therefore limit myself to indicating that it is a Community of - at this time - ten Nation States, with nearly 270 millions inhabitants, which are on their long way towards becoming an European Federation.

From its very beginning in 1958, the European Community aimed at providing industries and agriculture with an internal market nearly as large as the European continent. Its tools are essentially the legislation on equal rules of access to markets, on competition, a common agricultural policy and a common and liberal foreign trade policy based on a common external tariff vis-à-vis third countries. One major target is that of creating an optimal investment area.

In what follows I want to highlight, first, the general economic situation of the European Community. Second, I would like to develop some considerations specifically about investment and, third, I would like to deal with our attempt to create a single legal environment for business favourable to the enterprise and therefore to the investor.
As to the macroeconomic situation, the European Community has been drawn into the worldwide economic slump which began for different occasions about 1980—mostly national.

Economic growth, measured by the increase in real GDP per capita, is stagnating and will probably not exceed significantly 1% in 1983. Unemployment is high, at more than 11 million people, i.e. about 10% of the labour force. The only positive indicators are those of a decrease in inflation rates to less than 10% on the average and the balance-of-payments, which are rapidly coming into equilibrium in the current accounts.

Among the negative factors, the deterioration of public budgets and the intolerable growth of the public sector, have to be mentioned, besides the burden of extremely high interest rates.

One of the special points of concern in this European market is that the share of gross fixed capital formation in GDP is declining. Since 1970 this share has decreased from 23% to 20% in 1981. The perspective is for a decrease to about 19% in the medium term future.

This decay in investment is not unique to the European Community. The situation in Japan, for instance, is rather impressive too, where there is a decrease from more than 35% to about 30%.

Compared to this rather clear decline, the situation in this country, the USA, is a bit more comfortable because here the share has been stable for more than a decade. Of course, because of the high degree of development of this economy the share of 18% is somewhat lower than in the European Community.

However, the message I want to leave with you is that there is a remarkable change in the political climate in Europe which will make the European Community more attractive for investment in the future.
Heads of states and governments of the European Community, assembled in the European Council in March of this year, recognized the close link between investment, competitiveness and employment. Since that time at least all the Member States have come more and more to the opinion that economic policies have to focus essentially on the promotion of productive private investment. The common denominator in all Member States on which political approaches to this problem are based is identical, its name is uncertainty and our common goal is to restore business confidence.

This implies many national and Community actions to improve the international economic environment. For we need more reliable prospects for an open international trade and more confidence in international financial investments.

Uncertainty is also a major characteristic of the economic situation within the Community, for instance with respect to the central bank policies and public finance. Uncertainty has been provoked by numerous factors. Four Member States of the European Community have at least annual public deficits of more than 10% of the GDP. Another important reason for uncertainty has been erratic developments in business legislation. Sudden increases of taxation, utopian ideas in the areas of social policy and as the "improvement" of the welfare state. New technical norms and standards as well as restrictive regulations which have also increasingly fostered uncertainty. Recession has prompted the temptation of protectionism inside the EC.

The need for new policies has clearly emerged during recent elections in European countries. During the last three months governments in some Member States have been replaced by more conservative and/or christian/democratic governments.
The socialist French government have recently re-oriented their policy towards a consolidation of the budget.

The main target of the policies of these political forces is to release resources for investment purposes by decrease of public deficits and by shifting consumptive expenditure towards public investment. The contribution of the European Community consists essentially of providing the necessary general (European) environment in which higher production can result from higher investment. Only in this way can we subsequently promote real growth and reduce unemployment over a longer period.

II. The internal market

From the Community's point of view, the first and fundamental condition for stimulating investment is of course the defence and development of the Community's internal market for goods and services. Much has been achieved to create a common set of rules in many areas of legislation and also in the field of technical standards. But, as you know, problems remain to be solved. Moreover, the existing construction has to be continuously defended against the temptations of protectionism. The Commission is determined to fulfill its responsibility in this respect. The European Court of Justice and the European Parliament are our best allies.

Indeed, one of the major issues of the present economic policy of the European Commission consists of exploiting systematically the advantages stemming from a single market large enough to underpin the expansion of industrial activities that are internationally competitive.
We take as our inspiration our Dutch friends, who, for many years were filling dikes and bailing out before they could be sure of walking on dry ground, for most of the day. More seriously, ladies and gentlemen, we are convinced that a large, integrated internal market offers the best guarantee of economic health in the long term.

III. A single environment for business

But an internal market for goods and services is not enough. Also necessary is the replacement of national rules and procedures applying to business enterprises by a Community-wide framework that will permit enterprises, investors and other economic actors to treat the Community as a single environment for business. If each State continues to feel free to its own way and adopt whatever regulations it pleases, enterprises will continue to find it difficult to adapt themselves to the new dimension of the Community market and we will not reap the full benefit of it. We need a legal framework that matches our economic objectives.

A start has been made. The Community Treaty itself gave us some powerful tools in the competition field, based very much on our experience, that have proved their worth. As regards taxation, a significant beginning has been made in relation to value added tax. But much remains to be done. Firstly, as regards other forms of indirect taxation, such as excise duties, and subsequently concerning certain fundamental principles of direct taxation. In the context of a new initiative aimed at promoting the idea of a continental-wide internal market, the Commission intends to press the Council of Ministers to accelerate work on the proposals already made concerning the overall harmonization of tax rates. We nevertheless have to admit that economic conditions will probably have to improve considerably before the political conditions will exist that will permit significant breakthroughs to be made.
Finance Ministers just do not have the room to manoeuvre at present.

In the company law field, for which I am directly responsible, more progress is being made. The first four company law directives have been adopted and are being implemented in the Member States. Now, after a long period of deliberation, a clear majority view has emerged in the Council of Ministers in favour of a uniform approach to the problems of insolvency, though technical problems remain to be resolved. In addition, the seventh directive on consolidated accounts for groups of companies is already well into its final negotiating stage, and its adoption is now likely next year.

The seventh directive is a good example of how we are seeking to construct a framework that will produce convergent developments and thereby enable enterprises to benefit increasingly from the simplification that flows from the progressive harmonisation of national laws. Can anyone doubt that in the absence of our proposal, we would have witnessed the development of new national requirements for group accounts of a more divergent and therefore much more troublesome character? Similarly, if we were to ignore completely the more controversial issues of group law and the parent/subsidiary relationship, dealt with in our forthcoming "ninth directive" sooner rather than later, national initiatives having different characteristics would inevitably be taken.
In this real sense, harmonization is de-regulation. It eliminates, or at least reduces, multiple and divergent national rules. Even when normally for political reasons, Community standards are expressed as minimum rules, in practice the minimum often tends to be also a maximum and greater convergence results. This fundamental effect of our programme is of direct benefit to enterprises and investors alike. It should also be of interest to investors from abroad who otherwise would continue to be faced with an increasing divergence in the legislation of the ten Member States.

IV. Problems posed by legislative programme and some solutions
But, of course, our legislative proposals do pose some problems both within the Community itself and from an specifically American point of view.

Sometimes, their importance for the creation of a single environment for business through a coherent set of harmonized, calculable and transparent rules tends to be overshadowed by the discussion of some of their aspects stemming from the specific political climate in Europe.

Typical concerns voiced in the USA are:
- that Community rules on product liability would increase the burden placed on manufacturing industry at a time when governments should do everything to alleviate this burden;
- that a sinister effect would result from legislation tending to the parent/subsidiary relationship by abolishing the liability of subsidiaries;
- that the introduction of the idea of workers participation into company law would seriously temper the decision-making capability of management to the effect of by discouraging investment;
that more particularly the so-called Vredeling proposal would tend to subject the decisions of MNC's to the consultation of their workers all over the world;
- that the rules on consolidated group accounts would amount to introducing obligations having an extra-territorial effect outside the scope of the Community;
- or, to sum it up, that Community legislation is biased against the operation of US based MNC's.

What is our response? I obviously cannot deal with everything today. Nevertheless the following points seem to me to be of particular importance.

(a) Not attacking multinational business

First, it follows from what I have said concerning our objective of creating a single, more calculable and transparent environment for business throughout the Community that our proposals are not designed as an attack on multinational enterprises in general, much less American ones in particular. We have consistently rejected calls for legislation directed specifically at the multinational. All our proposals apply in an even-handed way to national and multinational enterprises alike. Moreover, our objective is always to achieve equal treatment of enterprises regardless of their national character or origin [even when the objectively different situation of multinational enterprises may oblige us to rely on a specific legislative technique].

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(b) Resistance to change requires a step-by-step approach

Second, the Community has learned that since harmonization and legislative convergence do require changes to be made in the ways in which people do business and live their lives, we cannot be over-ambitious. Because of the different traditions and cultures of the Member-States, we need to rely on a step-by-step approach.

For this reason, we are concentrating on company law harmonization for the time being rather than on the adoption of a complete federal-type European company law of which you may have read a few years ago. This proposal is, as you say, "on the back burner". In any case, it is not for immediate consumption, though it has been consigned to the garbage can either.

In my opinion, the kind of balanced compromise that will emerge from the legislative process should in no way be viewed as a negative factor from the point of view of the enterprise or the investor. While extension of liability may result in some jurisdictions, the risk will be insurable, and the laws of the Member-States will stabilize in a convergent manner, with a considerable gain in their clarity and predictability of operation.

Let me now come to the important field of labour relations in the enterprise.

The economic pressures of the recent past have sharply underlined the need for our economies, and our enterprises, to adjust to change. They have at the same time given fresh impetus to political demands for new information, consultation and participation procedures for employees.
We have been interested to note that these pressures have not been completely absent in the US and that, in some sectors, such as automobiles, they have already produced new approaches to labour-management relations. On this side of the Atlantic, while on this side of the Atlantic, such innovations may still appear to be limited in scope, they are much more widely discussed and even practiced on the Continent. Clearly, this must be seen against the background of the specific political climate prevailing in Europe, where efforts aimed at fully integrating the workers movement into society are an element of long-term stability. Recent Belgian polls tend to show that demands for more participation are high on the list of expectations of the working population, whereas the present economic difficulties have put a lid on the pressures for wage increases.

The challenge, as we see it, is to meet these demands for change while firmly resisting proposals that would interfere with enterprises' ability to manage effectively the process of continuous adjustment that they are called upon to achieve. Far from being obstacles to this process, the proposed measures are an important tool to enable us to carry through by ensuring an adequate degree of social consensus concerning changes that are sometimes painful for those affected.
(c) Need for careful adaptation

However, if we must accept certain limitations on the Member States' capacity for change, we must also insist on the necessity of certain adaptations.

In these circumstances, laws affecting business can hardly be expected to escape periodic re-evaluation and amendment. Indeed, too great a resistance to change would likely be re-bound on those resisting it. At some point, changes would almost certainly be made, but more explosively, subject to less careful control and management. And in the meantime, the stresses created by the unsatisfied pressure for change would not disappear, but would continue to cause problems of their own for enterprises and investors.

Of course, I am not preaching change at any price. Our reforms must be carefully considered and balance carefully all the interests involved. We have, in addition, no intention of abandoning the fundamental principles of an open economy, which have served us so well in the past.
What does this mean in more concrete terms? Let me give 2 or 3 examples.

To take product liability to begin with, throughout the industrialized world deep-rooted forces — economic, social and political — have been apparent for many years while leading States to move away from liability based only on proof of fault or negligence to solutions that do not necessitate such proof. Developments have occurred on both sides of the Atlantic, and some of them on this side, incidentally, have gone much further than we are likely to go. They have also occurred in countries as far apart as Japan, Israel and New Zealand.

For the Community, a common approach is clearly desirable. The Commission would have been failing in its most fundamental duty if it had simply looked on while the Member States responded in their various ways to the evident pressures for change. By proposing a strict liability solution to be realized within the context of our traditional legal systems, the Commission appears to have succeeded in excluding the adaptation of collectivist solutions à la New Zealand based on "no fault" compensation through a publicly administered fund. Discussion now centres on certain difficult questions concerning the scope of the liability, which we are trying to find reasonable compromises. Liability for development risk, for example, will clearly not now be included as a Community requirement, though individual Member States will probably have to be free to include it if they wish, provided that they do so in an legislative text and not simply by case law.
The dynamic objective pursued by our proposals is underpinned by a number of important safeguards that we are being careful to include. We have the impression, that sometimes these are not sufficiently understood by critics who, of necessity, are relatively unfamiliar with the operation in practice of European industrial relations systems.

To take the fifth directive on company structure and employee participation as an example, the Commission has from the start been careful to ensure that whatever employee participation systems are included, they should not permit the decision-making of the company to be blocked. For this reason, we have always opposed (simple fifty-fifty) schemes for equal representation of labour and management on company boards. We have also resisted demands for employee rights of veto to management's economic decision-making for the same reason.

I am pleased to say that the European Parliament, by a large majority, has recently endorsed this approach in a most explicit manner, by suggesting that a provision be included in the fifth directive limiting the maximum proportion of employee representatives on company boards to one-half, and further specifying that in such cases, the shareholder representatives shall have the ultimate power to decide disputed questions. The Commission has already decided to include such a safeguard in its amended proposal. Its enactment at Community level would, in my view, constitute a guarantee for investors that is hard to under-value.
Similarly, the relatively uniform solution of the original proposal has been abandoned in favour of a more flexible approach. Following the European Parliament's recent opinion, the amended proposal will consist of a framework permitting the Member States to take account of their differing social traditions, while at the same time promoting convergent development in the structure of public companies and the institutional recognition given to labour, management and capital.

Let me say the Community's approach to the "Vredeling" directive will be fundamentally the same. While many of us, including myself, have reservations about the language of the original proposal, we are convinced that the underlying objective of the proposal is sound: Employee information and consultation systems presently existing in most of the Member States should be adapted to take into account the increasingly multinational dimension of enterprises in the Community. Employees should be adequately informed both about the general development of the firm of which their company forms part and, on a "need-to-know" basis, on important decisions likely to affect them, even if those decisions are being made in another country. At the same time, it is not our intention to strangle enterprises with cumbersome, impractical procedures. Nor should the absence of an agreement between both sides be allowed to interfere with the decision-making process. Amendments are now under consideration in the European Parliament which should prove helpful in this respect.
Obviously, you will not expect me to commit the Commission at this stage before the parliamentary stage is concluded. But I can say that certain of the ideas that have been suggested, for example, to protect sensitive information and to ensure that local management is not undermined or bypassed, seem to me to be well-founded and are likely to find a place in the Commission's amended proposal. Similarly, I would favour special provisions to the effect of excluding such obligations, which could be seen as having an element of extraterritoriality, which would exclude obligations seen to have an element of extraterritoriality. As to parent-subsidiary relationships and the so-called "ninth" directive, we shall be seeking the same kind of balance. It is not our intention to force all enterprises into a contract-based group by imposing radical new liabilities if no contract is agreed. Nor do we intend to abandon the fundamental principle of a company's limited liability.

On the contrary, we seek only to re-affirm the equally fundamental principle that companies whose share capital may be held by the public should be managed in their own interest and not someone else's. We shall be seeking to develop as clear a text as possible to embody that principle and nothing more. In my opinion, such a principle is a necessary safeguard for the investor in public companies and not disruptive of the legitimate interests of parent undertakings.
(d) The give-and-take of an open legislative system

I would like to conclude by stressing an aspect of the Community's regulatory system that has been implicit in much of what I have said so far. Our legislative system is democratic in character. It is open to criticism, to influence, to change. It seeks consensus. Indeed, there are those who say that its concern with consensus is so pronounced that its effectiveness is insufficient. It all takes too long.

Be that as it may, from the point of view of the investor, including the foreign investor, the system has the advantage that its concerns can be adequately taken into account. I would refer you to the seventh directive on group accounts. One of the original proposal's provisions of greatest concern to US business was the requirement for so-called horizontal sub-consolidation of European subsidiaries of companies outside the Community. Following lengthy discussion of the problem in which American Chambers of Commerce amongst others played an important part, a consensus has emerged that this requirement should be dropped. The alternative possibility is now being considered of requiring certain additional disclosures in the annual accounts of the individual Community subsidiaries concerning their relations with the group. This seems to be a much more workable approach which is likely to find general agreement. It should also do much to resolve the problem of our treatment of groups controlled by US private companies that are not presently required to consolidate under US law and practice.
While they may continue to object to worldwide consolidation, it is hard to see how they can contest reasonable disclosure by their European affiliates of their role within the group.

V. Conclusion

Ladies and gentlemen, I would like to suggest that if we take this example as our guide, and take the trouble to listen carefully to each other's concerns, there is no reason why the Community's developing regulatory framework, far from being a source of problems, should not make a major contribution to the attractiveness of Europe as an investment area. We will indeed achieve the right balance between reform and adaptation on the one hand, and maintenance of the fundamental principles of an open, competitive economy on the other. Willingness to understand the other point of view, and to find compromises on that basis, is of course essential. We for our part are determined to make the effort.
Annex: Defensive point
Extra-territorial jurisdiction

I am glad to be able to comment briefly at this point on an important issue associated with some of our directives, even if it is something of a digression from today's central topic of investment: extra-territorial exercise of jurisdiction. I expected that you might feel cheated if I said nothing about it.

First, all of our measures apply above all to companies that are established and active within the Community's borders. Furthermore, they apply to actions having their effects (sometimes serious) inside a Community Member-State. By international accepted standards, this so-called "effects-doctrine" is in no sense an illegal extra-territorial exercise of jurisdiction. Therefore, the Community can stand easily international comparison. Conversely, measures have been taken recently and, not for the first time, by the US, which apply to Community firms that are not established nor active on US territory, and as regards matters having no effects there. These measures have serious consequences not only for the firms concerned, but for the economic policies of their countries of origin. We view this interference in our internal affairs with a mixture of irritation and sorrow, and hope that wiser counsels will still prevail. But, in any case, we reject firmly any suggestion that our measures are in any way comparable.
I would like to add a political comment. The argument that large multinational enterprises, long-established and active within the Community and often household names are sort of exempt from its collective jurisdiction could backfire on those who make it. Coupled with the recent attempts by the US government to extend the long arm of US law to Community firms for activities wholly outside the US, and not having effects inside its borders, the argument begins to look like a claim for a "off-shore" status, if you like, for these companies.

Such a concept strikes at the heart of the equal treatment and non-discrimination principles that have been the foundation for the remarkable development of international activities by enterprises since at least the end of the last war. It also plays into the hands of those who are no friends of the multinational enterprises or an open economy. They have always argued that multinational enterprises are a breed apart to be treated with suspicion and regulated separately. In my opinion, our critics would be better advised to concentrate on the merits of the rules that should apply equally to all enterprises doing business in the Community rather than seeking to use strained jurisdictional arguments to exempt one group of enterprises from the regime that will apply to everyone else.