

## Reasoned Opinion of the House of Commons

Submitted to the Presidents of the European Parliament, the Council and the Commission,  
pursuant to Article 6 of Protocol (No 2) on the Application of the Principles of Subsidiarity  
and Proportionality

concerning

### Draft Directive of the European Parliament and of the Council on improving the gender balance among non-executive directors of companies listed on stock exchanges and related measures 16433/12<sup>1</sup>

Treaty framework for appraising compliance with subsidiarity

1. The principle of subsidiarity is born of the wish to ensure that decisions are taken as closely as possible to the citizens of the EU. It is defined in Article 5(3) TEU:

“Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level.”

2. The EU institutions must ensure “constant respect”<sup>2</sup> for the principle of subsidiarity as laid down in Protocol (No. 2) on the Application of the Principles of Subsidiarity and Proportionality.

3. Accordingly, the Commission must consult widely before proposing legislative acts; and such consultations are to take into account regional and local dimensions where necessary.<sup>3</sup>

4. By virtue of Article 5 of Protocol (No 2), “any draft legislative act should contain a detailed statement” making it possible to appraise its compliance with the principles of subsidiarity and proportionality. This statement should contain:

- some assessment of the proposal’s financial impact;
- in the case of a Directive, some assessment of the proposal’s implications for national and, where necessary, regional legislation; and

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<sup>1</sup> COM(12) 614.

<sup>2</sup> Article 1 of Protocol (No. 2).

<sup>3</sup> Article 2 of Protocol (No. 2).

- qualitative and, wherever possible, quantitative substantiation of the reasons “for concluding that a Union objective can be better achieved at **Union level**”.

The detailed statement should also demonstrate an awareness of the need for any burden, whether financial or administrative, falling upon the EU, national governments, regional or local authorities, economic operators and citizens, to be minimised and to be commensurate with the objective to be achieved.

5. By virtue of Articles 5(3) and 12(b) TEU national parliaments ensure compliance with the principle of subsidiarity in accordance with the procedure set out in Protocol (No. 2), namely the reasoned opinion procedure.

Previous Protocol on the application of the principle of subsidiarity and proportionality

6. The previous Protocol on the application of the principle of subsidiarity and proportionality, attached to the Treaty of Amsterdam, provided helpful guidance on how the principle of subsidiarity was to be applied. This guidance remains a relevant indicator of compliance with subsidiarity. The Commission has confirmed it continues to use the Amsterdam Protocol as a guideline for assessing conformity and recommends that others do.<sup>4</sup>

“**For** Community action to be justified, both aspects of the subsidiarity principle shall be met: the objectives of the proposed action cannot be sufficiently achieved by Member States’ action in the framework of their national constitutional system and can therefore be better achieved by action on the part of the Community.

“The following guidelines should be used in examining whether the abovementioned condition is fulfilled:

- the issue under consideration has transnational aspects which cannot be satisfactorily regulated by action by Member States;
- actions by Member States alone or lack of Community action would conflict with the requirements of the Treaty (such as the need to correct distortion of competition or avoid disguised restrictions on trade or strengthen economic and social cohesion) or would otherwise significantly damage Member States’ interests;
- action at Community level would produce clear benefits by reason of its scale or effects compared with action at the level of the Member States.”<sup>5</sup>

“The form of Community action shall be as simple as possible, consistent with satisfactory achievement of the objective of the measure and the need for effective enforcement. The Community shall legislate only to the extent necessary. Other things being equal, directives should be preferred to regulations and framework directives to detailed measures”.

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<sup>4</sup> See, respectively, pages 2 and 3 of the 2010 and 2011 Reports on Subsidiarity and Proportionality (COM(10) 547 and COM(11) 344).

<sup>5</sup> Article 5.

## Proposed legislation

### *Purpose*

7. The purpose of the draft Directive is to improve the gender balance of corporate boards. Although it is drafted in gender-neutral terms, referring throughout to the under-represented sex, the recitals make clear that the objective is to increase the presence of women on boards for the following reasons:

- to achieve effective equality between women and men and narrow the gender employment and pay gap;
- to ensure the efficient use of human capital (60 per cent of university graduates are female) and to enhance the return on public investment in education; and
- to improve corporate governance, with beneficial spill over effects for financial performance and profitability, as well as economic growth.

### *Operation*

8. The draft Directive is based on Article 157(3) of the Treaty on the Functioning of the European Union (TFEU) which creates a specific competence to adopt measures “to ensure the application of the principle of equal opportunities and equal treatment of men and women in matters of employment and occupation, including the principle of equal pay for equal work or work of equal value.” It would require Member States to ensure that publicly listed companies in which women occupy fewer than 40 percent of non-executive director positions or one third of all director positions (executive and non-executive) base the appointment of non-executive directors on “a comparative analysis of the qualifications of each candidate, by applying pre-established, clear, neutrally formulated and unambiguous criteria.” It would also introduce a new preference rule to ensure that a female candidate would be given priority, provided that she is equally qualified as a male candidate in terms of suitability, competence and professional performance *and* that there are no other factors specific to the male candidate which should tilt the balance in his favour.

9. The objective of these new procedural requirements is to achieve 40% representation of female non-executive directors (or 30% of all directors) on the boards of publicly listed companies by 2020 (or 2018 in the case of listed public undertakings). There is an exemption for small and medium-sized enterprises (SMEs) and for companies whose workforce has fewer than 10% female employees. Where national measures have already been introduced with a view to increasing the level of female representation on corporate boards, companies need not apply the new recruitment and selection procedures, but they will be required to do so from 2018/20 if they have not reached the 40% target. The draft Directive also introduces specific monitoring and reporting requirements for listed companies with a view to ensuring that there is tangible progress towards achieving a higher proportion of executive board positions occupied by women.

10. The draft Directive requires Member States to introduce sanctions which may include administrative fines or annulment by a judicial body of the appointment or election of a non-executive director if the procedural requirements for recruitment and selection set out in national implementing measures have been infringed. It is not clear whether sanctions are intended to apply to a listed company which applies the procedural requirements but falls short of the 40% objective by 2018/20.

### *Subsidiarity*

11. The Commission advances three reasons to justify EU action. First, it says that EU action is **necessary because Member States acting individually “will not achieve sufficiently significant progress towards a more balanced gender representation on company boards by 2020 or at any point in the foreseeable future.”**<sup>6</sup> Taking into account current trends in Member States, the Commission estimates that the EU as a whole would not achieve 40 per cent of women on boards by 2040. The Commission highlights growing discrepancies in the approaches taken by Member States, and adds:

“**Whilst** Member States have the legal possibility to act in order to counter the under-representation of women in economic decision making, many of them do not show any willingness or face resistance from the business community to act at their own initiative.”<sup>7</sup>

12. The divergent approaches taken by Member States provide the second justification for EU action. The Commission suggests that different regulatory approaches can have a negative **impact on the internal market and lead to “practical complications.”** It cites, as **examples**, the difficulties which a listed company may encounter if it wishes to establish a subsidiary in another Member State, enter into a merger or acquisition, or bid for a public procurement contract.<sup>8</sup> Lack of transparency in selection procedures and qualification criteria for board positions may deter potential candidates from exercising their free movement rights within the internal market and also affect investor decisions.<sup>9</sup> Moreover, common minimum standards help to ensure **“a competitive level playing field.”**<sup>10</sup> The Commission adds:

“**Member States may indeed hesitate to regulate in this area on their own, as they could perceive a risk of putting their own companies at a disadvantage with companies from other Member States. This perception, reinforced by pressure from the business community, represents a major obstacle preventing Member States from taking adequate action. An EU-level initiative in this area is needed to ensure a comparable level of promotion of gender equality throughout the Union, as required by the EU Treaties.**”<sup>11</sup>

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<sup>6</sup> See p. 25 of the Commission’s Impact Assessment (ADD 1).

<sup>7</sup> See p. 26 of the Commission’s Impact Assessment (ADD 1).

<sup>8</sup> See recital 12, p. 17 of the draft Directive.

<sup>9</sup> See recital 13, p. 17 of the draft Directive and pp. 27-28 of the Commission’s Impact Assessment (ADD 1) .

<sup>10</sup> See recital 14, p. 17 of the draft Directive.

<sup>11</sup> See p. 26 of the Commission’s Impact Assessment (ADD 1).

13. The third justification for EU action places gender equality within the broader social and economic context of the Europe 2020 Strategy. The Commission suggests that a clear commitment to gender equality is essential to remove barriers to the participation of women in the labour market and to meet the Europe 2020 headline target of a 75 per cent employment rate for men and women aged between 20 and 64 by 2020. The Commission also anticipates that enhanced participation of women at the highest levels of economic decision making will have beneficial spill-over effects for the wider economy, boosting the competitiveness of European companies and stimulating economic growth.<sup>12</sup> It says:

**“The under-utilisation of the skills of highly qualified women constitutes a loss of economic growth potential. Fully mobilising all available human resources will be a key element in addressing the EU’s demographic challenges, competing successfully in a globalised economy and ensuring a comparative advantage vis-à-vis third countries.”**<sup>13</sup>

14. The Commission concludes from its analysis that the objective of increasing the proportion of women on the boards of listed companies,

**“can be better achieved through coordinated action at EU level rather than through national initiatives of varying scope, ambition and effectiveness.”**<sup>14</sup>

Aspects of the Regulation which do not comply with the principle of subsidiarity

15. The House of Commons considers that the draft Directive of the European Parliament and of the Council on improving the gender balance among non-executive directors of companies listed on stock exchanges and related measures does not comply either with the procedural obligations imposed on the Commission by Protocol (No 2) or with the substantive principle of subsidiarity in the following respects.

*i) Failure to comply with essential procedural requirements*

16. By virtue of Article 5 of Protocol (No 2) “any draft legislative act should contain a detailed statement making it possible to appraise compliance with the principles of subsidiarity and proportionality”. The requirement for the detailed statement to be within the draft legislative act implies that it should be contained *in the Commission’s explanatory memorandum*, which forms part of the draft legislative act and which, importantly, is translated into all official languages of the EU. The fact that it is translated into all official languages of the EU allows the detailed statement to be appraised for compliance with subsidiarity (and proportionality) in all Member States of the EU, in conformity with Article 5 of Protocol (No 2). This is to be **contrasted with the Commission’s impact assessment, which is not contained within a draft legislative act, and which is not translated into all the official languages of the EU.**

17. The presumption in the Treaty on European Union<sup>15</sup> is that decisions should be taken as closely as possible to the EU citizen. A departure from this presumption should not be taken

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<sup>12</sup> See recital 15, pp. 17-18 of the draft Directive.

<sup>13</sup> See p. 3 of the Commission’s explanatory memorandum.

<sup>14</sup> See p. 28 of the Commission’s Impact Assessment (ADD 1).

for granted but justified with sufficient detail and clarity that EU citizens and their elected representatives can understand the qualitative and quantitative reasons leading to a **conclusion that “a Union objective can be better achieved at union level”**, as required by Article 5 of Protocol (No 2). The onus rests on the EU institution which proposes the legislation to satisfy these requirements.

18. The **Commission’s explanatory memorandum and the recitals to the draft Directive do set out in some detail the justification for EU action**. However, for the reasons given below, we do not consider that the Commission has provided sufficient qualitative and quantitative substantiation of the necessity for action at EU level, given that a number of Member States have already taken measures to increase the presence of women on corporate boards. This omission, the House of Commons submits, is a failure on behalf of the Commission to comply with essential procedural requirements in Article 5 of Protocol (No 2).

*ii) Failure to comply with the principle of subsidiarity*

19. The first limb of the subsidiarity test provides that **the EU may only act “if and insofar as the objectives of the proposed action cannot be sufficiently achieved by the Member States.”**<sup>15</sup>

20. The Commission highlights the divergent approaches taken by Member States – with some introducing binding quotas, some setting non-binding targets, some proposing voluntary, business-led initiatives, and some taking no action at all – and suggests that progress towards more balanced gender representation on corporate boards will be too slow. The House of Commons notes, however, that many national measures have been introduced within the last year or two and considers that it is too soon to write them off as ineffective. We think that a further period of reflection and evaluation is needed to assess what does (or does not) work and how much tangible progress has been made before concluding that Member States are unwilling to act or that the measures they introduce will be ineffective.

21. The Commission cites resistance from the business community as a possible factor explaining why some Member States may be reluctant or unwilling to act, and advocates **action at EU level in order to ensure “a competitive level playing field.”** However, **much of the analysis underpinning the Commission’s proposal rests on the strength of the business case for introducing more diverse boards as a means of improving corporate governance and performance**. There would therefore appear to be more, rather than less, reason for Member States to take action individually to promote greater gender balance on corporate boards as a means of securing competitive advantage.

22. The second limb of the subsidiarity test requires evidence that the objective of achieving gender balance on corporate boards can be better achieved, by reason of its scale or effects, by action at EU level. The Commission suggests that EU action is justified because different **regulatory approaches may give rise to “practical complications” which can have a negative impact on the internal market**. Examples cited include the possibility that a company with too few female directors may be excluded from public procurement contracts or may find it

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<sup>15</sup> Article 5.

<sup>16</sup> See Article 5(3) TEU.

difficult to establish a subsidiary in another Member State. Lack of transparency in the recruitment and selection procedures for corporate board positions may also constitute a restriction on freedom of movement within the internal market and affect the basis on which investor decisions are made. Whilst we accept that these are all theoretically possible, we think that the Commission needs to establish a far stronger evidence base of problems actually encountered within the internal market before asserting that EU action is justified to reconcile divergent national approaches.

23 The Commission also suggests that increasing the participation and visibility of women in senior economic decision making positions may well have a positive spill over effect on **women's participation in** the labour market and contribute to the Europe 2020 Strategy headline target on employment. It is far from clear that the European Council contemplated that legislation of this nature would be necessary or desirable to meet the headline target. Moreover, as indicated above, we think it is too soon to conclude that EU level action of the type proposed by the Commission is necessarily the only, or the best, way of achieving the headline target.

## Conclusion

24. For these reasons the House of Commons considers this proposal does not comply with the principle of subsidiarity.