

Mr. Steven Maijoor
ESMA
103 rue de Grenelle
75007 Paris
France

Brussels, 4 October 2018

Subject: ESMA's draft guidance on prospectus risk factors

Dear Mr. Maijoor,

Accountancy Europe is pleased to provide you below its comments on ESMA's draft guidance for prospectus risk factors.

As you are aware, Accountancy Europe has engaged actively and provided its input throughout the legislative cycle to reform EU's prospectus rules. As such, our comments below are a consistent continuation of the views and positions that we have expressed in the past, and should thus be seen in conjunction with our previous prospectus work.¹²³

OUR VIEWS IN SUMMARY

We would like to express our support for and commend ESMA's draft prospectus risk factor guidance. Indeed, we feel that ESMA's draft guidance adequately incorporates materiality, focuses on risk factors that are specific to the issuer, and seeks to link the issuer's business to the disclosed risks. The publication of boiler-plate risk factor information in prospectuses is a long-standing concern in practice, and we are therefore content to see effective proposals to help improve the status quo. We have minor amendments to propose, in order to further improve an overall commendable guidance.

Beyond our overall endorsement of ESMA's proposed draft guidance, we would also like to highlight two further areas of work on risk factors where we see room for future improvements:

- Further alleviations and proportionality for EU Growth Prospectus (EUGP) issuers
- Clarifications on which risk factors should be included in prospectuses, and which ones in financial statements and management reports

¹ May 2016, Simplified prospectus paper: <https://www.accountancyeurope.eu/publications/prospectus/>

² June 2017, Model simplified prospectus: <https://www.accountancyeurope.eu/publications/model-simplified-sme-prospectus/>

³ September 2017, ESMA's prospectus consultation: <https://www.accountancyeurope.eu/consultation-response/accountancy-europe-responds-esma-consultation-prospectus-reform/>

GENERAL PRINCIPLES FOR SOUND RISK FACTOR DISCLOSURES IN PROSPECTUSES

Prospectuses should, in theory, provide investors with relevant information on an issuer that will enable them to make sound investment decisions. Moreover, investors must be made aware of potential risks.

Insufficient, vague or misleading disclosures hamper investor protection, expose them to undue risks and undermine trust in public markets. However, it is equally harmful if issuers disclose large volumes of legalistic, boiler-plate or overly standardised information that is generic and has the sole purpose of functioning as a liability shield. This will not provide investors with a realistic view of the issuer's business and significant risks.

As far as risk factors are concerned, this means that issuers should only disclose risks that are specific to its functioning, markets, sector and model. The disclosures should be material, and demonstrate how they affect the issuer's business model, key drivers and how they could influence its future results.

With this in mind, we are happy with and endorse ESMA's four guiding principles for prospectus disclosures: specificity, materiality, corroboration and categorisation of risk factors. We believe that this approach places investor protection at the heart of the risk factor disclosures, as are their purpose.

COMMENTS ON SPECIFIC DRAFT GUIDELINES

On top of our endorsement of the four guiding principles, we would like to express our satisfaction with and support in particular for the following draft Guidelines proposed by ESMA, as well as some minor suggestions for further tweaking and improvement:

- **Guideline 1:** overall, this Guideline ensures that the disclosures are not 'boiler-plate' and establish a clear link between the issuer's business and risk of being exposed to each of the events. However, we fear that the wording on the fourth line of paragraph 19 ("it would appear necessary to prevent the continuance of this practice where not relevant") could keep the door open for possible boiler-plate disclosures. We would, therefore, propose to make the wording more explicit, along the lines of "it is necessary to prevent" and remove "where not relevant"
- **Guideline 2:** in this section, ESMA has provided clear examples of issuer-specific risk factor disclosures that we find to be particularly helpful. The examples demonstrate that the risk factors should be quantifiable, whenever possible. Quantified information provides a more concrete illustration of the degree to which an investor is exposed to each risk, and the degree to which each risk can impact the issuer's business and viability
 - We encourage ESMA to use such examples more consistently throughout the guidance document, as these provide market participants with a clear standard and example to adhere to
- **Guideline 3:** in this Guideline, ESMA acknowledges that the Prospectus Regulation provides no definition for 'materiality'. However, it points to the definition in the IFRS Conceptual Framework, which we find to be fit for purpose. As outlined above, we would re-iterate that it is often unclear which risk factors are 'material' for prospectuses, which ones are 'material' for financial statements, and so on. Prospectus users need consistency in order to understand the full picture of the issuer. Therefore, we are glad to see that ESMA encourages issuers and investors to rely on the conceptual framework's definition, but would like to see a more explicit requirement to use it. Thus, the wording 'should' ought to replace 'may'
- **Guideline 4:** as noted above, we fully endorse the approach that the disclosures should be quantifiable when possible. When not possible, ESMA proposes that a qualitative approach may be used instead. Whilst we endorse this proposal, the qualitative descriptions should not be overly lengthy or provide superfluous information. We would encourage ESMA to explicitly state this in its Guideline 4. Moreover, whenever a risk factor is not quantifiable, the issuer should explain why this is the case, in accordance with the 'comply or explain' approach

- **Guidelines 7-10:** we have no specific views or recommendations on the draft guidelines on presentation of risk factors across categories. However, we would point out that if ESMA's guidelines lead to the disclosure of fewer and more specific risk factors, there will be less need for classifications of the risk factors in the future
- **Guideline 11:** we see this Guideline as aiming to cut the sheer volume of text in a prospectus by calling for more focused risk factor disclosures, rather than lengthy and superfluous explanations that add no value. This is in line with the principle that the disclosures should be relevant for investors, and not bury potentially relevant information under irrelevant statements

As for the other Guidelines not mentioned above, we have no additional or more specific comments at this stage.

AREAS FOR FUTURE WORK

The draft guidance proposed by ESMA will be helpful for issuers and National Competent Authorities alike, and will hopefully contribute to more consistent and common approaches to risk factor disclosures in the Single Market.

On top of this helpful guidance, we would see room for future work in the following two areas:

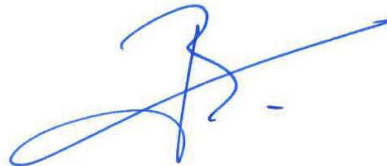
- **Further risk factor alleviations for EUGP issuers specifically:** ESMA's draft guidance is intended for all types of prospectuses – including both the full prospectus and the EU Growth Prospectus (EUGP). Whilst the draft guidance is a welcome first step, we would see the need for more specific and proportionate guidance for EUGP issuers in the future. Firstly, because smaller issuers are fundamentally different from larger ones, both in terms of business models and scale. And second, because full prospectuses are used for regulated markets, whilst EUGP can only be used for SME Growth Markets (SME GMs). As a general rule, the disclosure requirements and expectations for SME GM issuers should be lighter than issuers on regulated markets. In particular, we would like to make the following observations:
 - For SMEs filing a growth prospectus, only a limited number of key risks matter the most. For example, most often practitioners have seen a very strong reliance on the entrepreneur that owns or champions the company – as opposed to larger companies that have more established teams. Likewise, the ability of the company to change its organization to manage the expected growth is a key element that more critically affects risks. Smaller growth companies also often do not have the governance processes one would expect from larger entities filing prospectuses
 - The risk areas outlined above tend to apply to most smaller growth prospectus issuers. Thus, we could envisage a “buyer beware” statement for EUGP issuers combined with a few specific risks. The “buyer beware” statement would cover the most pertinent and imminent risks, hence less other risks would be needed
- **Align and clarify which risk factors should be in prospectuses, which ones in financial statements and which in management reports:** there are currently different requirements for what risk factors should entail depending on where they are disclosed. The risk factors in prospectuses are not necessarily aligned with those in the financial statements (where risk factors are often defined by the relevant IFRS or national GAAP), or even management reports. This means that prospective investors risk receiving different information on an issuer's risk factors depending on their source – whether prospectus, financial statements or management reports. In the future, it may be worthwhile to streamline risk factors to ensure that they are comparable for the same issuer regardless of whether these stem from its prospectus, financial statements or management reports. Or at the very least, we would invite clarifications as to which items should be disclosed where and under what understanding of ‘materiality’

The European accountancy profession is committed to continue enhancing the Single Market and the Capital Markets Union, and contribute to making the relevant proposals work in practice. For further information, please contact Johan Barros, Senior Policy Advisor (johan@accountancyeurope.eu, +32 (0) 2 893 33 88).

Sincerely,
(make sure you have enough space for the signature)



Edelfried Schneider
President



Olivier Boutellis-Taft
Chief Executive

ABOUT ACCOUNTANCY EUROPE

Accountancy Europe unites 51 professional organisations from 37 countries that represent **1 million** professional accountants auditors and advisors. They make numbers work for people. Accountancy Europe translates their daily experience to inform the public policy debate in Europe and beyond.

Accountancy Europe is in the EU Transparency Register (No 4713568401-1