Dr. Wolfgang Gerhardt
Senior Vice President
Sal. Oppenheim jr. & Cie. KGaA, Frankfurt am Main

Member of the Consultative Working Group

Position on

CESR's Advice on Level 2 Implementing Measures for the Prospectus Directive Consultation Paper and Annexes July 2003 – CESR/03-210b

for

The Committee of European Securities Regulators

Frankfurt am Main, 30 October 2003

Introduction

As a member of the Consultative Working Group nominated by CESR to assist in the process of implementing the Level 2 Measures for the Prospectus Directive I am pleased to provide my position on CESR's Advice on Level 2 Implementing Measures for the Prospectus Directive as of July 2003 (Document 03-210b including Annexes).

Member States, Non-EU States and their regional or local authorities: definitions (paragraphs 23 to 29)

It is common practice in the international bond markets that sovereign issuers benefit from less onerous disclosure requirements than corporate issuers. Furthermore, in many countries home sovereign issuers are exempt from any obligation to prepare a prospectus, as in Germany. Such practice is acceptable due to the in general lower insolvency risk and the better access to information regarding these issuers. However, the latter argument becomes arguable in a community of many countries. It could not be expected that the investors in country X have sufficient access to information on a regional authority in country Y. Therefore, the concept that all issuers have to prepare a prospectus to have access to the European Pass Port appears to be useful.

The group of issuers who should benefit from the respective Annex, however, should be revised in line with the following arguments:

- A difference should be made between issuers from the EU and issuers outside the EU. According to present experience, the insolvency risk is different between both groups. If such differentiation is discriminating the rules for EU issuers could be expanded to OECD issuers.

- A difference shall be made even among the EU issuers – not with regard to insolvency risk, but with regard to the aspect of information. Member states shall be favoured compared to second or third level authorities, which mean the regional and local authorities. It could not be expected that investors all over Europe are familiar for example with a city in country Y.

- Furthermore, international or national public bodies – the EU Commission or the World Bank are prominent names in this respect – should also be subject to the annex and not required to publish a prospectus according to the retail corporate debt schedule. Any definition, however, should be restrictive, so that especially non governmental organisations who are faced with an insolveny risk could not benefit from the annex. Such expansion is also necessary as the present wording of the retail corporate debt schedule is not applicable to non-profit organizations in many aspects.

Member States, Non-EU States and their regional or local authorities: minimum information (paragraphs 23 to 29)

The list of topics raised in paragraph 31 and Annex D, sections 3 and 4 should be differentiated to reflect the various types of potential issuers. The headline "public finance and trade" is misleading, as it only reflects the characteristics of states. Only such entities could make a disclosure on "foreign exchange reserves" or "foreign trade and balance of payment figures". The wording "financial position and resources" appears unclear to me.

A description of public issuers should cover the following aspects by merging sections 3 and 4 of Annex D:

- Legal system of the respective country - not regarding the issuer only (for example ranking of the respective issuer in the respective national legal system, including its financial interweavement with other entities of said country, protection against insolvency due to explicit guarantees and formal or legal structures by superior issuers, respectively).

- Economic environment (for example number of people, demographic structure, gross domestic product, economic growth, unemployment rate, major industries and sectors – for member states in addition foreign trade and balance of payment figures; highlight on material aspects concerning the economic development)

- Political system (for example structure of the legal system, government and parliament, list of major interests in companies and organisations, including public corporates)

- Financial conditions of the issuer (for example tax and budgetary system, income and expenditure figures, budget figures compared to effective income and expenditure, public debt in absolute figures as well as in relative figures, highlight on material aspects having an impact on the financial conditions)

- Trend infomation

Especially with regard to the economic environment and the financial condition of the issuer it appears important to me that the development over the last years shall be disclosed in the prospectus, as already outlined in section 3.4. With regard periods of time, the disclosure requirements should be the same for public issuers as for bank issuers. However, CESR should take into consideration that many statistical figures of sovereigns are only available with a significant delay after the close of the respective calendar year. Therefore, at least a grace period shall be included as for corporate issuers with regard to the date of the financial information.

Based on that statement I am not convinced that specific rules for investments and development plans should be required. If these investments and development plans are material, then they have to be mentioned based on Article 5 section (2) of the Prospectus Directive. If they are not material, then a disclosure would give a

misleading bias. At present, a prospectus of a member state should focus on detailed information on the social security systems but not on investments.

Trend information and information on economic indicators shall only be required if it could made sure that these disclosures are of the same legal and economic quality than the respective sections in prospectuses of corporate issuers.

Although the list looks very comprehensive, CESR should make clear that the information shall be provided in a very concise and brief manner reflecting the specific nature of these issuers.

Potential conflicts of interest have to be disclosed. In this respect, it has to be discussed, whether a prospectus of a member state checked by the competent authority of the same country should include a disclaimer stating that the competent authority is subject to instructions by the government of said country and is therefore not independent.

Financial information requirements in a prospectus (paragraphs 43 to 70)

As stipulated in the Consultation Paper, CESR considers IAS as the European benchmark for financial reporting for companies preparing consolidated accounts that are admitted to trading on a regulated market. I agree to that position. My general impression concerning paragraphs 43 to 70 and Annex E, however, is, that CESR pursues a very strict policy with regard to the implementation of IAS. The disclosure requirements regarding financial information should take the following aspects into consideration:

- Over the next years many issuers will be faced with the transition from national GAAP to IAS as well as with the transition from the national prospectus law to the new Prospectus Directive. Such process of transition should be smoothened as far as possible.

- The Level 2 Implementing Measures should not extend the scope of requirements stipulated by other EU regulations. CESR should not take up a position which is beyond these rules. In contrast to the description of the issuer and the description of the security the major objective of including financial information should be a “copy paste approach”. The disclosure requirements for prospectuses shall be based on such information which is available according to the respective accounting standard.

- As I have already stipulated in previous positions especially small and medium sized enterprises should be treated like other issuers, but not faced with onerous burdens. Any change in accounting, especially any comprehensive restatement of previous accounts, raises many complex questions of valuation and raises high cost as well as occupies human resources.

- Due to the present status of discussion and decision regarding the Level 2 Implementation Measures potential issuers of securities which do not already use IAS at present could start switching over to IAS for year end 2004, if they will

proactively prepare for the change in advance. In most cases the forerun for a proactive change for year end 2003 is too short. Any restrictive requirement will burden issuers with a restatement of financial statements already audited and closed.

Therefore, I recommend that CESR should follow a very flexible approach. It should be acceptable for a certain period of time that IAS and national GAAP statements are included into the same prospectus with sufficient explanatory statements. Based on that, as a consequence, I support the procedure according to paragraph 50.

Some more detailed aspects should also be taken into consideration:

- I reject the requirement, that audited financial information must be presented and prepared in a form consistent with that which will be adopted in the issuer's next annual financial statements. Such rule would mean that equity issuers could be forced to prepare their financials under a newly to be adopted standard not for two, but for three years. If an issuer intends to switch over to IAS by end of 2005, then it could only tap the market in late 2005 with IAS financials 2003 to 2004. Therefore, this principle will impair capital markets activities for those issuers.

- There should be made a difference between issuers which tap the market for the first time and such issuers which have already issues outstanding in the market. As the latter are already known to investors such issuers shall be exempt from a very strict regime. Otherwise companies, like the big number of small and medium equity issuers or banks whose shares are not listed, could be subject to major disruptions in increasing their share capital and debt refinancing, respectively.

- CESR requires that financial information according to local GAAP must contain a statement regarding changes in the equity position and a cash flow statement (for equity issuers) and a cash flow statement (for banks issuing debt), respectively. Such rule is not required by German GAAP. As already mentioned, CESR should not impose new accounting requirements.

- The question of comparability among different issuers of the same industry is only relevant for issuers of equity. With regard to issuers of debt, investors focus on the creditworthiness of the issuers, but not on their relative position within a certain industry.

- With regard to non EU issuers the disclosure requirements for financial information should reflect a higher degree of flexibility. Otherwise the European capital markets may become unattractive for non EU issuers, especially with regard to debt issues. Simply for cost and time reasons I have doubts whether an issuer will prepare specific financial information required by EU authorities. In addition the rule, that audited financial information must be presented and prepared in a form consistent with that which will be adopted in the issuer's next annual financial stetaments, could hinder foreign issuer to tap European markets whenever the accounting standards in their home market will be revised.

- It should be made clear what is meant with „fully audited". In my opinion the wording „audited" appears to be sufficient (Annex E).

Dissemination of advertising (paragraphs 71 to 83)

The Prospectus Directive clearly states that any advertising for a security must be in line with the content of the respective prospectus. Such principle is an essential prerequsite to ensure that the prospectus is the core element of information on a certain security. As a consequence the competent authority shall have the power to exercise control over the compliance of any advertising activity to accomplish the primacy of the prospectus compared to the variety of other communication channels. In principle, the aim shall be a harmonized approach. Otherwise issuers from various countries could be discriminated in accessing different European markets with deviating rules.

The German concept has been successfully proofed for more than a decade and has substantially contributed to the enormous acceptance of derivative securities in Germany. The BaFin created a framework based on the German Selling Prospectus Law which is applicable to advertising. In the case issuers do not comply with this framework the BaFin can impose sanctions, in the extreme case an offering could be forbidden. Practice in German advertising, however, has shown, that advertising only promotes the distribution of a security if the product meets the market expectation by investors. Many initial public offerings as well as many types of derivative securities, especially in the field of complex products, failed despite enormous advertising efforts.

Therefore, I recommend to use such German concept as a guideline for the Level 2 Implementing Measures to be established according to Article 15 section (7) of the Prospectus Directive. My advice is based on the following considerations:

The Prospectus Directive stipulates that the competent authority of the home member state shall be entitled to control the advertising activities. While such rule makes sense from the perspective of prospectus responsibility it does not make sense from the perspective of advertising.

- On the one hand, such control raises language issues. The competent authority of country X will normally not be able to directly check whether an advertisement in language Y will comply with the content of the prospectus.

- On the other hand, the question refers to the enormous cultural (and even legal) differences with regard to advertising practice, for example images, kinds of presentation or designs used, throughout Europe.

The latter aspect can only be solved in a national context. Therefore, any Level 2 Implementing Measures should be restricted to supervising measures whether texts are inaccurate, misleading or inconsistent compared to the prospectus. Otherwise, any tight and detailed contracts will end up in a huge bureaucracy.

Furthermore, the wording „power to control“ shall be interpreted as „entitlement to control“. The competent authorities shall only supervise any abuse of the guidelines.

- Only advertising gives investors the opportunity to get aware on the broad spectrum of financial products, including securities. Normally, an investor as client of a bank will be made acquainted only with a restricted number of portfolio offerings. Therefore, I am supportive to CESR considering advertising campaigns as an important tool for the retail market.

- Based on the extremely growing need for individuals to take care of their own private retirement arrangements, advertising plays - and has to play - an educational role. However, the wording of paragraph 80 that „marketing literature might be potentially riskier in terms of breaching the directive“ is certainly true but misleading. The educational aspect in informing on securities is of major importance. Investors must be provided with educational material on the characteristics of certain products thereby using all possible forms of communication. The competent authorities should explicitly support such education, but not implicitly express the reverse opinion of short information being good information. As I have already expressed in previous positions the issuers and the competent authorities shall cooperate in marketing the access to prospectuses as the main source of information. They should do advertising for prospectuses.

- The creativity of issuers shall not be restricted by any control or even inflexible guidelines implemented by the respective authorities. The competition of ideas is an essential element for the success of an issue and the acceptance by investors. Otherwise it could easily happen that even different opinions on the risk nature of certain products will be affected. It could not be the task of the competent authority whether a certain advertisement is „good“ or „bad“. Such decision shall be made by the market.

- Any prior approval process for advertising should not be established. Such prior approval would lead to time delays. The concept of the base prospectus would be undermined, if an issuer is allowed to continuously tap the market with new products, but not to market them continuously. Especially in the field of debt and derivative securities windows available for successfully placing new products have been dramatically shortened. Therefore, most newspapers and magazines have developed a „just in time“ delivery procedure for submitting advertising material. The closing time is almost the same as for texts written by the journalists. Not to mention, any use of the internet has to be based on timeliness.

- Furthermore, any approval process and even an information process on any advertising already done will simply overstrain the capacities of the competent authorities by the sheer mass. Especially issuers of derivative securities publish a lot of advertisements in newspapers and magazines each week, produce various leaflets and brochures on new products, prepare weekly or monthly newsletters and magazines, organise seminars for people interested in derivatives, run daily formats on television and constantly update their own websites as well as specifically

reserved advertising space of internet providers with banners and written information.

- Any detailed control to be implemented would also mean that CESR has to define in detail what is considered as advertising and what is considered as education or general promotion not to be considered as a public offering. Therefore, I support the approach chosen in paragraph 80 (except for the aspect on marketing literature). This approach is, however, only applicable to an attitude which focuses on setting a framework for advertising.

The concept of a „black out period" stems from the equity business. Black out periods will definitely hamper at least the market for debt and derivative securities as they are in contrast to the concept of continuous issuance under a base prospectus. As a general rule, advertising shall only be allowed for a certain securitiy as soon as the prospectus has been published. Prior to the date of publication advertising should be restricted to general information, especially not enabling any subscription or purchase.