

Submitted by email

15 July 2011

**ESMA's consultation paper regarding the technical advice on possible delegated acts concerning the Prospectus Directive as amended by the Directive 2010/73/EU (the "Consultation Paper")**

Dear Sirs,

Goldman Sachs International welcomes the opportunity to respond to the Consultation Paper.

Goldman Sachs International is an unlimited liability company under the laws of England and Wales and an indirect, wholly-owned subsidiary of The Goldman Sachs Group, Inc., a Delaware (U.S.) corporation, which together with its affiliates, including Goldman Sachs International (collectively, "Goldman Sachs"), is a leading global investment banking, securities and investment management firm that provides a wide range of financial services to a substantial and diversified client base that includes corporations, financial institutions, governments and high-net-worth individuals.

Goldman Sachs actively issues and distributes structured products in a number of European member states using issuance platforms with prospectuses approved by a number of competent authorities. The existing base prospectus regime is very important for this type of issuance activity because it allows issuers to quickly react to dynamic market conditions and ever-evolving investor demand. Overall, the base prospectus regime is advantageous for both the issuer who benefits from flexible processes and the investors who constantly seek new investment opportunities.

Goldman Sachs welcomes ESMA's attempt to strengthen and enhance the current EU Prospectus Directive regime. However, some aspects of the proposed technical advice set out in the Consultation Paper may not bolster the current prospectus regime's focus on the promotion of both investor protection and flexibility for innovation in the development of financial products, in particular, in relation to structured products and other hybrid instruments in the debt capital markets. Therefore, in spite of ESMA's finding that a more restrictive approach in relation to the disclosure content of the final terms is required, the proposed measures are likely to result in a considerable loss of the very flexibility which the existing base prospectus regime was intended to provide, whilst at the same time achieving few, if any actual benefits for investors.

Goldman Sachs would specifically raise the following points in relation to the Consultation Paper:

### **The proposed measures would not materially enhance protection for investors**

Goldman Sachs is of the view that investor protection is the key objective of the prospectus regulatory regime and, in particular, that the provision of clear and comprehensive disclosure in a prospectus is vital. Nevertheless, as currently drafted, the proposals may weaken the current level of transparency, instead potentially hampering innovation and increasing the administrative burden on issuers. In particular, we feel that:

- **the prohibition on integrated forms of final terms and of terms and conditions is not in accordance with current market practice:** Goldman Sachs is concerned about the proposal to prohibit the well-established practice of setting out the relevant terms and conditions and other relevant information relating to the securities in the final terms. This proposal is based on ESMA's view that final terms should be a brief document. We strongly disagree with this view. It is extremely important to provide investors, in particular retail investors, with a document which allows them fully to understand the benefits and risks of a security, rather than leaving them to form a view of the product on the basis of a short but potentially meaningless final terms which only becomes meaningful if read in conjunction with a very comprehensive base prospectus.
- **the proposed restriction on issuer-enhanced disclosure may reduce investor protection:** Goldman Sachs and other innovative issuers have deliberately chosen to go beyond the regulatory disclosure requirements by including additional information in retail security documentation, for example scenario analyses and plain-English descriptions of key risks and features. The proposed restrictive approach to the content of final terms would prevent issuers from providing such enhanced disclosure to their investors, thereby in our view potentially diminishing the quality of disclosure and the existing level of investor protection.
- **the proposals may reduce innovation in the European financial markets:** the proposals would significantly increase administrative burdens for issuance activities, mainly by extending the requirement to file prospectus supplements and making the handling of summaries (which will have to be annexed to final terms) more complex. This would lead to increased costs and would adversely affect the issuers' ability to innovate and to tailor financial products to their investors' requirements in a timely and efficient manner. As a result, it is possible that a significant part of the existing retail structured product market will be driven to exchanges and platforms outside of the European Union or conducted in transactions exempt from the Prospectus Directive.

### **The proposed categorisation of information would undermine flexibility**

The Commission's mandate specifically requested ESMA to preserve the flexibility of the base prospectus regime while developing the best possible format for disclosure in the final terms. The base prospectus and final terms regime (based on the previously widely accepted use of pricing supplements) has become the primary method for offering and listing debt securities in the EU marketplace and its efficiency and flexibility are of high importance for efficient debt capital market activities. These advantages of the Prospectus Directive regime may be put at risk by the current proposals. In particular,

- **the proposed categorisation system of information in the final terms restricts flexibility:** the proposed classification of information into Categories A, B and C restricts the issuers' flexibility for no obvious benefit. For example, the Consultation Paper classifies risk factors generally in developing disclosure as CAT. A information. However, certain types of underlying assets or other issue-specific features may involve highly specific risks which would be impracticable to set out in the base prospectus. For example, in relation to a base prospectus with commodities as underlying assets it should be possible to include specific risk factors if the secondary market of this underlying asset is less liquid than for other types of commodities (for example in the case of certain agricultural futures contracts, as opposed to oil futures contracts). Therefore, in our view, it should be possible to at least specify and tailor risk factors in final terms if they are disclosed upfront in the base prospectus on a generic basis and if it is indicated in the base prospectus that specific risks might be mentioned in final terms. The proposed blanket prohibition of the inclusion of risk factors in final terms would severely undermine the ability of issuers to react to highly dynamic markets conditions.
- **the distinctions between categories are inconsistent and give rise to unnecessary complexity:** the basis for the distinctions between the proposed information categories is unclear. For example, it is not clear to us why information regarding the representative of debt security holders (referred to at item 4.10 of Annex V) was designated as a Cat. A, rather than Cat. C item, especially since information regarding the calculation agent is classified as a Cat. C item. The effect of this apparently inconsistent designation would be a considerable increase in prospectus supplements being published, resulting in reduced flexibility for issuers of securities.
- **the proposed categorisation system is formalistic:** we are concerned that, if adopted, ESMA's proposed measures will replace the substantive assessment of individual issuances (the intention behind the Prospectus Directive) with a mechanical "box-ticking" check of transaction documents against the proposed exhaustive list of information. This will mean significantly less flexibility for market participants as there will be no scope for substantive arguments or discussion with the competent authorities as to the appropriate disclosure for specific securities, thereby putting both the issuers and the investors at a disadvantage.

### **The proposed summary would not enhance comprehensibility of prospectuses**

Goldman Sachs believes that it is important for financial products to be marketed in a way which makes them easily comprehensible and transparent to investors and it therefore welcomes the Commission's PRIPs initiatives aimed at achieving this. However, Goldman Sachs believes that ESMA's proposed changes to the summary of the prospectus may pre-empt and/or contradict the eventual outcome of the Commission's work in this area, specifically relating to the Key Investor Information Documents ("KIID").

- **the proposal would result in longer and potentially duplicative documentation:** ESMA's proposed modular approach would result in overly lengthy summaries and would prevent issuers from providing a succinct overview of the securities to the investors, instead forcing issuers to produce long and formalistic documents which would add little to comprehensibility and analysability. In particular, if a summary is included in the final terms, it would lead to duplication of information and the added value of the summary in

comparison to (i) the summary contained in the base prospectus, (ii) other information in the final terms (it should be possible to mention specific risks, see above), and (iii) the future EU Key Investor Information Document can be doubted.

- **the proposal for a prospectus summary is premature:** in our view, the process of developing the templates for prospectus summaries should be aligned as far as possible with the process of developing the templates for KIIDs pursuant to Directive 2009/65/EC (the UCITS IV Directive), which was also the view the Commission expressed in its Mandate to ESMA.

In summary, we believe that any changes to the existing regime must promote both transparency and innovation. With reference to ESMA's proposals, Goldman Sachs would specifically reiterate its view that the proposed prohibition on replication in the final terms of the information contained in the base prospectus would be detrimental to transparency. Furthermore, we feel that the approach to the content of summaries should be principles-driven, rather than exhaustive. Any new requirements in relation to summaries must also take full account of the Commission's PRIIPS initiative. We also believe that issuers should be afforded sufficient flexibility as to the contents of summaries and final terms in order to innovate and meet their investors' requirements.

Finally, we are particularly concerned about the impact of the proposals on cost and timing of issuances. The proposals mean that the information currently contained in the final terms, for instance information on proprietary indices, would in many cases require a supplement or an entirely new standalone or base prospectus. We are, therefore, of the view that as currently drafted, the proposals would have an adverse effect on the retail structured products market without enhancing investor protection.

Yours faithfully,

Goldman Sachs International