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EBF COMMENTS IN RESPONSE TO CESR'S CALL FOR EVIDENCE ON THE SUPERVISORY FUNCTIONING OF THE PROSPECTUS DIRECTIVE AND REGULATION

CESR Ref: 06-515

General remarks

1. The European Banking Federation (EBF)[1] welcomes the opportunity to share its views on the functioning of the Prospectus Directive (PD) and Regulation (PR) with CESR. We also welcome CESR's efforts to enhance the consistent application of the Directive and to promote further convergence amongst its members.

2. On a general note, it can be observed that the experiences made so far with these two pieces of legislation vary greatly across Member States, and that the implementation has worked comparatively well in some jurisdictions. However, difficulties have been **encountered in other jurisdictions, especially as regards the passport**. Most notably, there have been a number of cases where host authorities have refused passported prospectuses or have requested additional information. These practices undermine the underlying objectives of the Directive and we call on CESR to address them as an issue of priority.

3. We also refer to cases that might only be resolved through legislative measures, especially regarding the language regime and requirements that go beyond the scope of the Directive. These should be addressed once that a comprehensive review of the Directive is undertaken.

Specific remarks

4. **Recognition of the passport by host authorities (Article 17.1)**: there have been cases where host authorities have refused to recognise notifications on passported prospectuses received from other authorities. This was on the basis of alleged non-compliance with specific provisions of the PD, most often the language rules and the rules on incorporation by reference. We call on CESR to ensure that notifications received from other authorities be under all circumstances recognised and given effect. Where a host authority wishes to question the approval given to a prospectus it should communicate its concerns to the competent authority of the home Member State, as foreseen by Article 23 of the PD.

5. In this respect we emphasise in particular that **no exception to this principle** should apply to issues relating to the language regime. The provisions of Article 19 provide

[1] The European Banking Federation (FBE) is the voice of the European banking sector representing the vast majority of investment business carried out in Europe. It represents the interests of over 5,000 European banks, large and small, from 29 national banking associations, with assets of more than €20,000 billion and over 2.3 million employees.

a.i.s.b.l.
10 rue Montoyer B- 1000 Brussels
+32 (0)2 508 37 11 phone
+32 (0)2 511 23 28 fax
http://www.ebf-fbe.eu

clearly that it is up to the home Member State authority to verify that prospectuses are correctly translated. The scrutiny rights of host authorities pertain merely to the notification, with a view to ensuring that it complies with Article 18.1 of the PD.

6. **Additional information requirements by host authorities**: Several host authorities have requested additional information on already passported prospectuses. This has in particular happened in the case of structured instruments, and some supervisors have justified their requests with the right to establish conduct of business rules. These additional requests undermine one of the core objectives of the Directive and we call on CESR to clarify these cases as well as its understanding of the interaction of the PD with other applicable legislation.

7. **Rules on advertisement (Art. 15):** Some authorities make reference to the rules on advertisements to hinder the distribution of certain securities on their national markets. They require that securities which do not comply with specific characteristics defined by them be explicitly labelled in all adverts. This is in contradiction with Art. 15.6 of the PD, which provides that the responsibility for advertisements lies with the authority of the home Member State.

8. **Acceptance of prospectuses by the home Member State (Article 19)**: Regulatory practice so far has shown a wide-spread reluctance of authorities to accept language versions of a prospectus which are neither in their generally accepted language(s) nor in a language customary in the sphere of international finance (English). This problem arises where an issuer wants to provide investors in one or several host Member States with a version of the prospectus in their own language. Currently, authorities frequently merely submit these translated prospectuses, along with the notification, to the host authorities. This is in our view inconsistent with Art. 18.2, second subparagraph, which sets out that the home authority must also approve foreign language versions of the prospectus and can only demand a translation into its accepted language or into English for the purposes of its scrutiny. No distinction to this principle is made according to whether approval is sought for one or several foreign language versions, or if approval of the foreign language version is sought in addition to that of a version in the home Member State's accepted language or in English. We would request CESR to adopt a corresponding guideline to ensure this is respected by all its member authorities.

9. **Obligations of issuers in the case of "cascade" distribution of securities:** It is unclear what additional obligation the distribution of securities through a retail chain can trigger for the issuer. Questions arise especially as regards the announcement of offers and the scope of information to be covered by the prospectus. We call on CEBS to agree on common approach to this case.

10. **Confirmation of notification (Art. 17.1 and 18.1)**: At least one authority has requested issuers not to start making offers in its country until it has confirmed the reception of the respective notification. This confirmation is not foreseen by Articles 17.1 and 18.1. In our view, it is sufficient that the transmission of the notification be confirmed by the home country authority, as many authorities

already do. We would propose that CESR adopt a corresponding guideline to this effect.

11. **Publication of supplements (Art. 16.1):** The wording of Art. 16.1 leaves uncertainty about whether the requirement to publish supplements ends with the start of trading on a regulated market, even if the public offer still continues. This question is of high relevance especially for derivative securities, which are often offered on a continuous basis. In our opinion, the obligation under Art. 16.1 should be understood to end with the start of exchange trading, as it triggers a wide range of information requirements for the secondary market, meaning that there is no need for further supplements under the PD. We would therefore suggest that CESR agree on a corresponding common interpretation, which has already been adopted in some Member States.

12. **Use of registration documents (Art. 5.3):** In practice, there has been uncertainty about the use of registration documents on a trans-European level. Some authorities have argued that a registration document approved in one Member State (e. g. the country of the issuer's incorporation) cannot, after filing a securities note or by way of incorporation into a single-part prospectus, be used for prospectuses filed in another Member State. This is in our view not in line with the underlying objective of the creation of a registration document to provide a central description of the issuer as a basis for all its prospectuses, and it also contradicts with the spirit of Art. 17. Where registration documents have been approved in the issuer's home Member State, they should be fully recognised in all other Member States, either by way of completing the notification process as set out in Art. 18, or by allowing incorporation by reference to them from prospectuses filed in different Member States.

13. In that respect there have also been different interpretations of whether registration documents can as such be the object of supplements filed according to Art. 16 of the PD. This question has huge practical implications for issuers with a large number of prospectuses referring to one registration document, which would otherwise all have to be supplemented separately. It is our understanding that the reference to prospectuses in Article 16 implicitly also covers registration documents. Otherwise, the registration document would quickly be outdated and lose its function as the central source of information on the issuer.

14. **Extension of the time limit in the case of additional information (Art. 13.4):** Some authorities are making extensive use of the extension of the time limit in case additional information or documents are requested. Consequently, in these Member States prospectus approvals now take substantially longer than under the previous legal regime and the time frame needed for approval becomes difficult to predict. This implies difficulties particularly for securities which need to reflect current market conditions, such as derivatives. Whilst we appreciate that the time needed for approval of prospectuses is influenced by the authorities' resource capacities, we believe that in many cases procedures could be speeded up. We would therefore suggest that authorities commit to making use of Art. 13.4 on an exceptional basis, and only in the case of substantial omissions or mistakes. We also note that

otherwise, issuers are given an incentive for "forum shopping", i.e. to have their prospectus approved by the competent home authority that manages the process most efficiently.

15. **Denominations below € 1.000 under a base prospectus (Art. 2.1):** According to Article 2.1 lit m (ii) of the PD, issuers of non-equity securities can under certain conditions choose with which competent authority they wish to apply for admission of the prospectus. This provision has given rise to difficulties where a competent authority approves a base prospectus under which different issues are made. For the case that some issues under the base prospectus are denominated at less than 1.000 €, there is no harmonised interpretation on whether these are covered by the simple admission of the base prospectus. If they were not, issuers would be required to submit the same prospectus to a second competent authority. This interpretation would undermine the functioning of the EU passport in general as well as the particular intention of the base prospectus concept to facilitate issues for frequent issuers. It could furthermore give rise to practical problems, for example where the same prospectus is accepted by one authority but not by another. Indeed, in our view the **base prospectus is in this respect a special case** which has to be considered separately. As the base prospectus does not include the denomination data, in our view the regulatory approval cannot apply to the denomination in general. Accordingly, the 1.000 € threshold should be interpreted as not applicable to the base prospectus.

16. **Publication requirements (Art. 14.2.a):** Whilst the PD grants home authorities the right to require that publications be announced in the newspapers, only two authorities have chosen to make use of this discretion. We acknowledge that the requirement is in line with the wording of the Directive but underline that its practical value for investors is limited and does not in our view justify the costs it implies.

17. **Filing and publication of final terms (Art. 14.3):** Some authorities request that the final terms be filed with them in their capacities as the host supervisor, whereas most other authorities do not make this request. In addition, one authority also demands the separate publication of notices as regards all final terms. This is in our understanding not compatible with Article 14.3 of the PD, which grants the choice of making this requirement only to the home Member State. We call on CESR and the Commission to oppose these requests and enforce a common and strict interpretation of the rights and responsibilities given in this respect to home and host authorities, respectively.

18. **Exemptions for offers addressed solely to qualified investors:** pursuant to Article 3.2.a of the PD, offers of securities addressed solely to qualified investors are exempted from the obligation to publish a prospectus. According to the national rules of some Member States, an approved and published prospectus for these offers is still required. At least one Member State requests that this prospectus be made available to the public six working days before admission to trading. This timing stands in contradiction with the flexibility provided by the PD for offers to qualified investors. In our view, the requirement is also unnecessary as these offers are

typically marketed on the basis of a preliminary prospectus, which already includes a price range. We therefore request CESR to clarify that it is in these cases sufficient for the final and approved prospectus, including the final price and the overall volume of the offer, to be published upon the admission to trading.

19. **Calculation of the 10 per cent exemption**: Article 4.2.a exempts shares representing, over a period of 12 months, less than 10 per cent of the number of shares of the same class already admitted to trading from the obligation to publish a prospectus. It is not clear from the PD whether the offering of shares resulting from the exercise of stock options should be taken into consideration in the calculation of the 10 per cent limit, and different interpretations can have important implications on the costs of raising additional capital. Some authorities have already clarified that any securities that are subject to the application of other exemptions, such as employee shares, should be discounted in the calculation of this limit. We call on CESR and its member authorities to endorse this common interpretation.

20. **Scope of application of the 10 per cent exemption**: There is furthermore uncertainty on the scope of application of the 10 per cent exemption. Some supervisors have interpreted it to apply in the strict sense only to shares, but not to common units as they are for example issued in the case of limited partnerships. This discrimination of some legal structures is in our opinion not justified, as the instruments are equivalent from an investor point of view. Furthermore, when considering the PD as a whole it seems clear that the reference to shares in Article 4.2.a was not meant to exclude common units in partnerships. Indeed, the Directive does not define the term "share", but when defining the term "securities" refers to the definition of "transferable securities" in the ISD/MiFID (Art. 4.1.18). In line with this interpretation, we recommend that CESR clarifies that the term "share" includes other "securities equivalent to shares in companies, partnerships or other entities, and depositary receipts in respect of shares".

21. **Pro forma financial information**: In equity offerings to finance an acquisition interpretation questions have been raised in relation to the pro forma financial information required to be published in the prospectus, particularly in cases where the financial information available from the target and the acquirer do not cover the same period. Specifically two issues need to be clarified. First, some regulators may take the view that Annex II of the PR on pro forma financial information is not mandatory, and that it is up to the issuer to choose whether to include pro forma information. We would support this interpretation, which would allow the issuer to decide which type of information is most appropriate in the specific case. Second, where Annex II applies it is not clear which financial period it should cover. A possible interpretation would be that it should relate to the recent financial period of the issuer (Annex II.5.b of the PR). However, our understanding is that Annex II.5 provides a choice for the issuer on whether to produce the pro forma financial information on the basis of current, most recently completed or interim information. In order to provide certainty, we would request CESR to confirm that these two choices are indeed given to the issuer.

22. **Minimum denomination**: We note that the application of provisions referring to a minimum denomination can be affected by changes in currency exchange rates. For instance, an offer of securities in a currency other than Euro whose denomination per unit is equivalent to € 50.000 could fall below this equivalent value during the offer period. We would request CESR to agree among its members on how to deal with these cases.

23. **Language requirements:** The national implementation of the language and translation requirements varies widely and is in some countries perceived as particularly strict. These provisions have now been enacted into national law but we believe that they will have to be reviewed in the medium term.

24. **Requirements beyond the PD**: Pursuant to Article 1.2.j of the PD, non-equity securities where the total consideration of the offer is less than 50 000 000 Euro shall under certain conditions be exempted from the scope of the Directive. However, one authority has chosen to introduce an alternative prospectus for plain vanilla bonds which comply with these requirements. We acknowledge that this is in line with the wording of the prospectus but would suggest that CESR lead a dialogue on the underlying objectives of the PD and of this exemption.