7 August 2003

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Comments on CESR's consultation on possible Level 2 implementing measures for the Prospectus Directive

(Ref : CESR/03-162)

The Fédération Bancaire Française (French Banking Federation, FBF) is the professional body which represents over 500 commercial, co-operative and mutual banks operating in France.

FBF welcomes the changes made by CESR as a result of the latest consultation. We welcome, in particular, the provisional road map, published for the first time in the Consultation Paper (CP) which could eventually be helpful in generating some clarity. Nevertheless, further work is needed, especially on the sections related to derivatives, base prospectus, and the application of the road map.

General remarks

⇒ Definitions of Derivative Securities:

FBF is of the opinion that a working CESR definition of derivatives for the purposes of disclosure obligations would facilitate the use of the Banks Non-Equity and the derivatives SN and also the use of the Base prospectus. In this respect, we disagree with CESR's implicit definition on pages 11-12 of the CP which is based on whether or not the repayment of 100 % of the initial investment is guaranteed. We find this definition inadequate because in many cases derivative products can also incorporate a 100% guarantee of the original investment (for example, where the additional payoff is indexed to an underlying but the investment itself is guaranteed.

We would therefore recommend the following working definition for derivative securities :

« Derivatives securities are securities where the payment and/or delivery obligations are linked to an underlying (including but not limited to securities, currencies, commodities, indices or other measures), unless the payment of interest is merely linked to a fixed rate or to a recognised inter-bank interest rate ».

⇒ Registration Document for Derivative Products:

In the majority of cases, derivatives are issued by banks. We generally agree with the assertion that there should be no difference in the disclosure requirements for a derivative and a bank bond RD that could justify a separate RD for derivatives. However, under the current road map, an Equity RD would be required in the case of issuance of some derivative products, which CESR has classified as equity for the RD purposes, but as derivatives for SN purposes.

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We understand that this approach is based on the definition of equity securities in the Prospectus Directive. However, as we argue below, we believe that this definition should not prevent CESR from adopting a distinctive approach to derivative products, even if wrongly classified by the Directive as equity securities.

Furthermore, it is necessary to clarify that the Banks RD may be used by any financial institution independently of its corporate and/or issuing practices. Banks may use different types of structures to issue derivative and debt products; for example, some may be issuing using a special purpose vehicle (SPV) with the bank as the guarantor, whereas others issue as banks, with the holding company as the guarantor. In both cases, CESR should contemplate the possibility that the financial statements that are more relevant for the investor are used. For example, in the case of an SPV that issues a derivative product which is fully guaranteed by the bank to which the SPV belongs, the accounts of the bank are of greater relevance to the investor than those of the SPV. In the case of a bank issuing a derivative product which is fully guaranteed by the holding company to which it belongs, it should also be possible only to include the financial statements of the holding (parent) company since this information will be the most up-to-date (for example if the holding is a listed company, but not the bank itself). Both accounts (guarantor and issuer) should not be required in order not to confuse investors. This would allow the information most relevant to the investor to be provided.

In certain circumstances, there could be different entities involved in the process, i.e. the product manager, the SPV, the guarantor, a bank (distribution), so a flexible structure is needed to allow for different models of issuance.

Thus, we believe that CESR should provide further guidance on how these different and flexible current structures can be accommodated in the disclosure requirements to the benefit of greater transparency for the investor.

⇒ **Derivative SN:**

As for the SN for derivatives, we believe that examples should <u>not</u> be required. Although examples may well be useful in certain situations, in many situations they may not be helpful, and could even be misleading, for the investor. Generally, investors have a far better chance of understanding the key characteristics of the risks they are taking with the help of a description (ref. 2.2.1). Please see our response to questions 75-83 for more detail. Additionally, it should not be forgotten that there is a significant amount of assistance the customer could get from the manager/financial adviser in clarifying the risk profile of the offer.

Past performance of the underlying and its volatility (ref. 4.2.2) should not be required for the reason exposed by CESR in n° 85 of the consultation paper and their provision should be voluntary for the issuer. Given the competitiveness of these markets, best practices would evolve towards a solution most favourable to the customer.

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⇒ **Treatment of « bons d'option » (covered warrants) and « bons de souscription d'actions » :**

The FBF cannot understand the **treatment of « bons d'option » (covered warrants) and « bons de souscription d'actions » (warrant giving the right to receive newly created shares). A warrant giving the right to receive newly created shares (in French, « bons de souscription d'actions ») should not be issued under the same prospectus as the so-called covered warrant (in French, « bons d'option ») since the first ones are typically equity issues, whereas the second ones not**. For covered warrant, payment is only a cash difference between share price and exercise price.

Detailed responses to the consultative paper

DERIVATIVES SECURITIES

32 Do you consider that this disclosure is relevant for these products ? Please give your reasons.

Such information is not relevant for an issuer's decision to invest in these products.

1) Very often, the Issuer is just an SPV, which means that it has no real activity beyond issuing financial products.
2) The Issuer is currently a Bank or a financial institution.
3) The Warrant does not give any right in the share capital of the Issuer.

So, we find that items are irrelevant. In so far as the registration document is involved, investors in derivative products are concerned about the ability of the issuer to meet the payout obligations described in the product sheet. Issuers are generally financial institutions which are already supervised and are subject to capital adequacy requirements, thus mitigating the credit risk of the issuer.

34 Do you consider that disclosure about the principal markets in which the issuer operates is relevant for these products ? Please give your reasons.

Not relevant for same reasons. Plus, such products are very often issued by special purposes vehicles which very often do not operate in markets.

36 Do you consider that disclosure of an issuer's significant business developments is relevant for these products ? Please give your reasons.

Not relevant for same reasons.

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37 Do you consider that this disclosure is relevant for these products ? Please give your reasons.

Such a disclosure should not be requested since conflicts of interests may not always be known at the time the prospectus is published as they may arise at anytime; Anyway, for the same reasons a negative statement has to be rejected since it could be misleading.

38 Do you consider that disclosure about an issuer's major shareholders is relevant for these products ? Please give your reasons.

No. The issuer's major shareholders disclosure is not relevant for an issuer to make an investment decision in derivative securities.

40/41 Profit forecasts or estimates:

Inclusion of forecasts or estimates should indeed not be required. In our view, CESR's assertion that, where such forecast is included, an auditor's report must be added, will lead to an absence of forecasts. Many issuers will not want to incur the additional costs of the auditor's report. That would clearly be an unwanted effect.

57 SPV guaranteed by a bank:

We fear that the use of the retail debt disclosures will lead to increase of costs and loss of efficiency, since the issuer might very well end up having discussion with the Competent Authority about what is and what is not relevant/applicable. We would prefer to have separate schedules for this sort of issue.

59 Do you agree with CESR's revised approach in relation to retail non-equity securities and wholesale non-equity securities ? If not please give your reasons.

In line with the decision not to define derivative securities (which we contest), CESR proposes to differentiate between retail and wholesale derivative securities, for the purpose of the choice of the suited RD: if it is a retail derivative securities issue, a retail debt RD, and if it is a wholesale derivative securities issue, a wholesale debt RD.
The limit proposed by CESR would then be the following : if the repayment of 100% of the capital is not guaranteed, then it is deemed to be a derivative product. This proposed limit is however not in line with current practices as there are many derivative products with a guarantee of return of 100% of the investment, and an additional value depending on the underlying.

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In addition, the proposal from CESR to differentiate between wholesale and retail derivative products may be a source of uncertainty because of the difficulty to find an adequate criterion to differentiate a retail from a wholesale derivative issue : in certain cases, those securities have no or very low denomination (in particular warrants).

For such issues, applying the general threshold of the directive (50 000 euros) is thus of no help.

It is then of a truly common interest to find a definition of derivative securities. Cf. our observations on § 22 and our proposed definition.

61 Do you agree that information about investments should not be required for banks issuing wholesale debt securities ? Please give your reasons.

We agree with the proposal to delete the requirement to describe the investments in the RD for wholesale debt so as to make the wholesale non-equity RD and the bank non-equity RD compatible with one another.

64 Do you consider that information on investments is relevant for wholesale debt securities ? Please give your reasons.

- The information on past and current investment is not relevant for any investor in debt securities (retail or wholesale). Plus, information on future investments should never be required if this information is not public.
- If given, this information couldn't be relevant beyond the issue date (It will be necessary to update it)

75 Do you consider that examples are necessary in order to fulfil the principle that the prospectus must contain a clear and understandable explanation of how an investor's return is calculated and how the instrument works ? Please give your reasons.

While examples can sometimes be helpful, as a general rule, it would not be correct to state that examples always generate truly valuable information on the product. In fact, since by definition examples highlight certain cases without giving a coherent description, they often mislead investors. The inclusion of examples would draw the investor's attention solely to single scenarios, and fail to present the full economic nature and risks associated with the security.

An additional difficulty is that examples could lead to excessive legal risks for the issuer since they could be seen as the basis of a misleading fact in a prospectus, which is a legal document. In practice, if this were required, issuers would be compelled to provide an impractically large number of examples that do not benefit the customer but raise issuance costs for companies.

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Furthermore, examples would be difficult to prepare on the basis of base prospectuses, which are almost always used for derivatives and similar products. Given that issuers often issue a large number of derivatives on one day, it would be extremely difficult to provide examples tailored for the economic details of each single product.

Warrants' issuers generally produce user's guide explaining the nature of the investment. No need to give this type of information in the prospectus.

76 What other methods (if any) do you consider can be used to provide investors with a clear and understandable explanation of how an investor's return is calculated and how the instrument works ? Please give your reasons.

Products are not to be simplified.
We do not want to give any explanation of how an investor's return is calculated.
No need in this context to be very didactic.

77 If you do not consider that examples are necessary to provide investors with a clear and understandable explanation of how an investor's return is calculated and how the instrument works, do you consider that the provision of examples in the prospectus is useful for investors ? Please give your reasons.

No, same reason as 76 and 75 and also examples can be misleading. They should not be mandatory.

78 Do you consider that the use of examples in the prospectus is dangerous and misleading and should not be mandatory ? Please give your reasons.

They should not be mandatory. They could be misleading for certain types of investors, again this type of investment should only go to a certain type of investors.

As such, the examples are dangerous and misleading; An additional explanation is necessary. This explanation makes the propectus heavier and less readable for the investor.

79 If examples are to be included in the prospectus, do you consider that CESR should stipulate how the examples should be prepared, for example that they should be realistic, not misleading and should provide a neutral view of how the instrument works ?

No example.

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80 If your answer to the previous question is yes do you think that examples should also fulfil other requirements (for example : the need to insert the break even point for the investor) ? Please state these other conditions.

No.

81 Do you consider that examples should be provided for derivatives ? Please give your reasons.

No. Same reason as 75 and 76

82 If yes, for which types of derivatives should examples be provided ? Please give your reasons.

No.

83 Are there any other type of securities for which you consider examples should be provided, for example structured debt instruments that have a derivative component ?

No**.** We do not think such inclusion is appropriate since it can be misleading and may raise expectations on the side of the investor.

We think on the contrary that a clear drafting of terms and conditions, especially concerning the way the return is calculated and a risk warning indicating to the investor which risks he is facing, is enough.

Nevertheless, it should be up to the issuer to decide whether or not to include examples, that should not be mandatory.

89 Which of the above options do you consider should be adopted by CESR (1, 2 or 3) ? Please state your reasons.

There should not be a requirement to disclose past performance and volatility of the underlying, and we therefore recommend that CESR adopts option no. 1.

We support discretion on the part of the issuer for disclosure of this kind of information. Issuers will provide this information if they feel that it will be of use to investors. However, like examples, past performance data may not always be relevant or informative for the investor. It is a generally recognised fact that past performance of an asset does not indicate a similar development in the future. Current conduct of business rules in Europe already (as will almost certainly the future conduct of

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business rules under the forthcoming ISD) require that investors are made aware of this fact in marketing documents. In fact CESR would require the inclusion of a similar disclaimer (ref. 87). Furthermore, where the underlying is a security not admitted to trading on a regulated market, the information on past performance may be difficult to obtain, let alone disclose. On the other hand, where the security is traded, such information will generally be easily accessible to any investor.

BASE PROSPECTUS

101 Do you agree with this generic rule ?

Yes, we agree. French Domestic Market already comply with the generic rule. The base prospectus should contain the information required by the relevant building blocks, except the information that can only be provided at the time of the individual issue and its final terms are not known. Indication of the final terms might be inserted, but this rule should be flexible enough to avoid freezed situations.

112 Which of these two approaches do you think should be applied to base prospectuses ? Please give your reasons.

Approach 111 should apply, but only to those final terms that are crucial and should then be translated.
The translation of the summary is sufficient because its purpose is to convey the main characteristics and risks associated with the issuer.
It's this information that every investor has to understand; the precise financial data relating to the issuer, the Guarantor, for example, are less relevant.
Final terms that are crucial have to be translated for a better understanding of the investors.

115 Which of these views do you consider should apply to base prospectuses with multiple products ? Please give your reasons.

We believe that the issuer should be able to determine the composition of the summary, as every other aspect regarding the content of the summary. Requiring a summary for each product would contradict the rationale of a summary, which can, by definition, at most provide a brief description of the economic nature, which will be more or less identical for many derivative products.

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122 Which of these views do you consider should apply to the form of final terms ? Please give your reasons.

Approach 121 should apply: the document must always be read in conjunction with the base prospectus.
It is not necessary to repeat the terms of the base prospectus in the final terms. The base prospectus must be given to any investor who makes the demand for it.
An update of the base prospectus can be made in the final terms.

125 In relation to the publication of the final terms, should the method of publication be restricted as set out in Article 14 ?

A priori, the publication of final terms has to be made according to the described modalities (art 14-2-a/b/c/d)
The adverb "among others" is not used; so, the method of publication should be restricted as set out in Article 14.
Moreover, this argumentation comes true in the reading of the article16 (1): "*the supplement of the prospectus is approved in the same way and published according to the same modalities as the initial prospectus*".

127 Do you agree with this analysis ?

As long as we use one of the modalities of the article 14, it doesn't matter the way we publish the final terms.
The means of publication of the final terms and the base prospectus can be different.

131 Do you agree with the above additional disclosure requirements in relation to base prospectuses ?

The only utility of this additional disclosure requirements is to allow a harmonization of items contained in the various documents.

132 Are there any other disclosure requirements that are not specified above that you consider necessary for base prospectuses ? If so, please specify what these are and give your reasons for why you think they are necessary.

No

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136 Do you agree with the above types of base prospectuses ?

Yes, in principle. But, warrants giving the right to receive newly created shares (in French bons de souscription d'actions) should not be issued under the same prospectus as the so-called covered warrants (in French bons d'option) since the first ones are typically equity issues, whereas the second ones are not. 2.a) should therefore be excluded from the base prospectus.

137 Are there any other types of base prospectuses that you consider are necessary ? Please give your reasons.

No.

WHOLESALE DEBT SN

143 Do you agree with this approach ?

Yes.

144 Do you consider that the information provided for in Annex F is adequate for wholesale investors ? Please give your reasons.

Annex F is globally satisfactory. However, information required in points 4.9 and 6 is not relevant for the investor.

145 Are there any other items included in the retail debt SN that should be included for wholesale investors ? Please give your reasons.

No.

151 Do you agree with the disclosure obligations set out in Annex G as being appropriate for this type of issuer ? Please give reasons for your answer.

Yes. Nevertheless, section 2 provides for quite extensive information on underlying which may prove to be rather burdensome.

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154 Do you consider there is a distinction to be drawn between these two types of activities, as set out above ? Please give reasons for your answer.

Real estate and related investments generate a very large range of activities. Thus, classification of activities is somewhat impossible. The distinction drawn between the two extremes (ie: passive / active investment) is unlikely to ease the 2.7 disclosure requirement.

155 What would you consider to be an appropriate and sustainable distinction between both activities ?

Not relevant considering the above reasons.

162 Do you agree with this approach ?

Yes, but not for derivative securities issues which do not lead to a change in the share capital of the issuer. CESR should indeed not focus only on the definition of equity security as it results from the adopted directive (Article 2 1 b) for the purpose of the competent authority, but also on market practices. Warrants on the issuer's own **existing** shares (in French "bons d'option") function the same way as warrants on other shares of the market. Compelling the issuer of these products to produce a building block on the underlying would be useless.

BUILDING BLOCK ON UNDERLYING FOR EQUITY SECURITIES

163 Do you agree with the disclosure requirements of the building block concerning the underlying for equity securities as set out in Annex H ?

It is difficult to think of any further requirement since those set out in Annex H are rather exhaustive. We believe some disclosure requirements may prove to be over-killing, in particular those which will automatically derive from the legislation under which the shares have been or will be created.

165 Do you deem the Working Capital Statement and the information on Capitalization and Indebtedness necessary for an informed assessment of the securities in cases of products which can be converted or exchanged in newly created shares ? Please give your reasons.

We do not agree. We consider that this additional information (the Working Capital Statement and the information on Capitalization and indebtedness) will add no value for the investors when the base prospectus is filed. This information must be accurate

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and complete by the time the prospectus is issued by the Directors of the issuing company. Directors have a liability towards the investors at this time, not later.

166 Do you agree with this approach ?

We agree with this approach. The most important is the complete information given to investors.

167 Do you agree with this approach ?

Yes.

168 Do you agree with the combinations set out in the table?

We do not understand why item 4.2.2 solely of the derivatives SN should be produced for bonds exchangeable or convertible into third party shares, since all item 4.2 is relevant for such products. However, once again, information on volatility and past performance should not be required.

IV. FORMAT OF THE PROSPECTUS

172 Which of the options set out above do you support ? Please give your reasons for your choice.

We support the third option. It should be up to the issuer to choose the best way to present the information that has to be disclosed. It is also the best way to prevent from any duplication of information between the Registration Document and the Securities Note.

176 Which of the options set out above do you support ? Please give your reasons for your choice.

For same reasons as above (172), it should be up to the issuer to decide how to prepare a single document prospectus.

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182 Which of the options set out above do you support ? Please give your reasons for your choice.

The second option seems to be more suited; in fact, for the investor, the new information will be easier to display.
If the supplement of the prospectus reproduces at once the former information and the new ones, the supplement will be less legible.

ROAD MAP

237 Do you agree with the method of publication proposal?

Yes we agree.

238 Do you consider CESR should limit the issuer's choice to one or more methods of publication? Which ones?

No. It is the issuer's choice. The methods of publication should be disclosed on the cover page of the prospectus.

239 Do you consider that a deadline should be defined? If so, do you agree with the proposed deadline or would you suggest a different one? Please give reasons for you answer.

To define a deadline seems obvious and necessary. Your proposition of 7 business days is definitely too short as a standard that will apply in all European markets. A period of 30 business days seem to be more appropriate.

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