Background Document

Review of Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC (Prospectus Directive)

This document is a working document of the Commission services for consultation. It does not purport to represent or pre-judge the formal proposals of the Commission.

You are invited to comment on the proposals in this paper. The proposals are only an indication of the approach the European Commission may take and are not its final policy position.

Since this is a simplification and administrative burden reduction initiative we would welcome in particular the views of SMEs, investors and consumers.

As well as responding to the specific proposals and questions, we also ask you to describe any alternative approaches you think would achieve our objectives.

Your comments will help us develop our proposals to review the Prospectus Directive. We are keen to fully understand and assess the financial and other impacts of our proposals and any alternative approaches. Therefore, we ask you to comment on compliance costs, impacts on competition and other impacts, costs and benefits. These elements will be taken into account when we prepare our final policy position.

Where possible, we are seeking both quantitative and qualitative information.

We are also keen to hear from you on any other issues you consider important.

You can send your contributions until 10th March 2009 to markt-g3@ec.europa.eu

This document is an explanatory document of the Commission services accompanying the Commission's draft proposal related to the intended recast of the Prospectus Directive in the context of the Action Programme for Reducing Administrative Burdens in the European Union.

1. INTRODUCTION

In January 2007, the Commission launched the Action Programme for reducing administrative burdens in the European Union to measure administrative costs arising from legislation in the EU and reduce administrative burdens by 25% by 2012[1]. Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC (the Prospectus Directive) has been identified as one area that contains a number obligations for companies, some of which could possibly be alleviated.

The aim of this proposal is to improve and simplify the application of the Prospectus Directive in the EU. In addition, Article 31 of the Prospectus Directive requires the European Commission to review the application of the Directive five years after its entry into force and to present, where appropriate, proposals for its review. As a result of an extensive and continuous dialogue with stakeholders, including the Committee of European Securities Regulators (CESR)[2] and the European Securities Markets Expert Group (ESME)[3], the European Commission concluded that some particular elements of the prospectus regime merit a review. Since the objective of this proposal is to simplify and reduce administrative burden we are particularly keen to hear the views of SMEs, investors and consumers.

Following a request from the ECOFIN Council in May 2007, the Commission is currently examining the coherence of disclosure and distribution regimes in EU Law applying to different types of retail investment products. The Commission plans to publish a White Paper on Retail Investment Products by spring 2009. The White Paper will look into changes that are necessary for retail investment products structured as securities. Further analysis will be carried out and these changes will be implemented.

This document is divided into three parts:

(1) A general assessment of the overall functioning of the Prospectus Directive in terms of its effectiveness and efficiency in achieving its aims;

(2) A selection of issues that have been brought to the Commission's attention and may affect the functioning of the prospectus regime, notably because they create excessive administrative burden which may hamper the expected

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[1] See http://ec.europa.eu/enterprise/admin-burdens-reduction/home_en.htm.

[2] CESR is an independent committee established under the terms of the Commission Decision of 6 June 2001 (2001/527/EC). The role of the CESR is to improve coordination among securities regulators; act as an advisory group to assist the Commission; and work to ensure more consistent and timely day-to-day implementation of Community legislation in the Member States. Concerning the Prospectus Directive, this work is carried out by the Prospectus Contact Group, which meets regularly and posts its common positions on a dedicated section of the CESR website ("Frequently asked questions regarding Prospectuses"): http://www.cesr-eu.org/index.php?page=groups&mac=0&id=40.

[3] Established by the Commission Decision of 30 March 2006 (2006/288/EC) setting up a European Securities Markets Expert Group to provide legal and economic advice on the application of the EU securities directives.

benefits attached to this directive. The document explains the issues and suggests actions to address the problems identified.

(3) A selection of issues that have been brought to the attention of the Commission but that are not included at this stage in the draft proposal. We are particularly keen to receive contributions and suggestions from stakeholders on these issues.

The draft proposal does not address problems deriving from incorrect transposition into national legislation or from diverging interpretations by different EU securities regulators. In both cases, other tools are available, such as the Commission's enforcement activities or the permanent dialogue within CESR.

The draft proposal is the result of an extensive and continuous dialogue and consultation with all major stakeholders, including securities regulators, market participants (issuers and investors), and consumers. It takes account of the observations and analysis contained in the reports published by CESR[4] and by ESME[5]. It also makes use of the findings of the study completed by the Centre for Strategy & Evaluation Services (CSES)[6].

2. GENERAL ASSESSMENT OF THE PROSPECTUS DIRECTIVE

The reports and study considered for the draft proposal as well as the feedback received from stakeholders are all positive in their general assessment of the overall effect of the Prospectus Directive. In general, most market participants appear satisfied with the new regime, and consider the Prospectus Directive and its Implementing Regulation to be a step in the right direction in achieving a single European securities market. The Directive, in particular, has introduced a new mechanism for notification and has set up a harmonised and coherent structure of

4 The CESR's report on the supervisory functioning of the Prospectus Directive was adopted and published in June 2007. The report is based on evidence gathered from market participants by means of a call for evidence opened in November 2006, including an open hearing in January 2007, as well as on statistical data provided by regulators. The report contains a detailed summary and analysis of the 38 responses received, and it aims to assess whether, after almost two years in operation, the prospectus regime is achieving its objectives of investor protection, reduction in the cost of capital, and development of the single market for securities. It focuses in particular on obstacles that threaten the proper functioning of the single market and, more specifically, the operation of the passport under the Directive. Where appropriate, it suggests further steps that should be taken, including, in some cases, legislative action. Ref. CESR/07-225, available at www.cesr-eu.org.

5 The ESME report on the Prospectus Directive reflects the views and practical experience of ESME members. It assesses the effectiveness of the Prospectus Directive in achieving its primary objectives of investor protection and market efficiency; identifies significant areas where the Directive may not have achieved its intended effect, or where lack of clarity or flawed provisions are causing problems for market participants; and sets out detailed comments and suggestions on specific articles. The report, adopted and published in September 2007, is available at http://ec.europa.eu/internal_market/securities/esme/index_en.htm.

6 "Study on the Impact of the Prospectus Regime on EU Financial Markets", completed in June 2008 by the CSES in response to a request for services in the context of the Framework Contract for Evaluation and Impact Assessment of Internal Market DG activities. The study gives an overview of the impact of certain aspects of the Prospectus Directive on EU financial markets and supplements the evidence provided in the CESR and ESME reports. It also addresses some additional issues by providing qualitative and quantitative evidence. The study is available at http://ec.europa.eu/internal_market/securities/prospectus/index_en.htm.

disclosure requirements (able to take into account the specificity of various financial instruments as a result of a system of different building blocks and schedules).

The prospectus regime appears to have made it easier to offer securities and admit them to trading, either in one country or in several countries at the same time. The survey conducted by CSES as part of its study shows that a large majority of respondents are satisfied with the way the prospectus regime works. Many interviewees mentioned that, after some initial difficulties, both regulators and market participants are gaining experience of the prospectus regime, and most of the early problems have been overcome, progressively generating better quality prospectuses and reducing the average approval time[7]. Similarly, the cost of compliance decreased once participants had become used to the regime.

There may be areas in which, according to market participants, the legislative framework might be improved. Nevertheless, it should be borne in mind that any change in regulations entails a cost. This aspect should be taken duly into account when proposing legislative amendments. Legislative amendments will be put forward only if they are necessary and sufficiently evidence-based as well as subject to a thorough impact assessment.

The principal concerns expressed were focused on the lack of uniform implementation in Member States and the divergent supervisory practices. Where inconsistencies in implementation and supervisory application do not arise from legislative ambiguity, they should be addressed by work at "level 3" of the Lamfalussy approach[8]. In addition, if the conditions are met, enforcement action could also be undertaken by the Commission. The Commission would therefore encourage the CESR to carry on its work on supervisory convergence at level 3 on these issues, and will support that work wherever possible[9].

Market participants seem to be more concerned by the administrative burden, which they claim has become unjustified as a result of the entry into force of other directives of the Financial Services Action Plan, namely MiFID and the Transparency Directive[10]. In line with the target set by the Commission to reduce administrative costs by 25% by 2012, the current review focuses on reducing administrative burdens to bring relief to issuers by introducing a number of changes to the Directive which would not affect the high standard of investor protection.

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[7] This is confirmed by data on IPOs in the EU. According to the PricewaterhouseCoopers IPO Watch Europe Survey, the third quarter of 2005 saw a significant drop in terms of value and number of IPOs, which is mainly attributed to the fresh implementation of the Prospectus Directive. Both value and volume of IPOs increased in the following quarters, suggesting *ceteris paribus* a progressive adaptation of the market to the new disclosure regime for issues.

[8] Level 3 of the Lamfalussy approach refers to the cooperation among European regulators to achieve convergence in supervisory practices.
See http://ec.europa.eu/internal_market/securities/docs/lamfalussy/wisemen/final-report-wise-men_en.pdf.

[9] There are several issues identified by market participants that could be properly addressed by the CESR's level 3 work, such as the lack of a coherent regulatory approach to the use of final terms of a base prospectus or the calculation of certain thresholds.

[10] Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC.

Do you agree with the Commission services' preliminary assessment of the functioning of the Prospectus Directive?

3. CHANGES PROPOSED

3.1. Article 2(1)(e) — Definition of qualified investors

Under Article 3(2)(a), offers of securities to qualified investors are exempt from the requirement for a prospectus. Practical difficulties may arise from the fact that the concept of "qualified investor" in the Prospectus Directive is different from the scope of "professional clients" and "eligible counterparts" for the purposes of MiFID. ESME has recently completed a detailed and comprehensive analysis of the differences between the concepts of qualified investors in the Prospectus Directive, and of professional investors and eligible counterparts in MiFID, and has examined the justification, if any, for that difference[11]. These differences seem to create complexity and costs for investment firms. In particular, investment firms have to maintain systems to obtain relevant data from investors, keep records, and apply the corresponding MiFID categorisations. Such differences may also have an impact on issuers wishing to use investment firms as intermediaries for private placements of their securities, because they restrict issuers' ability to conduct private placements with some classes of experienced individual investors[12].

To promote simplification without undermining investor protection, it appears to be more appropriate to align via legislative amendment the Prospectus Directive with MiFID. This is mainly for practical reasons: since the enactment of MiFID, investment firms are categorising their clients in accordance with the definitions in MiFID, and changing those definitions would impose other costs and burdens on firms. On the contrary, it seems unlikely that issuers or intermediaries would have to make corresponding changes as a result of an amendment to the definition of qualifying investors in the Prospectus Directive.

Therefore, we propose to extend the scope of the persons to be treated as qualified investor in accordance with the Prospectus Directive in order to encompass also those natural and legal persons that request to be treated as professional clients in accordance with MiFID. This change would facilitate the activity of the intermediaries in the event of a private placement, because the firms will be able to define the target of the placement relying on their own list of professional clients. The amendment will require a modification in Article 2.1(e) of the Prospectus Directive.

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[11] The ESME paper analyses the difference between the concepts, stressing that, while the Prospectus Directive is basically "product-driven", MiFID is in essence "services-driven". As a consequence, the exemption for offers to qualified investors in the Prospectus Directive is based on the concept that certain categories of investors need less protection than others when making their investment decisions, while MiFID calibrates the operation of its conduct of business rules by applying differing levels of protection depending on whether the investment firm is providing services to or dealing with a retail client, a professional client or an eligible counterpart. Under MiFID, regulated investment firms do not need to provide eligible counterparts with certain protections (such as best execution) and firms can deal with professional clients with considerably fewer formalities than those that apply in relation to dealing with retail clients. The paper is available at: http://ec.europa.eu/internal_market/securities/esme/index_en.htm.

[12] *Ibidem.*

There are cases where the issuer or the offeror might want to carry out the private placement by itself, without the assistance of an intermediary. Therefore, the system of a central register of qualified investors mentioned in Article 2.3 of the Prospectus Directive should be maintained in the Directive.

Do you agree with this analysis? Do you agree with the change proposed in Article 2.1(e) of the Prospectus Directive?

3.2. Article 3 — Exempt offers

Article 3 requires the publication of a prospectus when securities are offered to the public (paragraph 1) and when they are admitted to trading on a regulated market (paragraph 3). Paragraph 2 sets out a number of circumstances in which an offer of securities to the public is exempt from the requirement to publish a prospectus.

These exemptions are generally regarded as working effectively. However, the last indent of Article 3(2) is causing problems for issuers in some markets where securities are distributed by "retail cascade". A retail cascade typically occurs when debt securities are sold to investors (other than qualified investors) by intermediaries and not directly by the issuer itself. The market has raised two points of uncertainty:

(1) it is unclear how the requirement to produce and update a prospectus, and the provisions on responsibility and liability, should apply in cases where securities are placed by the issuer with financial intermediaries and are subsequently, over a period that may run to many months, sold on to retail investors, possibly through one or more additional tiers of intermediaries;

(2) where a prospectus is produced, it is unclear how the disclosure requirements in Annex V of the implementing Regulation apply in relation to the multiple sales by intermediaries that make up the retail cascade.

As far as we are aware, the problem is only experienced by issuers in a limited number of EU markets. This may reflect established differences in distribution patterns (i.e. selling by retail cascade may be common in some markets but not in others); or it may arise from differences in national implementation and application of the final indent of Article 3(2), and in the way a prospectus is used by persons other than those responsible for drawing it up. However, in those markets where it is experienced, it may cause some issuers to suspend their retail debt programmes.

The final part of Article 3(2) was intended as an "anti-avoidance" provision, preventing the easy circumvention of the prospectus requirements. However, in the way it is shaped, it gives rise to a number of questions that have been only partially addressed by the CESR's level 3 work. The CESR has clarified, for instance, that where financial intermediaries are acting in association with the issuer, they are not required to draw up a new prospectus and they can rely on the prospectus published by the issuer. Concerning the supplement, the issuer is responsible for its publication only for the duration of the sub-offer conducted by the intermediaries acting in

association. Where the intermediaries are not acting in association with the issuer, they would be expected to draw up and update their own prospectus[13].

The CESR position, based on the concept of association between the issuer and the financial intermediary, can be considered as a satisfactory, but only temporary, solution because it does not provide a robust regulatory solution to the problem that would permanently remove the legal uncertainty in terms of information disclosure and responsibilities. For these reasons, following ESME's advice, we propose to delete the last sentence of Article 3(2) of the Prospectus Directive. Such a change will clarify the responsibilities of drafting and supplementing a prospectus as well as the level of information to be included in prospectuses used in a retail cascade scenario.

Do you agree with this analysis? Do you agree with the change proposed in Article 3.2 of the Prospectus Directive?

3.3. Article 4 — Exemptions for Employee Shares Schemes

Article 4 contains a series of exemptions which remove the need to publish a prospectus that would otherwise apply where securities are offered to the public (paragraph 1) or admitted to trading on a regulated market (paragraph 2). The exemptions cover a wide range of different situations, varying from securities offered free of charge, to securities offered in connection with a merger or a takeover. Particularly relevant is the exemption dealing with securities offered to employees.

Offers of transferable securities to employees are considered to be offers of securities to the public in line with the definition in Article 2(1)(d) of the Prospectus Directive. A prospectus is therefore required unless an exemption applies. Article 4(1)(e) grants an exemption specifically for offers of securities to employees, provided that two conditions are met:

- the issuer must have securities admitted to trading on a regulated market; and

- a document must be available containing information on the number and nature of the securities and the reason for and the details of the offer.

This exemption does not apply equally to all issuers but creates a less advantageous situation for two categories of issuers, namely third country issuers that do not have a listing on a regulated market within the EU, and EU non-listed companies or EU companies that have securities traded on EU "exchange-regulated" markets.

The exemption is not available to third country issuers that do not have a listing on a regulated market because the concept of regulated market is by definition limited to the EU, as provided for in Article 4(1)(14) of MiFID. In addition, it is equally impossible for EU non-listed companies or EU companies that have securities traded on EU exchange-regulated markets (i.e. AIM in London) to satisfy this condition, because once again they are not listed on a regulated market in line with the applicable MiFID definition.

[13] See question 52 of the CESR frequently asked questions regarding prospectuses at http://www.cesr-eu.org/index.php?page=groups&mac=0&id=40.

Employee share schemes run by all such companies will require a prospectus if there are more than one hundred scheme participants in a particular Member State. This may generate the perverse effect that executive share incentive plans will generally be exempted, while "all employees" schemes will require a (relatively costly) prospectus. The Directive could therefore be criticised as preserving the interests of directors while penalising ordinary employees.

Views have been expressed that, with its current structure, the exemption fails to address the concern expressed by the Commission in its 2002 Communication on a framework for the promotion of employee financial participation[14]. EU employees working for non-EU companies or companies listed in a non-regulated EU market or EU non-listed companies should not be penalised in comparison to EU employees of companies listed on an EU regulated market.

Share schemes for EU employees of companies listed on third country exchanges or in EU exchange-regulated markets or non listed companies should also be covered by the condition under Article 4(1)(e). Therefore, we propose to extend the exemption in Article 4(1)(e) of the Prospectus Directive accordingly. In this regard, the current CESR work on the establishment of a "short-form" disclosure regime as a temporary solution to the issue (pending an amendment of the Prospectus Directive) could constitute a suitable reference for establishing the set of information to be provided to employees.

Do you agree with this analysis? Do you agree with the change proposed in Article 4(1)(e) of the Prospectus Directive?

3.4. Article 10 — Information

Article 10 of the Prospectus Directive requires issuers with listed securities to provide annually a document containing or referring to all information published in the twelve months preceding the issuance of the prospectus. There is wide consensus among stakeholders on the need to delete Article 10. When the Prospectus Directive was being negotiated, Article 10 was intended only as an interim requirement that would be superseded (and repealed) by the Transparency Directive, which provides for a comprehensive regime for the disclosure of periodic and ongoing information about issuers with listed securities. The Transparency Directive entered into force on 20 January 2005, and was due to be transposed by all Member States by 20 January 2007. It did not repeal Article 10 of the Prospectus Directive; nevertheless, its provisions made the requirement of Article 10 redundant, generating a duplication of the same requirement for issuers.

Along the same lines, following a request by the Commission, ESME has recently completed a position paper on the issue, analysing in detail the wording of Article 10 *vis-a-vis* the requirements of the Transparency Directive[15]. As a result of the analysis, Article 10 should be abolished, as this would not have any negative consequences for public information or for the level of investor protection.

[14] COM(2002) 364.

[15] Available at http://ec.europa.eu/internal_market/securities/docs/esme/position_prospectus_directive_en.pdf.

Having listened to all these arguments, we share the view that there is duplication of requirements and that Article 10 should be removed from the Prospectus Directive in order to reduce the administrative burden on issuers[16].

Do you agree with this analysis? Do you agree with the removal of Article 10 of the Prospectus Directive?

3.5. Article 16 — Supplement to the prospectus

Article 16 regulates the publication of the supplement to the prospectus, which triggers a withdrawal right for investors. The wording of this Article leaves room for divergent application in the Member States. This has generated an intense debate among stakeholders. Some technical issues have already been addressed by the CESR[17], while other questions require further clarification in order to ensure legal certainty, such as, for instance, the meaning of "significant new factor"[18] and the question whether — in a situation where there is both an offer and an admission to trading — the obligation to supplement the prospectus ceases once the trading begins, even if the public offer is still open. We believe that issues of this kind should be addressed at level 3.

Do you agree with this analysis?

In the context of the current proposal, we believe that we should only aim to simplify the mechanism set up by the Directive in relation to the withdrawal period in Article 16(2). Every time a prospectus is supplemented in the course of an offer, the Directive grants investors the exercise of the right of withdrawal of their previous acceptances. Such a right can be exercised during a period – to be settled by Member States in their legislation – no shorter than 2 days following the publication of the supplement. The time frame for the exercise of such a right is not harmonised; indeed Member States have set different periods through national legislation.

Concerns have been raised with respect to cross border offers. It is unclear whether the time frame set out in the national legislation of the Home Member State of the issuer should apply or those stemming from the legislation of each of the Member States where the offer or admission to trading takes place.

We consider that further harmonisation of this time limit is positive. Therefore we propose to harmonise in Article 16.2 the time frame and establish a common period of at least two days.

Do you agree with this analysis? Do you agree with the change proposed in Article 16.2 of the Prospectus Directive?

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[16] It should be noted that a technical adjustment will be needed, for legal certainty reasons, in Article 2(1)(i)(i) of the Transparency Directive in relation to the determination of the home Member State for third country issuers because of a cross reference to Article 10 of the Prospectus Directive.

[17] See questions 19-22 in the CESR FAQs, dealing respectively with supplements in the case of interim financial information; profit forecasts; and the indication in the supplement of the actual period for the right of withdrawal.

[18] In this regard, ESME noted that there should be an element of proportionality in the application of this rule, and the withdrawal right should not be available, for instance, for positive news.

3.6. Modification of thresholds

Several provisions of the Prospectus Directive set thresholds for different purposes, for instance to determine exempted offers (Article 3(2)) or to identify certain categories of investors (Article 2(2)(b)). The thresholds are expressed in either absolute or relative terms, such as for example, the assortment of "50 000 euros exemptions" used in the Directive, or the 10% ceiling in Article 4(2)(a). The evidence collected during the review seems to suggest that at this stage most of the thresholds in the Directive are actually workable and efficient. For this reason, we are not inclined to change them.

There is, however, one provision where difficulties have been consistently reported by market operators. We are referring to Article 2(1)(m)(ii), which imposes a restriction on the free determination of the home Member State for issues of non-equity securities. The free choice is available only for debt securities with a denomination above 1 000 euros. It is argued that this restriction is causing practical problems for issuers, either because it obliges them to maintain additional debt issuance programmes or because the threshold does not accommodate certain structured products which are not denominated (i.e. certificates)[19]. It has been suggested that the removal of the threshold would allow issuers to choose the most appropriate competent authority on a case-by-case basis, and the choice would rest on considerations such as the language of the prospectus, the expertise of the competent authority in relation to the securities to be offered, and its knowledge of the issuer. We do not see concrete risks in terms of investor protection in a situation of free choice: in our view, the characteristics of and the risks associated with debt securities do not depend on the denomination. We believe that the removal of the 1 000 euros threshold would remove some burden from issuers and increase the flexibility of the regime without affecting the protection of investors. Therefore, we propose to delete the threshold of 1.000 € from Article 2(1)(m)(ii).

Do you agree with this analysis? Do you agree with the change proposed in Article 2(1)(m)(ii) of the Prospectus Directive?

4. OTHER ISSUES IDENTIFIED

4.1. Disclosure obligations: the prospectus and its summary

One of the principal objectives of the Prospectus Directive is investor protection[20]. This entails the need to ensure that complete and accurate information is provided concerning the issuer and the relevant financial instruments in order to facilitate access by investors to the necessary information to allow them to take the appropriate investment decisions.

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[19] See ESME report, section 3.2 and annex. See also CSES study, section 4.5.

[20] Recital 10: "The aim of this Directive and its implementing measures is to ensure investor protection and market efficiency, in accordance with high regulatory standards adopted in the relevant international fora." See also recitals 16, 18, 19 and 21.

To achieve this objective, the Directive and its Implementing Regulation take into consideration, among other elements, the nature of the investors. For instance, the Directive aims to ensure that the information provided is sufficient and adequate to cover the needs of retail investors.

On the one hand, Article 5 of the Directive prescribes the overriding standard that each prospectus should attain: a prospectus is required to contain all information which is necessary to assess the assets and liabilities, financial position, profits and losses and prospects of the issuer and any guarantor, and the rights attaching to the securities. That information must be presented in a form that is easily analysable and comprehensible. The minimum contents of a prospectus are further specified by the Implementing Regulation, and are intended to reflect the nature of the issue and the securities, including information on whether they are traditionally aimed at the wholesale or the retail market. The Regulation takes close account of IOSCO standards[21].

On the other hand, the requirement for a summary as an integral part of the prospectus[22] for "retail" securities was intended to ensure that the contents of a prospectus are more easily accessible to retail investors[23]. This provision aims to strike a balance between the provision of comprehensive information and accessibility to non-professionals, as well as to counterbalance the increasing trend to add detailed pieces of information in the prospectus as a way of shielding issuers from potential civil liability in relation to incomplete or inaccurate disclosure.

It is arguable whether or not the correct balance has been achieved between the provision of all necessary information for investors to make an informed decision and, at the same time, ensuring that the prospectus is comprehensible and "user friendly". In fact, concerns have been expressed that, due to the length and complexity of prospectuses, the primary aim of informing the investor may not actually be achieved. In addition, issuers (especially small and medium-sized companies) may be subject to excessive costs and burdens that are not justified by the aim of effective investor protection. In particular, it has emerged that, unlike qualified investors, retail investors do not (on the whole) make use of prospectuses for their investment decisions. The current regime allows long and complex prospectuses because there are no limits on the overall length of the documents (other than the summary), and there are potentially very severe penalties if information is omitted. In this context, some market participants argue that changes

[21] The members of the International Organization of Securities Commissions (IOSCO) are generally the supervisory authorities of the countries that are parties to the organisation. The IOSCO counts a total of 191 members, of whom 109 are ordinary, 11 associate and 71affiliate. They meet regularly to cooperate in promoting high standards of regulation; to exchange information on their respective experiences; to establish standards and effective surveillance of international securities transactions; and to provide mutual assistance to promote the integrity of the markets through rigorous application of the standards and effective enforcement against offences.

[22] Article 5 (2).

[23] With this in view, recital 21 limits the summary to 2 500 words. It has been argued that this limitation may prevent issuers from including relevant information in a more comprehensible way, obliging retail investors to use the marketing material to find more easily the information they are interested in.

to the current rules are needed in order to simplify the prospectus and ensure a more harmonised approach among different categories of products[24].

We are open to further debate in order to assess the effectiveness of the summary in reaching, in all cases, the objective to deliver a fully understandable and useful representation of the products' main features in the perspective of retail investors and would welcome views on this matter, in particular from SMEs, investors and consumers. We would also welcome views on whether a "Key Investor Information approach" such as the one followed under the UCITS IV proposal[25] would be a suitable alternative.

Do you agree with this analysis? Do you have any suggestion in this regard?

4.2. Disclosure obligations for retail investment products

In particular, the Commission is analysing the effectiveness of pre-contractual product disclosures produced for certain categories of 'packaged' retail investment products (such as structured securities or closed end funds), including their likely performance, any direct and indirect costs (also, as far as practicable, when they are embedded in the structure of the product or when there are multiple layers of cost resulting from the use of wrappers), the pay-off profile, the financial risks and the conditions of any capital guarantees in order to allow the investor to take an informed decision. The need to adopt a format that is more conducive to a clear understanding of the core characteristics of the products could be considered as part of the analysis.

In this debate, careful consideration should be given to the relationship between the function of the prospectus and the existing obligations of intermediaries (banks and investment firms) to ensure at the point of sale the appropriate level of information concerning the financial instruments, the risks associated with investments, the relevant costs and associated charges.[26] If modifications to the current framework are needed, it is important to consider the full picture of existing Directives aimed at protecting investors in order to direct any intervention in the most appropriate areas. These issues are currently being examined by the Commission services and will be reflected in a White Paper on Retail Investment Products to be published in the spring of 2009.

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[24] For instance, a comparison has been presented between UCITS requirements and prospectus requirements concerning structured products, in order to claim a detailed disclosure of costs, including implicit costs, especially in the case of prospectuses for complex financial instruments.

[25] Proposal for a Directive of the European Parliament and of the Council on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS).

[26] Proper information on financial instruments is ensured to investors (especially retail) by Article 19 (3) of MiFID Level 1 and Article 31 of Directive 2006/73/EC ("MiFID level 2"; also Recital 45 of the same Directive should be mentioned). In the perspective of ensuring adequate information on the nature of financial instruments and the risks associated with them, both MiFID Directives allow for the calibration of the information in the light of the nature of the client and the need to focus, depending on the circumstances, specifically on products rather than on their types.

4.3. Disclosure obligations for small quoted companies

In particular, concerns have been expressed that the disclosure requirements linked to the issuance of a prospectus could be overly burdensome and costly for small and medium size enterprises. This is mostly related to the exemption for offers with a total consideration below 2.5 million € set in Article 1.2 (h) of the Prospectus Directive. Small quoted companies consider that this threshold is too low and creates difficulties in raising funds in the EU. From a cost-benefit perspective they claim that it is not worth to raise capital below that threshold; above the threshold they are obliged to face the cost of producing a prospectus, which may be prohibitive taking into account their size.

The Commission services are determined to address this issue and propose, and seek views on, two alternative solutions:

a) the threshold of 2.5 million € could be raised;

b) a reduced amount of information could be required for the cases when a small quoted company offers equity to the public. This would result in the creation of a "mini" prospectus which might correspond better to the needs and size of small firms.

Do you agree with this analysis? Do you support any of the two alternative solutions mentioned? Do you have any other suggestion?

4.4. Disclosure requirements and Government Guarantee Schemes

In the context of the current financial crisis Member States have decided to guarantee the issuance of debt by banks. Due to the novelty of this scheme, uncertainties have been reported on the legal regime applicable to this type of offers concerning the information to be provided in the prospectus in relation to the State guarantor.

Article 5.1 of the Prospectus Directive sets out that the prospectus has to include information about the issuer, the securities and the guarantor of the offer. In accordance with the annex VI of the Prospectus Regulation, when an offer of securities is guaranteed by a third party, the issuer has to give in the prospectus information about the nature and scope of the guarantee and about the guarantor. In particular, the guarantor of the offer "must disclose information about itself as if it were the issuer of that same type of security that is the subject of the guarantee". In case the guarantor is a State, the information to be provided in the prospectus is contained in annex XVI of the Prospectus Regulation.

In accordance with Article 1.2 (d) the Prospectus Directive does not apply to securities unconditionally and irrevocably guaranteed by a Member State. However, in accordance with Article 1.3 of the Directive, the issuers benefiting from the guarantee of a State could opt to produce a prospectus, in order to benefit from the passport mechanism and make a multinational offer in the EU. In this case the prospectus must comply with the disclosure requirements mentioned above. The reason for the exemption foreseen in Article 1.2(d) of the Prospectus Directive is twofold: first, States are solid and very well known guarantors; second, the public

has constant access to sufficient information on the solvency and economic status of the States.

Member States should be treated differently from corporate guarantors, not least since important amounts of information concerning Member States (notably their public finances) are already public. Therefore, there is no added value in requiring the issuer to include in the prospectus the information about the State required by annex XVI of the Prospectus Regulation. Given that the aim of this proposal is to simplify and reduce administrative burden for firms, the Commission services intend to exempt issuers from providing additional information in cases where Member States act as guarantors.

Do you agree with this analysis?

4.5. Rights issues

Stakeholders have expressed concerns in relation to the obligation to publish a prospectus for rights issues or open offers, notably because of the fact that the cost for producing a full prospectus for this type of offer might not be justified. Stakeholders claim that due to the obligation of publishing a prospectus, rights offers have decreased since the entry into force of the Prospectus Directive.

In order to reduce the burdensome cost of the prospectus in this situation, it has been suggested that offer of rights could be exempted in Article 4 of the Prospectus Directive from the obligation to publish a prospectus, provided that a document is available containing information on the reasons for and details of the offer.

Do you agree with this analysis? Do you have any other suggestion?

4.6. Article 2(1)(d) — Definition of offer of securities to the public

Concerns have been expressed that there are divergences in the national implementation of the definition. The breadth and generality of the definition render it susceptible to varying interpretation in accordance with the specificities of national law. For example, it appears that some Member States have transposed the definition to include a requirement that a "public offer" must be a contractual offer under national law, while others do not do so. This is perfectly legitimate when the legal basis in EU law imposes the use of a directive, which allows a certain degree of latitude to Member States, provided that the spirit and the objective of the directive are met. For this reason, we do not recommend that the definition of offer to the public should be revised through a legislative amendment. A definition of this concept was introduced for the first time in EU law by the Prospectus Directive, and it has become the benchmark for the application of the Directive[27]. Moving a benchmark is always a delicate process, and we believe that prudence would be appropriate also in the case of the current definition of offer to the public, which seems to be capable of accommodating fairly well the different national laws of contract formation.

[27] The predecessor to the Prospectus Directive that regulated public offer prospectuses — Directive 89/298/EEC — did not define "offer to the public".

Nevertheless, in order to ensure an efficient functioning of the prospectus regime this definition should be understood in a convergent manner. The Commission will continue with its enforcement activities to remove inconsistent transpositions. Other points of legal uncertainty, identified by some stakeholders, should be also clarified. For example, it would clearly jeopardise the efficient functioning of securities markets if communications made in the course of normal secondary market trading were treated as offers to the public triggering the requirement for a prospectus, and any uncertainty on this point should be eliminated. We believe that guidance from the Commission and CESR level 3 are more effective tools to progressively remove the legal uncertainty on this issue compared to any legislative amendment[28].

Do you agree with this analysis?

4.7. Liability

Article 6(1) requires Member States to ensure that responsibility for the information given in a prospectus attaches to a clearly identified person (normally the issuer). Article 6(2) furthermore requires Member States to ensure that their laws on civil liability apply to the person responsible for the prospectus. Article 6(2) does not, however, provide for a harmonised liability regime under the Prospectus Directive. It is often argued that the same information is subject to different liability regimes, depending on the home Member State where the prospectus is approved, and possibly also on the Member State where it is being used, in case, under the relevant conflict of law rules, the host Member State's regime for civil liability applies[29]. The divergent intensity of the various liability regimes creates an un-level playing field; generates legal uncertainty since issuers may be liable for unexpected risks; and, consequently, may create a barrier to the effective use of the passport.

However, the constantly increasing numbers of passports notified among competent authorities since the implementation of the Prospectus Directive seem to suggest that issuers are coping quite well with the reality of a non-harmonised liability regime in the EU, and that they base their decisions on whether to approach investors in certain Member States on factors other than legal considerations on liability. Moreover, harmonisation of liability regimes is a far broader issue, deeply embedded in national civil law traditions. For this reason, it cannot simply be tackled in an isolated manner in the review of the Prospectus Directive: such an ambitious objective is outside the scope of this review, and can be achieved only in a longer time-frame.

Do you agree with this analysis?

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[28] In this context, for instance, the CESR has already made it clear that allocations of securities where there is no element of choice by the recipient are not considered "public offers" and fall outside the scope of the Directive. In reply to a specific question, the Commission has clarified that communications made in the course of normal secondary market trading should not be treated as offers to the public. Such communications should be regarded as integral to the trading of securities on a market, and the prospectus requirement in relation to that activity applies at the time of the admission to trading. It will not be triggered a second time unless there is a new event, such as an offer of those securities that is distinct from a normal trading activity. Furthermore, the Commission considers that the limited items of information made available on trading screens would not be sufficient to constitute a communication which falls within the definition of "offer of securities to the public".

[29] See, for instance, section 3.6 of the ESME report.

4.8. Equal treatment of shareholders

Concerns have been raised not only with respect to possible limitations to the range of investment opportunities, but also with respect to the general objective of equal treatment of shareholders. The Prospectus Directive gives issuers the right to choose the Member States where they want to make a public offer of securities, and does not cover the question of the equal treatment of shareholders. In this regard, the relevant piece of legislation is the Second Company Law Directive[30], which allows companies to restrict or withdraw the right of pre-emption, provided that this is done by a decision of the general meeting, and that certain other conditions are met. Currently, in listed companies the board can relatively easily restrict or exclude the pre-emption rights of shareholders in certain Member States because the different national rules on the organisation of general meetings have rendered it very difficult for "foreign" shareholders to participate in general meetings, and to voice concerns. In this respect, the Shareholders' Rights Directive[31], which improves the information rights of shareholders and their possibilities to cast votes in the general meeting, should improve the situation in the near future. In addition, we believe that the question of equal treatment of shareholders, though extremely pertinent, should be kept outside the scope of the Prospectus Directive, and therefore not be addressed in this review.

Do you agree with this analysis?

5. CONCLUSION

The current review suggests that the application of the Prospectus Directive is to be considered as broadly positive. In general, most market participants appear satisfied with the disclosure regime established by the Directive, and they consider it an important step towards the establishment of a single European securities market.

Notwithstanding this overall positive assessment, we have identified some elements in the Directive that create in practice unnecessary burdens and unjustified costs for companies and intermediaries. In the context of the Action Programme for reducing administrative burdens in the European Union, the Commission presents the proposal for amendment of the Prospectus Directive in an effort to improve and simplify the functioning of the prospectus regime.

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[30] Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent.

[31] Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies. To be transposed by Member States by 3 August 2009.