Securities and Markets Stakeholder Group

Date: 9 March 2018
ESMA22-106-911

ADVICE TO ESMA

Response to ESMA's Consultation Paper on draft regulatory technical standards under the new Prospectus Regulation

I. Executive summary

The SMSG welcomes the proposed RTS under the new Prospectus Regulation. We strongly believe that a successful review of the Prospectus rules should result in an increased level of investor protection and a true reduction of costs for issuers, without additional burdens imposed.

We believe that issuers should be given flexibility with regard to the number and format of the KFI to be included in the summary, e.g. flexibility to decide to include KFI extracted from the cash flow statement or not. The limit on the number of pages will already prevent unnecessary information being included in the summary.

Lastly, we recommend finding a balance between the technological evolution and state of the art solutions that could ease disclosure of information for investors and potential related issues in terms of security and liability for issuers.

II. Background

1. The role of the SMSG

1. The Securities and Markets Stakeholder Group (SMSG) advises ESMA on all regulatory and supervision matters. In compliance with EU Law, it is composed of expert representatives of financial market participants operating in the Union, of their employees, of consumers, of users of financial services and of independent top-ranking academics.

2. Purpose of this Advice

2. The SMSG welcomes the publication of ESMA's Consultation Paper on draft regulatory technical standards under the new Prospectus Regulation and wishes to comment on the issues set out below.

3. The SMSG believes that, in order to be successful, the review of the Prospectus rules should be designed in such a way that it improves investor protection by ensuring information produced is concise and understandable, while truly alleviating requirements and avoiding complexity of rules. Such complexity leads to excessive costs which discourages companies (especially smaller ones) from entering public capital markets, and results in disclosure of an excessive number of risk factors and boiler plate language not helpful to investors.

The SMSG recommends retaining flexibility for companies as this would allow them to better highlight to investors their distinct characteristics and features. Flexibility is also key to avoid duplication of information and make prospectuses more comprehensible. It takes on even more importance in the case of SMEs since they do not have as many resources to spend on disclosing information as large companies.

III. Summary of SMSG Views on ESMA's Consultation Paper on draft regulatory technical standards under the new Prospectus Regulation

1. Key financial information in the summary

4. The SMSG appreciates the intent of this review is to make summaries more relevant for investors and easier to understand by decreasing the length of these documents; however, the Group believes that certain new provisions may be unnecessarily prescriptive and could lead to increased legal costs for issuers.

5. In particular, the SMSG would suggest not to limit the number of KFI items, including alternative performance measures (APMs), but to leave flexibility to companies to:
    - determine the additional KFI they want to include in the summary; and
    - choose the format of presentation of the KFI.

6. As APMs are not clearly defined they may potentially be misleading for investors. Therefore, it is important to ensure a consistent methodology year by year is adhered to in order to allow for comparability.

7. Footnotes may be easily "overread" and it should be ensured that they do not contain material information or complex explanations that could hide important information from investors.

8. An alternative approach (bearing in mind the length limit for the summary) might be for issuers to include a prominent warning that the summary contains APMs and that investors should read the summary together with the rest of the prospectus (which will contain the relevant explanations in line with the ESMA Guidelines on APMs).

9. Flexibility would not lower investor protection because there would be no advantage for issuers to abuse this flexibility and display non-relevant KFI in numbers. The overall page limit of the summary will prevent unnecessary information being included in the summary.

10. Limiting the number of KFI could also raise liability issues by creating inconsistency between information disclosed in the summary, the prospectus and other reports and disclosures made public by the issuer, such as annual financial reports, registration documents, press releases, etc.

11. Furthermore, there is no specific piece of information that would be more meaningful or useful for retail investors. All information an issuer chooses to include in a summary is useful for a knowledgeable reader to make an investment decision and should be treated in the same way. However, the SMSG supports ESMA's view that the KFI position should correspond to the respective position in the issuer's financial statements and that (discretionary) APMs should not be given more prominence than the KFIs stemming from financial statements.

12. Cash flows from operating activities are expected to be in some degree recurrent for a business entity and thus they deserve special attention from the investment community. Nevertheless, cash flow from financing activities and cash flow from investing activities can be relevant for investors in certain equity securities, i.e. when the company is pursuing an acquisition strategy, when companies use significant hedging transactions (e.g. commodity companies) or for companies with high R &D expenditure and without significant revenues (e.g. Biotechs). Flexibility should be given to issuers to decide whether KFI extracted from the cash flow statement is relevant or not.

13. For credit institutions consideration should be given to the disclosure of the Supervisory Review and Evaluation Process (SREP) information and a measure related to the individual credit institution liquidity, such as the Liquidity Coverage Ratio (LCR) currently required by EU prudential regulation to monitor credit institution liquidity conditions.

2. Data and machine readability

14. The SMSG wishes to underline the fact that any new requirements regarding the collection of the data should not result in an increase of the administrative burdens and costs for the issuers.

3. Advertisements

15. The SMSG agrees that advertisements, other than oral advertisements, should contain a hyperlink to the specific page of the website where the prospectus was published or will be published.

16. It is also suggested that in written advertisements relating to securities aimed for retail investors, issuers should also include a statement encouraging / recommending such investors to seek prior advice from authorised / licensed financial intermediaries for the purposes of assessing suitability in accordance with their requirements and portfolio diversification.

4. Supplements

17. The SMSG believes that the proposal on the publication of audited financial statements by an issuer of retail debt or retail derivative securities should not trigger the obligation to publish a supplement. When an issuer holds information regarding its financial situation and its capacity to pay the interests or redeem bonds, for instance, this would be price sensitive information. Furthermore, pursuant to the provisions of MAR, the issuer would have to disclose without delay such information.

18. There is a divergence of views within the stakeholder group on the use of unaudited outstanding profit forecasts. A majority believe that these should not be included in the prospectus, regardless of the asset class. This is because forecasts are seen to be akin to a business plan and could be misinterpreted or could mislead investors in case they are not audited. The inclusion of unaudited profit forecasts could reflect badly on investor trust and could over time especially damage financing opportunities for all SMEs, as growth segments would suffer from a less robust reputation than the rest of the market.

19. Conversely there is a view that profit forecasts are a valuable part of the provision of issuer information in some member states and with a predicted fall in the amount of investment research there is a belief that the prohibition of profit forecasts in prospectuses would be to the detriment of investors when

making an informed investment decision. Where there is appropriate depth of due diligence and appropriate responsibility taken by the directors of an issuer, then the inclusion of unaudited forecasts should be at the discretion of the issuer.

5. Publication

20. The SMSG suggests considering technological evolution and state of the art solutions that could ease disclosure of information while ensuring it is useful for investors (apps, etc.).

21. As a principle and based on current practice, issuers of prospectuses are encouraged to look at all presentations and media formats in order to find solutions as to how the information can be made available.

22. Wide-spread electronic dissemination and storage of regulated information raise, however, issues in terms of security and liability that need to be addressed.

This advice will be published on the Securities and Markets Stakeholder Group section of ESMA's website.

Adopted on 9 March 2018

(Signed)

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