



WILMER, CUTLER & PICKERING

EU Financial Services Group Briefing

19 NOVEMBER 2002

PROPOSALS FOR A NEW PROSPECTUS DIRECTIVE: RAISING CAPITAL ACROSS BORDERS

Implementation of the Prospectus Directive, a cornerstone of the Financial Services Action Plan put forward to establish a fully integrated capital market in the European Union ('EU'), may be delayed beyond the anticipated date of June 2004. The proposed draft Directive will affect companies based within the EU as well as non-EU ('third country') firms. An amended proposal,¹ issued in August 2002 following the European Parliament's first reading, has addressed many concerns raised over the original May 2001 version. However, a number of measures put forward in the new proposal, in particular provisions that would effectively restrict a company's ability to choose the competent regulatory authority for a listing of its securities, face considerable resistance by several EU member countries. The Council reached a political agreement on a common position on the proposal at a meeting of EU Finance Ministers on 4 November 2002.² As a common position has now been agreed, the next step is that the proposal must go before the European Parliament again for a second reading, which is unlikely to occur before May 2003. However, the

agreed position does include the proviso that each Member State will have a transitional period of five years to implement the proposal.

THE AIM OF THE PROPOSED DIRECTIVE

Unrestricted access to capital is a vital foundation for a fully integrated single EU financial market. The proposed Directive would introduce harmonised standards for the public offer of securities and admission to trading throughout the European Union. Implementing a Financial Services Action Plan priority, the proposed Directive would overhaul the two existing directives covering this area — on listing particulars³ and on the public offer of securities.⁴

Securities issuers would obtain a pan-European 'passport,' based on (i) enhanced disclosure standards in line with IOSCO standards for the public offering of securities and (ii) "Home State" competent authority approval of admission to trading and the

¹ Amended Proposal for Directive on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC, COM (2002) 460 Final.

² IP/02/1607.

³ 80/390/EEC.

⁴ 89/298/EEC.

WILMER, CUTLER & PICKERING

prospectus. On this basis, listing could then take place in any other EU Member State, after a simple notification of the approved prospectus to the “Host State.” More generally, disclosure standards in line with IOSCO rules will also facilitate trading on global financial markets on the basis of a single set of requirements.

The proposed Directive would also define a “public offer.” Currently there is no common definition, which leads to a disparity of treatment among EU member countries. For example, some member countries define offerings *qualifying as a “public offer” in other jurisdictions* as private placements for which no prospectus is required, while others require a prospectus meeting local requirements.

THE SCOPE OF THE PROPOSED DIRECTIVE

The proposed Directive applies to securities that are (i) offered to the public or (ii) admitted to trading on a regulated market.⁵

The wholesale market and other exemptions.

The amended proposal, in response to fairly widespread comment and criticism of the earlier draft, acknowledges that wholesale, or purely inter-professional business, whilst within the scope of the Directive, requires a lighter touch. The proposed Directive therefore would provide that:

- an offering addressed to “qualified investors” shall not be considered an offer of securities to the public and therefore not be subject to the Directive. The proposed Directive includes within the definition of qualified investors authorised or regulated firms, government and national bodies, legal entities not classed as small or medium sized, and natural persons meeting certain experience and financial criteria who request to be treated as such; and
- the content of the prospectus in the event of admission of non-equity securities of denom-

inations of at least €50,000 to trading should be adapted where the investor is to be another professional so that no summary of the prospectus (see below) is required.

Other types of offers excluded from the obligation to publish a prospectus include:

- offers of securities addressed to less than 100 natural or legal persons (though not qualified investors) within each EU Member State (those offers are not considered to constitute offers to the public);
- offers of securities with a total consideration of less than €2.5 million (also not considered to be public offers);
- offers of securities in connection with a take-over or merger (exempted from the obligation to publish a prospectus);
- offers of securities which have been already listed on a regulated market in another Member State; and
- employee share schemes (likewise exempted from the obligation to publish a prospectus).

THE PROSPECTUS

Prospectus requirements. The proposal in the May 2001 draft Directive to require a three-part document has been replaced by a measure that gives issuers the choice between a single document or a set of documents. A set of documents consists of a two-part prospectus including a registration document (describing the issuer) and a securities note (containing information about the securities). In all cases a summary of not more than 2,500 words is required, written in “*non-technical language*” accessible to the ordinary investor.⁶

⁵ ‘Regulated market’ as defined in the 1993 Investment Services Directive.

⁶ See Article 5 of the proposed Directive.

Frequent issuers and those who programme their offers may elect to use a basic document plus supplements.

To ensure investor protection an issuer would be required to update, at least annually, the information that a prospectus or registration document must contain about a company. An earlier proposal to require annual shelf registration has been dropped in the face of widespread criticism of the burden this would place on small and medium sized companies (SMEs). However, the updating requirements in the amended proposal would extend to SMEs, although they are limited to reporting annual financial statements.

Concerns with national investor protection standards. The proposed Directive is a ‘maximum harmonisation’ directive. This means that national regulatory authorities cannot add requirements to the prospectus beyond what is included in the Directive. In the words of draft Article 17, “*competent authorities of host Member States shall undertake no approval or administrative procedures related to prospectuses.*” The UK Financial Services Authority has raised concerns that core UK investor protections could be lost, as they go beyond the requirements of the Directive. Arguably, the UK has the strictest listing regime in the EU, including corporate governance codes and the FSA is concerned that these codes would no longer apply on implementation of the Directive. However, the political agreement reached in November 2002 includes the suggestion that member states be able to apply their own national regimes to small offers made by SMEs and offers made by credit institutions in general.

THE “HOME STATE” PRINCIPLE

Provision of a single passport. The proposed Directive largely concentrates responsibility for approving the issue of securities with the competent authorities of the issuer’s Home State. Unlike the regime currently applicable under the Directives on listing particulars and public offers of securities, Host State regulators will no longer have any right to intervene in the approval process for a prospectus issued in another Member State or to request that any additional information be included in the prospectus when it is issued within their jurisdiction. Instead, a

simple notification by the Home State, including a certificate of approval stating that the Directive has been complied with, will allow multiple EU listings.

This principle of Home State control has extended to language requirements. Host States may not require full translations of prospectuses, but only of the summary section, provided that the full prospectus is drafted in a language which is customary in the sphere of finance (usually English).

New limits on choice of Home State. Under the proposed Directive, an issuer’s Home State would typically be the EU member country in which it has its registered office. Currently, issuers can choose the EU member country authority they wish to approve a prospectus. This can be the country where the registered office is located, the country where the offer will be made, or the country where the securities will be admitted to trading on a regulated market. Thus, the approach to definition of an issuer’s Home State under the proposed Directive is much more restrictive. It has garnered a great deal of criticism both from business and Members of the European Parliament (EP). Chief amongst industry complaints is the view that allocating the regulator by country of registration may throw firms into the jurisdiction of a local regulator that may have little or no knowledge or experience of the instrument concerned. At a hearing of the EP monetary affairs committee in October this year, Chris Huhne, the EP *rapporteur* for the proposed Directive, took the view that his committee would likely propose amendments on this point in its second reading of the proposed Directive. As noted at the outset, Member States were divided on this issue, with the potential of a blocking minority being formed on this point within the Council.

In this context, it is worth noting that, as of 5 November, the Council has adopted a different approach. Under the previous draft of the Directive, the ability of an issuer to choose its Home Member State *for issues of non-equity securities (i.e., high value bond issues)* depended on a denomination threshold of at least €50,000. Only where the denomination reaches at least this threshold was the issuer able to elect as his home Member State either the state: (i) where the issuer is registered; (ii) where the securities were or are to be admitted to trading on a regulated market; or (iii) where the securities are offered to the public. Otherwise, the

proposed Directive made provision for the Home State to be the country where the issuer has its registered office (EU issuers), or where the first application for admission to trading is made (third country issuers). This threshold amount has now been reduced to a minimum denomination of €5,000, which reduction preserves the status of Luxembourg as the listing jurisdiction of choice for such specialised issues as Eurobonds.

ISSUERS FROM NON-EU COUNTRIES (INCLUDING THE US)

Third-country issuers will have to register and file shelf documentation with the regulator in the EU member country in which the securities are to be offered. This regulator will have authority to approve prospectuses, *i.e.*, be deemed the 'Home State' for purposes of the Directive. The Home State may recognise the rules applicable to the issuer in the third country in which it is subject to regulation, provided that they require generally equivalent information, notably in compliance with IOSCO disclosure standards.

* * * *

For further information on this or related topics please contact Wilmer, Cutler & Pickering in:

London - 4 Carlton Gardens, Pall Mall
London SW1Y 5AA

Simon Firth +44 (20) 7872-1036
Simon.Firth@wilmer.com

James Greig +44 (20) 7872-1040
James.Greig@wilmer.com

David Capps +44 (20) 7872-1080
David.Capps@wilmer.com

Alix Prentice +44 (20) 7872-1064
Alix.Prentice@wilmer.com

Brussels - Rue de la Loi 15 Westraat
Brussels B-1040

Christian Duvernoy +32 (2) 285-4906
Christian.Duvernoy@wilmer.com

This document is for general informational purposes only and does not represent our legal advice as to any particular set of facts, nor does this document represent any undertaking to keep recipients advised as to all relevant legal developments. For further information on these or other financial services matters, please contact one of the lawyers:

James E. Anderson	+1 (202) 663-6180	Simon Firth	+44 (20) 7872-1036	Eric Mogilnicki	+1 (202) 663-6410
Philip D. Anker	+1 (202) 663-6613	James Greig	+44 (20) 7872-1040	Bruce Newman	+1 (212) 230-8835
Gregory A. Baer	+1 (202) 663-6859	Franca Harris Gutierrez	+1 (202) 663-6557	David Ogden	+1 (202) 663-6440
Robert G. Bagnall	+1 (202) 663-6974	Stephen R. Heifetz	+1 (202) 663-6558	Alix Prentice	+44 (20) 7872-1064
Brandon Becker	+1 (202) 663-6979	Kirk Jensen	+1 (202) 663-6182	Matthew P. Previn	+1 (212) 230-8878
Russell J. Bruemmer	+1 (202) 663-6804	Satish M. Kini	+1 (202) 663-6482	Victoria E. Schonfeld	+1 (212) 230-8874
J. Beckwith Burr	+1 (202) 663-6695	Michael D. Leffel	+1 (202) 663-6784	Marianne K. Smythe	+1 (202) 663-6711
David M. Capps	+44 (20) 7872-1080	Christopher R. Lipsett	+1 (212) 230-8880	Daniel H. Squire	+1 (202) 663-6060
Matthew A. Chambers	+1 (202) 663-6591	David A. Luigs	+1 (202) 663-6451	Natacha D. Steimer	+1 (202) 663-6534
David S. Cohen	+1 (202) 663-6925	Martin E. Lybecker	+1 (202) 663-6240	Todd Stern	+1 (202) 663-6940
Ricardo R. Delfin	+1 (202) 663-6912	James H. Mann	+1 (212) 230-8843	Manley Williams	+1 (202) 663-6595
Christian Duvernoy	+32 (2) 285-4906	David Medine	+1 (202) 663-6220	Soo J. Yim	+1 (202) 663-6958