THE
INVESTMENT
ASSOCIATION
INVESTMENT MATTERS

Review of the Prospectus Directive

The Investment Association's Response to the European Commission's Consultation Document

The Investment Association represents UK investment managers. We have over 200 members who manage more than £5 trillion for clients around the world. Our aim is to make investment better for clients so that they achieve their financial goals; better for companies so that they get the capital they need to grow; and better for the economy so that everyone prospers. Ultimately much of what they manage belongs to the man in the street through their savings, insurance products and pensions.

This document reflects The Investment Association's response to the European Commission's Review of the Prospectus Directive which was submitted on 13 May 2015 on the European Commission's survey webpage.

We do not respond to every question in the consultation but focus on those questions that are most relevant to our members as investors in securities listed in capital markets across Europe.

I. Introduction

1. Is the principle, whereby a prospectus is required whenever securities are admitted to trading on a regulated market or offered to the public, still valid? In principle, should a prospectus be necessary for:

√	• **Admission to trading on a regulated market**
√	• **An offer of securities to the public**
	• **Should a different treatment should be granted to the two purposes (i.e. different types of prospectus for an admission to trading and an offer to the public)**
	• **Other**
	• **Don't know / no opinion**

Additional comments on the principle whereby a prospectus is required whenever securities are admitted to trading on a regulated market or offered to the public:

The Commission should not introduce different types of prospectuses for an admission to trading and an offer to the public.

II. Issues for discussion

A2. Creating an exemption for "secondary issuances" under certain conditions

8. Do you agree that while an initial public offer of securities requires a full-blown prospectus, the obligation to draw up a prospectus could be mitigated or lifted for any subsequent secondary issuances of the same securities, provided that relevant information updates are made available by the issuer?

√	**Yes**
	No
	Don't know/no opinion

The Investment Association is a company limited by guarantee registered in England and Wales. Registered number 04343737. Registered office as above.

Justification
Equity - We do not believe that issuers should be required to issue a full-blown prospectus for secondary issuance. However, we do not support removing the obligation to produce prospectus altogether. Investors will typically have access to most of the relevant information as disclosed by the Issuer on an on-going basis under the TD and MAD.

Fixed Income - Where an Issuer is raising new money through an additional issue to be fungible with the original issue - a tap issue - the issuer should be required to produce a supplementary prospectus. There can be a significant time lapse between the original issue and subsequent issue and other differences such as the use of proceeds should be disclosed.

For both equity and fixed income instruments, issuers should be able to simplify their obligations by incorporating by reference any relevant information that has already been made publicly available under the TD and MAD requirements.

9. How should Article 4(2) (a) be amended in order to achieve this objective?

	The 10% threshold should be raised
	The exemption should apply to all secondary issuances of fungible securities, regardless of their proportion with respect to those already issued
√	**No amendment**
	Don't know / no opinion

Justification
There is no desire amongst investors to increase the threshold beyond 10%.

This threshold aligns with the maximum amount allowed under the UK Pre-emption Group Statement of Principles, which currently approves of placings for cash on a non-pre-emptive basis of up to 5% of ordinary share capital in any one year and up to 7.5% in any rolling three-year period. However, issuers can place up to 10% of ordinary share capital per year under specific and prescribed circumstances and following consultation with their shareholders.

The concept of pre-emption is widely acknowledged as a great strength of raising equity capital in the UK and investors value highly being consulted ahead of all non-pre-emptive placings above 5% in order to solicit their opinion and support. Issuers and advisors in turn appreciate the 10% flexibility in terms of speed and cost. The process overall ensures that any non-pre-emptive transaction is well received and priced favourably.

10. If the exemption for secondary issuances were to be made conditional to a full-blown prospectus having been approved within a certain period of time, which timeframe would be appropriate?

	One or several years
√	There should be no timeframe (i.e. the exemption should still apply if a prospectus was approved ten years ago)
	Don't know / no opinion

Justification

It is important to distinguish between an issuer coming to market with an initial public offering and an issuer that is already listed and is conducting a secondary offer. At IPO the level of disclosure should be higher as there is less information about the company that is available in the public domain.

However, for secondary issues, the company will have been subject to ongoing disclosure obligations under the Market Abuse Directive and the Transparency Directive. Requiring that this information is repeated in the prospectus for secondary issues detracts from the important new or offer-specific information. Reducing the amount of information required in the secondary offer by allowing issuers to incorporate by reference allows the prospectus to focus on the salient terms of the offer.

This information should be provided in simple language (not legal jargon) and presented in a way that is easily understandable to investors.

11. Do you think that prospectus should be required when securities are admitted to trading on an MTF? Please state your reasons

	Yes
	Yes, but only on those MTFs registered as SME growth markets
√	**No**
	Don't know/no opinion

Extending the scope of PD to MTFs would increase the barriers to issuance for issuers that desire a more flexible regime.

A6. Balancing the favourable treatment of issuers of debt securities with a high denomination per unit with liquidity on the debt markets

15. Do you consider that the system of exemptions granted to issuers of debt securities above a denomination per unit of EUR 100 000 under the Prospectus and Transparency Directives may be detrimental to liquidity in corporate bond markets?

√	**Yes**
	No
	Don't know/no opinion

Please justify your answer on whether the system of exemptions may be detrimental to liquidity in corporate bond markets:

Justification

The PD requires more disclosure from issuers of bonds with denominations below €100,000 creating a strong incentive for issuers to issue in denominations above €100,000. This was introduced to protect retail investors but has resulted in excluding retail investors from participating in a significant part of the market and removing a market participant that could be significant provider of liquidity.

For fund managers, the minimum denomination acts as a significant impediment when allocating a limited amount of new issue bonds across a range of funds. Eg. If a fund manager places an order for €1,000,000 on behalf of 5 funds but receives an allocation of €200,000 they would be unable to allocate across all the funds fairly.

The minimum denomination should be eliminated. Policy-makers should seek alternative measures to protect unsophisticated investors.

If so, what targeted changes could be made to address this without reducing investor protection?

MiFID II will significantly increase investor protections. Firms giving investment advice to clients will have to assess the suitability and appropriateness of any investment that they recommend to their clients. This will impact the way certain products are sold to retail clients.

Another, possible option is through product intervention. In the UK, the Financial Conduct Authority has restricted the promotion and sale of contingent convertibles to retail investors. Such an approach would help mitigate any concerns about the sale of structured finance instruments to retail investors if issued at lower denominations. However, any product intervention steps would need to be done following extensive consultation with market participants to ensure that there are no unintended consequences.

a) Do you then think that the EUR 100 000 threshold should be lowered?

√	**Yes**
	No
	Don't know/no opinion

Please specify to which amount (in euro) the EUR 100 000 threshold should be lowered:

€0

Please justify your answer on whether the EUR 100 000 threshold should be lowered:

Please see our responses to question 15 above.

b) Do you then think that some or all of the favourable treatments granted to the above issuers should be removed?

	Yes
√	**No**
	Don't know/no opinion

Removing the favourable treatments granted to issuers with a denomination of €100,000 and above would increase the costs for these issuers. This would act as a disincentive and, in the long run, may reduce bond issuance without any additional benefit for retail investors.

We are supportive of regulators seeking to protect retail investors. Regulators should look at alternative or better ways to achieve this objective. This should not be done through interventions or requirements that hamper the efficient functioning of capital markets.

c) Do you think that the EUR 100,000 threshold should be removed altogether and the current exemptions should be granted to all debt issuers, regardless of the denomination per unit of their debt securities?

√	**Yes**
	No
	Don't know/no opinion

Please see our response to Question 15.a above.

B2. Creating a bespoke regime for companies admitted to trading on SME growth markets

21. Would you support the creation of a simplified prospectus for SMEs in order to facilitate their access to capital markets financing?

	Yes
√	**No**
	Don’t know/no opinion

Facilitating financing of SMEs across Europe is a priority, however there is no investor appetite to see decreased disclosure or simplified prospectuses for SMEs listings on any regulated exchange.

B3. Making the “incorporation by reference” mechanism more flexible and assessing the need for supplements in case of parallel disclosure of inside information.

23. Should the provision of Article 11 (incorporation by reference) be recalibrated in order to achieve more flexibility?

√	**Yes**
	No
	Don’t know/no opinion

Please indicate how this could be achieved (in particular, indicate which documents should be allowed to be incorporated by reference):

The Investment Association would like to see greater use of incorporation by reference for financial information and constitutional documents. Issuers should also be able to incorporate by reference any and all regulatory filings made, voluntarily or otherwise, in accordance with the Prospectus and Transparency Directives. This information should made be electronically available on a website that is free to access by investors.

24. A) Should documents which were already published/filed under the Transparency Directive no longer need to be subject to incorporation by reference in the prospectus (i.e. neither a substantial repetition of substance nor a reference to the document would need to be included in the prospectus as it would be assumed that potential investors have anyhow access and thus knowledge of the content of these documents)?

	Yes
√	**No**
	Don’t know/no opinion

B4. Reassessing the objectives of the prospectus summary and addressing possible overlaps with the key information document required under the PRIIPs Regulation

27. Is there a need to reassess the rules regarding the summary of the prospectus?

√	**Yes, regarding the concept of key information and its usefulness for retail investors**
√	**Yes, regarding the comparability of the summaries of similar securities**
√	**Yes, regarding the interaction with final terms in base prospectuses**
	No
	Don’t know/no opinion

Please provide suggestions for re-assessment of the concept of key information and its usefulness for retail investors:

Retail investors would benefit from a Key Information Document ("KID") style summary, which presents key information and risk factors in a succinct and clear format. In any case, this should include the top 10 risk factors.

Please provide suggestions for re-assessment of the comparability of the summaries of similar securities:

The goal of the prescribed format summary is to increase comparability of different securities. However, this prescribed format is very difficult to understand.

For equity instruments, the prospectus summary is too long, repetitive and generic. It does not achieve the goal of providing the key information that investors need to make their investment decision. This not only damages retail investor understanding, but also impacts institutional investors abilities to perform their due diligence.

The Investment Association recommends a more free-form approach for equity prospectuses. Issuers should be required to ensure that the information contained in the summary is fair, balanced and understandable.

There should be more standardisation for fixed income instruments. Eg. Consideration could be given to the covenants that should be contained in the summary of the prospectus. However, there should be enough flexibility to ensure that the information is issue-specific.

Please provide suggestions for re-assessment of the interaction with final terms in base prospectuses:

No Comment

Please justify your answer on the possibility to reassess the rules regarding the summary of the prospectus:

The UK Corporate Governance Code requires that "the board should present a fair, balanced and understandable assessment of the company's position and prospects." This assessment extends to interim and other price-sensitive public reports and reports to regulators as well as to information required to be presented by statutory requirements

The Investment Association recommends that a similar approach should be adopted for prospectuses, including the summary. This will help focus the minds of issuers to ensure that the summary, registration document and the securities note, provide the information that is required under each section and at the same time ensures that investors are given a clear, issue and issuer-specific picture and are able to understand the company's prospects. Such approach to disclosure of information should also help stem the rise in generic risk factors that are currently prevalent in prospectuses.

B5. Imposing a length limit to prospectuses

29. Would you support introducing a maximum length to the prospectus? If so, how should such a limit be defined?

	Yes, it should be defined by a maximum number of pages
	Yes, it should be defined using other criteria
√	**No**

	Don't know/no opinion

Justification

At the moment, prospectuses are unduly long and contain too many generic or boiler plate risk factors that do not aid investor understanding. However, we do not believe that limiting the length of the prospectus will address this issue.

Issuers are liable for what is contained in prospectuses, and a strict limit could risk them being required to leave out relevant information that they are later held accountable for. This would benefit neither the issuer nor the investor. Instead, greater efforts should be made to ensure that the information contained in prospectuses is relevant and useful to investors. For example, we would welcome efforts to reduce the number of generic risk factors in the prospectus and to implement a requirement to include them in a declining order of relevance.

As noted in question 27, all issuers should be required to ensure that their prospectus presents a fair, balanced and understandable assessment of the company's position and prospects.

C1. Streamlining further the approval process of prospectuses by national competent authorities

34. Do you see a need for further streamlining of the scrutiny and approval procedures of prospectuses by NCAs? If yes, please specific in which regard.

√	**Yes**
	No
	Don't know/no opinion

Many equity investors feel that a prospectus is not available early enough in the IPO timetable for them to be able to build their models and prepare ahead of management meetings.

Similarly, fixed income investors state that they are not getting prospectuses on a timely basis to ensure that they have enough time to go through the terms and conditions before they place an order. This is of particular importance to insurers that apply the Solvency II Matching Adjustment (MA) to their portfolios. The MA sets out asset eligibility criteria that insurers need to consider before investing in a fixed income instrument. However, if insurers do not receive this information, which is contained in the prospectus, with enough time to assess the asset eligibility they will have no choice but purchase the instrument in the secondary market at a premium.

One way to address the availability of prospectuses is by addressing the complexity and delay experienced during the approval process.

C2. Extending the base prospectus facility

40. Please indicate if you would support the following changes or clarifications to the base prospectus facility. Please explain your reasoning and provide supporting arguments:

a) The use of the base prospectus facility should be allowed for all types of issuers and issues and the limitations of Article 5(4)(a) and (b) should be removed:

√	**I support**
	I do not support

Justification

It is crucial that the IPO process ensures that investors can understand the investment case and value the asset appropriately. If structured akin to a US registration statement in a non-offering format, the base prospectus facilities could be very useful in eliminating this information asymmetry. It will also enable investors to be better prepared for the management roadshow and to give more incisive feedback on the company and its valuation ahead of setting a price range, so improving the price discovery process for all parties.

The provision of research is also an important component of the IPO process. While pre-deal research prepared by syndicate analysts is still seen as valuable by investors, it is important to increase the ability for non-connected independent analysts to access information and publish research before pricing. The extension of the base prospectus facility to equity securities would also be useful in this regard.

b) The validity of the base prospectus should be extended beyond one year:

	I support
√	**I do not support**

Issuers should be allowed to update their base prospectus when they publish their annual financial statements. Therefore 12 month validity is logical.

c) The Directive should clarify that issuers are allowed to draw up a base prospectus as separate documents (i.e. as a tripartite prospectus), in cases where a registration document has already been filed and approved by the NCA:

√	**I support**
	I do not support

Issuers should have flexibility in how they structure their documentation, so long as all the relevant documentation is publically and electronically available to investors.

e) The base prospectus facility should remain unchanged:

	I support
√	**I do not support**

The base prospectus facility should be extended to all types of issuers and issues as a way of delivering company and security relevant information earlier in the process.

44. Should a single, integrated EU filing system for all prospectuses produced in the EU be created?

√	**Yes**
	No
	Don't know/no opinion

The Investment Association is supportive of a pan-EU filing system for all securities that are subject to the Prospectus, Transparency and Market Abuse Directives. To ensure that it is workable across all member states, we would propose that each NCA develops a filing system for all relevant documents that would be then integrated into a pan-EU filing system that is run by ESMA.

50. Can you identify any modification to the Directive, apart from those addresses above, which could add flexibility to the prospectus framework and facilitate the raising of equity and debt by companies on capital markets, whilst maintaining effective investor protection?

√	**Yes**
	No
	Don’t know/no opinion

As discussed in Q.40, publishing an approved prospectus earlier in the IPO process, complete apart from price range information, will enable investors to be better prepared for the roadshow and to give more incisive feedback on the company and its valuation.

This can be achieved through the elimination of a market practice known as the “research blackout period” - the practice of separating connected pre-deal research and the company prospectus. The PD can assist by providing a regulatory clarification that there is no need to separate pre-deal research from the publication of the prospectus or by creating a “safe harbour” for pre-deal IPO research distributed alongside the prospectus to authorised institutional investment firms.

We also would like to see a PD clarification on the flexibility of IPO price range. Price range revisions are very uncommon in the UK and Europe. This rigidity creates an unhelpful environment for a fair ultimate price discovery.