Deutsches Aktieninstitut

Flexibility Is A Must

The framework of the Prospectus Regulation already poses very stringent requirements for market participants – further restrictions need to be avoided

Deutsches Aktieninstitut's response to the ESMA consultation on draft RTS under the new Prospectus Regulation, 9 March 2018.

Introduction[1]

Deutsches Aktieninstitut (transparency register number 38064081304-25) represents the interests of publicly traded companies, banks, stock exchanges and investors in Germany since 1953. Its members represent 80 percent of the market capitalization of stock corporations listed in Germany. Deutsches Aktieninstitut keeps offices in Frankfurt am Main, Brussels and Berlin (www.dai.de).

Deutsches Aktieninstitut very much welcomes the intention to facilitate capital market access while ensuring adequate investor protection. Strengthening capital markets in Europe has become even more importantly against the background of the decision of the United Kingdom to leave the European Union. Unfortunately, we see the achievements of the objectives of the revision of the prospectus law jeopardized.

The objective was to reduce for all issuers administrative burdens and costs that seem unnecessary and to make the regime more appropriate for small and medium-sized enterprises and companies with reduced market capitalisation. In order to achieve these goals, it is necessary to allow issuers flexibility. Hence, the introduction of additional restrictions based on assumptions of investors interests should be avoided. A sufficient framework has already been established at level 1 in order to ensure the comparability of the different prospectuses. Now it is therefore important for issuers to have sufficient flexibility to provide only the information that is appropriate for their securities.

Furthermore it should not be overlooked that there have also been introduced new burdens on level 1 such as the limitation of the number of risk factors and the risk categorization. In order to achieve the above mentioned objectives, the new burdens on level 1 must be compensated on the one hand and, on the other hand, further alleviations need to be achieved.

The page limit imposed for the summary by the prospectus Regulation is a very stringent requirement. Companies consider that this requirement suffice to ensure that summaries remain short, useful and user-friendly. There is therefore no rationale for imposing a fixed number of additional lines available besides the mandatory templates for the description of KFI. The alternative performance measures (APMs) included in a prospectus may vary from one case to another, the

[1]This position paper summarizes the response of Deutsches Aktieninstitut to the consultation of European Securities and Markets Authority (ESMA) on draft RTS under the new Prospectus Regulation (ESMA31-62-802), https://www.esma.europa.eu/press-news/consultations/consultation-draft-rts-under-new-prospectus-regulation.

issuer should be able to include as many additional lines as required to describe all – but no more than – the APMs contained in the main body of the prospectus. As illustration, a company using four APMs in its financial communication (annual and half-yearly announcements, roadshows) and mandatory filings (annual and half-yearly financial reports) will have to lose one APM in the summary of its prospectus, creating thus inconsistency between the prospectus summary and other financial material disclosed and made available to the public throughout the year.

Companies consider that the best way forward would be to give flexibility to companies to:

- determine the additional KFI they want to include in the summary and
- to choose the format of presentation of the KFI.

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. Once again, the overall 7-page limit of the summary will prevent any unnecessary information to be included in the summary.

Limiting the number of items that can be included as KFI in the summary could also raise issues in terms of liability. As stated by recital 33 of the Prospectus Regulation: "*No civil liability should be attached to any person solely on the basis of the summary, including any translation thereof,* ***unless it is misleading, inaccurate or inconsistent with the relevant parts of the prospectus****, or* ***where it does not provide****, when read together with the other parts of the prospectus,* ***key information*** *in order to aid investors when considering whether to invest in such securities.*" This is reflected in the warning that must be included in each summary pursuant to article 7(5) of the Prospectus Regulation.

Bearing also in mind the 7-page limit, it would appear that one single table regrouping all KFI from the profit and loss statement, the balance sheet and the cash flow statement could be another option to help save space. Therefore, issuers should also be allowed to choose the format of presentation of the KFI.

1 Key financial information in the summary

Question 1:

Do you agree that the KFI extracted from the issuer's historical financial information should be sign-posted?

No comment.

Question 2:

Would you suggest the inclusion of specific templates for other types of issuer? Please specify and explain your reasoning.

We would not suggest the inclusion of additional specific templates. However we would like to stress, that issuers should be given express flexibility to add information. This should especially apply to holding entities consolidating subsidiaries that are active in different sectors e.g. the financial sector and non-financial sector or insurance, asset management and banking. The same applies to conglomerates.

Question 3:

Do you agree that cash flow from operations is the most useful measure of cash flow for non-financial entities issuing equity and that cash flow from financing activities and cash flow from investing activities are not so relevant for investors in equity securities?

No, companies disagree with ESMA's statement that cash flow from financing activities and cash flow from investing activities are not so relevant for investors in equity securities of non-financial entities. Both cash flows from investing and financing could be relevant to investors considering the opportunity to invest in a company pursuing, for instance, an acquisition strategy, in companies operating activities using commodities where significant cash flows would stem from hedging transactions with derivative instruments or Biotech companies. Again, we would like to insist on the need to give flexibility to issuers to decide whether KFI extracted from the cash flow statement are or not relevant to include in the summary of the prospectus (Please refer also to our preliminary comments).

Question 4:

Given the page limit for the summary please provide your views on which items of historical financial information would be most useful for retail investors.

The 7-page limit imposed for the summary by the prospectus Regulation is a very stringent requirement. This requirement suffices to ensure that summaries remain short, useful and user-friendly because there is not enough space to include unnecessary information. There is therefore no rationale for imposing a limitation regarding the number of key financial information (KFI), including alternative performance measures (APMs), nor any benefit to be gained from such measure.

In addition, due to the limitation, information that is meaningful or useful to investors may be missing. 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.

Companies consider that the best way forward would be to grant issuers the flexibility to include any KFI they deem necessary. 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 (e.g.: annual financial reports, registration documents, press releases…).

Question 5:

Do you agree with the proposal to allow the use of footnotes to describe APMs or could this result in lengthy footnotes and complicated explanations?

We do not agree with the proposal to use footnotes to explain/reconcile APMs in prospectus summaries. Generally speaking, it is not possible to draft summaries that comply with ESMA Guidelines on APMs and that also meet the requirements of the Prospectus Regulation (in particular as regards the page limit). As a result, ESMA Guidelines must be rephrased so that it is sufficient for APMs used in the summary to be defined/explained/reconciled elsewhere in the prospectus, or the level 2 text must allow referenced in the summary for that purpose.

Question 6:

Do you agree that issuers should be given flexibility to present pro forma financial information as additional columns to the relevant tables or as a separate table? If not, should a format be mandated, bearing in mind the page limit for the summary as well as the requirement for the summary to be comprehensible?

Yes, issuers should be given flexibility to present pro forma financial information. Furthermore, we question the need to require to disclose pro forma adjustments (paragraph 48 of the consultation paper and paragraph 5 of article 2 of the draft RTS). Including pro forma adjustments would result in lengthy tables that would not be consistent with the requirement to ensure that the summary remains short: where an issuer decides to add columns, this obligation would result in 2 additional columns (a pro forma adjustments column and pro forma KFI column). Once again, we stress the fact that the summary is an introduction to the prospectus. Therefore, only key pro forma financial information should be included in the summary. Investors will find all details regarding pro forma information in the prospectus.

Question 7:

Do you agree that complex financial information in the summary should be presented according to its presentation in the prospectus? If not, please specify and provide alternative ways of presentation.

Yes, we agree that complex financial information in the summary should be presented according to its presentation in the prospectus.

Question 8:

Which financial measures are most useful for retail investors to determine the health of a credit institution? Do you consider that the CET1 is comprehensible for retail investors? Please specify.

No comment.

Question 9:

Do you agree that it should be mandatory for credit institutions to disclose SREP information in relation to Common Tier One Equity, the

minimum prudential capital requirements, the Total Capital Ratio and the Leverage Ratio in the summary?

No comment.

Question 10:

Do you agree with the choice of measures for insurance companies?

We agree in general with the choice of measures for insurance companies. However, the definitions provided for IFRS based KFIs cannot apply to KFIs based on local GAAP. Issuers have to be provided with the flexibility to name the corresponding KFIs in accordance with the local GAAP.

The same flexibility has to be provided when it comes to the definitions of the APMs. Entities must be allowed to use their own APMs that correspond to the named APMs in the Annex. As there are no binding definitions of these APMs, issuers must be allowed to continue to use their existing APMs.

It has to be stressed that issuers cannot be bound to change their existing APMs due to prospectus requirements. They must be able to use their APMs in line with their financial reporting.

Question 11:

Do you think it would be useful for retail investors to include a measure of historical performance for closed end funds in the summary?

No comment.

Question 12:

Do you think that investment companies which are subject to capital requirements should be required to include regulated capital ratios in their summary?

No comment.

Question13:

Would the issuer, offeror or person asking for admission to trading incur costs if the proposed provisions are adopted? If so, please specify the nature of such costs, including quantifying them.

The European Commission in the Refit Scoreboard Summary published in October 2017 claims that the review of the prospectus directive could allow savings of approximately 130 million euros per year stemming from the secondary issuance regime and of around 45 million per year from the new EU Growth prospectus. We welcome these objectives and consider that one key element of success in meeting them is to allow for flexibility. Imposing stringent rules and templates that would not fit in all situations and be relevant for all issuers could generate additional costs in drafting prospectuses. Considering in particular the new requirements imposed for summaries (limitation in number of pages and risks) and potential liability issues (please refer to our preliminary comments), we fear that the fees of legal counsels drafting and reviewing prospectuses may rise significantly.

2 Data and machine readability

Question 14:

Do you believe that the data related to the amount raised should be made mandatory? Please explain your reasons.

No, we do not consider that the amount raised should be made mandatory. The amount raised is not required by the Prospectus Regulation- contrary to the ISIN of the securities, the LEI of the issuer or the guarantor or other information mentioned in article 47 of the Prospectus Regulation. Furthermore, the data mentioned in article 21 and 47 of the Prospectus Regulation shall be provided to ESMA at the same time as the Competent Authorities notify approval of prospectuses. The amount raised would not be known at the time of approval of a prospectus but after the closing of the offer or admission to trading of the securities. Requiring this piece of information to be provided would impose additional burden on the Competent Authority and also on issuers.

In addition, in those cases where for example notes, certificates or warrants are issued on the basis of final terms, they generally include a maximum amount that only relates to the maximum number of securities that an issuer may sell to investors. In most cases, this maximum amount is not fully used and is therefore no helpful information for investors.

Question 15:

Do you agree with the data items that have been identified as necessary for the purpose of classification as well as to allow for the compilation of the annual report under Article 47 of the Prospectus Regulation? Would you like to propose any additional items or suggest items that should in your view be deleted? Please explain your reasons.

We could agree with the data identified by ESMA as long as the collection of this data does not impose additional burden to issuers (Please refer to our answer to question 17). Nevertheless, we wonder which statistics ESMA could possibly draw from the language, the underlying or the maturity date of the securities. Furthermore, the purpose of the report mentioned in article 47 of the Prospectus Regulation is certainly not to replace statistic reports published by other institutions, including central banks and Eurostat.

When the number of submitted prospectuses and final terms is multiplied by the total number of fields in accordance with Annex VII (33 fields), then it is clear that the data collection will be very extensive. This means a higher burden to provide the relevant data, and this burden must not be imposed on issuers.

Question 16:

Do you agree with the ESMA proposal to maintain the current system in place whereby NCAs submit data to ESMA in XML format as the practical arrangement to ensure that such data is machine readable? Do you agree that, by keeping the data submission system unchanged, adaptation costs are minimised for the market at large?

We agree with ESMA's proposal to keep the XML format as a practical arrangement to ensure that data is machine readable. We insist again on the fact that the responsibility of the NCAs to provide the data in XML format should not be transferred to issuers. Such transfer would generate unjustified costs for issuers, in particular SMEs, and would be contrary to the objective to facilitate access to financial markets. Any future changes of the current system should be carefully assessed in terms of costs and benefits and should not result in imposing undue burden on companies.

Question17:

Do you agree that the proposed amendment to the technical advice on prospectus approval could contribute to provide clarity on the way data referred to in Annex VII are collected by NCAs?

No, we don't consider that the proposed amendment is appropriate. Companies are concerned that such an amendment would transfer the burden to collect the data to them whereas the responsibility to provide data to ESMA lies according to the Prospectus Regulation with the Competent Authorities. Companies would agree that when reviewing prospectuses, Competent Authorities are entitled to require some information that would not be public at the time of the approval but this should not result in a transfer of responsibilities to issuers. Furthermore, this data should be provided by issuers to the Competent Authorities in text format and not in XML format. It is the duty of the Authorities to deliver the data to ESMA in the appropriate format.

Question 18:

Do you have suggestions in relation to how the efficiency, accuracy and timeliness of the data compilation and submission process can be further improved? In your experience, is there any specific reporting format or standard that you would deem most appropriate in this context?

We would like to raise the issue of additional costs. As a matter of fact, ESMA included in the consultation paper, for each topic but this one, a question regarding additional costs that issuer, offeror or person asking for admission to trading would incur if the proposed provisions were adopted. Requiring issuers to provide additional data will certainly add to the administrative burden and the costs without benefits for issuers. Issuers also make their prospectuses available on their website and investors can also find these prospectuses on the websites of the Competent Authority, the stock exchange and eventually of the Officially Appointed Mechanism required by the Transparency directive. All these websites offer search functions. Furthermore, we don't believe that the reports which will be published by ESMA in accordance with article 47 of the Prospectus Regulation will have any impact on improving access to companies for investors or access to financial markets for companies. There is therefore no justification for imposing additional costs to issuers. This would be contrary to the objectives of the CMU and the objectives to save approximately 175 million Euros every year (Please refer to our answer to question 13).

3 Advertisements

Question 19:

Do you consider that an advertisement should contain at least a hyperlink to the website where it is published and where available and technically feasible additional information that would facilitate tracing the prospectus? Please provide examples of the additional information that you think would be helpful to include in the advertisement.

We agree 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. We don't see any additional information that would be helpful to include in advertisements.

Question 20:

Do you consider that the definition for complex securities set out in para 140 provides clarity to issuers and would be helpful in deciding when the comprehension alert referred to in Article 8(3)(b) of the PRIIPs Regulation should be included in an advertisement?

The PRIIPs Regulation contains under recital 18 the criteria to determine when an instrument should be qualified as "complex securities". Therefore, the definition of complex securities under MIFID 2 should not be used to determine what type of securities fall under the scope of PRIIPs or in other words, complex securities under MIFID 2 should not automatically be considered PRIIPs and vice-versa. Therefore, we do not consider that the definition set out in paragraph 140 of the consultation paper would be helpful as regards to when the PRIIPs Regulation's warning should be included in an advertisement.

Question 21:

Do you agree with the requirements suggested for Article 12 of the RTS? If not, please provide your reasoning.

Yes, we agree with the requirements suggested for Article 12 of the draft RTS.

Question 22:

In particular, do you agree with the requirement to include warnings in advertisements? Do you consider that the suggested warnings are fit for purpose in terms of investor protection?

Yes, we agree with the requirement to include warnings.

Question 23:

Would the issuer, offeror or person asking for admission to trading incur costs if the aforementioned provisions are adopted? If so, please specify the nature of such costs, including whether they are one-off or ongoing and, quantify them.

No, we do not foresee any significant new costs stemming from the proposed provisions. In this regard, if we consider that the proposed draft mainly follows, and carries over, the current requirements under Delegated Regulation EU 301/2016, there shouldn't be any additional burden from which we can assert new extra costs for the issuers, offeror or person asking for admission to trading.

4 Supplements

Question 24:

Do you agree that Article 2 of the First Commission Delegated Regulation should be carried over, in its entirety, to Level 2 under the new regime?

Yes, we agree that article 2 of Commission Delegated Regulation (EU) No 382/2014 should be carried over.

Question 25:

Do you agree that the additional requirements identified from ESMA's draft technical advice should also be included.

Yes, we agree that the additional requirements identified by ESMA regarding profit forecasts and estimates and changes in the working capital statement of the issuer of underlying securities of depositary receipts should be included in the draft RTS. However, regarding profit forecasts and estimates and in line with our answer to ESMA's 2017 consultation on format and content of the prospectus, we consider that especially bond issuers should have the flexibility whether to include an outstanding profit forecast in a prospectus. We welcome the idea to abandon the requirement to provide the audit /accounting report on profit forecast. This requirement is an unnecessary burden on issuers. Especially the necessary supplements increase this burden considerably. On the other hand, we question whether the audit reports are very useful for investors. The audit statement has no effect on the quality of the profit forecasts and estimates. The issuers themselves have a very high interest in the accuracy of the information.

Question 26:

Do you agree that the publication of audited financial statements by an issuer of retail debt or retail derivative securities should not trigger the requirement to publish a supplementary prospectus?

Yes, we agree that 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 per se. Material information about the financial situation of an

issuer, especially when it is relevant for the issuer`s capacity to pay the interests or redeem bonds, for instance, would be price sensitive information. Pursuant to the provisions of MAR, the issuer would have to disclose such information without delay. Compared to this relevant information, financial statements that are fully in line with market expectations are not (new) information relevant for investment decisions. Bearing in mind that especially debt base prospectuses are valid for 12 months, the publication of audited financial statements should therefore not systematically require the publication of a supplement.

Question 27:

Would the issuer, offeror or person asking for admission to trading incur costs if the aforementioned provisions are adopted? If so, please specify the nature of such costs, including quantifying them.

Considering that article 16 of the draft RTS mainly carries over the contents of article 2 of the Delegated Regulation (EU) No 382/2014, we do not expect additional costs for the issuer, offeror or person asking for admission to trading derived from the aforementioned provisions.

5 Publication

Question 28:

Do you agree that only Article 6(1)(c) and 6(3) of the Second Commission Delegated Regulation need to be carried over to Level 2 under the new regime?

Yes, we agree with ESMA's proposal to carry over only article 6(1)(c) and 6(3) of Commission Delegated Regulation (EU) 2016/301 should be carried over.

Question 29:

Do you agree that no other publication provisions of the new Prospectus Regulation need to be specified by way of RTS? If not, please identify the provisions which should be specified.

We would like to draw ESMA's attention on the fact that technology and in particular means of publication and dissemination of information have dramatically changed since the adoption and transposition of the 2003 Prospectus Directive. Wide-spread electronic dissemination and storage of regulated information raises issues in terms of security and liability that need to be addressed.

Question 30:

Do you believe that the proposed publication provisions will impose additional costs on issuers, offerors or persons asking for admission to trading? If yes, please specify the type and nature of such costs, including whether they are one-off or on-going, and quantify them.

No, we do not expect that the proposed publication provisions will impose additional costs on issuers, offerors or persons asking for admission to trading.

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