

The new Prospectus Regulation: Key features for equity issuers

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Overview

The long-awaited Prospectus Regulation (the Regulation), which repeals and replaces the Prospectus Directive (PD), was published in the EU Official Journal on 30 June 2017. The Regulation will come into force on 20 July 2017 (20 days after its publication) and will apply to all prospectuses approved on or after 21 July 2019. Certain of its provisions apply from an earlier date, however, including the two revised admission to trading exemptions (detailed below) which apply from 20 July 2017.

This article considers the changes that the new Regulation will make to the current prospectus regime for equity issuers.

The key changes for equity issuers include:

- **Admission to trading exemptions** – A new prospectus will not be required for the admission to trading of fungible shares representing less than 20% (up from 10%) of the same class of shares already admitted to trading on the same regulated market. The current conversion/exchange exemption has also been modified by the introduction of a cap, so that no prospectus will be required on admission of shares resulting from the conversion or exchange of other securities, providing that those shares represent less than 20% of the shares of the same class already admitted to trading (over a 12 months period.) Both of these changes are applicable from the date that the Regulation comes into force – 20 July 2017.
- **Offer exemptions** – No prospectus will be required for offers of securities with a total consideration in the EU of less than €1million (up from €100,000.) Also, individual Member States may exempt domestic offers where the total consideration of each offer in the EU is between €1million and €8million (up from €5million). Both of these changes are applicable 12 months after the Regulation comes into force – 21 July 2018.
- **Proportionate EU growth prospectus** – A new proportionate EU growth prospectus will be available for SMEs, mid-sized companies admitted to an SME growth market or for small issues (less than €20million) by non-listed companies.
- **Simplified disclosure regime for secondary issuances** – A new simplified disclosure regime will replace the current regime for pre-emptive offers. A simplified prospectus will be available for secondary offers where the issuer has had securities admitted to trading on a regulated market or an SME growth market continuously for at least the last 18 months.
- **Summaries** – The requirement for summaries to use the “elements” format has been removed and issuers will have more discretion over the information that they include. Summaries will be shorter - no more than 7 sides of A4 in most cases - and should only contain a maximum of 15 of the most material risk factors.
- **Risk factors** – The new Regulation introduces a more prescribed regime for risk factors. These must be limited to risks that are “specific to the issuer, and/or the securities and which are material for taking an informed investment decision.” The most material risks within each category must be mentioned first, with materiality based on “the probability of their occurrence and the expected magnitude of their negative impact.”
- **Universal Registration Document (URD)** – There will be a new form of shelf registration mechanism – the URD – for issuers admitted to trading on a regulated market or on a multilateral trading facility. After an issuer has had its URD approved by its competent authority for two consecutive financial years, subsequent URDs can then be filed without prior approval (though they will still be open to review by the competent authority.)

Background to the changes

In 2014, European Commission President Juncker kicked off the process of building a genuine EU [Capital Markets Union](#) (CMU) with a view to creating deeper, stronger and better capital markets in Europe to support jobs and growth.

A review of the prospectus regime was identified as a short-term priority under CMU and in February 2015, the Commission published a consultation looking at various aspects of the regime, including prospectus scope, form, content and approval process. This consultation was followed by the publication, in November 2015, of the Commission's legislative proposal for a new prospectus regulation to modernise the prospectus regime. This proposal was developed and debated by the EU institutions during the course of 2016, culminating in the publication of the Final Compromise Text on 16 December 2016.

The Regulation was published in the Official Journal on 30 June 2017 and will come into force on 20 July 2017 (20 days after its publication in the Official Journal). It will apply to all prospectuses approved on or after 21 July 2019 (two years after it comes into force) but certain of its provisions will be applicable from an earlier date (as detailed in "Exemptions from the requirement to publish a prospectus" below.)

Scope of new Prospectus Regulation

The basic triggers for the requirement to publish a prospectus are unchanged, namely: (i) an offer of securities to the public in the EEA; and (ii) admission to trading on an EEA regulated market.

In its initial consultation, the Commission did consider expanding the scope of the new regime to admissions of securities to multilateral trading facilities (MTFs) such as the Irish Stock Exchange Global Exchange Market. This proposal was not taken forward, however, and admissions to MTFs remain outside of the scope of the new Regulation.

There have also been discussions as to whether crowdfunding activities should fall within the scope of the prospectus regime. In 2016, the Commission concluded that there was not a strong case for EU wide regulation of crowdfunding at that time and this activity remains outside of the scope of the new Regulation. The Commission is, however, actively looking at this area as differing national regimes have been identified as a barrier to capital flows.

Format of Legislation

The changes to the regime are being enacted by way of an EU regulation, which has direct effect in each Member State, rather than by a directive, which requires individual Member States to pass their own implementing legislation. This should be helpful in achieving the goal of maximum harmonisation in the EEA as experience has shown that legislation with direct effect helps to avoid anomalies arising from separate implementation across Member States.

Certain elements of the Regulation need to be further specified in delegated acts to be adopted by the Commission. This must be completed no later than 18 months after it comes into force.

Key changes to the prospectus regime

Exemptions from requirement to publish a prospectus

- **Fungible securities:** A prospectus is not required under the Regulation for the admission to trading of securities representing less than 20% of the same class of securities already admitted

The basic triggers for the requirement to publish a prospectus remain unchanged

Revised admission
to trading
exemptions in
force 20 July 2017

to trading on the same regulated market (over a 12 months period). This is an increase from the 10% threshold under the PD. The PD exemption also only applies to “shares” whereas the provision in the Regulation has been expanded to cover all securities. This higher exemption threshold will apply immediately from the date that the Regulation comes into force – 20 July 2017.

- **Conversion/exchange:** The PD currently contains an exemption whereby no prospectus is required for the admission of shares resulting from the conversion, exchange or exercise of rights of other securities, provided that the resulting shares are of the same class as those already admitted to trading on the same regulated market. The Regulation maintains this exemption but introduces a cap on its use so that the number of new shares resulting from the conversion, exchange or exercise of rights must not exceed, over 12 months, 20% of the number of shares of the same class already admitted to trading. This change will apply immediately from the date that the Regulation comes into force – 20 July 2017.

In response to feedback to the Commission’s initial legislative proposal, the Regulation does, however, include a carve-out so that the 20% cap will not apply in specific circumstances. These include where a prospectus was drawn up in relation to the securities giving access to the shares, where those securities were issued before the date that the Regulation comes into force or where the resulting shares qualify as Common Equity Tier 1 (i.e. the shares result from the conversion of certain capital instruments issued by banks in the event that the bank’s capital ratios fall below set levels.)

The Regulation also expressly states that this conversion/exchange exemption can be combined with the 20% fungible shares exemption (see above). This is prohibited, however, if combining the exemptions could lead to the admission to trading without a prospectus of more than 20% of the shares of the same class already admitted, over a 12 months period. There is no equivalent restriction in the PD.

- **Small offers:** A prospectus will not be required for offers of securities to the public with a total consideration in the EU of less than €1,000,000 calculated over a 12 months period. This is an increase from the current threshold under the PD of €100,000. In addition, offers below this threshold are now entirely outside of the scope of the Regulation (as opposed to just being exempt, as was the case under the PD.) To ensure that Member States do not impose their own prospectus requirements in these circumstances, the Regulation specifically prohibits this but does allow Member States to introduce other disclosure requirements, provided that they are not disproportionate. This change will be applicable 12 months after the Regulation comes into force – 21 July 2018.
- **Higher offer threshold:** Offers with a total consideration in the EU of less than €5,000,000 are currently outside of the scope of the PD. This means that Member States can impose their own requirements for a prospectus in relation to offers below that level (though the UK has not done this.) In contrast, the new Regulation gives Member States the option to exempt offers where the total consideration of each offer in the EU does not exceed €8,000,000 over a 12 months period. However, this voluntary exemption only applies to domestic offers in the relevant Member State (i.e. those that do not require passporting.) Member States must notify the Commission and ESMA whether and at what monetary threshold they intend to exercise this discretion. This change will be applicable 12 months after the Regulation comes into force – 21 July 2018.

In practice, this change will mean that EU offers between €1,000,000 and €8,000,000 may or may not require a prospectus depending on (i) whether that offer is domestic or cross-border and, (ii) if domestic, the exemption threshold set by the relevant Member State in which the offer is being made. The fact that each Member State may impose national disclosure requirements for offers below its own exemption threshold adds to the uncertainty that will exist for offers falling within this monetary range.

- **Takeover/Merger exemption:** As is the case under the PD, the Regulation exempts securities offered in connection with a takeover or a merger/division from the requirement to publish a prospectus. However, a condition of the exemption under the PD is that a document regarded by the relevant competent authority as “equivalent” to a prospectus is available. This means that any such document has to be vetted by the relevant competent authority. In contrast, the Regulation still requires a document containing information “describing the transaction and its impact on the issuer” to be available but it does not specify any equivalence requirement. The minimum information to be included in this document has yet to be established, however, and so we must wait and see what the document approval process will involve.
- **Employee exemption:** To ensure equal access to employee share schemes, the employee exemption in the Regulation no longer differentiates between employer companies established in or outside the EU (as was the case under the PD.) The Regulation exempts securities offered to directors or employees by their employer (or an affiliate) provided that the securities are of the same class as those already admitted to trading on the same regulated market and that a document is available containing information on the securities and the details of the offer. The change to this exemption means that an “equivalence” decision relating to securities admitted to third country markets should no longer be required.

Simplified disclosure regime for secondary issuances

The reduced disclosure regime for secondary issuances has been expanded

The proportionate disclosure regime in the PD, (introduced by the 2010 Amending Directive), applies to certain pre-emptive secondary offerings of equity securities. Very few issuers have taken advantage of these reduced disclosure requirements, however, and for those that have, the European Commission believes that the regime does not go far enough and still requires unnecessary information to be disclosed.

Under the Regulation, the reduced disclosure regime for secondary issuances has been extended to cover not only shares, but also any securities where those securities have been admitted to trading on a regulated market or an SME growth market continuously for at least the last 18 months. Companies that issue more securities of the same class will have the option to make use of a “simplified” prospectus containing “reduced” information. The content requirements of the simplified prospectus will be set out in secondary legislation. The Regulation does specify, however, that financial information from the last 12 months will be required, as well as other items including a working capital statement, a capitalisation and indebtedness statement and the disclosure of relevant conflicts of interest and related party transactions.

Simplified disclosure regime for SMEs

One of the key political aims of CMU is to enable SMEs to gain easier access to capital markets. Although a proportionate disclosure regime for SMEs and companies with “reduced market capitalisation” was introduced in the PD in 2010, very few companies have taken advantage of this. Again, the Commission believes that this reduced regime in the PD does not go far enough and, therefore, the Regulation now includes an expanded and reformulated regime for SMEs.

The Regulation introduces the concept of the “EU Growth prospectus” – a proportionate disclosure regime for:

- SMEs;
- Mid-sized companies - less than €500 million 3 year average capitalisation with securities traded on an SME growth market or
- other issuers where the total consideration of the offer in the EU does not exceed €20 million calculated over 12 months and provided that the issuer does not have any securities traded on an MTF and its average number of employees during the previous year does not exceed 499.

In all cases, the EU Growth prospectus will not be available where the issuer/offeror has any securities admitted to trading on a regulated market.

Again, the precise disclosure requirements of the EU Growth prospectus will be set out in secondary legislation in due course.

Prospectus Summaries

Issuers will have more flexibility over summary contents

The format of prospectus summaries was changed in 2010 in an attempt to make them more accessible to investors. Changes at that time included the introduction of the “key information” concept and the requirement that all summaries have a common format and certain mandatory disclosure requirements known as “elements.” The Commission believes that these changes did not achieve their objectives and instead made summaries overly long and confusing.

Significant changes are being made to summaries under the Regulation. A summary will still have a uniform structure, but the “elements” requirement has been scrapped and the issuer will have more flexibility over its contents. The maximum length of a summary has also been considerably shortened - from 7% of the prospectus or 15 pages under the PD, to typically no more than 7 sides of A4 under the Regulation.

To ensure a uniform structure, the summary will be split into the following 4 sections:

- an introduction with warnings
- key information on the issuer
- key information on the securities and
- key information on the offer of the securities to the public and/or admission to trading.

ESMA will develop regulatory standards to specify the content and presentation of the key information referred to above. However, as set out in the recitals to the Regulation, provided issuers present it in a fair and balanced way, they should be given discretion to include the information that they deem to be material and meaningful. The summary must be written in a language and style that facilitates the understanding of the information, in particular, in language that is clear, non-technical, concise and comprehensible for investors. As under the PD, the Regulation prohibits any cross-referencing in the summary to other parts of the prospectus and also the incorporation of information by reference.

The summary must include a brief description of the most material risk factors specific to the issuer, any guarantor and the securities and controversially, the Regulation restricts the number of risk factors that may be included to 15.

The new format and length of a summary are modelled on the “key information document” (KID) that will be required for packaged retail and insurance-based investment products (PRIIPs) under the PRIIPs Regulation. Where an issuer is required to produce a KID under the PRIIPs Regulation, parts of the summary may be replaced by the information contained in the KID.

Risk factors

Perhaps in response to the perception that risk factors in prospectuses have become primarily a risk management tool for issuers, with the benefit for investors being of secondary concern, the new Regulation sets out more prescribed rules for risk factors.

Under the new regime, the risk factors featured in a prospectus will be limited to those risks “which are specific to the issuer and/or to the securities and which are material for taking an informed investment decision.....” Generic, disclaimer-type risk factors should not be included. Risk factors should also be presented in a limited number of categories with the most material risks listed first under each category. Materiality will be assessed based on the probability of a risk occurring and the expected magnitude of its negative impact.

Universal Registration Document

More prescribed rules for risk factors have been imposed

The Regulation introduces the concept of a “Universal Registration Document” (URD) along the lines of the North American “shelf registration” process. This will give frequent issuers with securities admitted to trading on either a regulated market or an MTF, the option of maintaining a generic document that will function as the registration document component for future prospectuses. The URD will contain information on the company’s organisation, business, financial position, earnings and prospects, governance and shareholding structure. Information can be incorporated by reference into the URD. The minimum information to be included will be set out in delegated legislation.

A URD will have to be filed annually and must be approved by the relevant competent authority for at least the first two years. Once a URD has been approved for two consecutive years, subsequent URDs may be filed without prior approval. The competent authority, will, however, still be able to review the URD and require amendments to be made. If an issuer fails (after two consecutive years) to file a URD, the benefit of filing without prior approval will be lost and subsequent URDs will need to be submitted for approval until the two consecutive years condition is met again.

Filing a URD gives an issuer “frequent issuer status” which may allow the issuer to benefit from a faster 5 days prospectus approval process (reduced from the current 10 days.) This accelerated process may well provide a useful benefit for some, but it should be noted that the competent authority must be given an additional five days’ notice before submission of the prospectus for approval and also that if a URD has only been filed with the competent authority (rather than being approved) it must be subsequently approved before it can be used as part of a prospectus.

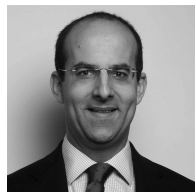
In order to retain the status (and potential benefits) of being a “frequent issuer,” a company must file a new URD each year and must, at that time, confirm in writing that it has filed all regulated information which it was required to disclose under the Transparency Directive and the Market Abuse Regulation.

Others

The Regulation introduces a number of other changes to the prospectus regime, including the following:

- **Incorporation by reference** – the Regulation increases the scope of the information that may be incorporated by reference into a prospectus. As well as incorporating by reference all historic annual and interim financial information, an issuer will also be able to include other documents such as corporate governance statements and asset valuation reports. When in electronic format, a prospectus will have to contain hyperlinks to all documents containing information that is incorporated by reference.
- **Prospectus publication** – the Regulation removes the ability to “publish” a prospectus by inserting it in one or more newspapers or in printed form. All prospectuses must now be published in electronic form and will be deemed to be published when made available on either (i) the website of the issuer, the offeror or the person asking for admission to trading; (ii) the website of the financial intermediaries placing or selling the securities or; (iii) the website of the regulated market where the admission to trading is sought, or where a regulated market is not relevant, the website of the operator of the multilateral trading facility. Investors may still, however, request a paper copy of the prospectus.
- **Supplements** – The Regulation introduces a shorter turnaround time for the approval of supplements from 7 down to 5 working days. It also requires the issuer, or financial intermediary if the securities are purchased through a financial intermediary, to inform investors of the possibility that a supplementary prospectus may be published and also that there could be a right of withdrawal after publication of any supplement.

For more information, please contact:



Chris Horton
Partner
 T +44 20 7825 3034
 E chris.horton@simmons-simmons.com



Colin Bole
Partner
 T +44 20 7825 3170
 E colin.bole@simmons-simmons.com

or your usual contact at Simmons & Simmons

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