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DG FISMA
European Commission
1000 Brussels, Belgium

Dear Sir, Madam,

13 May 2015

Consultation on the review of the Prospectus Directive

This is the response of the Financial Services Consumer Panel to the European Commission's consultation on the review of the Prospectus Directive.

The Panel provides advice and challenge to the UK's Financial Conduct Authority (FCA) on the extent to which the FCA's general policies and practices are consistent with its general duties. The Panel represents the interests of all groups of financial services consumers and operates independently of the FCA.

Overall, the Panel supports the Commission's aim of reviewing the Directive to ensure that prospectuses remain fit for purpose. Overlong prospectuses with repetitive "risk factors" do little to inform or protect retail investors. However, the challenge will be to change the nature of prospectuses to make them serve their intended purposes and serve as protection for consumers, whilst promoting healthy and active markets.

In this respect, the Panel is concerned that the consultation seems to confirm the Commission has already set its mind on significant changes to both the requirement to issue a prospectus and the content of the document, without any preliminary consumer research of the impact of such changes on retail investors.

We would urge the Commission to keep an open mind about its policy options, including the option to maintain at least some of the *status quo*, and to subject any proposed changes to thorough consumer testing before it issues a formal legislative proposal.

Drawing up a prospectus can never be expected to be a simple or cheap process. It is essential that the regulatory regime is tough enough to drive a thorough and responsible due diligence exercise every time a prospectus is produced. Without this there are clear risks to consumers.

The consultation seems focused mostly on lowering the administrative burden on firms. However, encouraging consumers to make long-term investment requires trust in the financial services industry, which is already perilously low. The presumed increase in availability of capital is unlikely to materialise if reducing consumer protection under the Prospectus Directive leads to investors making poorly-informed choices in ignorance of the risks they are taking.

This review is needed to make sure that time and money are not being wasted under the current Directive, making markets inefficient without any corresponding value in terms of consumer protection. However, prospectuses, and in particular the prospectus summary, remain a crucial piece of information for consumers before deciding to invest

their money. For this reason, the Panel opposes attempts to widen the exemptions from the prospectus requirement to more issuers by lowering the current thresholds.

The content of the prospectus should also be reviewed to ensure that it is fit for purpose. The Panel would emphasise the importance of information provided being concise, consistent, relevant, written in plain language and timely and meaningful. All work could be wasted if the final document were too long and complex, as potential investors would simply not read it.

On the other hand, the Panel wants the Commission to be aware of potential problems where the information provided is too simplistic to convey the complexities of risk. Disclosure must not operate to absolve issuers of responsibility or liability later on if the information provided was inadequate, oversimplified or too complex for retail investors to understand.

The Panel would therefore underline again the importance of subjecting any changes to the Prospectus Directive to thorough consumer testing and impact assessments to ensure that retail investors are not at a greater risk of detriment under a revised legislative framework.

Yours sincerely,

A handwritten signature in cursive script, appearing to read 'S. Lewis'.

Sue Lewis
Chair
Financial Services Consumer Panel

List of Consultation questions

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**

The Panel believes that a prospectus should be required where securities are admitted to trading on a regulated market or offered to the public. This is an essential safeguard to ensure retail investors make an informed choice.

3. Bearing in mind that the prospectus, once approved by the home competent authority, enables an issuer to raise financing across all EU capital markets simultaneously, are the additional costs of preparing a prospectus in conformity with EU rules and getting it approved by the competent authority outweighed by the benefit of the passport attached to it?

Drawing up a prospectus can never be expected to be a simple or cheap process. It is essential that the regulatory regime is tough enough to drive a thorough and responsible due diligence exercise every time a prospectus is produced. Without this there are clear risks to consumers. That said a review is needed to make sure that time and money is not being wasted so that markets are made inefficient without any corresponding value in terms of consumer protection.

The Panel does not see how more exemptions from the need to produce prospectuses helps consumers. The emphasis should be on the right kind of prospectuses which is another way of addressing the same problem.

4. The exemption thresholds in Articles 1(2)(h) and (j), 3(2)(b), (c) and (d), respectively, were initially designed to strike an appropriate balance between investor protection and alleviating the administrative burden on small issuers and small offers. Should these thresholds be adjusted again so that a larger number of offers can be carried out without a prospectus? If yes, to which levels?

Please provide reasoning for your answer.

- a) the EUR 5 000 000 threshold of Article 1(2)(h):**
- b) the EUR 75 000 000 threshold of Article 1(2)(j):**
- c) the 150 persons threshold of Article 3(2)(b):**
- d) the EUR 100 000 threshold of Article 3(2)(c) & (d):**

The Panel does not see how more exemptions from the need to produce prospectuses helps consumers. The emphasis should be on the right kind of prospectuses, which is another way of addressing the same problem.

5. Would more harmonisation be beneficial in areas currently left to Member States' discretion, such as the flexibility given to Member States to require a prospectus for offers of securities with a total consideration below EUR 5 000 000?

The Panel understands the Commission is re-considering the flexibility given to Member States to require a prospectus for offers of securities with a total consideration below €5 million due to concerns that such a requirement is deterring uptake of crowdfunding in countries where this *de minimis* threshold is not applied.

In the Panel's view, companies seeking equity-based crowdfunding should be obliged to issue a full prospectus if they are seeking to raise more than a certain amount (for example €1 million). In the UK, some companies are already trying to raise much larger sums than these with no investor protection.

In parallel to any changes to the Prospectus Directive to encourage crowd-funding, the Panel would encourage the Commission to ensure adequate levels of protection for investors in

crowdfunding and similar activities exist, including where such investments are transacted across Member State borders.

We believe that the requirements brought in by the UK's Financial Conduct Authority, such as checks on the creditworthiness of borrowers, will bring credibility and stability to this fast-growing industry. Consumers should also be made aware of the risks of lending money via crowdfunding platforms, and the high possibility of capital losses.

The biggest barrier to cross-border crowdfunding activity does not relate to regulation but to due diligence. Retail investors already struggle to perform due diligence on borrowers or companies seeking investment funds, meaning that most consumers have to rely on their platform to some extent. Where that platform is in another EU Member State, finding out about their due diligence track record is even more difficult.

This creates additional layers of information asymmetry, with the added risks to consumers who may make investment that are far riskier than they realise. Accordingly, the Panel does consider that a basic regulatory regime is required at EU-level to guarantee a minimum standard of investor protection.

An amendment to the Prospectus Directive requiring investors to receive a prospectus before they decide to invest their money through crowdfunding would be useful. This would also necessitate common EU rules around client money and reserves for platforms.

We would encourage the European Commission to consult on this issue in more detail before deciding on its next steps. Any new rules in this fast growing area need to be proportionate and not stifle growth. Peer to peer lending can be a valuable part of meeting unmet demand from both savers and borrowers and offers an alternative to mainstream borrowing.

7. Can you identify any other area where the scope of the Directive should be revised and if so how? Could other types of offers and admissions to trading be carried out without a prospectus without reducing consumer protection?

The Panel does not believe that more exemptions from the need to produce prospectuses helps consumers. The emphasis should be on the right kind of prospectuses which is another way of addressing the same problem.

21. Would you support the creation of a simplified prospectus for SMEs and companies with reduced market capitalisation admitted to trading on an SME growth market, in order to facilitate their access to capital market financing?

No, the higher risk profile of SMEs and companies with reduced market capitalisation justifies disclosure standards that are as high as for issuers listed on regulated markets.

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

Realistically, retail investors are only ever likely to read an "executive summary", and the Panel believes one of the key planks of consumer protection in this area is to ensure that there are accurate summaries of the contents of the whole documents.

Clearly, consistency across regulatory regimes is sensible and a three page summary seems much more likely to have value to retail investors than a longer summary which just ends up regurgitating risk factors set out elsewhere.

We would emphasise the importance of information provided being concise, consistent, relevant, written in plain language and timely and meaningful: all work could be wasted if the final document is too long and complex, as potential investors will simply not read it. On the other hand, the Panel wants the Commission to be aware of potential problems where the information provided is too simplistic to convey the complexities of risk. We remain opposed to the use of a single synthetic risk indicator because of the danger of over-simplification.

The Panel believes that it would be prudent for the Commission, in conjunction with ESMA, to undertake detailed consumer testing of the prospectus summary to identify how consumers interact with this document and how it influences their decision-making. This could be carried out alongside the work that has already started on consumer-testing the potential format and content of the 'Key Information Document' under the PRIIPs Regulation.

28. For those securities falling under the scope of both the packaged retail and insurance-based investment products (PRIIPS) Regulation, how should the overlap of information required to be disclosed in the key investor document (KID) and in the prospectus summary, be addressed?

- **By providing that information already featured in the KID need not be duplicated in the prospectus summary**
- **By eliminating the prospectus summary for those securities**
- **By aligning the format and content of the prospectus summary with those of the KID required under the PRIIPS Regulation, in order to minimise costs and promote comparability of products**
- **Other**

Realistically, retail investors are only ever likely to read an "executive summary", and the Panel believes one of the key planks of consumer protection in this area is to ensure that there are accurate summaries of the contents of the whole documents.

We are grateful that the Commission is consulting explicitly on the overlap and inconsistencies between the different disclosure regimes, in particular the Prospectus Directive and PRIIPs. If this overlap is not addressed, the resulting disclosure documents are likely to overwhelm consumers.

Clearly, consistency across regulatory regimes is sensible and a three page summary seems much more likely to have value to retail investors than a longer summary which just ends up regurgitating risk factors set out elsewhere. Accordingly, the Panel believes that prospectus summary should be replaced by a 'Key Information Document' (KID) under the PRIIPs Regulation where both pieces of legislation, but it would go further and suggest that a three page maximum KID should be the required form of summary for all prospectuses.

However, the Panel believes that it would be prudent for the Commission, in conjunction with ESMA, to undertake detailed consumer testing of the prospectus summary to identify how consumers interact with this document and how it influences their decision-making. Such research should occur before any formal legislative proposal is issued to alter, or abolish, the prospectus summary. This could be carried out alongside the work that has already started on consumer-testing the potential format and content of the 'Key Information Document' under the PRIIPs Regulation.

31. Do you believe the liability and sanctions regimes the Directive provides for are adequate?

The sanctions regime in the Prospectus Directive is significantly less developed than that which applies under the UCITS V and MiFID 2 Directives or the PRIIPs Regulation. Indeed, ESMA has found that penalties imposed vary widely from Member State to Member State¹.

Given that prospectuses are passportable and can thus be used in any EU Member State after being approved domestically, the Panel believes that it is important that the same standards of dissuasive sanctioning apply for breaches of the Directive across Europe so that issuers cannot exploit the existence of 'light-touch' penalties in particular Member States.

As such, we would support changes to the Prospectus Directive to make the standards for applicable penalties more prescriptive, leading to a greater degree of harmonisation across Member States.

¹ http://www.esma.europa.eu/system/files/2013-619_report_liability_regimes_under_the_prospectus_directive_published_on_website.pdf

37. What should be the involvement of national competent authorities (NCA) in relation to prospectuses?

National competent authorities should review all prospectuses ex ante (i.e. before the offer or the admission to trading takes place. If a prospectus is required then it should be a requirement that it is pre-approved. This is the underlying principle that ensures effective policing of the whole concept of due diligence.

51. Can you identify any incoherence in the current Directive's provisions which may cause the prospectus framework to insufficiently protect investors?

The core principle 'to act honestly, fairly, and professionally in accordance with the best interest of the customer' (such as incorporated into article 24 of MiFID 2) should be embedded across all measures which apply to intermediaries, including the issuance of prospectuses.

Similarly the core principle regarding all information (whether marketing or regulated disclosures) being 'fair, clear, and not misleading (MiFID Art 19; UCITS IV, Article 79) should apply to any revision of the Directive.