



**PROSPECTUS
CHANGES:
THREE-STAGE
IMPLEMENTATION
OF THE EU'S NEW
PROSPECTUS
REGULATION**

The new EU Prospectus Regulation (PR), adopted in June 2017, changes the current prospectus regime for listed issuers and companies making public offers of securities. It repeals and replaces the 2003 Prospectus Directive (PD) and the European Commission's 2004 implementing regulation on the form, content and publication of prospectuses and related advertisements.

“By reducing costs and administrative burdens, the new regime aims to improve access to capital markets, especially for small and medium-sized enterprises, and to simplify information for investors.”

As a regulation, the PR has direct effect in all EU member states, but may lead to consequential changes to domestic legislation – in the UK, the Financial Conduct Authority (FCA) rules have already been amended and the Government is expected to amend the Financial Services and Markets Act 2000.

The PR forms part of the EU’s Capital Markets Union Action Plan. It is a welcome modernisation of the prospectus regime which gives companies increased flexibility to raise capital either without publishing a prospectus at all or using a shorter, simpler document. By reducing costs and administrative burdens, the new regime aims to improve access to capital markets, especially for small and medium-sized enterprises (SMEs), and to simplify information for investors. In seeking to strike a balance between the interests of issuers and investors, the reforms are less substantial than some would have hoped, but they are nonetheless significant.

The changes

Key changes include:

- Some exemptions amended, generally setting higher thresholds beyond which a prospectus is mandatory for offers of securities.

- New rules for prospectus disclosure.
- A lighter prospectus regime for SMEs (as defined in the PR) and certain other issuers and secondary issues.
- Introduction of a shelf registration regime for frequent issuers.

The PR is being implemented in three stages over two years. Most of the regulation will not apply until the end of this period in 2019, but changes to two exemptions had immediate effect when the PR formally came into force on 20 July 2017 and two more important changes to exemptions will apply from 21 July 2018.

Changes applicable as from 20 July 2017

Exemptions for issuers with securities already trading on a regulated market

- An issuer with securities admitted to a regulated market (such as the Main Market of the London Stock Exchange (LSE)) may in any 12 month period issue further securities, in the same class and admitted to trading on that market, up to (but excluding) 20% of the existing securities. Previously

the threshold was 10% and the exemption applied only to shares.

- A new cap is introduced on the number of shares resulting from the conversion or exchange of other securities admitted to trading on a regulated market which can be admitted to trading on that market over a 12 month period without a prospectus. Previously there was no cap. Although the PR provides several exceptions, the new cap significantly restricts the scope for avoiding a prospectus through issuing convertible debt.

Some caution is likely in pursuing large issuances without a prospectus. In any event, institutional investor guidance on pre-emption rights may limit the use of these exemptions in the UK except in M&A.

Changes applicable as from 21 July 2018

Exempting the smallest capital raisings

The PR will not apply to offers of securities with a total consideration across the EU of less than €1 million in any 12 month period. (The current limit is €100,000.)

The threshold beyond which member states must require a prospectus

will increase from €5 million to €8 million; however, member states will have the discretion to exempt domestic issues of between €1 million and €8 million or establish other disclosure requirements for issues below €8 million. Accordingly, the threshold at which an issue requires a prospectus or other disclosure document will depend on:

- Whether the issue is domestic or cross border.
- If domestic, which member state since the threshold will vary according to national law.
- Whether other exemptions are available.

These changes significantly increase opportunities for crowd funding and other relatively small issues.

Changes applicable as from 21 July 2019

As mentioned above, most of the PR's provisions will apply from mid-2019.

Risk factors

Issuers will be required to set out risk factors in a limited number of categories, identifying the most material risks within each category first. No more than 15 risk factors may be included in the summary part of a prospectus.

Summary Format

Issuers will have more discretion over the information that they include, within a new format which comprises four main sections:

- An introduction containing certain warnings.
- Key information on the issuer.
- Key information on the securities.
- Key information on the offer itself and/or the admission to trading.

Summaries will be shorter than currently, generally limited to seven sides of A4.

Incorporation by reference

The range of information that may be incorporated by reference into

a prospectus will be extended to include not only filings under the prospectus and transparency regimes but also, for example, other regulated information, published financial data and information in existing prospectuses, supplements and final terms. This allows issuers and their advisers to reduce significantly the duplication of disclosure.

EU growth prospectus

For smaller companies, the PR introduces a new "EU growth prospectus". This lighter-touch "proportionate disclosure" regime will rely on a standardised, simple document: European Commission regulations will detail the format and content. The regime will be available to issuers that have no securities admitted to trading on a regulated market and are:

- SMEs.
- Issuers admitted to trading on an SME growth market (or seeking admission) if they have had an average market capitalisation of less than €500m on the basis of year end quotes for the previous three calendar years – SME growth markets are a category of multilateral trading facility (MTF) catering specifically for SMEs; the category is being introduced from 3 January 2018 under the EU MiFID II regime¹.
- Issuers without securities trading on a MTF, that had an average of 499 employees or fewer in the last financial year and are raising up to €20 million.

Simplified disclosure regime for secondary offers

A new simplified disclosure regime will replace the current, little-used regime for rights issues, that was introduced only in 2012. The new regime will apply generally to secondary offers by issuers that have had securities admitted to trading on a regulated market or an SME growth market continuously for at least the last 18 months. Many rights and other pre-emptive issues (such as open offers) on the LSE Main Market (and AIM, if it becomes an SME growth

market) may become cheaper and easier.

Fast-track and simplified frequent issuer regime

Frequent issuers of securities admitted to trading on a regulated market or MTF will be able to use the PR's "Universal Registration Document" (URD), akin to "shelf registration" in the US or Canada. The URD will contain key information about the issuer. The PR envisages that issuers will update it annually and thereby benefit from a fast-track prospectus approval process.

Wider exemption for offers of shares to EU employees

Non-EU issuers will be able to offer securities to their existing or former directors or employees in the EU without a prospectus, even securities not listed or traded on any market. This exemption is currently available only to issuers with a head office or registered office in the EU. A short information document is required instead of a prospectus.

What is not changing

The PR does not change the key triggers for a prospectus, namely when either an offer of transferable securities is made to the public in an EU member state or transferable securities are admitted to trading on an EU regulated market. And many of the key exemptions from the obligation to publish a prospectus remain the same, in particular the exemption for offers of securities made only to qualified investors or to fewer than 150 persons per EU member state, not counting "qualified investors", or where the total consideration per investor or denomination per security (i.e. per unit) is at least 100,000.

Impact of Brexit

The PR provides a cross-border regime for prospectuses and Brexit raises a number of uncertainties which seem unlikely to be resolved until the UK's future relationship with the EU becomes much clearer. As with the existing PD, the PR allows prospectuses approved in the home

¹ It is not yet known whether the London Stock Exchange's AIM market will become an SME growth market.

member state of an issuer to be used “passporting” across the EEA with minimal additional requirements. Although that facility is not available to prospectuses approved outside the EEA (i.e. in third countries), member states’ competent authorities may approve prospectuses that comply with third country requirements equivalent to the PD/PR. However, the rules for this have been tightened in the PR, and it may prove difficult post-Brexit to use UK-approved prospectuses in the EEA and vice versa.

The UK is scheduled to leave the EU on 29 March 2019, three months before most of the PR comes into effect. The British Government’s stated approach to ensuring an orderly transition from EU membership is to convert existing EU law into domestic law, after which Parliament (or devolved legislatures) can decide which elements to keep, amend or repeal once the UK has left the EU. However, the European Union (Withdrawal) Bill introduced to Parliament in July 2017 would save only those provisions of the PR that already apply at the moment of the UK’s exit from the EU. On this basis, even if the UK were treated as PR-equivalent at the point of Brexit, it might shortly cease to be so, unless additional steps are taken: these would probably require primary legislation for which little time may be available. Fortunately, wholesale offers may be little affected by this, since they tend to rely on exemptions from the obligation to publish a prospectus.

Conclusion

The adoption of the PR underlines that the EU is committed to enhancing integration of Europe’s capital markets and broadening participation. Success depends on various factors including, critically, the precise detail of implementing legislation to be adopted by the Commission. Issuers and prospective issuers in the EU who may be unable to benefit from clear exemptions should monitor the development of that legislation. Issuers, particularly those that have or will target retail investors, should monitor the Brexit negotiations and consider how different outcomes may affect the markets for their securities.

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