



## EU Parliament's Adoption of Amendments to the Prospectus Directive

On 17 June 2010, the European Union ("EU") Parliament passed a resolution (the "Resolution")<sup>1</sup> adopting the proposal by the EU Commission ("Commission") for amendments to the Prospectus Directive (2003/71/EC) ("PD"),<sup>2</sup> with certain modifications.

The Commission had conducted a public consultation on a review of the PD in early 2009<sup>3</sup> further to which it published on 24 September 2009 a proposed directive amending the PD.<sup>4</sup>

The aim of the review and the amendments is to simplify and improve the application of the PD, lessening the disclosure requirements, providing clearer exemptions and ensuring that adequate information is provided to meet the needs of retail investors in particular.

The following is a summary of the key amendments adopted by the EU Parliament.

### Exempt Offers of Securities, Which Are Outside the Scope of the PD

**Total consideration trigger (Article 1(2)(h)):** Currently where the total size (consideration) of an offer is less than €2.5 million over a 12-month period, such an offer is outside the scope of the PD. This threshold will be raised to €5 million.

**Non-equity securities (Article 1(2)(j)):** Currently non-equity securities that are issued in a continuous or repeated manner by credit institutions, where the total consideration of the offer is less than €50 million, are outside the scope of the PD. This was regarded as overly burdensome and so the threshold will be raised to €75 million.

In both Article 1(2)(h) and Article 1(2)(j), it will be clarified that "offer" refers to an offer in the European Union.

<sup>1</sup> Provisional edition of EU Parliament legislative resolution on EU Commission's proposal for a directive amending the Prospectus Directive (2003/71/EC) and the Transparency Directive (2004/109/EC) (17 June 2010).

<http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2010-0227&language=EN&ring=A7-2010-0102>.

<sup>2</sup> Directive (2003/71/EC) of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2003:345:0064:0089:EN:PDF>.

<sup>3</sup> European Commission consultation document: A review of Directive (2003/71/EC) of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading (9 January 2009),

[http://ec.europa.eu/internal\\_market/consultations/docs/2009/prospectus/background\\_en.pdf](http://ec.europa.eu/internal_market/consultations/docs/2009/prospectus/background_en.pdf) (closed 10 March 2009).

<sup>4</sup> European Commission's Proposal for a directive amending Directives on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market (23 September 2009),

[http://ec.europa.eu/internal\\_market/securities/docs/prospectus/proposal\\_240909/proposal\\_en.pdf](http://ec.europa.eu/internal_market/securities/docs/prospectus/proposal_240909/proposal_en.pdf).

## Exempt Public Offers, Where a PD-Compliant Prospectus Is not Required to Be Published

**“Qualified investors” (Article 2(1)(e)):** This definition will be conformed to that of “professional clients” under the Markets in Financial Instruments Directive (“Mifid”).<sup>5</sup> The current (lengthy and narrative) definition of “qualified investors” under the PD is different from that of “professional clients” under Mifid despite many similarities. As a result, investment firms have had to engage in the complicated and costly exercise of analysing whether their clients classified as “professional clients” under Mifid are also “qualified investors” under the PD. This amendment will allow them to rely on the clients’ categorisation under Mifid when conducting private placements (i.e., an offering under Article 3.2(a) that is “solely addressed to qualified investors”).

**100 persons exemption (Article 3(2)(b)):** The maximum number of investors will be raised to 150 (other than qualified investors) per member state from the current 100-person limit.

**Minimum total consideration exemption (Article 3(2)(c)):** The threshold will be raised to €100,000 from the current €50,000 per investor. It was considered that the lower threshold no longer reflected the distinction between retail and professional investors.

**Minimum denomination exemption (Article 3(2)(d)):** Likewise, this threshold will be raised to €100,000 from the current €50,000 per unit.

**Employee share schemes (Article 4(1)(e)):** The exemption for offers to employees will be extended to an issuer that does not already have securities admitted to trading on a regulated market, if either: (i) it has a head office or registered office in the EU; or (ii) the securities are admitted to trading on a third-country market as to which the Commission has adopted an equivalence decision. The existing provisions were found to be too restrictive to be of much use to companies operating employee share schemes.

**Retail Cascades (Article 3(2)(ii)):** Retail cascades (a chain of issuance and distribution/sub-distribution arrangements commencing with the issuer of securities and ending with the ultimate investors in the securities) are commonly used in the distribution of securities to retail investors. Since each level of the retail cascade could be regarded as a public offer of securities requiring the publication of a PD-compliant prospectus, there was confusion for a long time among distributors as to whether, and when, they could rely on a PD-compliant prospectus published by the issuer as fulfilling its own obligations under the PD. Guidance on this point was eventually issued by the Committee of European Securities Regulators (“CESR”) and the UK Financial Services Authority (“FSA”), and the proposed new Article 3(2)(ii) would confirm that guidance, i.e., that the distributor is not required to produce another PD-compliant prospectus where the prospectus produced by the issuer remains valid and the issuer has consented in writing to the use of the prospectus by such distributor.

## Other Amendments

**Prospectus summary (Article 5(2)) and civil liability (Article 6(2)):** The amendments require that a more tailored and useful summary be provided in the prospectus, focusing on certain “key information,” to enable investors “to take informed investment decisions and to compare the securities with other investment products.” As a “key source of information for retail investors,” the summary should be “short, simple, clear and easy for targeted investors to understand.” In addition, its format and content should ensure comparability with other similar investment products. In this regard, the Commission had considered in its public consultation whether it is appropriate to restrict the length of the summary to a fixed number of words, which can make it difficult for the issuer to cover all the relevant information in it. However, the amending directive has not removed the current limit of 2,500 words contained in Recital (21) of the PD.

<sup>5</sup> Directive (2004/39/EC) on markets in financial instruments, <http://eur-lex.europa.eu/LexUriServ/site/en/consleg/2004/L/02004L0039-20060428-en.pdf>.

A definition of “key information” is added in Article 2(1) to include:

- the risks associated with and essential characteristics of the issuer (and any guarantor), including the assets, liabilities and financial position;
- the risks associated with and essential characteristics of the investment in the relevant security, including any rights attaching to it;
- general terms of the offer, including estimated expenses charged to the investor;
- details of the admission to trading; and
- reasons for the offer and the use of proceeds.

In line with the added significance attached to the prospectus summary, civil liability may arise on the basis of the prospectus summary, but only if, “when read together with other parts of the prospectus,” it is misleading, inaccurate or inconsistent with other parts of the prospectus, or fails to provide key information. The summary must include a clear warning to this effect.

Under current rules, liability cannot attach to the summary unless it is misleading, when read with the rest of the prospectus. The revised provisions can now also lead to liability where the information in the summary is not sufficient when read together with other parts of the prospectus to provide key information to aid investors when considering whether to invest in such securities. This is, however, a relaxation from the previous draft of the proposals, which suggested liability could attach to the summary if by itself it did not contain sufficient key information allowing investors to make an informed decision and compare the securities with other investment products.

These provisions represent a significant change from the previous proposal that the summary should be replaced by a key information document (“KID”) similar to the KID,<sup>6</sup> which will replace the existing “Simplified Prospectus” under the new UCITS Directive (2009/65/EC) (known as “UCITS IV”).<sup>7</sup> However, the amendment to Article 5(5) provides that the Commission should be empowered to adopt implementing measures that detail the requirements under the PD, pursuant to Article 291 of the Treaty on the Functioning of the European Union (“TFEU”),<sup>8</sup> such as the detailed format and content of the summary, once the Commission concludes its consultation on the disclosure and selling practices for packaged retail investment products (“PRIPs”).<sup>9</sup> The scope of this consultation comprises, *inter alia*, (i) investment funds, including undertakings for collective investment in transferable securities (“UCITS”), (ii) insurance-based investments, (iii) retail structured products and (iv) structured retail deposits.

<sup>6</sup> See the draft EU Regulation as regards key investor information and conditions to be met when providing key investor information in relation to UCITS offerings, <http://register.consilium.europa.eu/pdf/en/10/st09/st09829.en10.pdf>. See also Morrison & Foerster client alert: Retail investor disclosure under the new UCITS KID (12 May 2010), [http://www.mofo.com/files/Uploads/Images/100512Structured\\_thoughts.pdf](http://www.mofo.com/files/Uploads/Images/100512Structured_thoughts.pdf).

<sup>7</sup> Directive (2009/65/EC) of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (recast), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:302:0032:0096:EN:PDF>.

<sup>8</sup> Treaty on the Functioning of the European Union (consolidated version), <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:115:0047:0199:EN:PDF>, previously called the “Treaty establishing the European Community,” as amended and renamed by the Lisbon Treaty of 13 December 2007, <http://eur-lex.europa.eu/JOHtml.do?uri=OJ:C:2007:306:SOM:EN:HTML>.

<sup>9</sup> European Commission’s Communication on Packaged Retail Investment Products (30 April 2009), [http://ec.europa.eu/internal\\_market/finances-retail/docs/investment\\_products/29042009\\_communication\\_en.pdf](http://ec.europa.eu/internal_market/finances-retail/docs/investment_products/29042009_communication_en.pdf) and Update on Commission Work on Packaged Retail Investment Products (16 December 2009), [http://ec.europa.eu/internal\\_market/finances-retail/docs/investment\\_products/20091215\\_prips\\_en.pdf](http://ec.europa.eu/internal_market/finances-retail/docs/investment_products/20091215_prips_en.pdf). See also Morrison & Foerster client alert: An update on EU actions on PRIPs (10 February 2010), [http://www.mofo.com/files/Publication/f17b0cfl-4d0f-469a-955d-e48fe44565bd/Presentation/PublicationAttachment/a7aa0212-967d-4490-940d-ff237efc43b8/100210Structured\\_thoughts\\_issue\\_3.pdf](http://www.mofo.com/files/Publication/f17b0cfl-4d0f-469a-955d-e48fe44565bd/Presentation/PublicationAttachment/a7aa0212-967d-4490-940d-ff237efc43b8/100210Structured_thoughts_issue_3.pdf).

These amendments result from the Commission's criticisms as to the current lack of any consistent approach to providing key information to retail investors in various investment products and its stated desire to use the UCITS KID as the "benchmark for the process of developing improved mandatory disclosures for the whole of the retail packaged investment product market."

**Rights issues (Article 7(2)):** A (reduced) "proportionate disclosure regime" will be applied to offers of shares by companies whose shares of the same class are already admitted to trading on a regulated market or multilateral trading facility (as defined in MiFiD), provided that the issuer has not disapplied the statutory pre-emption rights. As the same class of share would already be subject to appropriate ongoing disclosure requirements and rules on market abuse, there would already be substantial information about the company available to the public.

**Prospectus validity period (Article 9):** A prospectus, and a registration document, shall be valid for 12 months after its approval (rather than its publication). The Commission's previous proposal to extend the validity period for prospectuses to 24 months has not been adopted.

**Supplementary prospectuses and withdrawal rights (Article 16):** The requirement to publish a supplementary prospectus will end on (i) the final closing of the offer to the public or (ii) when trading on a regulated market begins, whichever occurs "later" (not earlier). This amendment clarifies the ambiguity in current rules as to whether the relevant date was the earlier or later of (i) and (ii) above.

Where the prospectus relates to an offer to the public (rather than an admission to trading only), the time period for exercising the withdrawal right will be harmonised to be "within two working days" after the publication of the supplement. Current provisions state "within a time limit...not...shorter than two working days," which resulted in a lack of consistent approach among member states in implementing the PD into their national rules. Coupled with a lack of clarity concerning whose national legislation should be applied for cross-border offerings (e.g., as between the issuer's home member state and the host member state where the offer or admission to trading occurs), this has caused significant confusion.

In addition, such exercise of the withdrawal rights will be restricted to those cases where the "significant new factor, material mistake or inaccuracy" triggering the need to publish the supplement arose before the final closing of the offer to the public and the delivery of the securities. The new restrictions clarify that investors are not entitled to withdraw their acceptance if the offer has already closed.

In addition, the issuer or offeror will be allowed to extend voluntarily the withdrawal period beyond two working days. Whether or not the period is extended, the final date for the exercise of withdrawal rights must be stated in the supplementary prospectus.

**Final terms (Article 5(4)):** In relation to offers of non-equity securities under a programme, the final terms (where not contained in the base prospectus or a supplement) must be communicated to the competent authority of the host member state(s), as well as investors and the competent authority of the home member state). The amendments also clarify that the final terms may only contain information relating to the securities note and cannot be used to supplement the base prospectus.

**Updating registration documents (Article 12(2)):** The securities note must provide information normally provided in the registration document if there has been a material change or recent development (which could affect investors' assessments) since the latest updated registration document, unless it is provided in a supplementary prospectus. By comparison, the timing under the current rules is since the latest updated registration document or any supplementary prospectus "was approved."

**Electronic publication of the prospectus (Article 14(2)(c)):** A prospectus will be deemed available to the public when published in electronic form either on the issuer's website "or, if applicable" on the website of the financial intermediaries placing or selling the securities (i.e., electronic publication will no longer be required on

both such websites). In addition, where the prospectus is published in physical form (i.e., either in a newspaper or in printed form made available at a relevant office under Article 14(2)(a) or (b)), the issuer must also publish the prospectus in electronic form in accordance with Article 14(2)(c).

**Other provisions:** Certain clarifying amendments will be made to Article 18 regarding the operation of the PD's passporting mechanics. Article 10, which currently requires the issuer to file an annual information update with the competent authority of its home member state, will be deleted.

## Next Steps

The EU Parliament will now forward its Resolution to the EU Council, the Commission and the national parliaments under the ordinary legislative procedure (formerly known as the "codecision procedure"). Once adopted, the amending directive will enter into force on the 20<sup>th</sup> day following its publication in the EU Official Journal and must be implemented by member states within 18 months thereafter.

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