



EUROPEAN SAVINGS BANKS GROUP
GROUPEMENT EUROPEEN DES CAISSES D'EPARGNE
EUROPÄISCHE SPARKASSENVEREINIGUNG

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DOC 1127/02

Brussels, 20 December 2002
JEA/STA/KAV/MIK

European Savings Banks Group (ESBG)

Response to CESR's Advice on possible Level 2
Implementing Measures for the proposed Prospectus
Directive (October 2002)

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Profile European Savings Banks Group

The European Savings Banks Group (ESBG) represents 26 members from 26 countries (EU countries, Norway, Iceland, Bulgaria, Czech Republic, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovak Republic) consisting of nearly 1000 individual savings banks with around 67,000 branches and nearly 730,000 employees. At the start of 2001, total assets reached almost EUR 2800 billion, non-bank deposits were standing at over EUR 1675 billion and non-bank loans at just under EUR 1550 billion. Its members are retail banks that generally have a significant share in their national domestic banking markets and enjoy a common customer oriented savings banks tradition, acting in a socially responsible manner. Their market focus includes amongst others individuals, households, SMEs and local authorities.

Founded in 1963, the ESBG has established a reputation as the advocate of savings banks interests and an active promoter of business cooperation in Europe. Since 1994, the ESBG operates together with the World Savings Banks Institute (WSBI, with 109 member banks from 92 countries) under a common structure in Brussels.



A. General Remarks

The European Savings Banks Group appreciates the opportunity to comment on the substantive and voluminous CESR consultation paper on technical implementing measures for the Prospectus Directive.

In saying that, it must also be considered that the consultation period has been too short. So as that the quality of response to future consultation papers be maintained, the duration of the consultation period should be extended. The fundamental basis for the adoption of the Lamfalussy process is that the quality of European regulation in terms of responsiveness but also *quality* be enhanced.

With respect to the CESR consultation paper on the proposed implementing measures for the Prospectus Directive, the substance of the ESBG comments are summarised as follows:

I The consultation paper is based on a version of the Directive which is no longer up to date. It is imperative that further differentiations regarding individual prospectus formats, rendered necessary on account of a new version of the Directive, should be taken into account in the consultation papers already announced!

II In the future proceedings, special consideration must be given to the development of the base prospectus regime and to the interests of credit institutions which issue debt securities continuously or in a repeated manner.

III The IOSCO Disclosure Standards should only be seen as guidance and not as a minimum standard to be extended further by CESR. In particular, IOSCO standards are designed as maximum standards for the issue of equity securities and should, therefore, not serve as pattern for debt and derivative securities also. Otherwise there is an imminent threat of excessive bureaucratisation of the procedure for drawing up and approval of the prospectus, which is not required from the investor protection's point of view.

IV It is imperative to ensure detailed coordination of the accounting standards drawn up by CESR for prospectuses with the IAS Regulation and the future Transparency Directive.

B. Broad appraisal of consultation paper.

I. A need to refine the consultation paper

The CESR consultation paper is suffering from the general shortcoming that the draft Prospectus Directive to which CESR proposals refer is obsolete in two respects. In the first instance, the EU Commission presented on 9 August 2002, a new proposal for a Prospectus Directive. This proposal supersedes the original proposal for a Directive of 30 May 2001. The heart of the CESR consultation paper is as yet based on the original proposal for a Directive. Secondly, on 5 November 2002, ECOFIN reached a political agreement on the Prospectus Directive. This political agreement is expected to form the basis of a common position of the Council, which will then be the subject of a second reading in the European Parliament (EP). It may be concluded therefore that essential points of the text of the Directive will change.

The CESR consultation paper is therefore a little dated with respect to the development of the European process. This is particularly evident in the fact that a series of key definitions of



standards and models of prospectuses are not given consideration in the consultation paper. These include proposals for the development of the **base prospectus regime** in accordance with Article 5(4) of the Prospectus Directive and **proposals for special building blocks** for:

- prospectuses for public offers and admissions to trading (Article 7(1), second paragraph, point b),
- offering programme (Article 7(1), second paragraph, point c),
- issuers issuing debt securities in a continuous or repeated manner (on tap issuers) (Article 7(1), second paragraph, point d),
- credit institutions in general (Article 7(1), second paragraph, point e).

Further differentiation is of the utmost importance in the debt security sector, as an insufficiently differentiated, single format for a prospectus would entail wasteful bureaucratisation from the investors' perspective and would place excessive demands on issuers. The savings banks therefore consider that more refined proposals for the above-mentioned special building blocks should be undertaken by CESR as soon as possible. The following regulatory principles should inform the work of the CESR:

The **base prospectus regime** serves to discharge so-called frequent issuers from the obligation of obtaining approval of the Securities Note, over and beyond the regulatory framework of Article 8. Provision should therefore be made so that the part of the base prospectus subject to regulatory approval is confined to the content of the registration document applicable for the respective issuers and general information on the securities issued. In contrast, the description of the securities and the conditions for admission to trading including the issue price are the subject of the final terms within the meaning of Article 5(4), third paragraph and must accordingly only be filed with the competent authority.

The special format for the prospectus for securities which are exclusively the subject of a **public offer** should recognise that such issues are usually undertaken by **small and medium-sized issuers**. So as not to subject such issuers to unduly inhibitive requirements, less detailed information should be required than for cases in which authorisation of the securities for trading on a regulated market is planned. The provisions of Article 11 with respect to the Sale Prospectus Directive (89/298/EEC) could serve as guidance in this respect.

A building block for **frequent (tap) issuers** – particularly with respect to credit institutions which issue debt securities on a continuous or repeated basis - should provide that the approval of a first prospectus provide for less stringent requirements of subsequent prospectuses. The necessary content of the subsequent prospectuses should be informed by the requirements of Article 29 of Directive 2001/34/EC.

In so far as that a particular prospectus format is provided for **credit institutions**, there should be recognition of the fact that they are the subject of continuous **prudential supervision**. Periodical information on the financial situation and business activities of the issuer is therefore of lesser importance for the investor in the case of credit institutions than in the case of relatively less regulated industrial undertakings. Accordingly, for example, publication of the previous, present and future investments of the issuer could be dispensed with in a prospectus for credit institutions. The same applies for the publication of related party transactions and material contracts, which in any case is open to criticism in general.



2. Further refinement of guiding principles.

The European savings banks believe that the use of IOSCO International Disclosure Standards as the basis for legislative standards is a flawed approach. IOSCO Standards are maximum standards, which do not necessarily reflect market practice. Although Art. 7 par. 2 of the Prospectus Directive proposal only requires that implementing measures be “based on” IOSCO standards (whereas the original Directive proposal of May 31 2001 stated that the prospectus “shall be **in accordance with** the information requirements set out by international organizations, and in particular by IOSCO”) it appears as yet that CESR places too much emphasis on IOSCO compliance. Furthermore, CESR transposes these maximum standards, which are drafted for the equities sector into the debt securities and derivatives sector, supplementing them with member proposals and specific clauses from Schedule A of Directive 2001/34. In this way, a “catch-all prospectus format” is derived in a manner, which takes no account of the principles of proportionality and appropriate investor protection. The ESBG recalls that a prospectus does not serve to replace comprehensive due diligence on the part of the individual investor.

Furthermore, CESR should consider that the IOSCO has so far presented no disclosure standards for debt securities. Apparently, work is currently being undertaken in this regard. The procedure followed by CESR, of simply transposing IOSCO Disclosure Standards, designed for equity issues, into the regulation of the non-equity security sector and extending them with contrived additions appears even less acceptable against this background. It would have been preferable had CESR used Schedule A of Directive 2001/34/EU as a basis and supplemented it with additional and appropriate provisions. The approach actually followed by CESR will now result in a complicated “subtraction procedure”, in which the market participants will have to take care that superfluous regulations are deleted from the prospectus format. We find this to be unsatisfactory.

For our detailed appraisal of the CESR proposals, we refer to our comments on the questions raised by CESR and our concrete proposals for amendments in Annexes I, L and M.

3. Accounting principles and financial reporting

The ESBG supports the CESR in emphasising the importance of employing suitable accounting principles when drawing up the prospectus. It is essential that the implementing measures at stage 2 of the Prospectus Directive are consistent with the corresponding requirements in the European Commission Regulation on the application of international accounting standards and the future Transparency Directive (Directive of the European Parliament and of the Council harmonizing core requirements for providing information about issuers whose securities are admitted to trading on a regulated market and for communicating with securities holders).

It is important to consider, in particular from the perspective of small and medium sized issuers that the EU Regulation on the application of international accounting standards determines that an obligation to apply the International Accounting Standards (IAS) exists only for consolidated accounts. As regards annual accounts, the Regulation details an option for capital market-oriented undertakings, according to which Member States are entitled either to permit or to require the application of the IAS to the annual accounts, or to leave it to the home country national accounting rules of commercial law (Article 5(a)). It is to be assumed that in many Member States no requirement will be provided for the application of IAS to annual accounts. The ESBG considers that the Prospectus Directive should ensure that



a savings bank, for example, which only draws up annual accounts, may also issue these accounts according to the national commercial law accounting rules for the purposes of complying with European capital market regulations. The ESBG considers that the uniform application of IAS in the field of securities prospectus would be inappropriate. The same applies with a view to interim financial reporting: Credit institutions which issue public retail debt securities without having any securities admitted to trading on a regulated market, will presumably not be subject to interim financial reporting obligations under the forthcoming Transparency Directive. The ESBG strongly believes that no such obligation should be imposed on such issuers under Level 2 implementing measures for the proposed Prospectus Directive.



Answers to CESR-questions



Preface: With a view to the significant impact the proposed prospectus directive will have especially on the issue of debt securities and derivatives of our members we confine our comments to the questions related to the debt securities and derivatives building blocks.

129. *Do you consider that the disclosure requirements for debt securities should be identical to those for equity, as set out in Annex A?*

Definitely no. Whereas the issuer-related risk for a debt or derivative security investor is confined to the insolvency risk of the issuer an equity investor is further exposed to the risk of an under-performance of the issuer which in only rare cases leads to an insolvency (hereinafter also referred to as “the relevant risk”). For this reason, there should be less disclosure requirements for debt securities and even less for derivative securities compared to equity securities.

134. *Do you consider disclosure about the issuer's bankers and legal advisers to the extent that the company has a continuing relationship with such entities to be relevant for corporate retail debt?*

No, such a disclosure is of no actual value for the investor.

135. *Do you consider that disclosure relating to bankers and legal advisers who were involved in the issue of that particular debt instrument to be relevant?*

No, see above.

137. *Do you consider disclosure about a company's past investments in other undertakings to be material for an investor to make an investment decision about investing in the company's debt?*

For the reason set out above in our answer to question 129, such information should not be required, as it would not help investors to assess the relevant risk.



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138. *Do you consider that disclosure about a company's current investments in other undertakings to be material for an investor to make an investment decision about investing in the company's debt?*

For the reason set out above in our answer to question 129, such information should not be required, as it would not help investors to assess the relevant risk.

139. *Do you consider that disclosure about a company's future investments in other undertakings to be material for an investor to make an investment decision about investing in the company's debt?*

For the reason set out above in our answer to question 129, such information should not be required, as it would not help investors to assess the relevant risk.

142. *Do you agree that these different interests should be reflected by different disclosure standards and in particular that retail bondholders do not need the same disclosures as shareholders in respect of these sections of the IOSCO IDS?*

Yes, for the reasons set out in our answer to question 129.

145. *Do you consider it necessary for a disclosure requirement that stipulates when interim financial statements should be disclosed in the registration document, to also stipulate what the form and content of these statements should be?*

There should not be specific rules on the form and content of such statements, since the purpose of such statements, in combination with the general rules on form (easily analysable and comprehensible) and content (all material information) enable the issuer to determine what has to be contained in such statements. It should, however, be noted that Level 2 implementing measures should not incorporate new obligations for the drawing up of interim financial statements going compared to the standard set up under the forthcoming Transparency Directive.

146. *If you consider that the reduced level of detail is more appropriate, should the same approach be taken for equity?*

See answer to question 145.

148. *Do you feel that issuers should be required to put on display all documents referred to in the prospectus (as set out in CESR reference VIII in Annex A)?*

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Only publicly available documents should be displayed. Other documents, in particular material contracts, often contain confidential information and therefore may not be publicly displayed. If a material contract exposes the issuer to a severe risk and might affect the issuer's ability to fulfil its obligation under the security this fact has already to be disclosed in the risk factors section of the prospectus. Finally, the prospectus or any documents relating to the issuer should not substitute a due diligence report but should inform the investor only about the nature and the risks of the security involved.

149. *On review of the list of documents set out CESR ref. VIII.E of the corporate retail debt building block in Annex "I", please advise with reasons: (1) Whether or not there are any documents that are listed that you consider do not need to be put on display? (2) Whether or not there are any documents that are not listed that should be put on display?*

See answer to question no. 148.

150. *Please give views on which if any of the documents that are not in the language of the country in which the public offer or admission to trading is being sought should be translated.*

No translation regarding documents on display should be required. This would be much too expensive and time-consuming. Since these documents are rarely read by investors (even less than the prospectus itself which is already hardly ever read before an investment is made) the costs and time delay would outweigh by far any benefit.

153. *On a review of the equity disclosure requirements (CESR ref. VIII.G of the Core Equity Building Block) set out in Annex "A", please advise which if any of these requirements you consider to be relevant for retail corporate debt. Please give your reasons.*

See amendments in Attachment (Annex I).

155. *Please advise which if any items of disclosure should not be required for corporate retail debt. Please give you reasons.*

See amendments in Attachment (Annex I).

156. *Please advise if there are any items of disclosure for corporate retail debt that are not set out in the schedule, but should be. Please give your reasons.*

No comments.



160. *Do you consider it necessary to have specific derivative registration document requirements, or do you consider this unnecessary as the registration document requirements for debt securities should be used for derivative securities as well? Please give your reasons.*

We recommend to set up a specific registration document for derivative securities since the disclosure requirements with respect to the issuer of derivative securities are much lower than for the issuer of equity or debt securities. Even though derivative securities do not principally differ from bonds and other debt securities with regard to the issuer risk, it should be considered that derivatives are almost always issued by credit institutions, which due to prudential supervision expose the investor to a lower insolvency risk. It would therefore seem logical if the special registration document for banks, which, as we understand, will contain lower disclosure obligations, would also be used as registration document for derivatives (see introductory remarks above).

170. *Do you think it useful to provide some form of definition for these securities?*

Yes. A definition is necessary if a special regime shall apply to these securities.

171. *If so, which of the two approaches set out above do you prefer? Please give your reasons.*

Neither of the approaches is preferable. The first approach is too limited as to the underlyings and does not give enough flexibility regarding the underlyings. The second approach is too complicated, too specific and therefore does not give enough flexibility with regard to new products.

A more general and shorter approach should be chosen to be flexible for new products. A possible definition could be as follows:

"Derivative securities are securities where the payment and/or delivery obligations are linked to an underlying [(including but not limited to the price of one or more securities, indices, commodities, energy, yields, currency (rates), weather events etc.)], unless the payment of interest is merely linked to a fixed rate or to a recognized inter-bank interest rate."

The second part of the sentence starting with "unless" should be inserted to make clear that plain vanilla fixed and/or floating rate bonds with EURIBOR or LIBOR interest payments are not regarded as derivatives. All other linkages to an underlying should, however, qualify the product as a derivative.



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173. *If you prefer the approach based on fundamental features, are there other features that should be but are not included in the above list?*

The definition should be as proposed in the answer to question 171 above.

179. *Do you agree with the above sub-categorisation of derivative products?*

No. We cannot see a convincing justification for the sub-categorisation into guaranteed and non-guaranteed return derivative securities:

In both cases the issuer is liable for the fulfilment of the obligations under the derivative securities. As a consequence thereof, the investor is at risk that the issuer might not be able to meet its obligations under the derivative securities. In this context it is not relevant whether this risk exists with respect to the fulfilment of the guaranteed or the non-guaranteed obligation of the issuer.

180. *Do you agree with the approach of having two distinct registration document building blocks to reflect this sub-categorisation?*

No (see comments to question 179 above).

185. *Do you agree that the nature of the decision that an investor is making about the issuer in the case of a non guaranteed derivative is different to the one an investor is making in the case of a guaranteed derivative? Please give your reasons.*

No (see comments to question 179 above).

190. *Do you consider that disclosure about the issuer's senior management, as set out in IOSCO reference I.A, is relevant for these products? Please give your reasons.*

The term "senior management" is not known in all Member States. Therefore any disclosure about such a management would not be possible. Instead one should only refer to "board of directors".

192. *Do you consider disclosure about the issuer's advisers, as set out in IOSCO reference I.B, to be relevant for these products? Please give your reasons.*

No. See answer to question 129.

199. *Do you consider the level of detail set in IOSCO disclosure standard IV.A to be inappropriate for these products? Please give your reasons.*

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Partially they are inappropriate for derivative securities. For further detail see below the answer to question 200.

200. *Which particular items of IOSCO disclosure in this section do you consider to be relevant for these products? Please give your reasons.*

The information set forth in IV.A.1.-3. seems to be appropriate information to be provided by the issuer of derivative securities.

The information required in IV.A.4.-7. should be deleted. The description of the history of the issuer and past expenditures and divestitures are not relevant for an investor of derivative securities when evaluating the capability of the issuer to fulfil its obligations under the derivative securities.

202. *Do you consider that a general description of what the issuer's principal activities are is a more appropriate level of disclosure for these products? Please give your reasons.*

Yes, a general description of the issuer's principal activities is sufficient since the investor of the derivative security is not making an investment in the equity of the issuer.

203. *Please advise what, if any, other items of Section IV.B of IOSCO you consider to be of relevance for these products? Please give your reasons.*

IV.B.1. should be limited to the past financial year (instead of the last three financial years) because the history is not relevant for an investor of derivative securities.

IV.B.2. should be limited to the description of the principal markets in which the company competes. The breakdown should be deleted.

IV.B.3.-8. should be deleted completely because these items do not apply to the issuers of derivative securities.

205. *Do you consider that a brief description of the issuer's group and the issuer's position within it, as set out in IOSCO reference IV.C, to be an appropriate disclosure requirement for these products?*

Yes.

207. *Do you consider Section IV.D of IOSCO to be relevant disclosure for these products? Please give your reasons.*

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The information set forth in IV.D. (property, plants and equipment) is not applicable to the issuers of derivative securities and should be deleted.

209. *Do you consider Section V.D of IOSCO to be relevant disclosure for these products? Please give your reasons.*

This section is not relevant to the issuer of derivative securities. It is applicable only for producing companies (see terminology such as "production, sales, inventory").

212. *Do you consider that the name and function of the directors of the issuing company to be the appropriate level of disclosure for these products?*

Yes. Name and function of the directors are appropriate and sufficient.

213. *Please advise what if any other items of Section V of IOSCO you consider to be of relevance for these products. Please give your reasons.*

No further information is of relevance since the investment in derivative securities is not an equity investment in the shares of the issuer.

215. *Do you consider that a statement setting out whether or not the company is directly or indirectly owned or controlled by another entity and the name of that entity to be the appropriate level of disclosure for these products?*

Yes, but only to the extent that the company has been notified by the shareholders about the shareholding and is obliged to publish such notifications according to national law.

217. *At this stage do you have views about whether the following types of financial information about the issuer are relevant and as such should be disclosed in the registration document for these products? Please give your reasons.*

- a) *balance sheet*
- b) *profit and loss account*
- c) *statement showing either (i) changes in equity other than those arising from capital transactions with owners and distributions to owners; or (ii) all changes in equity (including a subtotal of all non-owner items recognised directly in equity)*
- d) *cash flow statement*
- e) *accounting policies*
- f) *related notes and schedules required by the comprehensive body of accounting standards to which the financial standards are prepared.*



a), b) and e) should be required. All other information are redundant since an investor of derivative securities does not invest into the equity of the issuer.

218. *For how many years should the above disclosure be given?*

- a) *for the last year, or*
- b) *for the last two years.*

For the last two years.

222. *At this stage do you have views about which of the following sections of IOSCO regarding the issuer's share capital you consider to be relevant information to be disclosed in the registration document for these products? Please give your reasons.*

- a) *Section X.A.1.*
- b) *Section X.A.2.*
- c) *Section X.A.3.*
- d) *Section X.A.4.*
- e) *Section X.A.5*
- f) *Section X.A.6.*

X.A.1.: items a), b) and c) should be provided. Any reconciliation of outstanding shares at the beginning and the end of the year does not seem to be required for a derivative security. The last sentence should also be deleted.

X.A.2. and 3.: meaning is unclear.

X.A.4.-6: should be deleted. These sections are only suited for convertibles but not for derivative securities.

223. *At this stage do you have views about which of the following sections of IOSCO regarding the issuer's Memorandum and Articles of Association you consider to be relevant information to be disclosed in the registration document for these products? Please give your reasons.*

- a) *Section X.B.1.*
- b) *Section X.B.2.*
- c) *Section X.B.3.*
- d) *Section X.B.4.*
- e) *Section X.B.5.*
- f) *Section X.B.6.*
- g) *Section X.B.7.*
- h) *Section X.B.8.*
- i) *Section X.B.9.*



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j) Section X.B.10.

X.B.1.: to be disclosed.

X.B.2-10.: not to be disclosed, only relevant for investments in issuer's equity.

224. *In relation to Section X.C of IOSCO which sets out the Material Contracts disclosure requirements, at this stage do you have views about which material contracts for these products should be summarized in the registration document for these products? Please give your reasons.*

For the reasons set out in our answer to question 148 we object the summary of any material contracts in principle.

226. *Do you consider that the information about the issuer's dividend policy as set out in Section X.F of IOSCO to be relevant for these products? Please give your reasons.*

The dividend policy of the issuer of the derivative security is not relevant for the holder of the derivative securities as the holder is not entitled to any dividend payment of the issuer of the derivative security.

227. *In relation to Section X.H of IOSCO which sets out the Documents on display disclosure requirements, at this stage do you have views about which documents should be put on display for these? Please give your reasons.*

The following documents could be made available for the public on display:

1. most recent annual report of the issuer;
2. published interim figures of the issuer, if any;
3. articles of association of the issuer;
4. paying agency agreement, if any;
5. calculation agency agreement, if any.

No translation should be required. The translation costs and time would outweigh by far the benefits for the investors.

232. *Should all guaranteed derivative securities, irrespective of the percentage return they offer an investor, be treated in the same way, or should there be some form of minimum return that is guaranteed for these instruments in order to be classifiable as a guaranteed return derivative as opposed to a non guaranteed return derivative?*

Guaranteed and non-guaranteed derivative securities should be treated alike. Both categories should be treated like derivative securities and not as debt.

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233. *If you consider that a percentage benchmark should be set to distinguish between those products where the return is high and therefore additional disclosure about the issuer is justified, please specify what this percentage of return should be, and give a reason for your answer.*

No percentage benchmark should be set.

234. *Do you consider that in addition to the percentage return on the investment, the life of the product should be taken into consideration, so that an instrument that has a 100% capital guarantee return with only a 6 month life cycle should be treated for disclosure purposes differently than a product with 100% capital guarantee but with a 10 year life cycle? Please give reasons for your answers.*

The life should not be taken into account. One should avoid making too many distinctions. Otherwise the applications of the rules becomes too difficult. Furthermore, a risk of return also exists with regard to short term products.

249. *Do you consider it an appropriate approach to obtain flexibility by creating specific building blocks on particular characteristics of some issuers, offers, markets and securities?*

There should be further specific building blocks for public offers and frequent issuers according to the distinction required under Art. 7 par. 1 lit a) and d) of the proposed Prospectus directive.

252. **Section I.2.** - *Should advisers be mentioned in all cases, or only if they could be held liable by an investor in relation with the information given in the prospectus?*

Advisors should only be mentioned if they could be held liable by an investor.

254. **Sections I.6. and I.7.** - *Sections I.6. and I.7. both concern the responsibility attached to drawing up a prospectus. Although under the proposed directive it is possible to choose a format consisting of three documents (Registered Document, Securities Note and Summary), these three documents are considered as making one prospectus. Is it therefore correct to assume that responsibility for each of these three parts must rest with the same persons?*

No. It may be that also in a single prospectus various people take responsibility for various parts. This should be possible for the single as well as for the three part prospectus.

255. **Section III.A.** - *Under Section III.A., all securities notes must contain a statement of capitalization and indebtedness. Is such a statement necessary for derivatives?*



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No. At least for derivative securities the capitalization and indebtedness is irrelevant. With regard to the other securities, this information should appear in the registration document rather than in the securities note.

256. **Section III.B. (III.B.1. for the derivatives schedule)** - Section III.B. asks to list the reasons for the offer and the use of proceeds. While this is an important item for shares and bonds, is it also the case for derivatives?

No.

257. **Section III.C.2.(d)** - Under Section III.C.2.(d) requires inclusion of a worked example of the "worst case scenario".

- 1) Does this information provide material information for investors?
In many cases of derivative securities it should be enough to state that the investor may lose its entire invested capital. A worked example would not make this more evident.
- 2) Are there circumstances in which an example of the worst case scenario is not appropriate?

It could be superfluous and its drafting too time-consuming if the entire investment may be lost. A risk warning along the lines of 3)a) is enough.

- 3) Would the disclosures as set out below be an appropriate alternative:
 - a) a risk warning to the effect that investors may lose the value of their entire investment, and/or
 - b) if the investor's liability is not limited to the value of his investment, a statement of that fact, together with a description of the circumstances in which such additional liability arises and the likely financial effect.

The alternative a) is better.

260. **Section V.B.12, first indent of Annex M** - Section V.B.12, first indent of Annex M requires a statement concerning the past performance of the underlying and its volatility. Is this disclosure necessary? Should the requirement for disclosure vary depending upon whether the underlying instrument is admitted to trading on a regulated market and the nature of the market? Should the requirement for disclosure vary depending upon the nature of the underlying instrument?

A statement concerning the past performance of the underlying and its volatility should not be required. The past performance of the underlying does not give any reliable information with regard to the future performance of the underlying. As a consequence thereof, the information on the past performance is of no additional value

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for the investor. Such information could even be misleading, in particular if a good performance in the past makes an investor believe that the performance will continue as it did in the past. Misleading information should be avoided. In addition, a description of the past performance would be extremely cumbersome on the issuer since it would take quite some time and would thereby affect the necessity for a speedy process.

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DOC 1130/02

Brussels, 20 December 2002
JEA/STA/KAV/MIK

Specific remarks to Annex M

Securities Note: Derivative Schedule



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I. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT, ADVISERS, AUDITORS AND PERSONS RESPONSIBLE FOR THE SECURITY NOTE <i>Note: As far as reasonable this section should appear in the Registration Document only. There is no reason to repeat any information in the Securities Note contained already in the Registration Document.</i>	
1. Directors and senior management (company's directors; members of its administrative, supervisory or management bodies; partners with unlimited liability; nominees to serve in any of the aforementioned positions; founders if the company has been established for fewer than 5 years): names and functions.	IDS I A-
2. Advisers that have taken part in the issue/offer: Provide the names and addresses of the company's principal bankers and legal advisers to the extent the company has a continuing relationship with such entities, the sponsor for admission to trading (where required by the host country regulations), and the legal advisers to the issue.	IDS I B
3. Auditors: names and addresses of the company's auditors (together with their membership in a professional body) for the period covered by the consolidated financial statements included in the prospectus, as required by the relevant schedules in accordance with national law.	IDS I C DIR. 2001/34, Schedule A, 1.3
4. Statement whether the annual accounts have been refused by the official auditors or if they contain qualifications, such refusal or such qualifications must be reproduced in full and the reason given.	DIR. 2001/34, Schedule A, 1.3
5. Indication of the other information in the prospectus which has been audited or reviewed by the auditors.	DIR. 2001/34, Schedule A, 1.3
6. Names, addresses and functions of the natural or legal persons responsible for the prospectus or, as the case may be, for certain parts of it with, in the latter case, an indication of those parts.	DIR. 2001/34, Schedule A, 1.1
7. Declaration by those responsible for the prospectus that, to the best of their knowledge, the information given in that part of the securities note, for which they are responsible, is in accordance with the facts and contains no omission likely to affect the import of the prospectus.	DIR. 2001/34, Schedule A, 1.2
II OFFER STATISTICS AND EXPECTED TIMETABLE	
<u>II. A Offer statistics</u>	
Total amount of the issue/offer; distinguishing the securities offered for sale and those offered in subscription. <i>Note: Distinction is unclear</i>	FESCO/01-045, II. 5. a. i) and DIR. 2001/34, Schedule A, 2.2.0

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If the amount is not fixed, a statement to this effect must be made.	DIR. 2001/34, Schedule B, 2.1.0
Describe arrangements and time for announcing to the public the definitive amount of the offer.	Members' proposal
II.B Method and expected timetable	
For all offerings and separately for each group of targeted potential investors:	
1. The time period during which the offer will be open and where and to whom purchase or subscription applications shall be addressed.	IDS II-B.1
2. Describe whether the purchase period may be extended or shortened and the manner and duration of possible extensions or possible early closure or shortening of this period. Describe the manner in which the latter shall be made public.	IDS II-B.1
3. Describe the possibility to reduce subscriptions and/or size.	Members' proposal
4. If the exact dates are not known when the document is first filed or distributed to public, describe arrangements for announcing the final or definitive date or period.	IDS II-B.1
5. Indication of when, and under what circumstances, the offer may be revoked or suspended and whether revocation can occur after dealing has begun.	FESCO/01-045, II. 5. e. ii) and iii)
6. Method and time limits for paying up securities; where payment is partial, the manner and dates on which amounts due are to be paid.	IDS II-B.2
7. Method and time limits for delivery of the securities (including provisional certificates, if applicable) to subscribers or purchasers.	IDS II-B.3
8. A full description of the manner and date in which results of the distribution of securities are to be made public and when appropriate, the manner for refunding excess amounts paid by applicants (including whether interest will be paid). <i><u>Note: Meaning unclear</u></i>	IDS II-B.5
III. KEY INFORMATION ABOUT THE ISSUER	
III.A Capitalization and indebtedness	
A statement of capitalization and indebtedness (distinguishing between guaranteed and unguaranteed, secured and unsecured indebtedness and the total amount of any contingent liabilities) as of a date no earlier than 60 days prior to the date of the document shall be provided. Indebtedness also includes indirect and contingent indebtedness. An appropriate negative statement shall be given, where relevant, in the absence of any loan capital, borrowings and indebtedness and contingent liabilities.	IDS III-B



<u><i>Note: Should be included in registration document only.</i></u>	
III.B Reasons for the offer and use of proceeds	
Reason for the offer and, where applicable, the estimated net amount of the proceeds broken down into each principal intended use thereof. If the anticipated proceeds will not be sufficient to fund all the proposed purposes, the order of priority of such purpose should be given, as well as the amount and sources of other funds needed. If the company has no specific plans for the proceeds, it should discuss the principal reasons for the offering.	IDS III-C.1
<u><i>Note: This does not make sense with regard to derivative securities.</i></u>	
III.C Risk factors	
1. Prominent disclosure of risk factors that are specific to securities to be offered and/or admitted to trading in order to assess the market risk associated with these instruments. Provide also, if applicable, update disclosure of risk factors included in the Registration Document when useful to readers assessing the risk associated with the securities to be offered. To the extent that an item has been disclosed fully in other sections, only a summary should be included in this section and a cross reference to the section where a more detailed discussion is contained should be made.	IDS III-D
2. Risks involved in purchasing the derivative securities. This section should include:	Members'proposal
a) direct or indirect specific risk factors affecting the value and trading price of the derivative securities; and	
b) specific risk factors affecting the realization of the value of the derivative securities.	
c) examples of the way the instrument works <u><i>Note: One example is sufficient. It should be taken into account that in most cases the retail investor is informed about the key features of the derivative by the intermediary (investment firm) being under strict governance of conduct of business rules.</i></u>	
d) examples based on the best and Explanation of the worst case scenario <u><i>Note: Examples of the best case scenario could be misleading for potential investors because these examples could create false expectations for a very high return which, however, most likely will not happen.</i></u>	
e) Mentioning of hedging instruments and whether the investor can buy such instruments <u><i>Note: It is unclear whether the hedging instruments of the issuer or potential hedging instruments of the investor are meant. Whatever is meant, hedging instruments should not be disclosed. How the issuer hedges itself is often confidential and therefore</i></u>	



<u>may not be disclosed. An advice as to the hedging of the investors depends largely on the individual composition of the portfolio of the investor and his investment strategy. It therefore cannot be given generally for all investors in the prospectus.</u>	
IV.A Interests of Experts in the issue/offer	
If any of the named experts or counselors was employed on a contingent basis, owns an amount of shares in the company or its subsidiaries which is material to that person, or has a material, direct or indirect economic interest in the company or that depends on the success of the offering, provide a brief description of the nature and terms of such contingency or interest.	IDS VII-C
IV.B Conflicts of interest in the issue/offer	
Provide a description of any conflict of interest in the issue, detailing the entities involved and the nature of the interest.	Members' proposal
V. OFFER AND ADMISSION TO TRADING DETAILS	
V.A Description of the securities to be offered/ admitted to trading	
1. Describe the type and the class of the securities being offered and/or admitted to trading.	IDS IX-A.5
2. Indicate the Law applicable to the securities.	Members' proposal
3. Indicate whether the securities are registered or bearer ones.	FESCO/01-045, IX-A-8 a)
4. Indicate the currency of the securities issue.	Members' Proposal
5. Means of representation: where book-entry system is to be used, name and address of the entity in charge of keeping such records	Members' proposal
6. Status of the securities being offered and/or admitted to trading: Covenants: Negative pledge, cross default, pari passu and others similar clauses, if any (event of default...)	Members' proposal FESCO/01-045, IX-A-8 a)
7. A description of the rights attached to the securities and procedure for the exercise of any right attached to the securities.	DIR. 2001/34, Schedule A 2.2.2.
8. If the rights evidenced by the securities being offered or admitted to trading are or may be materially limited or qualified by the rights evidenced by any other class of securities or by the provisions of any contract or other documents, include information regarding such limitation or qualification or its effect on the rights evidenced by the securities to be admitted to trading or offered. <u>Note: This information is irrelevant for derivative securities.</u>	IDS IX-A.6
8. A statement of the resolutions, authorisations and approvals, if any, by virtue of which the securities have been or will be created and/or issued. <u>Note: In some jurisdictions such resolutions, authorisations and approvals are not required. Therefore, such information should not</u>	DIR. 2001/34, Schedule A 2.2.0 and Schedule B. 2.2.0.



<u>be compulsory.</u>	
9. The issue date of the securities.	Members' proposal
10. Arrangements for transfer of the securities and (where permitted) any restrictions on their free transferability.	DIR. 2001/34, Schedule A 2.2.4 and IDS IX-A.5 (b) and FESCO/01-045, II. 5. j.
11. Other specific legislation regarding the issue/offer.	Members' proposal
12. the exercise price or final reference price of the derivatives securities <u>Question: What is a final reference price?</u>	2001/34/EC Sch B 2.1. – 2.2.
13. the price at maturity <u>Note: Meaning unclear.</u>	
V.B Terms and conditions of the offer and action required to apply for the offer	
1. Description of the application process, details of where application forms are available, if any. <u>Note: Derivative securities will often be bought through banks or via a stock exchange, and there is no formal application process. Accordingly, the description of an application process should not be compulsory.</u>	FESCO/01-045, II.5. i. i) and ii)
2. Details of the minimum and/or maximum amount of application, if any (whether in number of securities or aggregate amount to invest).	FESCO/01-045, II.5. i. iv)
3. Process for notification to applicants of the amount allotted and indication whether dealing may begin before notification is made, if any.	FESCO/01-045, II.5. i. vi)
4. Possibility of multiple and/or joint applications, if any, and description of the penalties for infringements.	FESCO/01-045, II.5. i. vii)
5. Indication of the period during which an application may be withdrawn, provided that investors are allowed to withdraw their subscription.	Members' proposal
6. Dealing conditions to which the offering is subject, if any.	FESCO/01-045, II.5. f. i)
7. a section setting out the definitions applicable to the terms and conditions <u>Note: The definitions do not necessarily have to be contained in one section but may be contained in the terms and conditions in various sections, wherever appropriate. Rather the complete terms and conditions should be set forth.</u>	Members' proposal
8. all applicable exercise rights <u>Note: Identical to V.A.7.</u>	
9. a description of the exercise procedures, if any, and any limitations in relation to the same	Members' proposal
10. a description of the settlement procedure of the derivative securities detailing the following:	Members' proposal



1. for cash settlement, how holders are to receive or make payments 2. for physical settlement (=cashless exercise) how holders are to receive take or make delivery of the underlying instrument and make payment, if any.	
11. a description of how any return on derivative securities takes place, the payment date, and the way it is calculated • for cash settlement: disclosure setting out how the cash settlement amount is calculated • for physical settlement: disclosure setting out how the amount of the underlying instrument to be delivered is determined • in the case of a choice between cash and physical settlement: disclosure as set out above	Members' proposal
12. information required in respect of the underlying, a statement setting out the type of the underlying and details of where information on the underlying can be obtained: ○ past performance of the underlying in a practical form or otherwise and its volatility over a period corresponding to at least the maturity of the derivative security; in any case a period of two years is sufficient <i>Note: The past performance of the underlying does not give any reliable information with regard to the future performance of the underlying. The good performance in the past could even make an investor believe that the performance will continue as it did in the past, which may be misleading.</i> ○ where the underlying is a security ▪ the name of the issuer of the security ▪ the ISIN (International Security Identification Number) or other such security identification code ○ where the underlying is an index ▪ the name of the index ○ where the underlying is an interest rate ▪ a description of the interest rate ○ others ○ where the underlying does not fall within the categories specified above the securities note must contain equivalent information. ○ where the underlying is a basket consisting of more than one asset of derivative securities ▪ Disclosure of the relevant weightings of each asset in the basket	2001/34/EC Schedule B 2.4.1. FESCO 01-045 Schedule B IV, p.2 / 3
13. a description of any market disruption or settlement disruption events	
14. adjustment rules with relation to events concerning the underlying	
15. expiration or maturity date of the derivative securities, if any.	
16. exercise date or final reference date, if any.	



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<u>Question: What is a final reference date?</u>	
17. nomination Name of a calculation agent, if any .	

V.C Plan of distribution	
1. The various categories of potential investors to which the securities are offered. If the offering is being made simultaneously in the markets of two or more countries and if a <i>tranche</i> has been or is being reserved for certain of these, indicate any such <i>tranche</i> .	FESCO/01-045, II.5. b IDS IX-B.3
2. If securities are reserved for allocation to any group of targeted investors, including, for example, offerings to existing shareholders, directors, or employees or past employees of the company or its subsidiaries, provide details of these and any other preferential arrangements.	IDS IX-B.4
3. To the extent known to the company, indicate whether major shareholders, directors or members of the company's management, supervisory or administrative bodies intended to subscribe in the offering, or whether any person intends to subscribe for more than five per cent of the offering.	IDS IX-B.2
V.D Placing	
1. Details of the co-ordinator(s) of the global offering and of single parts of the offering.	FESCO/01-045, II.5. c. i)
2. Details of the placers in the various countries where the offer takes place.	FESCO/01-045, II.5. c.) ii)
3. Name and address of any paying or depository agents in each country.	Members' proposal
V.E Pricing	
1. Indicate the expected price at which the securities will be offered or the method of determining the price, and the amount of any expenses specifically charged to the subscriber or purchaser. <u>Note: The process of the disclosure of the initial offering price is sufficient (see below).</u>	IDS IX-A.1 IDS II-A
2. Process for the disclosure of the initial offering price.	FESCO/01-045, II.5.d.iv)
V.F Admission to trading and Dealing arrangements	
1. An indication as to whether the securities offered will be the object of an application for admission to trading, with a view to their distribution in a regulated market or other markets. This circumstance must be mentioned, without creating the impression that the admission to trading necessarily will be approved. Indication as to whether the issuer has already filed the application to trading, and, otherwise, indication of the dates when the issuer has the intention to file this application, and, if known, the earliest dates on which the securities will be admitted to trading should be given. An indication of the markets where admission to trading is or will be sought, and if	IDS IX.C

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securities of the same class are already traded on one or more regulated markets, indication of the most relevant.	
2. If simultaneously or almost simultaneously with the creation of the securities for which admission to a regulated market is being sought securities of the same class are subscribed for or placed privately or if securities of other classes are created for public or private placing, details are to be given of the nature of such operations and of the number and characteristics of the securities to which they relate. <u><i>Note: Not relevant for derivative securities.</i></u>	IDS IX.B.8
3. Entities which may act as intermediaries in secondary trading, providing liquidity through bid and offer rates. If any, A description of the terms of their commitment will be included.	Members' proposal
V.G Markets	
Disclose all stock exchanges and other markets on which, to the knowledge of the issuer, the securities to be offered or admitted to trading are traded.	IDS IX-C (reviewed by members)
V.H Selling securities holders- <u><i>Note: Information completely irrelevant for derivative securities. It only relates to share issues.</i></u>	
1. Name and address of the person or entity offering to sell the securities, the nature of any position office or other material relationship that the selling persons has had within the past three yrs. with the company or any of its predecessors or affiliates.	IDS IX-D.1
2. The number and class of securities being offered by each of the selling security holders.	IDS IX-D.2
V. I Expense of the Issue/Offer	
1. The total amount of the discounts or commissions agreed upon by the underwriters or other placement or selling agents and the company issuer or offeror shall be disclosed, as well as the percentage such commissions represent of the total amount of the offering and the amount of discounts or commissions per security.	IDS IX-F.1.
2. A reasonably itemized statement of the major categories of expenses incurred in connection with the issuance and distribution of the securities to be admitted to trading or offered and by whom the expenses are payable, if other than the company. If any of the securities are to be offered for the account of a selling securities holders, indicate the portion of such expense to be borne by such security holder. The information may be given subject to future contingencies: If the amounts of any items are not known, estimates (identifies as such) shall be given. <u><i>Note: an itemized statement of all major expenses risks would be materially misleading for potential investors and does not contribute at all to the assessment of the relevant risk.</i></u>	IDS IX-F.2



VI ADDITIONAL INFORMATION	
<u>VI.A Articles of Association</u> <i><u>Note: To be included in the Registration Document only.</u></i>	
Indicate the register and the entry number therein, if applicable, and describe the company's objects and purposes and where they can be found in the memorandum and articles.	IDS X-B.1
VI.B Exchange controls	
Describe any governmental laws, decrees, regulations or other legislation of the home country of the company which may affect: - the import or export of capital, including the availability of cash and cash equivalents for use by the company's group; - remittance of dividends, interest or other payments to non-resident holders of the company's securities.	IDS X-D
VI.C Taxation	
Provide information regarding taxes to which securities holders may be subject. Information should be included as to whether the company assumes responsibility for the withholding of tax at the source and regarding applicable provisions of any reciprocal tax treaties between the home and host countries, or a statement, if applicable, that there are no such treaties.	IDS.X-E
<u>VI.D Statement by Experts</u> <i><u>Note: To be included in the Registration Document only.</u></i>	
Where a statement or report attributed to a person as an expert is included in the document, provide such persons' name, address and qualifications and a statement to the effect that such statement or report is included, in the form and context in which it is included, with the consent of that person, who has authorized the contents of that part of the document.	IDS X-G
<u>VI.E Documents on display</u>	
Provide an indication of where the documents concerning the company <u>issuer</u> which are referred to in the document may be inspected, by physical or electronic means.	IDS X-H
VI.F Registration Document	
1. Indication of where the Registration Document of the issuer is available for consultation.	Members' proposal
2. The securities note shall provide information that would normally be provided in the registration document if there has been a material change or recent development since the registration document was published.	Draft Directive