
**INTERNATIONAL PRIMARY MARKET
ASSOCIATION**

**Response to CESR's second call for evidence of 7
February 2003**

The International Primary Market Association is the organisation which represents the managers and lead managers of debt and equity securities in the international capital market. A list of IPMA members may be found on its website at www.ipma.org.uk

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EXECUTIVE SUMMARY

Debt Programmes

- The vast majority of issues in the international debt market use a programme structure. Total annual volume of straight debt using programmes approaches €2,000,000,000,000. The programme structure is an efficient and cost-effective way to issue debt securities, which are issued by agreement between EU and non-EU issuers and investors at short notice – sometimes only a few days - to take advantage of market conditions or to meet a specific funding or investment requirement. In addition, many other types of security also use programmes, for instance, asset-backed issues, warrants and debt repackagings. Speed, flexibility, cost-effectiveness and an ability to respond to market conditions are essential. It is extremely important to the EU economy that disruption to this market is avoided.
- The opportunity to do a particular trade at a particular price is only available for a very short time and so it is imperative that there should be no prior approval process for the terms of each drawdown. The base prospectus sets out the most common of the expected terms of issues under the programme. If an opportunity arises in the market for an issue that represents a variation on those common terms, it must be possible to conclude the transaction without a further approval process. Accordingly, in order to preserve the flexibility and speed of the current system, any information which under the CESR proposals would otherwise be in a securities note should be capable of inclusion in the final terms if it forms part of the terms of the debt being issued.
- Many programmes contemplate not only multiple issuers but also multiple types of credit support including guarantees from several guarantors. The proposals need to contemplate this and ensure that issuer-specific information, such as accounting information, is not required when the true credit risk is with the provider of the credit support. Similarly not all providers of credit support will be in the same group as the issuer and only public information will be able to be provided and/or cross referenced.
- A mechanism should be provided for the identification of a single home member state in the case of multiple issuer and guarantor programmes.
- Article 5 of the Directive is paramount. Article 5(1) sets out the basic requirement for the prospectus to contain, in easily analysable and comprehensible form, all information which is necessary to enable investors to make an informed assessment. Our comments in this paper are designed to achieve this objective.
- The base prospectus plus the final terms should contain the same information in substance as the tripartite prospectus.
- Article 7(2)(b) requires that account be taken of the different requirements of investors in non-equity securities (as defined) having a denomination of at least

€50,000. The wholesale treatment should therefore be carried through into the offering programme structure.

- The issuer must be free to present information in the format which it and its advisors consider best achieves the objective of Article 5(1).
- It is important that issuers of programmes can incorporate by reference future disclosure required, for example, under other Directives such as the Market Abuse Directive or Transparency Directive, including financial information, without the need to file a supplementary prospectus.
- Where a supplementary prospectus is required, it should be clear that a complete new prospectus is not required and that the supplement need only contain the specific information which is being updated.
- The nature of an offering programme means that only the information in the base prospectus as updated is capable of being summarised. To summarise the final terms would not only be meaningless but would render them liable for approval, thus making it impossible to operate the offering programme structure.
- Disclosure, if any, of risk factors in the base prospectus should be of those applicable to the issuer and to the types of issue contemplated by the base prospectus. Risk factors which are specific to the issue itself should be capable of being included in the final terms without the final terms document requiring approval.

Derivatives

- The approach to derivatives should be simplified. Some derivatives are well established in the market and disclosure can be easily defined, but a large volume of derivatives are 'ad hoc' and are purchased and retained by professional investors. These critical facts need to be reflected in the disclosure requirements.

Non-EU Issuers

- Non-EU issuers are significant users of the European market and play a vital role in the economy of Europe. The prospectus regime should recognise this reality by enabling them to continue accessing the market without imposing unacceptable costs, for example, by requiring IAS accounting and audit standards.

IOSCO as a basis

- Although the Prospectus Directive refers to IOSCO as a basis, this means using those standards as a guideline and not as a floor of minimum requirements. This is particularly relevant to non-equity securities as IOSCO expressly applies to equity securities only.

Non EU sovereign and quasi sovereign issuers

- Non EU sovereigns and quasi sovereigns are a major sector of the market and a specific Annex (or Annexes) should be provided to cover them.

COMMENTS ON SECOND CALL FOR EVIDENCE

INTRODUCTION

We welcome the opportunity to submit first contributions on the further issues which CESR should consider. Our approach in responding to CESR's second call for evidence has been to use the issues raised as headings in our paper and to comment on those issues.

FORMAT OF THE PROSPECTUS

Format of the Single Prospectus

We support the proposals to permit the publication of a prospectus as a single document. In order to ensure that information is presented in a way which is easily analysable and comprehensible as required by Article 5(1) of the Directive, it should be made clear that there is no requirement to follow the specific layout of any building block. Among other benefits, this will help minimise the obstacles to mutual recognition of third country prospectuses.

Offering Programmes

General Comments

We have set out below how the present base prospectus regime works in relation to offering programmes to assist in ensuring that programmes can continue functioning efficiently within the framework of the proposed Directive. Article 5(4) covers the issue of a wide range of securities by means of a wide range of "programmes", such as debt issuance programmes, as well as programmes for asset-backed issues and all sorts of derivatives, from equity warrants to repackaging of obligations such as bonds and loans. Our analysis below focuses on debt issuance programmes but the underlying principles apply to other programme issues.

Outline of debt issuance programmes

Debt issuance programmes are uncommitted facilities which permit an issuer (or issuers) to put in place most of the documentation for a debt issue (save for the final terms of the securities themselves) and subsequently issue debt securities under this standard documentation by completing a pricing supplement containing the particular final terms of that debt issue. The issuer(s) and the dealers negotiate and agree these standard terms at the time the programme is established, and the work involved in producing the programme documentation reduces the negotiation and detailed drafting required at the time of each issuance. The standardising of the documentation therefore allows the issuer to issue debt on very short time scales with reduced costs and is a way for issuers to receive debt funding on a regular or continuous basis.

Debt issuance programmes allow for issues of virtually any maturity, for example from one month to 30 years or more, and in many currencies, the most common being Euro, U.S. Dollars, Yen and Sterling. The documentation also sets out standard terms and conditions for a variety of possible types of issue including senior or

subordinated, fixed rate and floating rate debt, debt securities which change rates of interest during their term and rates of interest linked, for example, to shares listed on a regulated market. Programmes are also used for asset-backed notes where the underlying assets are revenue-generating on a continuing basis, e.g., credit card receivables.

The documentation provides that the standard terms and conditions may be varied by the pricing supplement to accommodate other structures and currencies.

Another common feature of debt issuance programmes is that there is often more than one possible issuer under the programme. For example, the issuers may include several members of a group of companies located in different countries both within and outside the EU. In such circumstances it is also possible that junior members of the group may issue under the guarantee of their parent company (which may also be a potential issuer on the programme), so the programme may allow the issuance of both guaranteed and unguaranteed debt.

A programme enables an issuer more easily to ensure that it will have sufficient cash to meet its daily needs and provides investors with timely and efficient access to investment and risk management opportunities. Drawdowns are often made over very short time scales to meet issuer and investor needs, for example, three or five days in total from the date of agreement between issuer and dealer. Another major benefit of the use of programmes is reduced costs for issuers and investors. These advantages are so significant that programme issuance now accounts for as much as 80% of the primary publicly announced international debt market and an even higher proportion of the private placement market for debt.

Final Terms

In order to preserve the current system and in particular its flexibility and speed, any information which, under the CESR proposals, would otherwise be in a securities note, should be capable of inclusion in the final terms, if it forms part of the terms of the debt being issued. To achieve this, as wide a definition as possible of “final terms of the offer” under Article 5(4) is required at Level 2. Such a definition could be as follows: “final terms are those terms of the security or the offer which are specific to the particular issue”. Alternatively, CESR could offer guidance as to the interpretation of the phrase if it were felt that a formal definition was inappropriate.

Other Comments on Programmes

Multiple Issuer Programmes

Multiple issuer programmes raise a question as to which competent authority should approve the base prospectus. If the denominations allowed under the programme are below €5,000, EU issuers cannot choose their competent authority. So a programme with issuers from France, Spain and Germany would potentially have three competent authorities, even though in many cases there might be a common guarantor, perhaps from outside the EU. The alternative of setting up three separate

programmes, one for each issuer, is very unattractive as it will be much more costly and time consuming.

Wholesale Programmes

The distinction between retail and wholesale issues mandated by Article 7 (2) (B) of the directive also applies to programmes. Discrete requirements for wholesale programmes will be necessary.

MINIMUM INFORMATION

Derivative securities

General Comments

Our views on the approach to derivatives are as set out in Part 1, sections 8 and 9 and in response to questions 160 to 234 of the first consultation paper and also in response to questions 66 to 93 of the second consultation paper. For your convenience these views are summarised in Appendix 2 to this paper.

Issues by credit institutions

General Comments

Banks (including for these purposes credit institutions and regulated firms such as investment banks) should be subject to special treatment. As banks are under close regulatory control and prudential supervision, less information about the issuer is required. The large number of such entities issuing securities on a frequent basis justifies a specialist approach.

Our views on the treatment of banks are set out in our response to your second consultation paper in Part I, section 8 and in our response to questions 43 to 59. For ease of reference we have summarised these views in Appendix 3.

Other regulated entities

Special recognition should also be given to other regulated entities such as insurance companies which are under close regulatory control and prudential supervision in a comparable way to banks. To deny such recognition would effectively be to disadvantage entities which in many respects are competing against banks but might be subject to greater costs if more onerous disclosure requirements applied.

Non EU entities

The above points apply equally to EU and non EU banks and regulated entities.

Wholesale issues

General Comments

Some of these points have been addressed elsewhere in our responses but as they are of great importance in market terms we are setting them out again.

Treatment must extend to all non-equity securities

CESR's current proposals appear to interpret the Directive as only permitting separate wholesale treatment in the context of pure debt securities. They do not even extend to convertible bonds, which the Directive specifically states are debt securities (see Recital 11 inserted by ECOFIN). It is not only debt securities that have denominations. Derivative securities and global depository receipts may meet the threshold requirement. Recommendations should therefore be made in relation to the wholesale treatment of all non-equity securities.

Equity Securities

In addition, and as set out in our first round of comments, we strongly believe that CESR should permit the adaptation of the equity disclosure requirements in circumstances where the issue is targeted at professionals – this is frequently the case for non-EU issues where such adaptation is both appropriate and consistent with the professionals' ability to assess information.

Wholesale Disclosure regime prevails

It must also be clear that the wholesale disclosure regime prevails over all other disclosure requirements. There should be no doubt that it is not to be applied in conjunction with any other requirements but supersedes all other requirements. For example, the wholesale regime should apply to all depository receipts with a minimum denomination of €50,000, regardless of whether the underlying security is debt or equity. It should be clear that in this case the equity disclosure regime, which is designed to provide retail disclosure, does not apply.

Wholesale Non-EU Issues of non-equity securities

Provisions made at Level 2 should not be permitted to take the substance out of the differentiated wholesale regime mandated at Level 1. Investors in wholesale securities need such disclosure as will enable them to make a sufficiently well informed investment decision. They do not need standardised disclosure. Level 2 should not create thresholds based on the quality of information and put up barriers to a fluid market in wholesale securities whether of EU or non-EU issuers. Investors in wholesale securities should be permitted to make their own risk assessments and to take their own risks.

Non-EU Issuers of equity securities

CESR should consider a more appropriate disclosure regime for non-EU issuers of equity securities targeted at professional investors especially where the securities are

already listed on a home country exchange (outside the EU). The regime should take account of those facts, as envisaged by Recital 33 of the Directive. If the EU disclosure regime is so costly and inconvenient that such issuers decide to avoid it, EU investors can still buy the securities by going to the non-EU issuer's home market (where there may be less protection than a more reasonable EU regime would have afforded). It will damage the EU market by reducing its size and liquidity. If non-EU issuers are welcomed to the market on terms that are appropriately adapted to their circumstances, EU investors have a degree of protection they might not otherwise have were they to buy on the issuer's home market.

Guaranteed Issues

While not only applicable to wholesale issues, this is an important issue because a significant number of issues are guaranteed. Where an issue is guaranteed, the focus of the disclosure requirement should be on the guarantor and not the issuer, and there should be correspondingly reduced disclosure requirements in relation to the issuer itself.

Issues by sovereign states and municipalities

General Comments

We note that CESR will consider the position of issues by sovereign states and municipalities. The disclosure requirements should be adapted for issues by EU sovereign states and municipalities where they choose to produce a prospectus. This could be done, not by a separate building block, but by indicating which sections of the relevant core building block do not apply or need to be modified.

Non-EU States

We would also draw your attention to our previous comments on issues by non-EU states, non-EU regional or local authorities and public international bodies of which no Member State is a member set out in Part I, section 1.5 of our response to CESR second consultation paper. We have summarised our views below.

Issues by or guaranteed by non-EU states accounted for 15% of the global debt securities market as at September 2002. There is neither a clear exemption which covers non-EU states and quasi-states, nor any positive set of provisions as to how the requirements of the Directive shall apply to them. We fear that because such entities are not covered in any way by the Directive they may be precluded from issuing in the EU at all. We realise that CESR cannot affect the wording of the Directive itself, but we request clarification on this point at Level 2 so that the Directive as it stands can be made to operate in a way that is at least consistent with the present EU market approach to such issues.

ANNUAL INFORMATION

Method of publication of the annual disclosure document

Our suggested approach to publication would be by way of a statement detailing where the annual disclosures can be found. The document should not need to contain the actual information; cross references should suffice. This statement should be disseminated in the same way as other regulatory announcements such as through a designated news service or by filing it with a competent authority.

We also think that Level 2 should make it clear that the information list published under Article 10 can include information that has become out of date (or, indeed, will be required by Article 10 to do so). For example, one of the listed items of information could be nine months old. It will have been overtaken by events (that will have been disclosed to the market, when required by provisions of the Market Abuse Directive). But when the Article 10 list is published at the end of the year, investors in the market are being effectively invited to review this out of date information. This could make the issuer liable to such investors, unless the Level 2 regime expressly contemplates that the information referred to need not be updated by reference to more recent materials. It should also be made clear that the list itself can contain a warning statement to this effect.

Alternatively, issuers should be allowed to omit information that has become redundant.

Finally, we believe that, by publishing the Article 10 list, an issuer should not be extending its liability to investors. If information is filed in Country X, it will have been prepared to Country X's standards and the issuer will be liable for it under Country X's laws. If the Article 10 list includes a reference to this information, this may amount to republication under EU States' laws and thereby result in liability for the issuer under the law of a Member State. This seems wrong, particularly given the different standard of preparation of the original information. It should be possible to disclaim such additional liability by inclusion of an appropriate legend in the Article 10 list and the Level 2 provisions should make this clear.

INCORPORATION BY REFERENCE

There should not be any limitations on the documents that can be incorporated by reference provided that the requirements of the Prospectus Directive are met in relation to that document. We would suggest that competent authorities should be allowed general flexibility to allow documents to be incorporated by reference.

In relation to accounts and other documents of a routine nature, an issuer should be able to incorporate by reference these as they are issued. This could be done in one of two ways. Either the issuer could file a statement with the competent authority that it is incorporating by reference future accounts. Alternatively, the competent authority could pre-approve certain documents such as the quarterly accounts. This is the approach adopted by, for example, the Commission des Opérations de Bourse (COB) in Paris, subject to the COB's power to intervene at a later stage if necessary. Such a power could be reserved to the competent authority. All regular financial information should be capable of incorporation by reference or pre-approval. This would ensure consistency between the various Directives in this area, especially the Market Abuse Directive and the proposed Transparency Obligations Directive. It does not make sense that a set of accounts, for example, produced under the

Transparency Obligations Directive should then be subject to an additional approval requirement under the Prospectus Directive.

This concept is particularly important in relation to programmes. If the publication of interim financials triggers an updating and approval requirement, then frequent issuers will be prevented from issuing under the programme at regular intervals throughout the year, while the relevant approval period runs.

In relation to third country issuers, we believe that they should be permitted to incorporate by reference any document that is publicly available, or alternatively, to file documents with the competent authority which could then be incorporated by reference.

PUBLICATION OF THE PROSPECTUS

Method of publication

The notice should be disseminated in the same way as other regulatory announcements such as through a designated news service or filed with the competent authority. There should not be any requirement to publish a notice in a newspaper.

Advertising

We have no further comments at this stage and await the consultation paper.

RECOGNITION OF PROSPECTUSES DRAWN UP IN THIRD COUNTRIES

We encourage the Commission to give CESR a mandate on drafting implementing rules on the interpretation and application of the term “equivalence” in the context of the treatment of prospectuses drawn up by third country issuers. In relation to wholesale issues of securities, a prospectus drawn up by non-EU issuers should be recognised in the EU. The wholesale regime in the Directive is intended to provide certain investors with continuing access to a diverse range of issuers and investments. Investors in wholesale securities need such disclosure as will enable them to make a sufficiently well informed investment decision. They do not need standardised disclosure. For example, it may be that a non-EU issuer’s accounts are not prepared on a “true and fair” basis – we understand that this is as true of issuers using US GAAP as of issuers using systems of GAAP current in non-OECD countries. But wholesale investors should be able to buy the securities of such issuers on EU markets, provided the accounting basis is properly disclosed. They should be permitted to make their own risk assessments and to take their own risks.

In relation to retail securities, provided the prospectus contains sufficient information for investor requirements it should be capable of being recognised in the EU. It should not need to contain identical information.

CONCLUSION

The second call for evidence addresses questions which are at the same time extremely complex and of enormous importance to the international and EU securities markets. IPMA stands ready to assist CESR and the European Commission at any time to develop appropriate regulation.

APPENDIX 1 : DERIVATIVE PRODUCTS

Well-established derivative products

Derivative products which are well-established, such as covered warrants, should be subject to appropriate disclosure requirements. Rather than separate building blocks, the disclosure requirements should be dealt with by indicating which elements of the core building block apply. This building block could be expressed at such a level of generality that it would be capable of capturing the wide range of present and possible derivative products. The disclosure required in relation to each particular product could then be determined by the competent authority exercising its discretion and acting together with other EU competent authorities at Level 3. Derivative securities are issued by a wide range of issuers and not just SPVs or financial institutions. Broadly drafted disclosure requirements in respect of derivative issues will cater for this.

For those derivative products issued mainly to wholesale investors, there should be a disclosure regime that should consist of a description of the terms of the product, disclosure on the underlying security or index and so on only insofar as it is publicly available and disclosure on the issuer only if there is material credit exposure that is relevant in a professional to professional situation. If the issuer is a bank or other regulated entity, no disclosure at all should be required in relation to that issuer.

For derivative products targeted at retail investors such as covered warrants, information on the issuers of the underlying instrument should not be required to be disclosed in the prospectus even when they are offered to retail investors. Investors in covered warrants can be compared to investors in equities in the secondary market who make investment decisions without the need to be supplied with the most recent publicly available information on the issuer. They could, after all, buy the share itself in the secondary market for forward delivery or buy an over-the-counter option and there would be no disclosure requirement in either case. Investors in covered warrants can similarly be assumed to have knowledge of the issuer of the underlying instrument and there should not be any requirement to provide this information in the prospectus.

In addition, most covered warrants are issued by issuers within a financial institution group. Given the fact that financial institution groups are regulated and the credit exposure on the issuer of the covered warrant is limited, issuers should not need to provide any detailed disclosure. A short form of disclosure should therefore be developed which requires minimum disclosure on the issuer, no disclosure on the underlying instruments where they are securities admitted to trading on an EU-regulated market or any mutually recognised market, and very limited disclosure where they are not. Clearly, the terms of the warrants such as exercise terms would need to be included.

Other derivative products

There are many other types of derivative products. Derivative products are innovative products and as such difficult to define precisely. Rather than attempting an overly complex approach to definitions and distinctions which attempt to capture all types of

derivative products we have previously suggested a definition that provides broad guidelines of the products falling within this category. The definition we have suggested is:

“**derivative** means any security:

- (a) under any material term of which the amount of any payment fluctuates or is determined by reference to an asset or index or the occurrence of an event unless such term is supplementary or customary in international debt markets;
or
- (b) under a term of which any asset may or will be delivered

and which security (in either case) is not an equity security, asset backed security, convertible or exchangeable or covered warrant”.

APPENDIX 3: BANKS AND OTHER REGULATED ENTITIES

All issues made by banks should be addressed

Any building block for banks must address all types of issue made by banks for which different types of disclosure will be appropriate. It is not clear how the disclosure requirements as presently conceived by CESR would apply to a bank issuing, for example, equity securities. To the extent that the disclosures required by CESR Annex 1 would apply in whole or in part, those requirements would need to be modified to cater for banks as opposed to corporates. For example, the working capital requirement should not apply to banks, and the requirements as to indebtedness, contingent liabilities, plant and equipment and other inappropriate disclosures would need to be modified. Contingent liabilities are a particular problem for banks because they form a significant part of their day-to-day business (for example in issuing cheque guarantees) and therefore vary on a daily (in fact minute by minute) basis.

Group companies of banks

In defining banks for these purposes, holding companies and other group companies of banks should be included. Such companies often are the entity within the group from which the issue is made and the disclosure regime will require similar modification in respect of such companies as for banks themselves. For example, holding companies will have the same difficulties as banks with the requirement to produce a capitalisation and indebtedness statement.

Non-EU banks

The specialist treatment for banks should be applied to non-EU banks also. A large number of banks would otherwise be unjustifiably excluded and subject to disclosure requirements which are not relevant for banks. We suggest that the requirements of the CESR Annex for banks are applied to OECD-regulated banks without the need for any equivalence or similarity test in terms of the level of prudential and regulatory supervision.

Non EU regulated entities

The points made above with regard to other regulated EU entities apply equally to comparable non EU issuers.