

Prospectus Directive: Significant changes for summaries and final terms

ESMA's technical advice to the European Commission dated 4 October 2011 on, among other things, final terms and summaries could lead to significant changes to capital markets documentation. If adopted by the Commission, proposals would include longer summaries for prospectuses and, more significantly, individual summaries to accompany each set of final terms. ESMA acknowledges that structured debt products will be most affected, but there would also be an impact on "vanilla" debt programmes and issues.

Background and timeline

Directive 2010/73/EU, which amended the Prospectus Directive (2003/71/EC), came into force on 31 December 2010. Member states have until 1 July 2012 to implement the amending Directive provisions. For certain changes, the amending Directive provides for delegated acts and, in January 2011, the European Commission mandated the European Securities and Markets Association (ESMA) to advise on certain of these delegated acts and to report back with technical advice by 30 September 2011. Following a short consultation period in June and July, ESMA has published its Final Report to the European Commission with advice on:

- the format of the final terms for a base prospectus;
- the format and detailed content of the summary; and
- a proportionate disclosure regime.

Further advice from ESMA to the European Commission is due to follow later this year on additional matters, including the form of issuer consent for use of a prospectus. This short briefing highlights key proposals relating to the first two bullets - that is, final terms and summaries - for which the European Commission is required to adopt delegated acts by 1 July 2012.

Final terms - A more restrictive approach

Following the introduction of the Prospectus Directive in 2005, a constant debate has been over how much additional information could be included in final terms, as opposed to requiring a supplement to a base prospectus. In response to what ESMA sees as abusive practice in the market, stretching the boundaries of what may be included (in light of the fact that final terms are not reviewed by competent authorities), the Final Report proposes clearer guidelines and a restrictive approach. Proposals include:

- *A set format:* The ESMA Final Report rigidly classes different types of information as Category A, B or C, in a very detailed table, with an indication of whether such information may be included in final terms or can only be included in the base prospectus. ESMA is still considering what "Additional Information" (such as securities legends) may be included in final terms.
- *"Not applicable" items deleted:* "Not applicable" items will need to be deleted, with the consequence that it will be difficult to compare the final terms for different series from the same issuer with each other and with the pro forma in the base prospectus.
- *No new algebra:* Any formula must be checked by the competent authority and, therefore, be contained in a base prospectus, not final terms. Amendments to formulae contained in a base prospectus will generally need to be dealt with in a supplement, not final terms.

Key Issues

ESMA's technical advice to Commission

Background and timeline

Final Terms

- Restrictive approach and set format
- "Not applicable" items deleted
- No new algebra
- No descriptions of indices, etc.
- Bespoke summary to be annexed to each final terms
- No "integrated" final terms

Summaries

- A new disclosure annex for summaries
- Summaries should be self-standing
- No word limit but up to 15 pages long or 7% of length
- Same length for final terms
- Some similar concepts

Outstanding questions

- How will the transitional period be handled?
- Will issuers resort to multiple programmes? Or wholesale only programme?
- How will this fit with "PRIIPS"?

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- *No new disclosure of indices / market disruption events / cashflows:* All of these may only be disclosed in a prospectus.
However, if, as a consequence, a supplement to the base prospectus is required in relation to a specific issue of securities, ESMA advises that the walk-away right will only apply to that particular issue.
- *Summary to be annexed to final terms:* Possibly the most contentious of the proposals is the concept that a separate, issue-specific summary must be produced and annexed to each set of final terms – with the same overall length limit as for a prospectus summary. This will have cost and timing implications for issuers, including translation costs as the issue summaries would need to be translated into the same languages as the base prospectus summary. The individual summaries will be prepared by selecting a mixture of information known and disclosed at the time of the base prospectus (presumably taken from the base prospectus summary) and certain limited additional information relating to the particular securities issue originally indicated in placeholders in the base prospectus.
- *No "integrated" final terms – "Integrated" or "consolidated" final terms,* which repeat much of the disclosure already made in a base prospectus and are intended to be read as a stand-alone document, will not be permitted. This will present issues for the German market where such an approach to final terms is customary.

Summaries – up to 15 pages long or 7% of the length of a prospectus

The amending Directive contains a requirement for summaries to contain "key information". The Final Report contains proposals for a common format and content for summaries. These broadly follow the earlier consultation proposals, for example:

- *A new annex for the Prospectus Regulation ((EC) No 809/2004), with a checklist of items to be included in all summaries:* The draft annex comprises five sections for content and would include risk factors.
- *Summaries should be self-standing:* No cross-referencing to the prospectus is permitted.
- *Length:* The Final Report proposes an end to the 2,500 word limit contained in the Prospectus Directive. Instead, the suggestion is that the summary should be no longer than 7 % of the length of the prospectus or 15 pages long, whichever is the shorter.
- *Same length for final terms:* The same limit on length is imposed on the summaries to be annexed to final terms.
- *Some similar concepts remain:* For example: summaries are not generally required for wholesale programmes (but will need to fulfil the requirements if denoted as a "summary", as opposed to an "overview"); no civil liability attaches unless the summary is misleading, inaccurate or inconsistent, or does not provide key information, when read with the base prospectus; summaries will need to be translated in the same circumstances as under the current regime.

Outstanding questions

If the European Commission is to meet the 1 July 2012 implementation deadline, then it is likely that a draft Regulation will be published before the end of 2011. If so, then there will be a five or six month window for issuers to prepare for the new rules. It is, moreover, not a foregone conclusion that the European Commission will adopt all of the technical advice contained in ESMA's Final Report – indeed, lobbying is still taking place regarding certain of the suggestions. However, if adopted in the current form, questions remain, such as:

- *How will the transition be handled by competent authorities?* The Report indicates that a base prospectus approved before the 1 July 2012 deadline may continue to be used, supplemented and passported after 1 July 2012. Given the variance between pre- and post-July 2012 documentation, though, it is unclear how competent authorities will address this or whether certain issuers might update programmes earlier than usual to accommodate the changes. In any event, a prospectus drawn up for the first time on or after 1 July 2012 and incorporating a registration document approved before July 2012 will be required to comply with the new requirements.
- *Will we see a multitude of programmes for different products? Or a move away from retail programmes because of the summary requirements?* A common question has been whether changes will encourage issuers to split out different products into different programmes. The Report indicates that ESMA does not see a problem with lengthy programmes with multiple products, as long as the prospectuses are clear and readable, but, for programmes with complex products, it is difficult to see how the mandated disclosure in the summary can be achieved within the overall limits on length. Moreover, the fact that the use of prospectus

supplements may compromise readability leads ESMA to state that it expects and encourages the use of specialised base prospectuses or stand-alone prospectuses.

- *How do summaries sit with Packaged Retail Investment Products (PRIIPS) Key Investor Information Documents (KIIDs)?* ESMA asks the European Commission to consider how the summary proposals and the shorter KIIDs under the delayed PRIIPS initiative might be aligned. In contrast to the long summary suggested in ESMA's Final Report, the KIIDs proposals have contemplated much more concise summaries.

Links

European Commission's mandate to ESMA - "Formal Request to ESMA for Technical Advice on possible Delegated Acts Concerning the Amended Prospectus Directive (2003/71/EC)", January 2011: http://ec.europa.eu/internal_market/securities/docs/prospectus/esmaadv_en.pdf

ESMA Consultation: "ESMA's technical advice on possible delegated acts concerning the Prospectus Directive as amended by the Directive 2010/73/EU", 15 June 2011: http://www.esma.europa.eu/index.php?page=document_details&id=7601&from_id=40

ESMA Final Report: "Final Report - ESMA's technical advice on possible delegated acts concerning the Prospectus Directive as amended by the Directive 2010/73/EU", dated 4 October 2011: <http://www.esma.europa.eu/popup2.php?id=7983>

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