

Response to

CESR's Advice on Level 2 Implementing Measures for the Proposed Prospectus Directive

Ref. CESR/03-066b, 03-67b, 03-128, 03-129

16 June 2003

Introduction

Deutsches Aktieninstitut e.V. is the association of German exchange-listed stock corporations and other companies and institutions which are engaged in the capital markets development. Its most important tasks include supporting the relevant institutional and legal framework of the German capital market and the development of an harmonised European capital market, enhancing corporate financing in Germany and promoting the acceptance for equity among investors and companies.

A. General Comments

We welcome that, in accordance with the proposed Prospectus Directive, CESR has changed its approach and does not regard the IOSCO disclosure standards as the minimum disclosure requirements to be included in a prospectus and that at large the degree of abstractness has get higher. In particular, we welcome that CESR has decided not to include advice in relation to most specific issuers/industries. Despite the large number of changes made following the comments of the various parties, there remain some issues which we believe are still outstanding.

First, the ranking among the various registration documents should be clear. It should be possible for issuers to base a bond issue, for instance, on a registration document for equity issues as long as this registration document is still valid. In other words, each "higher ranking" registration document should cover the issue of other securities which, as such, would only require a less comprehensive registration document. An unnecessary duplication of registration documents would lead to a lack of transparency instead of giving



any additional benefit to investors. Therefore, as CESR announced in the April Advice in paragraph 30, it would be extremely useful to have clear guidance to the effect how the various building blocks and schedules may be combined and/or applied to specific issues of securities which do not entirely fall within one of the types of securities for which schedules have been provided for. We therefore welcome that a "Road Map", which we have just received, has been issued. We will review it with respect to the above and let you know any comments we may have.

Furthermore, we would like to draw your attention to the proposed tax disclosure requirements which would lead to a time consuming legal survey of the tax treatment of the relevant securities in respect of all jurisdictions where the securities are offered and, as a consequence, also to very high costs for issuers. By contrast, for transparency reasons, only any withholding or deduction from the amounts paid out by the issuer prior to the amounts being credit to the accounts of the investors is of particular interest for an investor while there should be no requirement to provide investors in all relevant jurisdictions with general tax advice on the products offered by the issuer.

B. Detailed Comments

I. Advice April 2003

Paragraph 35:

Although it is not a strict requirement to reconcile the consolidated financial statements for the previous years, CESR considers such reconciliation as "sensible". We do not believe that it is practicable and reasonable with respect to time and costs to produce such restated or reconciled financial statements retrospectively for the previous year or possibly even for two years. Such exercise would constitute an enormous burden for issuers. Even the IASB itself has considered to limit the reconciliation to the previous year only in paragraph 29 of the Exposure Draft 1 relating to the First-time Application of International Financial Reporting Standards.

Paragraph 70:

Annex A – Equity Registration Document

- 1.1 CESR should clarify that only the persons who, according to the law applicable, are responsible for the prospectus are to be named in the prospectus. Such persons could be either natural persons or (and not "and") legal persons or both depending on the legal concept which the relevant country has chosen.

- 14.1.** We welcome that paragraph 14.1(ii) is now limited to convictions in relation to fraudulent offences for at least the previous five years and that paragraph 14.1(iii) refers to three general concepts of insolvency scenarios rather than setting out a detailed list of a number of various possible (partly voluntary) liquidation procedures.

However, with respect to 14.1(iii), the terms “with which a director was associated” is very broad and might even comprise scenarios where a director was involved in an insolvency as a non-executive employee. The previous draft was much clearer regarding the function of a director in which he must have been involved in a liquidation of a company. We therefore believe that CESR should use the previous expression “where such person was a director with an executive function at the time of or within the 12 months preceding such events”.

Furthermore, as far as “public criticisms” are concerned, however, it should be described more clearly what, precisely, is meant by this term. In particular, it should be made clear that a public reprimand or criticism (public criticisms) should only be included in the prospectus if a violation of capital market laws is involved, which could be relevant for an assessment of the security and thus for an investment decision. In addition, it should be clarified that only official public criticism in the form of written statements of the competent authority are to be included.

- 20.1** A cash flow statement should only be required if such requirement exists under local GAAP. Under German GAAP for instance, such statement is not required so that issuers, which have not prepared their accounts in accordance with the rules of the international capital markets so far, would need to produce such statements retrospectively for the last three years. This would be very burdensome for such issuers and should therefore be avoided. Accordingly, the IAS Regulation provides for an opening clause where national GAAP contain different requirements.
- 20.2** As set out in our response to questions 51 to 55 of the first Consultation Paper, it should not be mandatory to include pro forma financial information into a prospectus. In judging the relevance of pro forma information, such information regularly has a high hypothetical character and therefore can also only have a limited relevance. Ultimately, the difficulty also lies in the fact that it is often not possible to make a meaningful comparison of the financial figures, since these are based, for example, on different accounting practices, or because the same accounting principles were applied differently. Moreover, only a comparison of the figures themselves takes place, but fails to take into account precisely other factors which result from the purchase of another company, such as completely different planning or wholesale

prices and conditions, for example. For this reason, there is a great danger, as also addressed by CESR in paragraph 48, that the pro forma information will be misleading. In other words, pro forma information ultimately may only give the illusion of accuracy. It is therefore not appropriate to force an issuer to include such information into a prospectus. CESR should, as a consequence, only provide for a voluntary disclosure of pro forma information.

20.4 CESR should clarify, at least by providing an example, which standards fulfil the requirement of an “equivalent standard” pursuant to which the financial statements are not drawn up so as to give a true and fair view.

20.7.1. Although CESR’s Advice does not require that the interim financial statements have been reviewed by an auditor, such a review may have indeed taken place. In this case, the result of this review should be included in the prospectus in the form of a reprint of the relevant certificate as already set out in our comments on Annex A.II.2 of the first Consultation Paper.

20.10 It is not quite clear what is meant by the issuer’s “trading position” which is referred to in addition to the issuer’s financial position (which should be the only relevant position in this context).

22. We welcome that material contracts must not be put on display and that certain detailed requirements to be included in the summary of each material contract have been removed. However, the objective of such summary could still be made clearer. Only the risks resulting from such material contracts for the relevant investment are to be pointed out, ie. there is no requirement to provide an investor with superfluous information even if such information is contained in a material contract.

24. The audit report should be available on display. It is not quite clear whether the audit report is covered by no. 24 as it is currently drafted. Thus, a clarification to this effect would be useful.

Paragraph 72:

Annex C – Equity Securities Note

1.1 CESR should clarify that only the persons who, according to the law applicable, are responsible for the prospectus are to be named in the prospectus. Such persons could be either natural persons or (and not “and”) legal persons or both depending on the legal concept which the relevant country has chosen.

- 3.3** We recognise that, by contrast to Annex K, IV.B under the first Consultation Paper, Annex C, 3.3 now limits the interest to be disclose to material interest. However, the scope of this requirement and the circle of persons to whom this requirement remains somewhat unclear. CESR should therefore either remove this requirement in whole (in general, such conflicts of interest are already covered by other regulatory requirements) or at least give some examples of particular types of conflicts of interests envisaged by CESR.
- 4.11** As set out in our response to the first Consultation Paper, it is crucial for multinational offers and an integrated pan-European capital market that the tax disclosure is limited to withholding tax together with information to the effect that each investor should seek to obtain its own tax advice. Disclosure on withholding tax is necessary because any tax deductions or withholding directly affect the amount paid out to investors. By contrast, a prospectus does not and may not serve as individual tax advice on an investment in a specific financial instrument. Therefore it may not replace individual tax advice which an investor may need with respect to his home jurisdiction. Information regarding taxes to which holders in the „targeted“ country may be subject could even be misleading since each tax advice has to take into account the individual circumstances and taxation of the relevant investor. By its nature, a prospectus can therefore not reflect all relevant tax issues which might be relevant for each investor individually in each country where the securities are offered. And even an attempt to cover the most important tax matters in all relevant countries would result in huge costs of the issuer and the prospectus being a voluminous book. Such far reaching tax „disclosure“ (which would in fact be an investment advice rather than disclosure relating to the securities offered) would therefore constitute a significant barrier to the creation of a harmonised pan European capital market.
- 5.3.4** It is not clear how the “material disparity” between the public offer price and the purchase price of securities acquired by the directors or senior management during the past three(!) years could be determined since, in general, any price movements are to a very large extent based on the movement of market prices and market volatility in general. This new disclosure requirement should therefore be removed.
- 5.4.3** The individual commissions and quotas of underwriters are of particular interest to competitors rather than for investors. Only the aggregate amount of commissions should therefore be disclosed as part of the expenses for the relevant issue of securities (see no. 8 of the schedule). Moreover, the quotas of the underwriters are often specified only at the end of the subscription period, i.e. after the prospectus has been published. As a consequence, a separate supplementary prospectus would be required only for disclosure on the relevant quotas.

Paragraph 73:
Annex D – Debt Registration Document

- 1.1 CESR should clarify that only the persons who, according to the law applicable, are responsible for the prospectus are to be named in the prospectus. Such persons could be either natural persons or (and not “and”) legal persons or both depending on the legal concept which the relevant country has chosen.
4. For the sake of clarity, the risk factors disclosure requirement should be amended to the effect that such risk factors are only to be described if such risk factors exist.
- 5.1.5 This disclosure requirement is not contained in Annex A (Equity Registration Document). This inconsistency would hinder issuers to use the Equity Registration Document for debt issues (see also our General Comments).
- 5.2 As set out in our response to the first Consultation Paper, current and future investments are normally not of any particular relevance for investors in debt securities. It should therefore only be disclosed in particular circumstances under the general disclosure requirement if, due to the specific nature and risks of the relevant investments, the current and future investments may have any impact on the ability of the issuer to pay interest or to repay the principal.
- 5.2.3 This disclosure requirement is not contained in Annex A (Equity Registration Document). This inconsistency would hinder issuers to use the Equity Registration Document for debt issues (see also our General Comments).
- 6.1.2 New products as such are not relevant for the assessment of the insolvency risk in respect of debt securities. Only if new products may have a material impact on the business of the issuer disclosure would be required. In this case however, such material products would be expected to be referred to in a description of the principal activities of the issuer (see 6.1).
- 10.2 In general, conflicts of interest are already covered by other regulatory requirements. In addition, we still believe that such information is not of any particular relevance for investors in debt securities.
- 11.2 With respect to corporate governance rules the same reasoning as for a description of conflicts of interest applies. This means that, in general, corporate governance issues are already covered by other regulatory requirements. In addition, we still believe that such information is not of any particular relevance for investors in debt securities.

12. Disclosure on major shareholders is of no particular relevance for the assessment of debt securities investments and should therefore be deleted. Also, it is not clear what “control” means in this context. This should be clarified.
- 13.3 CESR should clarify, at least by providing an example, which standards fulfil the requirement of an “equivalent standard” pursuant to which the financial statements are not drawn up so as to give a true and fair view.
- 13.6.1 Although CESR’s Advice does not require that the interim financial statements have been reviewed by an auditor, such a review may have indeed taken place. In this case, the result of this review should be included in the prospectus in the form of a reprint of the relevant certificate as already set out in our comments on the first Consultation Paper.
- 13.8 It is not quite clear what is meant by the issuer’s “trading position” which is referred to in addition to the issuer’s financial position (which should be the only relevant position in this context).
15. We welcome that material contracts do not have to be put on display and that certain detailed requirements to be included in the summary of each material contract have been removed. However, the objective of such summary could still be made clearer. Only the risks resulting from such material contracts for the relevant investment are to be pointed out, ie. there should not be any requirement to provide an investor with superfluous information even if such information is contained in a material contract. This is of particular significance for debt securities where even contracts which are material for the issuer often are of no particular relevance for the debt investor’s risk that the issuer may, in future, not be able to repay its debt.

Paragraph 74:

Annex E – Debt Securities Note

- 1.1 CESR should clarify that only the persons who, according to the law applicable, are responsible for the prospectus are to be named in the prospectus. Such persons could be either natural persons or (and not “and”) legal persons or both depending on the legal concept which the relevant country has chosen.
- 13.1 We recognise that, by contrast to Annex L, IV.B under the Consultation Paper, Annex E, 13.1 now limits the interest to be disclosed to material interest. However, the scope of this requirement and the circle of persons to whom this requirement remains somewhat unclear. CESR

should therefore either remove this requirement in whole (in general, such conflicts of interest are already covered by other regulatory requirements) or at least give some examples of particular types of conflicts of interests envisaged by CESR (see our comments on Annex L, IV.B).

14.14 As set out in our response to the first Consultation Paper, it is crucial for multinational offers and an integrated pan-European capital market that the tax disclosure is limited to withholding tax together with information to the effect that each investor should seek to obtain its own tax advice. Disclosure on withholding tax is necessary because any tax deductions or withholding directly affect the amount paid out to investors. By contrast, a prospectus does not and may not serve as individual tax advice on an investment in a specific financial instrument. Therefore it may not replace individual tax advice which an investor may need with respect to his home jurisdiction. Information regarding taxes to which holders in the „targeted“ country may be subject could even be misleading since each tax advice has to take into account the individual circumstances and taxation of the relevant investor. By its nature, a prospectus can therefore not reflect all relevant tax issues which might be relevant for each investor individually in each country where the securities are offered. And even an attempt to cover the most important tax matters in all relevant countries would result in the cost of the issuer being huge and the prospectus being a voluminous book. Such far reaching tax „disclosure“ (which would in fact be an investment advice rather than disclosure relating to the securities offered) would therefore constitute a significant barrier to the creation of a harmonised pan European capital market.

15.4.3 The individual commissions and quotas of underwriters are of particular interest of competitors rather than for investors. Only the aggregate amount of commissions should therefore be disclosed as part of the expenses for the relevant issue of securities (see no. 17.1 of the schedule). Moreover, the quotas of the underwriters are often specified only at the end of the subscription period, i.e. after the prospectus has been published. As a consequence, a separate supplementary prospectus would be required only for disclosure on the relevant quotas.

Paragraph 76:
Annex G – ABS Registration Document

1.1 CESR should clarify that only the persons who, according to the law applicable, are responsible for the prospectus are to be named in the prospectus. Such persons could be either natural persons or (and not “and”)

legal persons or both depending on the legal concept which the relevant country has chosen.

Paragraph 77:

Annex H – ABS Securities Note

- 1.2** If information on an undertaking/obligor is to be disclosed which is not involved in the issue, such information can either have been published by the undertaking/obligor itself, or it can be taken from publicly available sources. Accordingly, the words "or contained in publicly available sources" should be included into the language proposed under this number as and where appropriate.
- 2.2.1** The assessment by which jurisdiction the pool of assets is governed may itself vary in the different jurisdictions concerned. Moreover, it is not clear which factors determine the jurisdiction by which the assets are governed.
- 2.2.3** It is not clear what is meant by "legal nature" of the assets. This term should be clarified.
- 2.2.13** For practical reasons, it should be made clear that this information may be given by specifying ranges of yield and maturity etc. since the number of assets may be high.
- 2.2.15** Similar to the correspondent requirement set out in 2.2.11, the requirement to disclose information about assets which comprise equity securities should be restricted to information that the issuer is aware of and/or is able to ascertain from information published by the issuer(s), or from publicly available sources. Alternatively, both requirements (2.2.11 and 2.2.15) could be merged into one.
- 2.2.16** The requirement to provide a valuation report for real property is too burdensome to issuers and should therefore be removed.

Paragraph 106:

The last sentence should be clarified. We presume that it is not intended that each constituent document, i.e. also the documents which are incorporated by reference, shall indicate where the other constituent documents are available. Such reference should only be contained in such documents in which another document is incorporated by reference.

II. Additional Draft Advice May 2003

Annex 1 – Wholesale Debt Registration Document

- 1.1** CESR should clarify that only the persons who, according to the law applicable, are responsible for the prospectus are to be named in the prospectus. Such persons could be either natural persons or (and not “and”) legal persons or both depending on the legal concept which the relevant country has chosen.
- 3** For the sake of clarity, the risk factors disclosure requirement should be amended to the effect that such risk factors are only to be described if such risk factors exist.
- 4.2** As set out in our response above to Annex D, 5.2, current and future investments are normally not of any particular relevance for investors in retail debt securities. This is much more true for debt securities offered to wholesale investors, who have their own facilities to assess and evaluate the potential future developments of the issuer. It should therefore only be disclosed in particular circumstances under the general disclosure requirement if, due to the specific nature and risks of the relevant investments, the current and future investments may have any impact on the ability of the issuer to pay interest or to repay the principal.
- 7.2** Given that the risk of debt securities can often not be assessed on the basis of forecasts given by the issuer, and that wholesale investors can usually make their own assessments about the issuer’s future development, this information should not be required for wholesale debt.
- 9.2** In general, conflicts of interest are already covered by other regulatory requirements. In addition, we still believe that such information is not of any particular relevance for investors in debt securities.
- 10** In general, disclosure about major shareholders is not relevant for investors to assess the risk that the issuer becomes unable to fulfil its obligations under the securities. In particular, it should not be required for securities to be offered to wholesale investors who are able to assess the risk involved in the purchase of the securities.
- 11.3** CESR should clarify, at least by providing an example, which standards fulfil the requirement of an “equivalent standard” pursuant to which the financial statements are not drawn up so as to give a true and fair view.
- 11.8** It is not quite clear what is meant by the issuer’s “trading position” which is referred to in addition to the issuer’s financial position (which should be the only relevant position in this context).

- 12 We welcome that material contracts do not have to be put on display and that certain detailed requirements to be included in the summary of each material contract have been removed. However, the objective of such summary could still be made clearer. Only the risks resulting from such material contracts for the relevant investment are to be pointed out, ie. there should not be any requirement to provide an investor with superfluous information even if such information is contained in a material contract. This is of particular significance for debt securities where even contracts which are material for the issuer often are of no particular relevance for the debt investor's risk that the issuer may, in future, not be able to repay its debt.

Annex 2 – Depository Receipts Prospectus Schedule

With regard to this building block, as set out in our response to the Addendum to the Consultation Paper, we believe that a separate building block for depository receipts is not necessary. This is clearly illustrated if, as it is now possible, a tripartite document is produced. The Feedback Statement shows that it is somehow odd to produce a registration document for a mere depository institution which assumes a mere technical role and which, in general, is not relevant at all for assessing any market or credit risks regarding the security or the underlying. As a consequence, there should be no particular disclosure on a depository other than a brief explanation of its role. A separate building block is not required. The additional Feedback Statement issued in May 2003 has, in our view, not given an explanation for such requirement either.

With respect to the disclosure regarding the issuer and the underlying shares, please see our comments on the Equity Registration Document and the Equity Securities Note above.

Annex 3 – Banks Registration Document

- 3 For the sake of clarity, the risk factors disclosure requirement should be amended to the effect that such risk factors are only to be described if such risk factors exist.
- 7.1 With respect to bank debt, the risks of a failure to pay and the insolvency risk are already covered by the general banking supervision. Thus, CESR decided for good reasons that the Banks Registration Document for debt issues does not require the same amount of disclosure as the Equity Registration Document or the Registration Document for corporate retail debt. Accordingly, we believe that the "Trend information" disclosure requirements should also be in line with the

disclosure requirements for wholesale debt issues. It should therefore be sufficient if banks state that there is no material adverse change since the latest annual accounts.

- 7.2 For the reasons referred to above in respect of paragraph 7.1 and because any evaluation of risks based on forecasts involve a certain degree of uncertainty, we do not believe that this disclosure requirement gives any particular benefit to investors. Such information should therefore not be required.
- 9.2 As set out above with respect to the Debt Registration Document, in general, conflicts of interest are already covered by other regulatory requirements so that such disclosure should not be required under the prospectus regulations. In addition, we still believe that such information is not of any particular relevance for investors in debt securities.
- 11.1 In general, disclosure about major shareholders is not relevant for investors to assess the risk that the issuer becomes unable to fulfil its obligations under the securities. Similar to debt securities offered to wholesale investors (for whom such disclosure is clearly not necessary), such disclosure should not be required for securities issued by banks as the supervisory regime exercised over them also extends to major holders of shares in a bank.
- 11.3 CESR should clarify, at least by providing an example, which standards fulfil the requirement of an “equivalent standard” pursuant to which the financial statements are not drawn up so as to give a true and fair view.
- 11.6 For the reasons referred to above in respect of paragraph 7.1, the level of disclosure required for debt securities issued by banks should, in general, correspond to the level of disclosure required for wholesale debt issuances. As the Wholesale Debt Registration Document does not require the issuer to include interim financial statements into the prospectus, it would also be reasonable not to require such additional disclosure in the Banks Registration Document.
- 11.8 It is not quite clear what is meant by the issuer’s “trading position” which is referred to in addition to the issuer’s financial position (which should be the only relevant position in this context).
- 12 We welcome that material contracts do not have to be put on display and that certain detailed requirements to be included in the summary of each material contract have been removed. However, the objective of such summary could still be made clearer. Only the risks resulting from such material contracts for the relevant investment are to be pointed out, ie. there should not be any requirement to provide an investor with superfluous information even if such information is con-

tained in a material contract. This is of particular significance for debt securities where even contracts which are material for the issuer often are of no particular relevance for the debt investor's risk that the issuer may, in future, not be able to repay its debt.