



European Securities and
Markets Authority

Response form for the Consultation Paper on Guidelines on risk factors under the Prospectus Regulation



Responding to this paper

ESMA invites responses to the questions set out throughout its Consultation Paper on Guidelines on risk factors under the Prospectus Regulation. Responses are most helpful if they:

- respond to the question stated;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all responses received by 05 October 2018.

Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

- Insert your responses to the questions in the Consultation Paper in the present response form.
- Please do not remove tags of the type <ESMA_QUESTION_GRF_1>. Your response to each question has to be framed by the two tags corresponding to the question.
- If you do not wish to respond to a given question, please do not delete it but simply leave the text “TYPE YOUR TEXT HERE” between the tags.
- When you have drafted your response, name your response form according to the following convention: ESMA_GRF_nameofrespondent_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA_GRF_ABCD_RESPONSEFORM.
 - Upload the form containing your responses, **in Word format**, to ESMA’s website (www.esma.europa.eu under the heading “Your input – Open consultations” → “Consultation on Guidelines on risk factors under the Prospectus Regulation”).

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. **Please clearly indicate by ticking the appropriate checkbox on the website submission page if you do not wish your contribution to be publicly disclosed.** A confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

**Data protection**

Information on data protection can be found at www.esma.europa.eu under the heading “Data protection”.

Who should read the Consultation Paper

This Consultation Paper may be of particular interest to investors, issuers, including issuers already admitted to trading on a regulated market or on a multilateral trading facility, offerors or persons asking for admission to trading on a regulated market as well as to any market participant who is affected by the new Prospectus Regulation.



General information about respondent

Name of the company / organisation	International Capital Market Association (ICMA)
Activity	Other Financial service providers
Are you representing an association?	<input checked="" type="checkbox"/>
Country/Region	Europe

Introduction

Please make your introductory comments below, if any:

<ESMA_COMMENT_GRF_1>

Introduction to ICMA

ICMA is a membership association, headquartered in Switzerland, committed to serving the needs of its wide range of members. These include private and public sector issuers, financial intermediaries, asset managers and other investors, capital market infrastructure providers, central banks, law firms and others worldwide. ICMA currently has 540 members located in over 60 countries. See: www.icmagroup.org.

This response is given by the ICMA primary market constituency comprised of borrowers and banks that lead-manage syndicated debt securities issues throughout Europe. This constituency deliberates principally through:

- the ICMA Corporate Issuer Forum¹, which gathers senior representatives of a number of major corporate issuers;
- the ICMA Financial Institution Forum², which gathers the heads or senior members of the capital raising, funding and treasury departments of a number of ICMA member banks active in capital markets issuance in Europe;
- the ICMA Primary Market Practices Committee³, which gathers the heads and senior members of the syndicate desks of a number of ICMA member banks active in lead-managing syndicated debt securities issues in Europe; and
- the ICMA Legal and Documentation Committee⁴, which gathers the heads and senior members of the legal transaction management teams of a number of ICMA member banks active in lead-managing syndicated debt securities issues in Europe.

We set out responses to the questions posed by ESMA below and some general introductory comments in this section.

Introductory comments

ICMA welcomes the opportunity to comment on ESMA's proposed guidelines on risk factors under the

¹ <https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Primary-Markets/primary-market-committees/icma-corporate-issuer-forum/>

² <https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Primary-Markets/primary-market-committees/icma-financial-institution-issuer-forum/>

³ <https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Primary-Markets/primary-market-committees/icma-primary-market-practices-committee/>

⁴ <https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Primary-Markets/primary-market-committees/icma-legal-and-documentation-committee/>

Prospectus Regulation. Many of the draft guidelines appear to be flexible and proportionate, and the position set out in the consultation paper is a helpful starting point. The precise impact of the draft guidelines on issuers will depend on the approach taken by NCAs in applying the guidelines. We discuss this further below.

Of the comments below, two key areas of concern are: (a) the need for NCAs to tailor their review of risk factors depending on whether the prospectus is aimed at retail or wholesale investors; and (b) the disclosure of quantitative information under guideline 4.

We also note the following general points.

The flexibility envisaged by ESMA is welcome and must be applied in practice by NCAs

The references in the draft guidelines to different approaches being taken in relation to different types of prospectuses is very helpful. This concept is in line with the general approach to prospectus content in the Level 1 regime. It will be particularly important that NCAs observe this flexibility and incorporate it into their application of the guidelines and review processes, in order to give effect to the spirit of the Level 1 regime.

Set out below are two examples of where flexibility of approach should be adopted by NCAs, but there will be others.

- a. For debt securities typically issued under multi-product base prospectuses, it is very helpful that ESMA has acknowledged that a more flexible approach to risk factor disclosure may be required.
- b. NCAs should also tailor their review depending on whether the prospectus is aimed at retail or wholesale investors. Where the prospectus relates to wholesale debt securities, there will be fewer concerns in relation to the ability of wholesale investors to navigate, read and understand risk factors. This means that a more flexible approach should be taken in the application of those guidelines relating to the presentation of risk factors across categories in the context of prospectuses related to wholesale debt securities.

The general concept of different approaches to disclosure being appropriate for wholesale and retail investors is enshrined at Level 1. Given the importance of observing this key Level 1 principle, it would be helpful if the guidelines included this point, for example in the “Background” section and in the notes to draft guidelines 7, 8, 9, 10 and 11 relating to presentation of risk factors across categories and focused/concise risk factors (to the extent those draft guidelines are retained in the final guidelines).

Example risk factors should not be viewed as templates

It will also be important that the example risk factors given in the proposed guidelines are viewed by the NCAs as examples, and not templates against which risk factor disclosure should be matched. We discuss this further below.

<ESMA_COMMENT_GRF_1>

Specificity

Q1 : Do you agree with the suggested draft guidelines on specificity? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_1>

The guidelines on specificity are broadly workable. ESMA may wish to consider the following comments.

The guidance notes to draft guideline 1 note that risk factors should not use ‘boiler-plate’ disclosures and risk factors should not be copied from other documents **if they are not relevant to the issuer/guarantor and/or the securities**. The final part of this guidance is very important. Even if a risk factor is of a type that appears in many prospectuses, it is still entirely appropriate for an issuer to disclose it where it is relevant to that issuer, the guarantor or the securities. For example, risk factors relating to certain types of securities are, by their nature, likely to be relevant in any prospectus relating to that type of security. In addition, risk factors relating to an issuer may well be relevant for more than one prospectus that the issuer produces, if there has been no change to the circumstances giving rise to the need to include the risk factor. Risk factors relating to the issuer’s industry may also be relevant to any issuer in that industry.

As noted in our introductory comments above, it is important that the example risk factors are viewed by NCAs just as examples and not anything more. They should not become templates against which NCAs will review equivalent risk factors. Issuers should have discretion to draft the text of their own risk factors (provided they comply with the Prospectus Regulation and the guidelines) even where the guidelines provide a ‘sample’ risk factor, such as the BRRD risk factor. To illustrate, the first example under draft guideline 2 describes the risk of a main production site of the issuer flooding but could equally relate to the issuer’s main product site being damaged or destroyed by fire or any other natural disaster. It would be counter-productive for NCAs to consider that risk factors relating to natural disasters can only deal with one type of natural disaster per risk factor in order to be specific, because the example in the ESMA guidelines relates only to flooding. This approach would lead to lengthened risk factor disclosure.

It is not clear why the words “subject to an assessment by the persons responsible for the prospectus pursuant to the obligations under Article 16 of the PR” are included in paragraph 18 of the draft guidelines in Annex II to the consultation paper, and not elsewhere, as presumably all risk factors are subject to this assessment.

<ESMA_QUESTION_GRF_1>

Materiality

Q2 : Do you agree with the suggested draft guideline 3? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_2>

We have no specific comments on the drafting of draft guideline 3 or the accompanying guidance notes.

However, we do not agree that an analogy of the IFRS definition of materiality should be used when assessing the materiality of a risk factor, or indeed for assessing materiality for the purposes of the Prospectus Regulation more generally, per paragraphs 27 and 28 of the consultation paper. The IFRS definition of materiality does not seem relevant, or particularly appropriate, in the context of prospectus disclosure. Article 16 of the Prospectus Regulation, in conjunction with Article 6(1), already sets out the tests that an issuer will apply when determining appropriate risk factor disclosure.

The Prospectus Regulation indicates in Article 6(1) that the “necessary information which is material to an investor [to make an informed investment decision]” may vary depending on (among other things) the type of securities and whether debt securities are “wholesale” or not. In the context of debt securities, information will be material for investors if it affects the issuer’s ability to fulfil its obligations under the securities to investors. In other words, investors in debt securities want to know if they will be repaid their principal investment and paid interest. Investors in equity securities, on the other hand, may be interested in factors that might affect the price of the securities and/or any dividend expectations. The use of the IFRS definition of materiality fails to acknowledge that materiality depends on, among other things, the type of the security in question, as well as the issuer.

It is helpful that the IFRS definition of materiality and associated paragraphs are not included in the proposed draft guidelines.

<ESMA_QUESTION_GRF_2>

Q3 : Do you agree with the suggested draft guideline 4 on quantitative information? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_3>

Draft guideline 4 is one of the more problematic areas of the draft guidelines.

Disclosure of quantitative information to illustrate the potential negative impact of risk factors is currently rare in debt securities prospectuses. It is likely to be very difficult to disclose quantitative information on the negative impact of the risk factor in a manner that is not misleading for investors. By way of example, it would be very difficult to quantify and disclose in a non-misleading way the negative impact of any reputational damage an issuer or guarantor might suffer as a result of a particular risk factor.

The guidance seems to indicate that qualitative information can only be provided when quantitative information is not available. This is likely to be problematic for issuers. For example, it may not always be clear whether quantitative information is “available” or not. Even where some form of quantitative information is available internally, it may be very difficult for an issuer to disclose that quantitative information publicly in a manner that is not misleading to investors. The guidance could therefore be very challenging for issuers who may need to spend a considerable amount of time and costs diligencing whether quantitative information is available for a particular risk factor and, if so, modelling that information to ensure it can be appropriately disclosed in a non-misleading manner.

We suggest that the emphasis on the need to disclose quantitative information is recalibrated. For example:

Where available, the disclosure of quantitative information, in order to illustrate the potential negative impact of a risk factor should be considered included. ~~However, where quantitative information is not available~~ Otherwise, the description of the potential negative impact of the risk factors may be described using a qualitative approach.

If this is not palatable to ESMA, then we would suggest that the requirement to disclose quantitative information is restricted to circumstances in which it would be required to disclose quantitative information under IFRS. This would reflect ESMA’s comment in the consultation paper that issuers could tailor their IFRS disclosure of quantitative information concerning financial risks for the purposes of including it in the prospectus. Currently, the guideline could be interpreted to require disclosure of quantitative information even where such disclosure would not be required under IFRS.



<ESMA_QUESTION_GRF_3>

Q4 : Do you agree with the suggested draft guideline 5 on mitigating language? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_4>

Mitigating language may be relevant to ensure that risk factor disclosure is fair, clear and not misleading.

Draft guideline 5 therefore seems reasonable in that it relates to mitigating language that compromises the materiality of the risk factor. In other words, it is not a complete prohibition on mitigating language. The guidance note stating that mitigating language can be used to illustrate the probability of occurrence and expected magnitude of the risk factor's negative impact is useful.

It will be very important that this guideline is not interpreted by NCAs as prohibiting mitigating language.

<ESMA_QUESTION_GRF_4>

Corroboration

Q5 : Do you agree with the suggested draft guideline 6 on corroboration of specificity and materiality? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_5>

As a general comment, the inclusion of a draft guideline relating to corroboration is surprising because corroboration is not an area in which ESMA is mandated to develop guidelines. In addition, the final sentence of the guideline (stating that a competent authority should not approve a prospectus where it is not apparent that materiality and specificity are corroborated) does not seem to add a great deal to the existing Level 1 requirement for corroboration in Article 16(1).

More specifically, it is welcome that ESMA notes that in certain cases it will be sufficient that materiality and specificity of risk factors is identifiable by reference to the overall picture of the issuer/guarantor and the securities. However the default position seems to be that materiality and specificity will normally be demonstrated via the inclusion of corresponding information elsewhere in the prospectus.

This seems to be the wrong way around. It seems more likely that the materiality and specificity of risk factors will be corroborated by the overall picture of the prospectus, rather than a specific other piece of information elsewhere in the prospectus. This is likely to be the case in prospectuses relating to non-equity securities. For example, market risks are unlikely to be corroborated by specific information elsewhere in the prospectus, but will be corroborated by an overall picture of the securities.

If draft guideline 6 is retained, we would suggest re-drafting the guidance note as follows:

While ~~direct/clear~~ corroboration of the materiality and specificity of the risk factor ~~may be is normally~~ demonstrated via the inclusion of corresponding information elsewhere in a prospectus, this is not necessary in all circumstances. In ~~certain~~ many cases, it is sufficient that materiality and specificity of risk factors is identifiable by reference to the overall picture of the issuer/guarantor and the securities presented in the prospectus.

<ESMA_QUESTION_GRF_5>

Presentation of risk factors across categories

Q6 : Do you agree with the suggested draft guidelines on Presentation of risk factors across categories? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_6>

Subject to our general comment that NCAs should take a more flexible approach in the application of these draft guidelines in the context of prospectuses aimed at wholesale investors (see our introductory comments above), ESMA appears to have struck a sensible balance in draft guidelines 7 to 10 on presentation of risk factors across categories.

Some areas that ESMA may wish to consider further are as follows:

- a. *The requirement under draft guideline 7 that a risk factor should only appear once, in the most appropriate category.* The rationale for this restriction is not clear, and there is a risk that this could result in misleading disclosure for investors if a risk is relevant to more than one category. If this requirement is intended to help shorten risk factor disclosure, might it be more helpful for investors if there is at least a cross-reference in each relevant category to the risk factor that is disclosed elsewhere?
- b. *The restriction on sub-categories in draft guideline 10.* Again, the rationale for this restriction is unclear, as it is likely to be helpful for investors if risk factors are ordered logically according to categories and then sub-categories. The acknowledgement that sub-categories might be necessary in the case of a base prospectus is helpful, but sub-categories might also be necessary and helpful for investors in prospectuses for a single issue of securities as well. For example, risk factors might be categorized according to risks relating to the issuer, risks relating to the guarantor, risks relating to the securities and risks relating to the market for the securities. Within the category of risks relating to the issuer, there might be sub-categories of business risks, operational risks, legal and regulatory risks and so on. This approach is clear to understand and helpful to investors, who can easily navigate the different categories and sub-categories. If sub-categories are restricted, it is likely to mean that either different types of risks are disclosed together in one category or issuers will be required to use a greater number of categories. Both options are unlikely to be helpful for investors, and seem to cut across the Level 1 requirements to categorise risks according to their nature and present risk factors in a limited number of categories.
- c. *Draft guideline 9 refers to risks to the issuer/guarantor but not risks related to the securities.* ESMA may wish to address this as follows:

The competent authority should ensure that the number of categories included in the prospectus is not disproportionate to the size/complexity of the transaction and risk related to the issuer/guarantor or the securities.

<ESMA_QUESTION_GRF_6>

Q7 : Do you agree with that the number of categories to be included in a risk factor section, should not usually exceed 10? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_7>

Numerical caps on the number of risk factors or the number of categories can be problematic if they fail to take into account the range of circumstances under which a prospectus may be drawn up under the Prospectus Regulation. It is therefore very helpful that ESMA has suggested a maximum of 10 categories

as a guideline for a “standard, single-issuer, single-security prospectus” and noted that this may be reduced or extended depending on the circumstances, such as multi-product base prospectuses. It will be very important that NCAs observe and apply this flexibility in their review of risk factors in practice. In particular, multi-product base prospectuses are not the only situation in which more than 10 categories of risk factors may be required. For example, an emerging market issuer involved in volatile jurisdictions and/or industries (e.g. mining in Africa) may also need to set out their risk factors across more than 10 categories in order to ensure they can present their risk factors in a manner that is comprehensible and helpful for investors. Similarly, financial institutions and other regulated entities may also find it challenging to use only 10 categories given the various types of risks that they need (and are expected by NCAs) to disclose. **It will be very important that NCAs take the flexibility envisaged in the draft guidelines into account and consider all the circumstances in their application of the guidelines.**

As mentioned in the response to Q.6 above, restricting the use of sub-categories is likely to mean that issuers have to use a greater number of categories when presenting risk factors (and the guideline limit of 10 categories may become challenging to adhere to). As noted above, further flexibility with regard to sub-categories would be welcome.

In addition, this is an area where NCAs should take into account the intended audience of the prospectus. While we believe categorisation and sub-categorisation to be helpful to investors (as noted above), we note the overall Level 1 obligation to present risk factors in a limited number of categories. In the context of a prospectus relating to wholesale debt securities, the professional investors that will be reading the prospectus will be able to navigate risk factor disclosure more easily and so a more flexible approach to the number of categories may be appropriate (noting that the persons responsible for the prospectus are still subject to the overall Level 1 obligation to present risk factors in a limited number of categories).

<ESMA_QUESTION_GRF_7>

Focused/concise risk factors

Q8 : Do you agree with the suggested draft guidelines on focused/concise risk factors? If not, please provide your reasoning.

<ESMA_QUESTION_GRF_8>

The inclusion of a draft guideline relating to focused/concise risk factors is surprising because it does not relate to an area in which ESMA is mandated to develop guidelines.

It is also not clear whether this guideline is required, as there is an overall obligation to ensure that all prospectus disclosure (including risk factors) is written in a concise form in Article 6(2) of the Prospectus Regulation.

Please also note our general comment that NCAs should take a more flexible approach in the application of this draft guideline in the context of prospectuses aimed at wholesale investors (see our introductory comments above).

<ESMA_QUESTION_GRF_8>

Summary

Q9 : Do you agree with the suggested draft guideline on risk factors in the summary? If not, please provide your reasoning.



<ESMA_QUESTION_GRF_9>

The inclusion of a draft guideline relating to risk factors in the summary is surprising because it does not relate to an area in which ESMA is mandated to develop guidelines.

That said, the draft guideline seems sensible and reflects the current approach of issuers in practice.

<ESMA_QUESTION_GRF_9>

General

Q10 : Do you agree with the proposed draft guidelines? Have you any further suggestions with regard to draft guidelines addressing a particular section or the guidelines in general?

<ESMA_QUESTION_GRF_10>

Please see our introductory comments above.

<ESMA_QUESTION_GRF_10>

Q11 : Do you believe that market participants will bear any additional cost as an indirect effect of the suggested draft guidelines? If yes, please indicate the nature of such costs and provide an estimation.

<ESMA_QUESTION_GRF_11>

Market participants are likely to face increased costs as a result of these draft guidelines. The level of such increased costs will depend on the approach of NCAs in applying the guidelines.

Where a flexible, proportionate approach is adopted, with NCAs considering the type of prospectus, type of investor and the circumstances of the issuer in their review of the risk factors, the costs in complying with the guidelines should be minimal.

However, if NCAs take a rigid approach, borrowers could face significantly increased legal costs in re-drafting their risk factor disclosure in a manner that they feel is appropriate but which meets the requirements of the relevant NCA. This will be particularly relevant for issuers who issue debt securities in markets outside of Europe, such as the US, which have their own rules and investor expectations in relation to risk factor disclosure. Such issuers will wish to ensure that the information they disclose to investors is consistent across all markets in which they are offering securities. Departing from such approach is likely to lead to significant liability concerns, and therefore costs for issuers.

In the light of this, we reiterate the importance of NCAs taking a more flexible approach in the application of those guidelines relating to the presentation of risk factors across categories and concise/focused risk factors (to the extent those draft guidelines are retained) in the context of prospectuses related to wholesale debt securities, and the need for ESMA to re-consider the focus on disclosure of quantitative information under guideline 4.

<ESMA_QUESTION_GRF_11>