

point in 2017, shortly after the Prospectus Regulation is published in the *Official Journal*. Broadly, the provisions introduce a new requirement to prepare a prospectus in respect of shares resulting from the conversion or exchange of other securities if the resulting shares represent 20% or more of the number of existing shares. Following extensive advocacy by ICMA, the agreed text now includes various carve-outs from this provision, including for shares qualifying as Common Equity Tier 1 of certain institutions issued as a result of the conversion of their Additional Tier 1 instruments on a trigger event. As with all provisions, the precise language used in the final agreed text will need to be studied carefully to determine the precise practical implications.

In terms of next steps, it is anticipated that the text will be adopted by the co-legislators following the usual jurist-linguist checks. It is expected that the final text would then be endorsed by the European Parliament and the Council before being published in the *Official Journal*, likely in the second quarter of 2017.

ICMA will continue to engage with members and official institutions as the legislative process progresses, in particular on Level 2 measures which are expected to be developed during 2017 and 2018.

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Market soundings under the Market Abuse Regulation

The Market Abuse Regulation (MAR) introduced a new market soundings regime which applies to the disclosure of both inside information and non-inside information.

This is a key area of focus for ICMA's members with profound implications, particularly because the new regime gives rise to a number of questions and uncertainties. ICMA has been discussing the implications of the new regime with its primary market sell-side constituency through its Committees and Working Groups in Europe and Asia. This topic has also been discussed in a number of other fora, including regional conferences, the ICMA Board and the ICMA Committee of Regional Representatives.

The main focus has been on the implications of the rules for sounding information other than inside information, especially in relation to investor meetings (where a transaction might subsequently follow) and the posting of MTN (and SSA) price levels. Considerations have included what constitutes a "transaction announcement", "acting on the issuer's behalf" and "gauging interest", noting that there is currently limited (or no) guidance from regulators

on these and other relevant points. In addition, there is a question surrounding the scope of the MAR soundings regime, which ICMA understands is being considered by ESMA.

ICMA, with input from major law firms, has been developing a paper outlining the emerging sell-side thinking on these points. ICMA is intending to discuss this with relevant regulators before making it available more broadly to assist market participants in their practical dealings with market soundings. In the meantime, ICMA has also held a number of briefing calls that have been open to members, investors and issuers, the [slides for the most recent of which on 13 December 2016](#) are available, amongst other things, on the [ICMA MAR \(primary aspects\) webpage](#). The next briefing call on MAR soundings for members is expected to be scheduled for late January.

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Packaged Retail and Insurance-based Investment Products (PRIIPs)

As noted in the [last edition](#) of this Quarterly Report, various Member States expressed a view in autumn 2016 that the date of application of the PRIIPs regime should be delayed by 12 months. Since then, the date of application has indeed been delayed to 1 January 2018 by an [amending Regulation](#) published in the *Official Journal*. This delay is welcome as it will give market participants more time to familiarise themselves with the new regime and allow legislators to finalise the necessary Level 2 measures.

Notwithstanding the delay, ICMA continues to work towards consensus on the practical steps that issuers and underwriters could take to avoid making vanilla bonds that could fall within the product scope of the PRIIPs regime available to MiFID II retail investors, in the expectation that the PRIIPs KID is an unworkable concept at least in the vanilla context (see [previous editions](#) of this Quarterly Report, notably the [2014 Third Quarter edition](#)). Such practical steps may include updated selling restrictions, related warning legends on prospectuses and final terms and additional diligence of order books. In addition, it may be necessary to consider whether admission to trading on a particular market or markets could mean that a relevant product has been "made available" to retail investors if, for example, retail investors have direct access to that market. ICMA will continue to discuss these practical questions with its primary market members and plans to work towards finalising suggested language for prospectuses in the first part of 2017. Such suggested language could be relevant for debt programme updates taking place in 2017.



MiFID II explicitly states its product governance regime is to be applied "proportionately".

It is important to bear in mind that the PRIIPs Regulation will enter into force at a similar time to the new product governance regime introduced by MiFID II (discussed in a separate article in this section of the ICMA Quarterly Report). ICMA's discussions on the PRIIPs Regulation are therefore framed with this in mind, with a view to developing a consistent practical approach for compliance with the PRIIPs Regulation and MiFID II product governance regime and, in due course, the new Prospectus Regulation.

In addition, ICMA has discussed the implications of the PRIIPs regime in its Platform Working Group and held an initial call for secondary market legal colleagues. Market consensus and practice will need to develop among secondary market participants also, given the PRIIPs regime applies whenever a relevant product is "made available" to retail investors and it is expected that issuers of vanilla bonds will be unlikely to prepare KIDs (as noted above).

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MiFID II: product governance

Among other topics under MiFID II (in effect from 3 January 2018), ICMA has been grappling for over a year with how product governance – traditionally a retail structured market concept – can operate in the institutional funding markets. How does one ensure that a fixed rate bond (a concept in existence for hundreds of years) by a car manufacturer (to, say, fund a new factory creating thousands of jobs to make green vehicles) is "designed" by underwriters for specified "target market" investors' "needs, characteristics and objectives"? (In this respect, professional investors need and want to access the market freely to pursue their often complex, evolving and confidential investment strategies).

At least MiFID II explicitly states its product governance regime is to be applied "proportionately". This will be particularly important in relation to the wholesale debt markets, which provide significant funding to the real economies of Member States, and the approach is consistent with the objectives of Capital Markets Union, which is in part to facilitate such funding, rather than to add unnecessary regulatory burdens to it.

The answer to the above question would then be arrangements to limit distribution to professional investors, who are appropriate target investors for all types of debt securities. This would involve primary market selling restrictions, warning legends and other procedures to restrict distribution to retail investors in the secondary market. Such arrangements would also represent a consistent approach across the MiFID II, PRIIPs and prospectus regimes.

Packaged Retail and Insurance-based Investment Products (PRIIPs)

Various legislative and market developments have occurred ahead of the PRIIPs regime's scheduled coming into application on 31 December 2016.

Legislative process: On 14 July, the European Commission adopted a Level 2 [Delegated Regulation on product intervention powers](#) (an aspect of PRIIPs ICMA has not been focusing on). However, on 14 September, the European Parliament [objected](#) to the earlier Level 2 [Delegated Regulation on KID presentation, content, review/revision and provision](#) (and [related annexes](#)) adopted by the Commission on 30 June (see [First Quarter edition](#) of this Quarterly Report). The Parliament also called for a delay to the PRIIPs regime's scheduled application date. It was subsequently [suggested](#) in Council to not object to this earlier Delegated Regulation (noting the Parliament's objection) but 23 (subsequently [corrected](#) to 24) Member States [expressed](#) the view that the PRIIPs regime's coming into application be postponed by 12 months. ICMA and market practitioners are continuing to work, for the time being, on the assumption that the PRIIPs regime's application date remains 31 December.

Retail scope: At a Commission PRIIPs Implementation Workshop on 11 July, staff from the European Supervisory Authorities (EBA, EIOPA and ESMA) helpfully confirmed that discretionary managers are not retail clients (see "portfolio manager, [...] in the name and for the account of a retail investor" under Question 3 in some of the workshop's [published slides](#)), which addresses some prior uncertainty and seems at least consistent with both a plain reading of the professional client concept under MiFID II and PRIIPs' policy focus on retail investor decision-making.

Product scope: In terms of the scope of products that fall within the definition PRIIPs as being "packaged", and further to prior coverage (in the [2016](#) and [2014 Third Quarter](#) editions of this Quarterly Report), there currently seems to be a market consensus that basic fixed or floating rate notes are not PRIIPs and that features such as an exotic currency, a guarantee, a put or a call would not, on their own, result in such securities being characterised as PRIIPs (to the extent made available to retail investors). However, consensus in relation to other vanilla debt securities may take some time to emerge. In the meantime, it seems likely that specific legal advice will be sought case-by-case (where transaction timelines allow) or that such securities will, for practical purposes (at least in the IG Eurobond syndication context), be treated as "packaged" as a matter of convenience (where specific legal advice is either not desired or impractical within desired transaction timelines).

Market approach to new vanilla issuance: As briefly alluded



ICMA and market practitioners are continuing to work, for the time being, on the assumption that the PRIIPs regime's application date remains 31 December.

to in the [Third Quarter](#) edition of this Quarterly Report, ICMA is working (ahead of late 2016 debt programme updates/supplements) on practical means for vanilla issuers to generically avoid MiFID II retail investors, especially where securities are treated as "packaged" for practical purposes as noted above - in the expectation that the PRIIPs KID is an unworkable concept at least in the vanilla context (see prior editions of this Quarterly Report, notably the [2014 Third Quarter edition](#)). Such practical means would include updated selling restrictions (sales limited to MiFID II professionals), related warning legends and probable additional order book diligences.

Secondary vanilla trading/legacy bonds: It is possible that secondary traders may take a practical approach similar to their new issue counterparts for convenience: treat all securities as potentially "packaged" (absent market consensus or specific conclusion/advice otherwise) and only deal with MiFID II professionals in the absence of KID produced by the issuer. This would be equally applicable for legacy securities issued prior to the coming into application of the PRIIPs regime (in respect of which it seems highly unlikely that issuers will produce a KID).

JAC work: On 19 September, the Joint Associations Committee (JAC) on retail structured products filed (with ICMA's support) a [response](#) to a UK FCA [Consultation Paper](#) on changes to disclosure rules in the FCA Handbook to reflect the direct application of the PRIIPs Regulation.

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~~Market Abuse Regulation: primary markets~~

~~Several months into the new regime, ICMA continues to work to facilitate market consensus around MAR's soundings regime that preserves smooth and swift execution of new Eurobond issues.~~



The extent to which market soundings and stabilisation will continue to be effective tools to mitigate market volatility remains to be seen.

Market Abuse Regulation: primary markets

Further to the [Second Quarter 2016 edition](#) of this Quarterly Report, the new Market Abuse Regulation (MAR) regime came into force on 3 July, with various Level 2 measures being finalised and published only recently around the soundings and stabilisation topics that ICMA has been focusing on in the primary markets context:

- [Delegated Regulation EU/2016/960 on sounding procedures](#) published on 17 June;
- [Implementing Regulation EU/2016/959 on sounding templates](#) published on 17 June;
- [Delegated Regulation EU/2016/1052 on buy backs and stabilisation](#) published on 30 June; and
- [Implementing Regulation EU/2016/1055 on public disclosure of inside information](#) (relevant also to public disclosure of stabilisation) published on 30 June.

ESMA also published [responses](#) to its [January consultation](#) *inter alia* on buy-side sounding guidelines.

ICMA's most recent committee and working group deliberations have mainly focused on the implications of the rules for sounding information other than inside information, especially in relation to investor meetings (where a transaction might subsequently follow) and MTN (and SSA) price levels – with considerations notably on what constitutes transaction announcement, acting on issuer behalf and gauging interest (in contrast to negotiating terms). ICMA also organised a [workshop for investors](#) in Stockholm on 22 June (with publicly available slides on [MAR generally](#), on [insider lists](#), [managers' transactions and investment recommendations](#) and on [soundings, stabilisation and STORs](#)). ICMA is also updating Chapter 9 and Appendix 15 on stabilisation of the ICMA Primary Market Handbook, with publication targeted over the summer. There have also been some regulatory discussions on investment recommendations, including in the new issues context, which are covered in the [secondary markets](#) section of this Quarterly Report.

It may well take some time (months, if not more) for market practitioners to become comfortable with the implications of all ramifications of the new regime. The

extent to which market soundings and stabilisation will continue to be effective tools to mitigate market volatility (particularly in the context of a future bear market) remains to be seen.

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Packaged retail and insurance-based investment products (PRIIPs)

Further to the Level 2 ESAs' [consultation](#) (reported in the [First Quarter 2016 edition](#) of this Quarterly Report) and the [response](#) (and related letters) of the Joint Associations Committee (JAC) on Retail Structured Products (reported in the [Second Quarter 2016 edition](#) of this Quarterly Report), the ESAs adopted [final draft regulatory technical standards](#) on 31 March (and published them on 7 April), with European Commission adoption of a consequential [Delegated Regulation](#) following on 30 June. The PRIIPs regime is due to enter into effect from January 2017.

The European Commission also [responded](#) to one of the JAC's related letters, including noting that the PRIIPs' regime territorial scope does not extend to offers by an EU manufacturer via a non-EU intermediary to a non-EU retail investor.

ICMA's focus, other than supporting the JAC, continues to be on ensuring the vanilla funding markets are not adversely impacted by the PRIIPs regime's ambiguous scope and incoherent substantive provisions. In this respect, it seems there is emerging market consensus that straight fixed rate and floating rate notes are out of PRIIPs scope – with ongoing focus on whether additional product features may have an impact from a product scope perspective. ICMA is also intending to foster in the early autumn (ahead of late 2016 debt programme updates/supplements) practical means of otherwise remaining out of PRIIPs scope – namely in terms of avoiding MiFID retail investors (such as updated selling restrictions, document legends and possible additional order book diligences).

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Other primary market developments

Packaged retail and insurance-based investment products (PRIIPs): As anticipated in the [First Quarter 2016 edition](#) of this Quarterly Report, the Joint Associations Committee on Retail Structured Products (JAC) [responded](#) on 29 January to a Joint Committee of the European Supervisory Authorities' (ESAs – gathering EBA, EIOPA and ESMA) [Joint Consultation Paper](#) on PRIIPs key information documents (KIDs). The JAC subsequently filed on 17 February a [letter](#) to the European Commission, ESMA, EIOPA and ESAs on significant uncertainties relating to the PRIIPs Regulation and a further [letter](#) (annexing the first letter and the above response) to ESMA, EIOPA and EBA on interpretation and application of the PRIIPs regime.

Negative interest: ICMA continues to respond to various member queries relating to the impact of negative interest rates on floating rate notes. While the impact of negative interest rates will depend on the terms and conditions applicable to the debt security concerned, terms and conditions for a vanilla bond will customarily only provide a “promise to pay” by issuer, with no countervailing contractual promise by investors to pay anything. It is unlikely that the terms and conditions for a vanilla bond would provide that any negative interest can be offset against subsequent positive interest payments or capital redemption amounts. Furthermore, clearing and settlement infrastructure is unlikely to be set up to execute negative coupon cash flows.

Benchmarks: As reported in [previous editions](#) of this Quarterly Report, ICMA has been engaging with the process for the evolution of LIBOR and EURIBOR. The latest development is the publication of an [ICE LIBOR Roadmap for the evolution of LIBOR](#). It appears that many of the changes suggested in IBA's position papers in relation to evolving LIBOR will be taken forward.

ICMA has been supporting initiatives to improve the robustness of benchmarks, while highlighting the need to ensure that there are no negative side effects for outstanding contracts that reference that benchmark. In this respect, it is helpful that LIBOR will continue to be published at 11 am London time each day, and it is to be hoped that other practical measures, such as LIBOR continuing to be published on the same screen pages on which it is currently published (or notices being posted on current and new publication sites in relation to any change in publication venue) will also be adopted. In addition, the statement in the Roadmap that LIBOR “will continue to measure the same underlying interest being the rate at which banks can fund themselves

in the wholesale markets” is helpful. IBA has stated that the standardising and updating measures set out in the Roadmap will be implemented progressively during 2016.

IBA is also asking global users of LIBOR rates to complete a brief questionnaire to help it understand the current level and nature of use for each of the 35 daily LIBOR rates. The questionnaire can be found on the [IBA website](#).

In relation to the evolution of EURIBOR, ICMA [responded to an EMMI consultative position paper on the evolution of EURIBOR](#) (mentioned on page 46 of the [First Quarter 2016 edition](#) of this Quarterly Report) on 29 January 2016. ICMA's response supported EMMI's goal for a “seamless transition” in the evolution of EURIBOR and noted that, in this regard, it is desirable to evolve EURIBOR in such a way as to maintain a rate that is commercially as close as possible to the current rate.

Separately, ICMA reiterated its previous comments in relation to the importance of contractual continuity in the process of evolving benchmarks in a short response to the [ESMA Discussion Paper on the Benchmarks Regulation](#) on 31 March 2016.

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regime (at both Level 1 and Level 2) to allow an orderly implementation.

ICMA will continue to discuss the implications of the proposed Prospectus Regulation in relevant committees and working groups. ICMA also intends to continue to engage with various regulators at national and European level to discuss the proposed Prospectus Regulation.

Other developments under the current Prospectus Directive regime

Omnibus II Delegated Regulation concerning prospectus approval and publication and advertisements: As anticipated, the European Commission adopted a Delegated Regulation concerning prospectus approval and publication and advertisements on 30 November 2015. This follows ESMA submitting final RTS to the European Commission in June 2015, which was reported on page 34 of the previous edition of this Quarterly Report. It is understood that the Council has invoked its extension on the objection period and the objection period will last until 30 January 2016. As such, the Delegated Regulation would be published in the Official Journal in February 2016 at the earliest and would enter into force on the twentieth day following publication in the Official Journal. It is also understood that ESMA envisages producing two Q&A on the advertisements section of the RTS (as noted on page 34 of the previous edition of this Quarterly Report), which would be published in late March.

ESMA Q&A on Prospectuses: ESMA published a revised version of the [ESMA Q&A on Prospectuses](#) in December 2015. There is a new Q&A 96 relating to disclosure for securities subject to conversion or write-down powers under the BRRD, where ESMA states: "Where the issuer considers the possibility of bail-in to be material ... this should be reflected in the risk factors section and summary of a prospectus", and gives some detail on the minimum content of a bail-in risk factor. It is not anticipated that this new Q&A will require changes to existing market practice. There is also a revised question (Q26) relating to the calculation of the €5 million limit in PD Article 1(2)(h) and the €75 million limit in PD Article 1(2)(j), which is less likely to be relevant to the wholesale bond market.

Omnibus II filing final terms with host national competent authorities: The [Omnibus II Directive](#) amended Article 5(4) of the Prospectus Directive so that the home National Competent Authority, as opposed to the issuer, has responsibility for filing final terms with a host National Competent Authority. This change was due to take effect in Member States' legislation from 1 January 2016. In this regard, we understand that the Luxembourg, Irish and UK

National Competent Authorities will require final terms and certain information to be provided to a specific email address. More information is available on this [UKLA webpage](#) and page 2 of this [CSSF Newsletter](#).

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Packaged Retail and Insurance-based Investment Products (PRIIPs)

On 11 November 2015, the Joint Committee of the European Supervisory Authorities (ESAs) – EBA, EIOPA and ESMA – published a [Joint Consultation Paper](#) (subsequently followed on 6 January 2016 by a [one page errata document](#)) on PRIIPs key information documents (KIDs), which are primarily for structured products. (See further the [Third Quarter 2014 edition](#) of this Quarterly Report in respect of product scope). The Consultation Paper includes draft Regulatory Technical Standards (RTS) under the PRIIPs Regulation. The European Commission also published its earlier [Final Report](#) on a consumer testing study on KID format and content.

Background: These publications follow (i) the ESAs' November 2014 [Discussion Paper](#), to which the Joint Associations Committee (JAC) [responded](#), with ICMA's support; (ii) December 2014 [Official Journal publication](#) of the PRIIPs Regulation; and (iii) the ESAs' June 2015 [Technical Discussion Paper](#), to which ICMA [responded](#). See further the [past editions](#) of this Quarterly Report, which detail *inter alia* historic concerns around residual ambiguity of KID purpose and related liability (despite previous highlighting efforts) and the (consequentially limited) feedback given to the ESAs as they have sought to define the KID's detailed format and content requirements in this ambiguous context.

KID purpose/investor understanding: In this regard, the Recitals to the draft RTS state that (emphasis added):

- the KID "designed to ensure that it is easy for retail investors to read, understand and compare";
- the KID's summary risk indicator "should be accompanied by sufficient narrative explanations of the risks of the PRIIP to allow for an informed decision";
- the KID "can be expected to be also used as a summary of the main features of the PRIIP";
- the "information contained in the [KID] should be capable of being *relied* on by a retail investor when making an investment decision";
- "Given that changes may be important for retail investors and their future allocation of investment



The consumer testing study seems to indicate a KID misunderstanding rate of between 30% and 60%.

assets, existing retail investors should reliably be able to locate the new [KID].”

It is worth bearing in mind in this context that the consumer testing study seems to indicate a KID misunderstanding rate of between 30% and 60% (with 70% understanding being exceeded in respect of a few aspects only). This would seem to be consistent with the Commission’s 2009 *UCITS Disclosure Testing Research Report* that seemed to indicate retail investor 30% misunderstanding rates for simple UCITS’ KIIDs.

KID content: Concerning the KID’s synthetic risk indicator, the current consultation sets out more detail around computing a VaR-based market risk measure (MRM), computing an obligor credit risk measure (CRM) and combining the two into a 1-7 scale as per the table below – which seems *inter alia* to mask MRM changes at the higher CRM ranges and CRM changes at the higher MRM ranges (colour emphasis added). In this respect, it is interesting that the consumer testing study states that consumers “were mainly concerned about the possibility of losing their investment if the manufacturer went out of business [...]”. The CRM is to be worked out primarily by reference to third party credit ratings (as “At this point no suitable methodology other than the current external rating was found.”), but otherwise by reference to a “credit quality step” depending on the type of obligor. Liquidity risk is proposed to be mainly addressed by way of narrative warning/explanation.

MRM class

CRM class	MR1	MR2	MR3	MR4	MR5	MR6	MR7
CR1	1	2	3	4	5	6	7
CR2	1	2	3	4	5	6	7
CR3	3	3	3	4	5	6	7
CR4	5	5	5	5	5	6	7
CR5	5	5	5	5	5	6	7
CR6	6	6	6	6	6	6	7

Distinctly, three “what-if” performance scenarios are proposed: “unfavourable”, “moderate” (based on “normal market circumstances”) and “favourable” (with the draft RTS recitals noting that “it is essential that forecasts are included in the KID”). In this respect, the consumer testing study notes that consumers “often wrongly assumed likelihoods when shown performance scenarios” and “where no information was provided on how probable the scenarios were – including where narrative text was included to underline that the scenarios had no implied probability – respondents tended to read an implied probability anyway”.

Costs and charges are also covered, both as reduction-in-yield and monetary figures, with structured debt securities covered by a “fair value” approach (contrasting the offer price with an expected or notional secondary trading value). In this respect, it is interesting that the consumer testing study seems to indicate consumer preferred focus on net returns (rather than on gross returns through the extraction of “embedded” costs as the PRIIPs regime will require) and that a “minority” of consumers “understood that the costs shown might not represent actual costs”.

Otherwise, the requirement for individual KIDs to identify the regulator with PRIIPs jurisdiction seems to be expected to be satisfied by reference to the regulator of the EEA Member State where the relevant manufacturer is located.

KID format: The current consultation sets out (at pages 32-33, 49-50 and 55-56 and 73) the proposed visual format of the KID and its risk indicator, performance scenarios and costs presentation (the combination of which reportedly fits within the KID’s length limit of three sides of A4). Length challenges may come in fitting in additionally required information, including notably “sufficient narrative” text necessary to ensure the above indicators are not misleading. Annex 10 to the consumer testing study final report also sets out earlier full mock-ups for several types of PRIIPs, including four (C1, C2, C3 and C4) for a “note” form of PRIIP.

KID review: The draft RTS provides for periodic and (where there is “material” change) *ad hoc* KID reviews and revision. In this respect, the draft RTS’s Recital 20 notes (further to the draft RTS’s Article 20): “Where a PRIIP is not currently *available* for retail investors, the continued review and revision of the [KID] would be disproportionate [...]. The trading of a PRIIP on a secondary market however would *not* exempt the PRIIP manufacturer from the obligation to continue to review and revise the key information document for that PRIIP.”

Potential practical considerations for industry: Given the residual ambiguity on KID purpose/liability, the KID’s length cap and the KID’s relatively ambitious content requirements, there may be some further practical considerations for market practitioners to consider (particularly since there seems to be no grandfathering or transition for non-UCIT existing products). For example, would the prescriptive nature of some of the PRIIPs regime’s disclosure requirements mean such disclosure is deemed to not be misleading? Might market practitioners seek to ensure that PRIIPs can only be made available to retail on an advised basis to mitigate the risk of investors being misled (including in terms of secondary market access)? Might this involve potential restrictions on PRIIPs transferability (which might also be relevant in terms of retail “availability” and the KID review/revision obligation)? Might this reduce the range and choice of products that might be offered to retail investors? (It might distinctly be interesting to see how this would fit with the Commission’s Capital Markets Union agenda and its December 2015 [Green Paper](#) on retail financial services seeking feedback by 18 March.) The answers to these and other questions may only become apparent as the new regime takes its final shape.

Next steps: Despite the residual ambiguity on KID purpose/liability and the highly technical and granular nature of the current consultation, the JAC is working to respond on at least certain aspects by the prescribed deadline of 29 January. It is expected that the ESAs will then deliver final draft Technical Standards under the PRIIPs Regulation to the Commission at the end of March, with the Commission adopting final standards in early summer and the PRIIPs regime coming into application from end-2016 (regardless of any delay to the implementation of MiFID II).

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~~Market Abuse Regulation (MAR)~~

~~On 28 September 2015, ESMA published its *Final Report: Draft Technical Standards on the Market Abuse Regulation*. This follows ESMA’s preceding July 2014 consultation to which ICMA responded on 15 October 2014 (as noted in the First Quarter 2015 edition of this Quarterly Report). ICMA’s focus continues to be on the aspects of MAR that most exclusively impact new bond issuance: stabilisation and market soundings.~~

~~Regarding stabilisation, the Final Report’s draft technical standards seem to replicate the existing Market Abuse Directive (MAD) regime, albeit with one significant difference. That is that “details” of stabilisation trades must be published within seven daily sessions and not just reported to regulators as currently under MAD. This possibility was not mentioned in the July 2014 consultation or in the consultation feedback included in the Final Report. It is hopefully not the official intention to include counterparty identification information among such details and so override client confidentiality (which has been specifically preserved in the context of MiFID II’s transaction reporting/publication provisions). Either way, regulatory clarification would seem relevant to help market participants comply with their client confidentiality obligations. Distinctly, the detailed proposals in ICMA’s October 2014 response to streamline the stabilisation regime were neither included in the draft technical standards nor acknowledged in the Final Report’s feedback statement. The draft Technical Standards also envisage reporting to multiple regulators. This was not unexpected, but it might be helpful for ESMA to maintain a public list of regulator contact details for receiving such reports.~~

~~Regarding market soundings, the Final Report’s draft Technical Standards seem much improved (though still highly prescriptive) compared to the July 2014 consultation, though there seem to be a few residual inconsistencies – for example between the Final Report’s draft Regulatory Technical Standards’ Article 3.3(e) and its implementing technical standards’ Annex I, item vii. Queries remain, however, as to the practical application of MAR’s procedural requirements for market soundings that do not involve inside information.~~

~~The MAR regime is due to come into force on 3 July 2016, so there remains limited time for the Technical Standards to be adopted (and then for industry to put into place the consequently related processes and systems).~~

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Other primary market developments

Pricing references for new sterling Eurobonds: A new ICMA Recommendation 1.33 (since reorganised as ICMA Recommendations 7.3 to 7.5) on pricing references for new sterling Eurobonds was introduced into the ICMA Primary Market Handbook in February 2015 (and referenced in the Practical Initiatives section of the *Second Quarter 2015* edition of this Quarterly Report). The purpose of the Recommendations is to clarify the appropriate gilt to use when pricing new sterling Eurobond issues. The Recommendations reference generic reasons why a gilt might not be appropriate as a benchmark but do not reference specific gilts for future proofing reasons. However, primary market practitioners currently seem generally to consider that:

- three existing gilts are inappropriate as credit benchmarks in the context of ICMA Recommendation 7.3: 8% 2015, 8.75% 2017 and 8% 2021; and
- new gilts should be considered appropriate as credit benchmarks, in the context of ICMA Recommendation 7.3, when they approach £10 billion of free float.

In this last respect, UKT 2% September 2025 has been increased through auctions over the last six months, taking it over the £10 billion free float threshold.

PRIPs: On 17 August, ICMA submitted a response to the ESAs' 23 June Technical Discussion Paper on risk, performance scenarios and cost disclosures for KIDs (reported in the *Third Quarter 2015* edition of this Quarterly Report). The response, covering the "vanilla" bond perspective only (and not structured securities), mainly emphasised concerns around potential impact on vanilla issuers coming to retail markets, KID purpose and liability, as well as risk indicators and performance scenarios.

Bank of Italy reporting requirements under Article 129 TUB: On 25 August 2015, the Bank of Italy issued a final measure pursuant to Article 129 of the Italian Banking Act (TUB) concerning post-issuance reporting requirements to be fulfilled when financial instruments are (i) placed in Italy by any entity, (ii) placed or offered by an Italian resident issuer in any country or (iii) placed or offered in Italy by non-Italian resident entities belonging to an Italian resident group parent company that is subject to supervision in Italy. The reporting obligations will take effect from 1 October 2016 and cover a variety of quantitative and qualitative information in relation to the securities, which must be reported via an online platform within the working day following the

filing of the prospectus with the competent authority or, if a prospectus is not required, within the settlement or issue date. Certain other data must also be reported within 20 days of that date. The measure is likely to represent a significant additional administrative burden for affected market participants, and it will be interesting to see if it affects levels of bond market activity in Italy and by Italian issuers. More generally, it is out of step with EU aspirations to create a Capital Markets Union, by imposing administrative burdens on issuers at a national level.

LIBOR: ICE BA published a second position paper on the evolution of LIBOR on 31 July 2015, which calls for comments by 16 October 2015. This follows the first position paper, to which ICMA replied by e-mail in April 2015 outlining the importance of contractual continuity. The second position paper is similar to the first position paper but with some adjustments reflecting submitters' concerns and a new proposal for the definition of LIBOR (among other things). ICMA will be considering carefully the need to respond to this second position paper.

UK HMRC consultation on deduction of income tax from savings income: ICMA responded to a UK HMRC consultation, entitled *Deduction of Income Tax from Savings Income: Implementation of the Personal Savings Allowance*, on 18 September 2015. The Personal Savings Allowance (PSA) will be introduced in the UK from 6 April 2016 and will exempt the first £1,000 of "savings income" for basic rate taxpayers, and the first £500 for higher rate taxpayers, from income tax. The PSA will cover interest paid under funding bonds, among other things. The consultation invited views on whether changes are required to tax deduction arrangements currently in place for certain types of savings income, including interest paid under funding bonds. There was no direct suggestion in the consultation that the quoted Eurobond or other similar exemptions for interest paid under bonds would be affected by the proposals. However, there is a possibility that in making any changes to the Income Tax Act, the quoted Eurobond and other exemptions could be impacted in some way. In summary, ICMA's response states that we do not have a strong preference between the various options suggested for adjusting the current regime, but it is important that any amendments made to the regime do not affect the gross-paying market nature of the international bond market.

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market in Europe. Applying changes to the PD to encourage SME and/or retail access to capital markets should be done in a way which avoids any adverse effect on the functioning of the wholesale market.

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UK FCA investment and corporate banking market study

The [Terms of Reference \(ToR\)](#) for a UK FCA investment and corporate banking market study were published on 22 May 2015. This follows the FCA's Wholesale Competition Review [call for inputs](#) in July 2014 (to which ICMA filed a [response](#) in October 2014) and consequent [feedback statement](#) in February 2015 (see further coverage in the [Fourth Quarter 2014 edition](#) and [Second Quarter 2015 edition](#) of this Quarterly Report) and related [feedback from roundtables](#). The UK Fair and Effective Markets Review's [Final Report](#) (see further in the Capital Market Initiatives section of this Quarterly Report) has also since concluded that bundling and cross-subsidisation and the transparency of the corporate bond allocation process will be assessed as part of the FCA's market study.

In terms of process, the FCA intends to engage stakeholders (notably including issuers as well as investors) during its study and, though not formally consulting on the ToR, welcomed any inputs by 22 June. Hopefully Eurobond issuers (who have been less vocal historically on new issue processes than investors) will continue to engage with the FCA in this respect, with ICMA's support. An FCA interim report is expected around year-end 2015 and a final report is expected in spring 2016.

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Other primary market developments

FCA CoCo rules: The FCA has published its [Policy Statement](#) containing the final permanent marketing restriction (PMR) relating to CoCos. ICMA is working with the ICMA Legal & Documentation Committee and ICMA PDGM Compliance Working Group to discuss the practical implications of the final PMR.

Omnibus II Directive RTS: ESMA has submitted a [Final Report](#) containing draft RTS on prospectus-related issues under the Omnibus II Directive to the Commission. The draft RTS relate to the Prospectus Directive approval, publication and advertisement

regimes, and follow an ESMA consultation to which ICMA responded in December 2014 (as reported in the [First Quarter 2015 edition](#) of the ICMA Quarterly Report). Helpfully, the concerning proposals relating to incorporation by reference that were included in the Consultation Paper have been removed from the final draft RTS. The Commission has three months to decide whether to endorse ESMA's draft RTS.

MiFID II complex / non-complex instruments: On 15 June 2015, ICMA filed a [response](#) to an ESMA [Consultation Paper](#) on draft guidelines on complex debt instruments and structured deposits. The response highlighted notably that complexity for MiFID's narrow purpose (availability of execution only) should not be taken to equate either to toxicity or to a universal definition of complexity.

ICMA also supported a Joint Associations Committee (JAC) 15 June [response](#) on retail structured products (RSP) in further depth from the RSP angle. Distinctly, ICMA also supported a 1 June JAC [response](#) to JAC response to the UK FCA's [consultation TR15/2 \(Structured Products: Thematic Review of Product Development and Governance\)](#). The response focused on the recognition of the requirement for tailored solutions, coordination with global regulators, identifying the target market, proportionality and the read-across to other products.

PRIPs: The Joint Committee of the ESAs (EBA, EIOPA and ESMA) published a [Technical Discussion Paper](#) on risk, performance scenarios and cost disclosures for KIDs for PRIPs on 23 June 2015, with a deadline for comment of 17 August. ICMA will be considering carefully what feedback would be relevant, bearing in mind historic ICMA concerns (outlined in various prior editions of this Quarterly Report) around the residual ambiguity of the purpose (and related liability) of the PRIPs key information document (KID) and around the mandatory use of simplistic and potentially confusing synthetic risk indicators.

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Other primary market developments

There have been a variety of other primary market developments over the past quarter.

- UK FCA restrictions on the retail distribution of CoCos:** On 27 January 2015, ICMA responded to the UK FCA's consultation on restrictions on the retail distribution of regulatory capital instruments, raising the points noted in the previous edition of this Quarterly Report.
- Securitisation:** On 14 January 2015, ICMA, jointly with AFME, the BBA and ISDA responded to the EBA's Discussion Paper on Simple, Standard and Transparent Securitisations and on 13 February 2015, ICMA, jointly with GFMA, the IIF and ISDA, responded to BCBS/IOSCO's Consultative Document on Criteria for Identifying Simple, Transparent and Comparable Securitisations.
- PRIPs:** On 17 February 2015, the Joint Associations Committee on retail structured products submitted with ICMA's support a response to the ESMA Discussion Paper published on 17 December (and reported on at some length in the First Quarter 2015 edition of this Quarterly Report). The response addressed technical aspects arising in the context of retail structured products. ICMA did not respond from the vanilla markets perspective as vanilla bonds appear to be out of scope of the new regime.
- UK FCA Wholesale Competition Review:** On 19 February 2015 the UK Financial Conduct Authority (FCA) published a Feedback Statement to its July 2014 Wholesale Sector Competition Review – Call for Inputs (to which ICMA briefly responded on 6 October 2014 simply flagging press coverage indicating robust competition amongst bond underwriters). The Call for Inputs had discussed various aspects of equity underwriting (as this had been the focus of previous competition work by the UK Office of Fair Trading), noted hypothetically that “similar mechanisms might be at play in the issuance of debt securities” and welcomed evidence on whether these or other issues exist in the supply of debt. In this respect, the Feedback Statement notes the following feedback from respondents in the context of debt issuance transactions specifically: competition for debt underwriting is effective; large corporate clients have relationships with several banks and rotate the lead firm in separate DGM transactions, which incentivises banks to provide a good service and promotes competition; and in this context, fees cannot fall much further before debt underwriting becomes unprofitable. The FCA has announced plans to launch a wholesale market study into investment and corporate banking (with related terms of reference to be published in the spring), including debt underwriting (presumably for consistency and completeness). In this respect, there is likely to be much interest in the final recommendations of the UK's Fair and Effective Markets Review (FEMR) scheduled for June 2015 (see a summary of ICMA's response to FEMR towards the beginning of this

Quarterly Report). This is because (i) the FCA's Competition Review extends beyond a classic competition focus to touch on conduct of business elements also covered by the FEMR; and (ii) the FEMR also specifically includes competition aspects.

- ICMA Standard Form ECP Documentation:** ICMA has recently completed work on updating the ICMA Standard Form ECP documents contained in the ICMA Primary Market Handbook. The updated documents have been circulated to various ICMA Committees and Working Groups and will be officially published in the forthcoming revised ICMA Primary Market Handbook.

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In relation to *soundings*, the response mainly sought to re-emphasise the scope of the sounding procedures as applicable only to the extent of providing a safe harbour where there is disclosure of inside information (rather than as standalone obligations). Creating an additional forecasting obligation in relation to cleansing was also flagged as valueless, burdensome and inconsistent with the provisions of MAR itself. Distinctly the response emphasised regulation needs to recognise that much information is “treated as” inside in light of widening and nonsensical regulatory enforcement interpretations of the definition of inside information. The response also sought to minimise potentially confusing duplication between various legislative provisions and to highlight certain other inconsistencies (including the need to recognise established information barriers between “private” and “public” sides within sounding entities).

Soundings: the implications

It is worth noting that an inability to sound effectively may result in issuers and lead managers: (i) pricing too aggressively (with a likely sell-off in the immediate after-market and a need for stabilisation that or may not be forthcoming as noted above); (ii) pricing too cautiously and generously (with issuers suffering in relation to their cost of funding); (iii) increasing and widening the public pricing iterations (a longer and more strenuous process for all, including investors); (iv) abandoning funding transactions (with real economy implications) or launching them outside the EEA.

Some may consider that too few investors will accept soundings if stricter obligations are not imposed by MAR on sounders, but the converse risk of stricter obligations is that there will be few soundings for investors to even consider refusing. The risk of refusal is diminishing to an extent as the larger and more sophisticated investors nominate segregated “gatekeepers” and, especially, their own dedicated “syndicate” desks that participate in new issues but do not manage underlying funds (and so do not suffer from trading restrictions).

ESMA is expected to submit by 3 July 2015 its draft Technical Standards to the European Commission for its review and then adoption by the 3 July 2016 deadline when MAR’s Level 1 provisions are due to come into force.

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PRIIIPs

Summary

Legislative progress continues on the forthcoming Packaged Retail and Insurance-Based Investment Products (PRIIPs) regime, with official publication of the PRIIPs Regulation and of a Discussion Paper on implementing measures – notably concerning potential options in terms of KID reviews and KID presentation of costs and of risk and reward.

On 17 November 2014, the three European Supervisory Authorities (ESAs), that include ESMA, published a Level 2 Discussion Paper (DP) on Key Information Documents (KIDs) for Packaged Retail and Insurance-based Investment Products (PRIIPs). Shortly thereafter, on 9 December 2014, the final PRIIPs Regulation (Regulation EU/1286/2014) was published at Level 1 in the EU’s *Official Journal*, followed by a minor *corrigendum* to the penultimate paragraph of Article 8 on 13 December 2014. The ESAs also published on 18 November 2014 a call for expressions of interest (to be received by 15 December 2014) in joining a consultative Expert Group (for the PRIIPs Sub-Group of the ESAs’ Sub-Committee on Consumer Protection and Financial Innovation).

Final PRIIPs Regulation: The final PRIIPs Regulation seems substantively unchanged from the post-trilogue version published by the European Council on 3 April 2014 and commented on in the *Third Quarter*

2014 edition of this Quarterly Report. Aside what seem to be multiple primarily stylistic changes, the main points of note seem to be in terms of the timings applicable to the legislative process:

- 29 December 2014: coming into force of the final PRIIPs Regulation;
- 30 December 2014: start of period for the European Commission’s exercise of delegated powers;
- 31 December 2015: deadline for delivery to European Commission of draft RTS on KID delivery and reviews;
- 31 March 2016: deadline for delivery to European Commission of draft RTS on risk and reward indicators and costs;
- 31 December 2016: deadline for enactment of national administrative sanctions and *coming into application* of the final PRIIPs Regulation;
- 29 December 2017: nominal end of period for the European Commission’s exercise of delegated powers (subject to tacit extension);
- 31 December 2018: deadline for European Commission’s review of the PRIIPs regime; and
- 31 December 2019: end of UCITS exemption from scope.

DP in general: The DP examines, *inter alia*, potential options in terms of risk and reward indicators (including performance scenarios), costs and KID reviews. The DP outlines pros and cons of the various alternatives, often noting the challenges (given the heterogeneity of PRIIPs) in selecting an approach that is (i) easily comprehensible, (ii) enables comparison with other products and (iii) is not misleading to investors. In respect of the first limb, consumer testing would indeed seem to be crucial (presumably testing accuracy of understanding rather than merely noting superficial preferences), though accuracy should take precedence over simplicity as a regulatory priority. Concerning comparability, prior commentary has noted the need for this to be sensibly limited to comparing like with like – eg two apples or two pears (but not



It follows that the KID *cannot* contain sufficient information to allow consumers to make an informed investment decision.

comparing an apple and a pear as apples and pears should rather be compared generically). In terms of the last limb, it is concerning that many of the options discussed in the DP involve assumptions, estimates and/or a past performance basis that seem unlikely to be apparent on the face of the KID and so (regardless of any reasonable basis) could well be misleading to investors (not forgetting the mantra – acknowledged in the DP – that past performance is no guide to future return). The DP interestingly notes that a “measure that is overly sophisticated in relation to [...] accuracy [...] could be seen as disproportionate”. One may wish more thought had been given to all this during the Level 1 process. The DP also considers interaction with other EU legislation, examining MiFID II, Solvency II, the Insurance Mediation Directive, the UCITS Directive, the AIFMD and the Distance Marketing Directive for Financial Services – but strangely ignoring the Prospectus Directive.

Liability: It is worth bearing in mind that the PRIIPs Regulation’s Article 11 does *not* limit civil liability where the KID is (i) misleading, (ii) inaccurate, (iii) inconsistent with the relevant parts of legally binding pre-contractual and contractual documents, or (iv) inconsistent with the requirements laid down in Article 8 (on detailed KID content requirements). This gives particular salience to the KID’s purpose (in terms of potential damage causation) and the meaning of the “key” qualifier that is embedded throughout the PRIIPs regime (regarding information, risks, etc.) and considered further below.

KID purpose: The DP recognises that “the KID should have a clear behavioural purpose for the retail investor”. It has been recognised at various times that the KID itself, which is limited to three pages in length, cannot be exhaustive. It follows that the KID *cannot* contain sufficient information to allow consumers to make an informed investment decision. (That would be the role of the prospectus, which is required under the Prospectus Directive to contain “all information [...] necessary to enable investors to make an informed assessment”.) The DP notes the KID’s

purpose is set out in the prescribed legend to be included in the KID: “to *help* [the investor] understand the [PRIIP] and to *help* [the investor] compare it with other products” (emphasis added). Incidentally, the DP also notes “the KID should be understood by the retail investors with the assumption that the consumer may not have an adviser, distributor or seller on hand to explain the information”.

Key information/templates: The DP notes the need for specific “Key Questions” to help construct the KID. The concept of prescribing what information is “key” through specific questions is an interesting one, as there is no generally accepted conceptual definition of what “key” information is as a sub-set of the established concept of information that is “material” to an informed investment decision. The DP also notes that the use of prescribed KID templates might provide legal certainty for manufacturers, but queries whether this might also reduce the extent to which manufacturers take responsibility for developing the KID (as well as reducing innovation), suggesting that certain templates could operate as non-compulsory safe harbours. A relevant consideration might be the level of detail of any such templates. (The DP notes in this respect the relevance of the ESAs’ substantive conclusions in respect of individual information items.)

Risk and reward indicators: In terms of risk indicators, the DP focuses for convenience more on visual presentation than on methodological substance (which will be subject to subsequent distinct consultation). The ESAs consider that risk factors can be reduced to three main types of risk:

- market risk (the risk of changes in PRIIP value due to movements in the value

of the underlying assets or reference values);

- credit risk (risk of loss arising from a PRIIP obligor’s failure to meet some/all its contractual obligations, having accounted for seniority and any collateralisation); and
- liquidity risk (the absence of a sufficiently active market on which a PRIIP can be traded or of equivalent arrangements).

In terms of quantitative risk measures, the DP notes there may be no fully accepted and already standardised methodologies, whilst, for qualitative measures, a combination of factors might be envisaged, given that single factor qualitative measures may not be sufficiently effective or indicative. Several of the possible measures cited seem to be short term and ultimately based on past performance (volatility/VaR-related) or relatively subjective. The DP considers the aggregation of distinct risk measures (as a way of simplifying presentation), but it is unclear what non-misleading basis might be used for such aggregation. The possibility of a single indicator which shows more than one dimension is raised, but a radar graph is not specifically contemplated. Narratives are noted as a way of explaining what an indicator shows and how to use it (including covering the risks not included or aggregated in the risk indicator) – however it is unclear how that would fit with the KID’s length limitations of three sides of A4 paper. In terms of performance scenarios, the DP notes these could be based on hypothetical situations or on data (historical or modelled) and considers two, three and five scenario options. The DP also notes the potential relevance of accounting for costs information in the context of performance scenarios and consequential consistency between the two sets of measures (eg in terms of investor time horizon).

Costs: The DP considers various elements around identifying direct and indirect costs. Though indirect (embedded) costs are specified in the PRIIPs Regulation, it would seem unclear what value investors will place on these since their natural focus will presumably be on their net return. The cost of investment advice is explicitly acknowledged as something the KID cannot capture, as it is paid for separately by the investor and may not be known by the PRIIP manufacturer. This would seem to be equally true for any third party cost relating to an investment, for example custody or trading services. The DP acknowledges there is no guarantee that two manufacturers would agree on the costs of a product. It raises the possibility of cost being the difference between (i) the amount received by the manufacturer and (ii) the liability the manufacturer records on its balance sheet (loosely termed “fair value” though no intrinsic fairness seems to be involved).

KID review, revision and republication: The DP considers distinct periodic assessments and, where “change is *materially* important enough to require a revision” (emphasis added) punctual reviews of KIDs. In the latter case, it remains to be seen whether there will be any cross-over from the “significance” test for Prospectus Directive supplements (linked in turn to the underlying prospectus “materiality” test). The DP suggests situations in which an investor might be informed of a changed KID could include “where there is a *significant* change – such as a reclassification of the risk of the product, or a *major* change in its likely costs, or in its objectives and how they are to be achieved” (emphasis added). Again, any Prospectus Directive cross-over remains to be seen. Otherwise, concerning PRIIPs with limited offer periods, the DP notes that “the continued updating of *all* sections of the KID *may* not be relevant” (emphasis added) but that secondary trading would also be a relevant consideration (with KID updates at least where secondary trading involves the issuer). The DP acknowledges the KID’s design as pre-contractual information and so queries the extent to which it might be used to inform investors of changes.

Other Sections of the KID: The DP notes that under the “How can I complain?” section, information should be included both about the manufacturer and distributor. It is however acknowledged that the manufacturer may not know who the distributor is and so may not be able to include specific related information, with a possible solution mused to be the inclusion of generic information or a reference to where further information can be found. Otherwise aspects covered in the DP are title, explanatory statement, identity, comprehension alert; “What is this product?” (PRIIPs type classification, objectives, consumer types, insurance benefits, term); “What happens if [the PRIIP manufacturer] is unable to pay out?” (investor compensation/guarantee schemes); “How long should I hold it and can I take money out early?” (penalties); other relevant information (information on other official documents with website links permitted). The DP also considers products offering many options (likely to be of limited potential relevance to the Eurobond markets). Regarding KID delivery being “in good time”, the DP notes the potential relevance of Recital 83 of MiFID II.

ICMA engagement: ICMA is working to respond by the DP’s 17 February deadline:

- in respect of retail structured products, through the Joint Associations Committee on retail structured products; and
- possibly also in respect of “vanilla” Eurobonds, directly (see further the [Third Quarter 2014 edition](#) of this Quarterly Report in relation to the extent to which Eurobonds are, or may in future come, within the scope of the PRIIPs regime).

Next steps: The DP is expected to be followed by:

- in the spring, a more technical ESAs’ Discussion Paper (on more complex aspects of the RTS such as on the methodology for calculation of the summary risk indicator);
- until August, a European Commission consumer testing exercise (initiated in the autumn of 2014);

- prior to the summer (estimated), a specific Consultation Paper on the review, revision and republication of KIDs;
- prior to the summer (estimated), a specific Consultation Paper on the timing of delivery of KIDs;
- in the autumn, a Consultation Paper on draft RTS, setting out the ESAs’ conclusions (hopefully with a feedback statement);
- at some stage, an impact assessment (building on that prepared in support of the original legislative proposal) to accompany the draft RTS being submitted to the European Commission (for which stakeholders views and data are welcome).

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~~acceptance of a disclaimer and the obligation to provide an email address, where a charge is made for that electronic access or where consultation of parts of the prospectus free of charge is restricted to two documents per month. This point was the most contentious point of the case, but most issuers should be able to comply (and already do comply) with the ECJ's ruling. However, those issuers that do not have their own websites on which to publish prospectuses might face difficulties if their other options for electronic publication include the barriers to access described in the ruling. The Luxembourg Stock Exchange announced that all published prospectuses (including supplements, final terms and documents incorporated by reference) on its website will be accessible to potential investors without any access restrictions from 13 June 2014.~~

~~Finally, Omnibus II was published in the Official Journal on 22 May 2014, with the provisions amending the PD being substantially in the form reported in the Second Quarter 2014 edition of this Quarterly Report. Member States have to publish laws, regulations and administrative provisions required by Omnibus II and relating to the PD by 31 March 2015, and apply those measures from 1 January 2016.~~

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PRIIPs and vanilla bonds

Following reports of initial political agreement on 1 April (see the [Second Quarter 2014 edition](#) of this ICMA Quarterly Report), the European Council published on 3 April a [final compromise text](#) for a Regulation on Packaged Retail and Insurance-based Investment Products (PRIIPs). This was followed by European Parliament plenary [adoption](#) of the dossier on 15 April, accompanied by a European Commission

~~press statement and memo of frequently asked questions.~~ One of the main aspects of the Regulation is the requirement for key information documents (KIDs) for retail investors that are a maximum of 3 sides of A4 paper. Anticipated next steps are formal publication of the Regulation in the *Official Journal* (following jurist linguist review) and industry consultation on implementing subsidiary Level 2 measures (potentially an ESMA discussion paper later in 2014 followed by a consultation paper in 2015). While the final compromise includes notable improvements on prior drafts, several concerns remain particularly salient, beyond those outlined in prior editions of this ICMA Quarterly Report.

Scope: It would seem that the scope of the Regulation does not extend to vanilla bonds, as these do not involve an amount “repayable” being subject to fluctuations in underlying reference values or asset performance. This would also be consistent with the explicit confirmation of the exclusion of deposits solely exposed to interest rates and assets that would be held directly, such as corporate shares or sovereign bonds. That said, (i) the Commission seems to believe that hybrid securities may be somehow covered within this scope (citing the example of 12 year subordinated notes) and in any case (ii) national governments may extend the scope domestically. The scope is due to be reviewed four years down the line. Hopefully, vanilla bonds will continue to be excluded, as the Commission considers that, in contrast to simple products where investors generally only consider different interest rates, (i) packaging raises costs and complexity and makes instruments more difficult to compare and (ii) this warrants stronger investor protection and transparency measures. (This incidentally would also seem to illustrate why the focus of KID content should be on “packaging” information rather than on, say, corporate information about an issuer.) KIDs will also be required when dealing with discretionary asset managers, which seems strange



While the final compromise includes notable improvements on prior drafts, several concerns remain particularly salient.

since they are professionals whose fiduciary obligations would require them to review the fuller disclosure documentation, notably under the Prospectus Directive (PD).

KID purpose: It seems the purpose of KIDs will be to “enable” or (more realistically) to “help” investors to understand and compare products (both forms of wording confusingly appear in the text). Interestingly, the Commission has said KIDs should provide “basic” information on products, which might seem to be conceptually more intuitive than the “key” information terminology that has been actually been used in the legislative text.

Liability: There should be no civil liability unless the KID is misleading, inaccurate or inconsistent with certain documents or with specific disclosure requirements – which seems muddled compared to the clear status of the summary under the PD. More significantly however, this does not exclude further civil liability claims in accordance with national law – so there will be no pan-European consistency as in the PD. It is also not entirely clear to what extent compliance with all the specific disclosure requirements will be possible. For example, the Regulation envisages the use of synthetic risk indicators, though none have been put forward as not being likely to mislead; it may be impossible to set out, within the KID length cap, a narrative explanation of things that are not adequately captured by the indicator.

Who prepares KIDs and when: Retail intermediaries must provide KIDs to retail investors in good time before investors are bound, whilst issuers must prepare KIDs before products are made available to retail investors. One hopes there will be no potential for an intermediary to try to sell institutional products to retail investors without an issuer's knowledge or consent and so cause the issuer to be in breach of the regime (that would seem inconsistent with natural justice). Issuers will have to review KIDs "regularly" (and not just during offering periods), potentially until maturity.

Regulators: Regulatory jurisdiction seems unclear, which may result in overlapping (and potentially inconsistent) regulatory interpretations.

Legislative process: It seems the Regulation will start applying about two years following *Official Journal* publication, but the Commission's deadline for implementing subsidiary Level 2 measures seems to be about three years following *Official Journal* publication. So the regime could conceivably start applying without the detailed provisions being in place. Additionally, there does not seem to be any grandfathering for existing securities. The Commission is required to review the legislation about four years following *Official Journal* publication, so potentially on the basis of just 12 months actual experience of the regime working in practice.

The success (or failure) of the forthcoming PRIIPs regime would now seem to depend on what implementing Level 2 measures are ultimately adopted, with much more debate still needed.

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~~MiFID II Level 2: underwriting and placing~~

~~On 22 May, ESMA published *inter alia* a 311 page Consultation Paper (with a 1 August response deadline) on implementing subsidiary Level 2 measures under the MiFID review. Much of the consultation relates to secondary markets (see the next section of this ICMA Quarterly Report), but section 2.10 (12 pages) relates to conflicts of interest and provision of information to clients in the context of underwriting and placing that are relevant to the primary bond markets.~~

~~The consultation is not always clear as to its application between the debt and equity markets, but otherwise seems to mainly suggest that underwriters be required to have appropriate policies in place, which would be generally consistent with the points made in paragraphs 45-63 of ICMA's February 2011 response to the Commission 2010 MiFID consultation (see the First and Second Quarter 2011 editions of this ICMA Quarterly Report) and most notably with the Commission's subsequent 390 page impact statement (sections 3.8, 5/9.4, 6.9/9.4, Annex 3/13.9 and Annex 4/9.4).~~

~~However there are various points of granular detail that do not seem workable from a practical perspective, such as recording individual allocation rationales when allocating a book with 500 accounts within a couple of hours. It is also worth noting that many of the conflict risks highlighted by ESMA seem to be of a mainly theoretical nature. ICMA will be responding to these points by the 1 August deadline.~~

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There are various points of granular detail that do not seem workable from a practical perspective.

Other primary market developments

- ESMA has launched a “one-stop shop for EU regulated investment information”. The ESMA Registers provide, *inter alia*, a list of prospectuses, supplements and certificates of approval that have been approved under the PD. There are also registers for MiFID investment firms, UCITS management companies, Alternative Investment Fund Managers and sanctions under MAD, MiFID and UCITs.
- A corrigendum to the amended Transparency Directive was published in the *Official Journal* on 18 January 2014. The corrigendum changes the date by which the European Commission shall report on the operation of the Directive from 27 November 2015 to 27 November 2018.
- The US Internal Revenue Service issued on 20 February 2014 the last substantial package of regulations necessary to implement FATCA. The key amendments and clarifications relate to: (i) the accommodation of direct reporting to the Internal Revenue Service, rather than to withholding agents, by certain entities regarding their substantial US owners; (ii) the treatment of certain

securitisation SPVs; (iii) the treatment of disregarded entities as branches of foreign financial institutions; (iv) the definition of an expanded affiliated group; and (v) transitional rules for collateral arrangements prior to 2017. These regulations are not expected to impact on documentation in the primary DCM space.

- Anticipated trilogue negotiations concerning PRIPs opened between the European Council, Parliament and Commission on 29 January. An agreement was announced by the Parliament on 1 April, with possible formal adoption by the institutions concerned ahead of the European elections due in May. In this respect, the JAC (Joint Associations Committee on retail structured products), whose PRIPs work ICMA supports, has recently produced a paper recapping the KID content/length, purpose/liability, product intervention and synthetic risk indicator concerns expressed in prior editions of this quarterly report. Though technically focused on structured securities, the papers’ concerns are equally relevant to vanilla securities.

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~~employment, profession or duties” should not be prohibited, even if it occurs outside the safe harbour.~~

~~A particular focus is likely to be on the detailed administrative burden imposed by the new pre-sounding safe harbour (eg in relation to cleansing obligations), as an excessive burden in this respect might risk jeopardising the market benefit the safe harbour is designed to provide.~~

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Packaged Retail Investment Products

On 20 November 2013, the European Parliament adopted in plenary session its report (the [provisional version](#) of which has been published) on the text of a draft Regulation under the Packaged Retail Investment Products (PRIIPs) initiative. The terminology of the Parliament’s text refers to key information documents (KIDs) for “investment products” rather than “packaged retail investment products” – following a proposed widening of scope beyond structured products (though still limited to retail investors as defined under MiFID).

The Parliament’s text would, *inter alia*, seemingly require corporate bond issuers to:

- produce a non-misleading four-sided KID (including a summary risk indicator) that can be relied on by investors;
- publish the KID on a website, whether their own and/or perhaps that of the “relevant” regulators;
- notify the KID to the relevant regulator and provide additional information on request;
- keep the KID updated (the impact of which would presumably depend on the KID’s official purpose, with the European Commission to specify exactly when this would be needed);
- produce an annual report on the “achievement” of the bond concerned against “comparable” bonds, tailored to any individual investor’s portfolios that include several different securities of that issuer;
- maintain a complaints procedure;
- maintain an internal product governance process (involving target market approval and ongoing monitoring and review); and

- submit data quarterly for the ESA’s online fund calculator.

In this respect, delegation (eg contracting-out of administrative processes) would not relieve issuers of responsibility or liability and KIDs would be subject to potential regulator comment (as well as the bonds to potential regulator prohibition). Issuers would have the power to withhold consent to third party use of their KIDs, which might help somewhat to manage issuer risk. There would however be no equivalent to the Prospectus Directive’s €100,000 exemptions.

The Parliament’s text would seem likely to involve major logistical cost (even where the relevant processes are contracted out), as well as significant liability risk (which cannot be contracted out), for issuers. This might call into question the viability of many bond issues to retail investors, though only time would really tell. This would be ironic, given the text’s purported proportionality and stated purpose “to reduce costs and uncertainty for product providers and distributors”.

The Parliament’s text is, however, just one of three competing texts that have been expected to enter trilogue negotiations in early 2014. Some commentary on the other two texts – the European Commission’s original [July 2012 proposal](#) and the European Council Presidency’s [24 June compromise proposal](#) that was adopted as the Council’s general approach – is set out, respectively, in the [Fourth Quarter 2012](#) and [Third Quarter 2013](#) editions of the ICMA Quarterly Report. Distinctly from the specificities of the competing texts, it remains unclear whether the Regulation will be adopted by next May’s Parliamentary elections, as there are other legislative proposals which might take priority in this limited time period.

Distinctly, the Joint Associations Committee on retail structured products has published, with ICMA’s participation, a



ICMA Legal & Documentation Committee



review) should hopefully follow later this year, with the new MAR then coming into effect in late 2015. Industry focus will now have also to encompass MAR's Level 2 measures and ensuring that such measures are properly consulted on and finalised and published to allow the markets sufficient notice of their requirements before they come into application.

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PRIPs: key information documents

Following the European Council's [24 June general approach](#) (reported in the [Third Quarter edition](#) of this Quarterly Report), the European Parliament's ECON Committee continues to work towards adoption of its report to enable trilogue negotiations with Council and the European Commission to begin. Timing is now a particularly relevant consideration as trilogue will need to complete with sufficient time to spare for a subsequent Parliamentary plenary vote (currently scheduled for 24 February 2014) before the Parliamentary elections scheduled for May 2014. Extension of scope to vanilla products seems to be one of the major elements at this stage – any such extension certainly needing to be properly studied with actors in the relevant vanilla markets being formally consulted (something which has not happened so far). Even if this dossier is not completed under the current outgoing Parliament or picked up by the next incoming Parliament, the key information document

(KID) concept is here to stay – with multiple ongoing national and global initiatives. Consequently, the point (articulated in prior editions of this Quarterly Report) that short form disclosure *inter alia* cannot include, in words, all information for an informed investment decision (at least on the likelihood of a specific issuer of bonds being able to honour its related obligations) remains pertinent.

In this respect, it is worth most recently noting the [Consultative Document on Point of Sale Disclosure in the Insurance, Banking and Securities Sectors](#) published in August by the [Joint Forum](#) (which gathers IOSCO and its banking and insurance sister bodies) with a comments deadline of 18 October (the Joint Associations Committee that ICMA supports is considering a possible response). The Consultative Document acknowledges that concise point of sale disclosure cannot be exhaustive and is not a cure-all (noting the need for strong requirements on advice). Also of interest is the [update report on the work to support the implementation of the G20 high-level principles on financial consumer protection \(Principles 4, 6 and 9\)](#) published by [G20/OECD Task Force on Financial Consumer Protection](#) in September. This somewhat confusingly contemplates disclosure that is short and complete for “informed” assessments, whilst also acknowledging that transparency is not sufficient – needing to be complemented *inter alia* with business conduct measures. Last, but not least, and in the retail structured products context, is ESMA's July [Economic Report on Retailisation in the EU](#), the tentative conclusions of which may need to be further reviewed (particularly given the relatively limited sample of products analysed).



Stabilisation will no longer be subject to prior regulatory approval as was worryingly envisaged in the European Parliament's October 2012 report on MAR.

Packaged Retail Investment Products

ICMA continues to focus on the Packaged Retail Investment Products (PRIIPs) initiative, particularly from the vanilla debt securities' perspective, with several developments in recent months.

The European Council has [adopted](#), as a General Approach, a [24 June Presidency compromise proposal](#) (subject to a [reservation](#) by Italy concerning life insurance and administrative sanctions). This follows an earlier [28 May compromise proposal](#), which seemed slightly better.

Scope: The General Approach seems still to limit the scope of the proposed PRIIPs Regulation to “packaged” products, excluding vanilla debt securities. However, this seems subject to Member States' power to extend the scope on a national basis and also continues to be subject to a four-year review clause for the possible extension of scope. It is therefore important to continue focussing on how aspects of the proposed Regulation can inhibit vanilla bond issuance.

Jurisdiction: It seems that the scope itself of the Regulation may be a minimum harmonisation element, so that individual Member States can either impose national requirements on out-of-scope products or extend the scope to cover such products – presumably only if sold or advised on in their territories. However, it seems the European Commission would expect the content and format of the PRIIPs KID to be a maximum harmonisation element. This would certainly be essential if one wishes to support the single European market philosophy. In this respect, the Regulation should include a provision similar to the Prospectus Directive (PD) Article 17.1, to the effect that host competent authorities should leave it to the competent authority of the PRIIP manufacturer's home jurisdiction to decide to challenge a particular KID's conformity to the Regulation and should not be able to impose any additional procedures. Otherwise, issuers are likely to have to prepare up to 30 different KIDs for each product. However, the General Approach provides that the competent authorities in the jurisdictions where a product is marketed will have the right to suspend the marketing of a PRIIP “in cases of non-conformity with this Regulation”.

This needs to be clarified further. At the very least, the suspension power should be clearly limited to actual distribution (ie contractual offers) and not merely to the communication of information (the PD offer definition) – otherwise the PD pan-European passport itself will have been undermined.

The General Approach provides for Member States to designate competent authorities “to supervise the requirements this Regulation places on PRIIP manufacturers and the persons advising on or selling PRIIPs”, adding such authorities should be “consistent” with those “appointed with competence for the marketing under an existing passport”. Concerning securities, the overlapping application of the Prospectus Directive (including its thus entirely superfluous issue specific summary) is maintained and would seem to be a basis for any “passport” for offering PRIIPs that are debt securities. This would seem to imply that PD competent authorities would be designated as PRIIPs competent authorities. However, one may query whether other passports (for example concerning the MiFID reception and transmission of orders) might also be relevant, in which case there could be some ambiguity as to who would be the PRIIPs competent authority (at least in jurisdictions where responsibilities are not centralised within one regulator). Further clarity may be needed in this respect.

Filing: Member States in which PRIIPs are marketed may require the *ex-ante* notification of KIDs.

Duration/updating: It seems the KID obligation “will apply as long as the PRIIP is traded on secondary markets”, though it is unclear if such trading needs to involve the manufacturer/issuer. This could potentially result in due course (if vanilla securities are brought into scope) in European real-economy corporate issuers having to maintain updated KIDs on a 24/7 basis until maturity of their bonds – which could be decades or even more. Presumably this would strongly incentivise such issuers to avoid European retail issues.

Publication: This would have to be on the manufacturer/issuer's website, which may also prove challenging for many European real-economy corporate issuers, given the potential need to account for, eg third country rules on deemed directed selling efforts.



A critical point is to ensure that the PD regime exemptions, created to protect the wholesale markets from retail restrictions, are replicated in the PRIIPs Regulation.

Purpose: The KID purpose is stated as being “to help [investors] understand the nature, risks and rewards of [the] investment product and to help [them] to compare it against other investment products.” Whilst an improvement on other “informed investment decision basis” renditions (discussed in prior editions of this Quarterly Report), it could be further clarified that KIDs can only act as an introduction to either a full reading of the prospectus (for the minority of investors who are able and allowed to do so) or to regulated intermediation under MiFID (where the intermediary is required to know the product as well as its client in order to establish suitability/appropriateness).

Liability: The civil liability standard has been amended so that it is now stated as not being applicable “unless the KID is inconsistent with pre-contractual or contractual documents [...] or is misleading or inaccurate.” This is inconsistent with the PD summary and UCITs KID liability standards (where liability only arises if the KID is “*misleading, inaccurate or inconsistent when read together with [the prospectus]*”) and applies an administrative liability standard to civil liability – which may have a further chilling effect on European real-economy corporate issuers considering whether to engage with European retail investors.

Other changes: These include the apparent deletion of specific ADR provisions, nuances on distance communication and product options available to investors.

Unchanged aspects of the Council’s drafting have been previously commented upon in the [1Q2013 edition](#) (at page 32) of this Quarterly Report; whilst ICMA’s concerns about the PRIIPs debate more generally have been articulated most recently in the [2Q2013 edition](#) (at pages 32-34) of this Quarterly

Report. Pervasive concerns relate to (i) purpose/liability, (ii) distributors, who act independently of (and are even unknown to) manufacturers/distributors, causing such manufacturers/distributors to incur substantial liability, (iii) the inability of manufacturers to include distributor-level information in their KIDs and (iv) the adequacy of synthetic risk indicators. A critical point is to ensure that the PD regime exemptions, created to protect the wholesale markets from retail restrictions, are replicated in the PRIIPs Regulation – it would be absurd for a KID to be imposed where no prospectus is required under the PD.

The Council’s General Approach will be its starting point for the expected trilogue negotiations with the European Commission and the European Parliament (EP), which has not yet adopted its own position in this respect. However, internal opinions were adopted in April by the EP’s [LIBE](#) and [IMCO](#) committees. These reiterate many points previously noted, though also raise some new aspects, notably: (i) responses to complaints having to be in the same language as the complaint (with no qualification on the range of languages envisaged), (ii) reference having to be made to appropriate “risk-free” and comparable benchmarks (the existence of which may be debatable), (iii) publication of KIDs having to be on websites investors are “familiar” with (which may be highly subjective) and (iv) KIDs having to include disclosure on money laundering laws.

In the background to all this, the three European Supervisory Authorities have hosted a joint [Consumer Protection Day](#), which involved lively, and hopefully fruitful, debate and is expected to be replicated in 2014.

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Packaged Retail Investment Products

The European Commission's proposed Regulation on Packaged Retail Investment Products (PRIIPs) would mandate a very short pre-contractual key information document (KID) as the basis for "informed" investment decisions by retail investors in Europe.

Recent developments concerning the PRIIPs initiative have been in the area of the European Parliament, with publication of various further proposed MEP amendments to the European Commission's [original Level 1 legislative proposal](#) (discussed in the [Fourth Quarter 2012 edition](#) of this Quarterly Report):

- [amendments #65 to #367](#) and [amendments #368 to #680](#) by MEPs in the lead [Economic and Monetary Affairs \(ECON\) Committee](#) (completing the earlier amendments set out in the ECON Committee's draft report noted in the [First Quarter 2013 edition](#) of this Quarterly Report);
- [amendments #26 to #151](#) by MEPs in the [Internal Market and Consumer Protection \(IMCO\) Committee](#) (completing the previous amendments set out in the IMCO Committee's [draft opinion](#) noted in the [First Quarter 2013 edition](#) of this Quarterly Report);
- amendments in the [Civil Liberties, Justice and Home Affairs \(LIBE\) Committee's draft opinion](#) and subsequent [amendments #13 to #48](#) by MEPs in the LIBE Committee.

Several of these amendments seem fund/insurance-focused (and not relevant to debt securities), not entirely clear/consistent,

merely permissive, focused on negative statements or to stray into Level 2 detail or into other legislation. It is not entirely clear how the proposed amendments will play out, both within the Parliament and subsequently in Trilogues with the Commission and the Council. The Council has not yet adopted a general approach, though the previously reported [Council Presidency initial compromise](#) (noted in the [First Quarter 2013 edition](#) of this Quarterly Report) seems the most promising single text so far. That said, it may be helpful to consider some of the aspects and themes that have been raised by MEPs' suggested amendments more generally.

Generally: Too tight and ambitious a KID regime, especially in terms of liability (as not just an "incremental" cost), risks stunting supply, starting with the most conservative/reputable providers (manufacturers/issuers). This could lead to increased costs for investors given lower competition and increased concentration risk given reduced choice – ultimately perhaps limiting investment to just exempt UCITS and government securities (all in a context of challenging EU demographics and state finances). This would be unfortunate given the potential for a more modest KID concept to help empower investors, particularly noting that most retail investors rely on MiFID intermediation for their decision-making process.

KID purpose: There seems to be a danger with a KID being the sole basis for "informed" investment decisions, given:

- retail investor 30% misunderstanding rates reported in the [Commission's 2009 UCITS Disclosure Testing Research Report](#);
- suggested retail investor irrationality (for example cited [by the UK FCA's Martin Wheatley](#));
- consequential redundancy of the Prospectus Directive prospectus;
- impossibility of including, in a very

short space, all information relevant to "informed" investment decisions (at least relating to issuer "credit" information not present in the UCITS context);

- the potential risk that some distributors might try to limit their product understanding to just what is in the KID.

This could result in all PRIIPs effectively becoming contingent liabilities for those producing them, liable to rescission/refund at any time (distinctly from the civil liability considerations noted below) – quite the opposite of a reduction in costs and uncertainty that is avowedly being targeted. An alternative, workable, KID purpose could be as a basis to decide what *not* to invest in – ie to determine what investments to consider further. For the majority of retail investors, such further consideration would be done with MiFID intermediaries who have read the full prospectus or, failing which, the relevant contract(s) – which would need to be identified in the KID (so out of necessity and not mere "interest" as suggested in some MEP amendments). For an able minority of retail investors, if politically accepted, such further consideration would involve such investors doing such reading themselves. A secondary purpose could be for the KID to act as an *aide-memoire* if/when discussing possible investments with MiFID intermediaries. It has been suggested by some MEPs that the KID should help

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There seems to be a danger with a KID being the sole basis for "informed" investment decisions

financial education, though it is unclear what this would involve.

Product/conduct regulation: Various suggested amendments seem to be straying into the space of product/conduct governance, regulation and intervention (through direct obligations or through KID disclosure requirements that cannot be met except by conduct/structural changes). Some product regulation, such as fixed range of state-defined "simple" products, might be an alternative regime worth considering, but only for low value savings that do not justify the cost of MiFID-regulated intermediation. Conduct and product governance regulation certainly would seem best left to the most relevant legislative spheres such as MiFID, rather than be duplicated and potentially contradicted. In this respect, any perceived intermediation weaknesses can and must be addressed by strictly enforcing existing legislation (notably MiFID at Level 4) before creating more legislation.

Regulator KID involvement: Various suggestions have been made for KIDs (and any updates) to be notified to regulators, to be vaguely subject to potential regulator amendment/prohibition or more specifically to be subject (systematically or just occasionally) to regulator pre-approval. Distinctly from the product regulation/intervention points noted above, the value in pre-approving a highly prescriptive short document allowing no discretion is not clear – unlike the likely work burden for regulators having to review and/or approve thousands of KIDs each year. Any approval regime would at the very least have built-in realistic deadlines to ensure certainty and commercial viability. A particular suggestion is that certain complex characteristics in a product would (i) cause the product to be deemed as not targeted at retail investors and (ii) trigger an automatic legend in the related KID to the effect that the regulator considers the product to be unsuitable or too complex for retail investors and so has not assessed the information in the KID.

Aside from imputing to the regulator a view that it may not have consciously taken, it would seem such a product should not be distributed to retail investors at all and therefore should not have or need a KID.

Regulator competence also needs to be clear – some amendments suggest the regulator in the jurisdiction where the product is offered should assume this role (rather than the regulator of the manufacturer's home jurisdiction). This would effectively make PRIIPs a national regime (rather than a pan-European regime), in which case PRIIPs legislation should perhaps be left to individual EU Member States. A similar consideration arises if KIDs are required to be individually drafted in each jurisdiction (rather than translated) or are required to set out national "intermediary-specific" information (such as describing national tax requirements).

KID liability: Civil liability should only arise where a KID is misleading/inconsistent with the full documentation (the full prospectus or, failing which, the relevant contract(s)) – as is currently the case for the UCITS KID and Prospectus Directive summary (which has been noted in several amendments). Civil liability remains distinct from any regulatory oversight and sanctioning powers. Incidentally, referring to the relevant contract(s) only, where a prospectus exists, would only be consistent with KID content being limited to "structure"/"packaging" information only (and so excluding "credit" information on the issuer).

KID content: As noted above and below, various consequential implications arise for scope, responsibility and updating, depending on whether KIDs would include (i) "credit", as well as "structure", information, (ii) "intermediary-specific", as well as "product-specific", information and "dynamic", as well as "static", information. Even with clearly limited KID purpose/liability, it is unlikely that "credit" information can meaningfully be expressed within just a few short pages, short of just saying that



There should, in any case, be a clear exemption for securities with denominations of €100,000 or more.

the issuer is a rail company and that 100% loss could result if it becomes insolvent. Synthetic risk indicators and performance scenarios are much touted – legislators suggesting them should however be absolutely certain that such measures do not have the potential to mislead investors. In this respect, one may wonder whether European authorities would accept that credit ratings can be relied upon to indicate simplified "credit" information given the existence of the new European [Credit Rating Agency Regulation](#) regime.

Distinctly, there have been various suggestions for ethical information to be included in the KID, such as whether an investment is in the real economy or synthetic, speculative or a bet or what its contribution is to limiting global warming to +2° Celsius. Some of these are more subjective than others, which would seem inappropriate for an objective disclosure document. It is also not entirely clear that many investors would be interested in such information. Rather a limited and defined range of ethical labels could be approved by an appropriate authority, if satisfied as to their and/or their relevant sponsor. Manufacturers could then choose to include such labels on their KIDs if they consider it to be of interest to their potential investors (assuming the relevant criteria are satisfied).

PRIIPs' regime scope: Limiting the content of KIDs to "structure"/"packaging" information (and so excluding "credit" information on the issuer) would be

consistent with limiting the scope of KIDs to just packaged products (and so excluding vanilla products that do not have complex “structure”/“packaging”). As noted above, it is impossible to include, in a very short document, all information relevant to “informed” investment decisions about an issuer’s “credit”. It may be simplest at this stage provisionally to limit the scope to packaged products and review it in a few years, as per the Commission’s proposal. There should, in any case, be a clear exemption for securities with denominations of €100,000 or more, as this is one of the clearest practical delimitations (*inter alia* under the Prospectus and Transparency Directive regimes) between the retail markets that are targeted by the PRIIPs initiative and the institutional markets that are not.

KID length/style: There have been suggestions of 2-3 pages for KID length, with potentially one extra page for additional, “intermediary-specific”, information. This is not surprising given the UCITS KID history underlying PRIIPs and consumer behavioural research, but in turn emphasises the natural limitation on what information KIDs can include and in turn what purpose they can serve.

KID drafting responsibility: Unlike “product-specific” information, “intermediary-specific” information (eg on local taxation or intermediary costs) is not consistent with manufacturer KID drafting responsibility, as that information is not within the knowledge of the manufacturer (issuers may not even know who the ultimate retail distributors are under a retail cascade). Even if it were so, this would absurdly require KIDs to be thousands of pages long, in order to document each actual distributor/investor permutation. MEP amendments have variously suggested an intermediary annex to the KID, a separate intermediary document and intermediary disclosure under MiFID generally. Any of these approaches might work, if well structured. However these challenges and others

discussed in this article would not arise if KIDs were drafted by the intermediaries themselves, who are in any case required to know their products as well as their clients.

KID trigger/distribution responsibility: KIDs would be required prior to an intermediary “selling”, “acting as an intermediary in the sale” of, “distributing” and/or “advising” in-scope investment products (the terminology is subject to various amendments). However, an intermediary should not be able to force a manufacturer to draft a KID for a jurisdiction in which the manufacturer has no interest or desire for the product to be distributed – which is exactly what is implied by some amendments. This seems odd in any case from a logistical perspective if KIDs are required to be published on the manufacturer’s website, a website of the manufacturer’s choice and on a “central” website of the ECB and the competent national regulator (a seemingly contradictory concept). Rather, an intermediary should have the manufacturer’s consent, in some form, to distribute the manufacturer’s KID in satisfaction of the intermediary’s PRIIPs obligations – which has been noted in some amendments.

KID updating: Requiring KIDs to include information that is too “dynamic” and very likely to change over short periods of time (unlike “static” information) could result in an unworkable frequency of KID updates (potentially daily). There must be an up-to-date KID at a point of sale, but not otherwise – or some issuers would have to update KIDs daily for decades, though having issued securities on just one day. There are suggestions of annual reports that would be additional or alternative (unclear which) to updated KIDs. Issuers of listed securities are already required to publish periodic reports under the Transparency Directive and it is unclear what value yet another report would bring, particularly if no further “selling” is planned (the recent review of the Prospectus Directive abolished an annual report

requirement that was considered pointlessly duplicative with the Transparency Directive).

Litigation procedures: Such procedures have been established and regularly revised over decades and more at both national and European level. Litigation procedures concerning KIDs, including burden of proof and alternative dispute resolution should follow the existing *acquis* in this respect – a point made in several amendments.

Prospectus Directive overlap: Distinct from the potential overlap with the prospectus itself under the Prospectus Directive, the PRIIPs KID also overlaps most notably with the issue-specific summary (ISS) under the Prospectus Directive. The ISS was introduced in the recent review of the Prospectus Directive, seemingly because a KID regime did not yet exist. As the ISS is not a full prospectus, a summary of a prospectus document or a KID (the ISS is much longer), it therefore seems to serve no valuable purpose. As such, the ISS requirement in the Prospectus Directive regime should be abolished altogether by the time the PRIIPs KID requirement enters into force.

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~~Other primary market developments~~

~~In other developments, the Joint Associations Committee (JAC) on retail structured products that ICMA supports has submitted a response (restating earlier JAC positions) to a UK FSA consultation on the FGA’s use of temporary product intervention rules (restating earlier JAC positions) and also a response to an ESMA consultation on guidelines on key concepts of the AIFMD (notably highlighting the risk that sukuk and other securities may be inadvertently caught within AIFMD scope).~~

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PRIPs

Work on the EU's Packaged Retail Investment Products (PRIPs) initiative continues with the Joint Associations Committee on Retail Structured Products (JAC), of which ICMA is a participant, publishing a [position paper](#) on the preceding [Commission proposal](#) (discussed in the [Fourth Quarter 2012 edition](#) of this Quarterly Report, together with the main underlying considerations now picked up in the JAC position paper). Subsequently at Council level, an [initial Presidency compromise text](#) was published, which in many ways is a marked improvement on the Commission proposal.

Most notably, civil liability for the "key information document" (KID) only arises where the KID "is misleading, inaccurate or inconsistent with the other binding contractual documents" and the KID's purpose is narrowed to just "helping" investors take informed investment decisions. Whilst much improved, the liability focus (as referenced to contractual documents rather than prospectuses where available) seems to imply that KID content will focus on structure and market information and not on issuer credit information, which would be sensible but will need to be confirmed. The compromise includes a distinct heading for manufacturer default, separate from payout outcomes, but it is unclear whether this is intended to (i) simply flag the theoretical risk and consequence of default (which could seem workable) or (ii) involve a substantive assessment of such risk occurring and even likely loss given default (which could not be meaningfully addressed). The limited KID purposes – effectively (i) helping investors to sort which PRIPs to consider further and (ii) acting as a basis or a "map" for subsequent discussion with a MiFID intermediary or subsequent reading of a full prospectus – though improved, could be clarified further.

The compromise seems to limit the scope to only those retail products that are structured, though the drafting seems at risk of also catching simple floating-rate notes. Other products are left open to national rules, though one may wonder whether the maximum harmonisation provisions of the Prospectus Directive might limit this to an extent. Other improvements include abandoning the inclusion of various non-commercial ethical "labels", no longer reversing the burden of proof and emphasising

existing national ADR processes. The compromise also extends scope to advising on PRIPs (and not just selling them), establishes a regulatory power to ban marketing of some PRIPs (which implies KIDs will not be subject to prior regulatory approval but also seems to overlap with similar intervention powers being developed under MiFID) and includes a target market description within the KID. Some ambiguities and areas of potential concern include: (i) who will be the competent regulator; (ii) KID updating obligations once a PRIP is no longer being offered by, or on behalf of, its manufacturer; (iii) how a risk indicator could meaningfully operate; (iv) whether some distributors might be characterised as manufacturers in ways that might not be intended; (v) capping KID length at 3 pages; and (vi) ongoing incoherence with the Prospectus Directive's summary requirements.

Separately, at the time of writing of this article, the European Economic and Social Committee, the European Parliament's ECON Committee and the European Parliament's IMCO Committee had just published their respective [opinion](#), [draft report](#) and [draft opinion](#) on the PRIPs proposal. Opinions of the European Parliament's JURI and LIBE Committees are also expected. On initial reading, the ECON draft report seems *inter alia* to: (i) split KID responsibility between manufacturers and distributors according to the type of information concerned; (ii) immediately extend the scope of the KID concept to all vanilla bonds distributed to retail; and (iii) grant KID pre-approval and MiFID product intervention powers to regulators. Further coverage will follow in the next edition of this Quarterly Report.

In continuing work on the PRIPs initiative, it may be worth reflecting on a point made by ESMA's Chair, Steven Maijor, in his opening statement at ESMA's 12 December Investor Day: "*Behavioural finance suggests that biases and competence failures are unlikely to be dealt with through disclosure. And the problem of information overload has also been well documented. Disclosure has considerable attractions as a retail market tool, but the challenge for regulators is to resist the temptation to make disclosure the panacea for investor protection.*"

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Packaged Retail Investment Products

On 3 July the European Commission published its much anticipated [proposal](#), over 32 pages, for a directly-applicable Regulation on Packaged Retail Investment Products (PRIIPs), together with a 99 page [impact assessment](#).

The proposal envisages a “key information document” (KID) as a very short document (expected by many to be two/three pages along the lines of the existing UCITS KID), upon which retail investors will be able, without “being required to read other documents”, to “take an informed investment decision”. Investors relying on the KID will be able to claim for loss suffered through its use, unless the KID fully complies with the Regulation, including being “accurate, fair, clear and not misleading”. The proposal raises several, appropriately “key”, questions.

Concerning PRIIPs that are securities, the proposal envisages the Prospectus Directive (PD) regime continuing to apply separately, with merely “matching” key information obligations under the PD being disapplied where a KID is prepared. The proposal however seems effectively to render the entire PD prospectus redundant (and not merely its summaries) since: (a) the prospectus purpose (to contain “all information which [...] is necessary to enable investors to make an informed assessment”) is the same as that of the KID; and (b) the proposal explicitly states that retail investors do not need to read the prospectus.

It is unclear to what extent it is possible

to ensure that a two or three page KID contains *all* information relevant to an informed investment decision. In this respect, it is also unclear whether the KID will cover credit risk – information material to an investment decision in a securities context (where whatever payout is due under a PRIIP’s structure depends further on the issuer’s solvency to honour it) though not generally in the UCITS context (where the KID represents more of an investment mandate than a specific individual investment). Describing the issuer’s “credit” means describing the issuer’s business, which in today’s world is generally international and highly complex – so including this meaningfully in the KID would seem open to question and any partial attempt to do so could well be misleading (whilst unqualified reliance on credit ratings has been criticised following the financial crisis).

Though consumer behavioural research indicates that retail investors (a) may indeed not generally read long documents (such as prospectuses), it also indicates that retail investors (b) misunderstand short documents (a 30% misunderstanding rate being noted in the Commission’s KID [2009 testing report](#) for simple UCITS) and (c) act irrationally (a concern [reiterated](#) this year by the incoming head of the UK’s Financial Conduct Authority). So it does not seem evident that retail investment decisions will actually be better informed by the KID. Though the proposal acknowledges that disclosure rules (such those relating to KIDs) complement rules on sales (such as under MiFID), it states that PRIIPs legislation is to be developed

independently of legislation relating to distribution/advice (and that financial education and product regulation are to be equally out of scope).

The proposal envisages product “manufacturers” having responsibility for preparing and publishing the KID (in the accepted languages of the Member States where the PRIIP will be sold) and reviewing/updating it “regularly” (and also having liability for the KID’s content), whilst distributors would be responsible just for providing the KID to retail investors – *inter alia* so as to ensure the same KID is used for a particular PRIIP by all distributors. In this respect, it seems a manufacturer could be liable to retail investors where the manufacturer’s (public) KID is used by a third party distributor, long after the manufacturer has stopped offering the PRIIP (and so presumably ceased updating it as no further retail investor decisions require informing) and without the manufacturer’s consent (or even knowledge), to re-offer the manufacturer’s PRIIP securities (acquired in the secondary market) – potentially in EEA Member States that the manufacturer never targeted (and thus prepared appropriate KID translations for). Further, being a manufacturer document, the KID could presumably not include distributor-level (i.e. investor-facing) information such as distributor costs and individual investors’ tax treatment – but the proposal is open in this respect.

Other points of concern that may need clarification include, *inter alia*, the reverse burden of proof (particularly when combined with the above substantive liability questions), whether costs other



In brief

The Commission proposes a very short KID as the sole basis for retail investors to take informed investment decisions, which raises questions as to investor misunderstanding and potential liability for PRIIPs providers as well as potentially real economy businesses seeking to issue simple bonds. The continued relevance of the Prospectus Directive regime is also brought into question.

than those to be deducted from the investment return require disclosure, the definition of “manufacturer” and the Directive-like nature of many provisions that seem to be addressed to Member States themselves.

Though the proposal notes that PRIIPs are “essential for meeting the needs of EU citizens” (allowing risk spreading, other benefits not individually available to retail investors, more efficient participation investment markets, deeper capital markets and better diversification options), there are concerns that the KID, as proposed, may well reduce the supply and choice of investments available to EU citizens without better informing their investment decisions. The scope of the proposal is not strictly limited to PRIIPs, as extension to other, non-packaged, financial products is contemplated after four years – potentially including vanilla fixed and floating rate corporate bonds (which gives additional salience to current concerns).

The KID proposal seems to allow scope for investment misunderstanding, whilst it is crucial that retail investment decisions are actually well informed (merely assigning responsibility for

misunderstanding could promote systemic risk). This would be a pity, since a well-configured KID has the potential to empower retail investors in their engagement with savings and investment. An option worth exploring would be a KID that acts just as an overview of a product’s structure (a “taster”) that would help retail investors engage with the retail intermediaries assisting them (notably under MiFID’s suitability and appropriateness provisions – appropriately enforced). In this respect, such intermediaries would have accounted for the full product information (available in the relevant prospectus) as part of their “know your product” procedures. Self-directed retail investors, where permitted, would have to make the appropriate commitment to review the full prospectus. In either case, KID liability would be referenced to the prospectus as is currently the case in the new UCITS KID regime that came into full effect on 1 July.

ICMA continues to support the Joint Associations Committee on retail structured products (JAC) in engaging European authorities on the PRIIPs project.

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It is crucial that retail investment decisions are actually well informed.

French pre-sounding rules

In France, a 14 June Ministerial order was published on 11 July in the *French Official Journal*, amending, with effect from 11 October, Art. 216-1 of the *General Regulation (RG)* of the French regulator AMF regarding pre-soundings. The new and old versions of Art. 216-1 are included in the RG (and its non-binding English translation). The French financial markets association AMAFI published in parallel a *Code of Conduct* (together with a non-binding English translation), also applicable from 11 October and approved by the AMF as professional rules. AMAFI also published a commentary on the Code (and a non-binding English translation).

Under the new provisions, “sounding” requirements are triggered where investors are questioned in the context of preparing a transaction (though the Code only seems to apply where the querying is done at issuer/seller request). Specific requirements include: (a) keeping records (even where no inside or even seemingly any non-public information is communicated) *inter alia* of the basis for the “inside” (or not) qualification of information communicated and of the persons sounded; and (b) investor prior consent to being wall-crossed.

It is unclear to whether firms are subject to these requirements concerning pre-soundings where they are not directly regulated by the AMF. In any case, similar developments have been taking place at the European level (see separate article).

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Prospectus Directive review and PRIPs

On 25 February, as the latest step in the on-going review of the EU Prospectus Directive (PD) regime, ICMA submitted a response to ESMA's call for evidence on the European Commission's request for technical advice on possible delegated acts concerning the PD. The response focused on the form of, and interaction between, summaries, final terms and supplements, as well as on the consent to third party prospectus use and on specific suggestions for amendments to the PD Regulation. Regarding final terms in particular, ICMA is aware there has been regulatory concern regarding the type of information that has been included in some final terms over the past few years. Imposing both a strictly prescribed and limited form of final terms could however substantially hamper the flexible and speedy issuance of securities that underpins the base prospectus concept. ICMA has pointed instead to the base prospectus summary as the point of reference for the PD's "significant new factor" test in terms of establishing whether additional information should be included in a supplement to the base prospectus rather than in final terms. ICMA has been engaging in a round of bilateral meetings with national regulators on all these aspects.

ICMA is also considering any consequent changes to standard market practice and documentation flowing from the publication of the December 2010 amendments to the PD (discussed in the [First Quarter](#) edition of this Newsletter). In particular, ICMA will shortly be publishing revised standard form debt selling restrictions. A revision of the equity selling restrictions is being considered and may follow in due course.

Furthermore, on 1 February ICMA, via the Joint Associations Committee on retail structured products, submitted a detailed response to the European Commission's [Packaged Retail Investment Products \(PRIPs\) consultation](#), notably concerning the proposed key information document (KID) previously discussed in the [July 2009](#) edition of this Newsletter. ICMA has in particular been concerned that, in formulation of the PRIPs KID, proper account is given to its intended purpose. If it is anticipated that such a document be strictly limited to two pages (the maximum length the European Commission's [UCITS Disclosure Testing Research](#) seems to indicate that retail investors will read), then it cannot include all information necessary for an informed assessment (which is specified under the PD as the role of the full prospectus). Rather a KID should be a quick first point of comparison for investors before seeking more detailed information (in the case of the more sophisticated investors) or as a good introduction to the

PRIP and a means of arming themselves with questions to ask a financial advisor (for the least sophisticated investors) – as noted in the Commission's research. Any liability deriving from information in the KID should accordingly be qualified by reference to the full prospectus. Distinctly, it is fairly likely that the information presented in a KID might be customised to specific and differing types of investor and would include such things as distributor charges and investor specific tax aspects – all knowable only at distributor level (and this dynamic would be similarly applicable should a KID ever need to include updated information on a distributor's later re-offering of the PRIP). Consequently, responsibility for preparing KIDs should be left open for issuers and distributors to agree as necessary.

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ISMAG: issuer and agent letters of representation

Previous editions of this Newsletter ([January and April 2008](#), and [January and July 2009](#)) have reported on the "ISMAG" process – the International Securities Market Advisory Group established and led by the two International Central Securities Depositories (ICSDs), Euroclear Bank and Clearstream Banking. ICMA is an observer at meetings of the group, rather than an actual member of the group itself.

The reports covered the ICSDs' related Market Practice Book (MPB) first published in 2008 with 48 pages and then subsequently revised, with the 176 page February 2011 version being available as of 31 March on both the [Clearstream ISMAG webpage](#) and the [Euroclear ISMAG webpage](#). The MPB is stated to describe what the ICSDs consider to be "best practices" for operational processes in new issues, corporate actions and income payments for international securities primarily issued through, and deposited with, the ICSDs. ICMA has advised the ICSDs that some other market constituencies may have differing views as to what constitutes good, let alone best, practice in these areas. In particular, issuers may feel that all information they have carefully prepared for delivery to their investors should simply be delivered to the end investors in its original form (and not subject to being summarised, truncated or otherwise interpreted along the way). Specifically concerning the extent of lead manager responsibilities (including their advisers), ICMA issued [Guidance Note 8](#) in the [IPMA Handbook](#) (being rebranded the [ICMA Primary Market Handbook](#)).

Prospectus and Transparency Directive amendments and PRIIPS consultation

On 11 December 2010, Directive 2010/73/EU was published in the *Official Journal* of the EU. It amends the Prospectus Directive (PD) and the related Transparency Directive (TD).

The amending Directive entered into force on 31 December 2010 (the 20th day following its publication), with EU Member States required to transpose its provisions into national law by 1 July 2012. ICMA anticipates that some Member States may seek to transpose the amending provisions in stages and/or well ahead of the July 2012 deadline. ICMA is seeking to monitor developments in the main financial jurisdictions in this respect and is also working on revising the model EU selling restrictions set out in its *IPMA Handbook* (to be re-branded as the "ICMA Primary Market Handbook").

The main changes are substantially unchanged from those described in the Third Quarter edition of this Newsletter (at page 19) and include an increase in the €50,000 thresholds to €100,000. (See the next article below on these aspects). A specific consequence of *Official Journal* publication is that €50,000 denominated bonds issued from 31 December 2010 are subject to the TD's full transparency regime rather than, as previously, its lighter "institutional" transparency regime (for new issues henceforth limited to bonds satisfying the €100,000 thresholds).

Whilst it is the national law of the "home" Member State for any particular transaction (ie where its prospectus will be approved) that will be most relevant, the laws of other Member States may also be relevant (notably in relation to public offer prospectus exemptions). Issuers may find it easier to work on an assumption of immediate pan EU transposition of some of the amending provisions rather than attempting continuously to monitor a likely EU transposition patchwork. Another consideration for issuers in this respect will be the ability to effect subsequent issues of fungible bonds without impacting the applicable regime under the PD.

Distinctly, on 15 December 2010, Directive 2010/78/EU was also published in the *Official Journal*. It makes some further amendments (in Articles 5 and 7 respectively) to the PD and TD in the context of the transformation of the Committee of European Securities Regulators (CESR) into the European Securities and Markets Authority (ESMA) from 1 January

2011. Transposition of the relevant provisions into national law was therefore required by 31 December 2010.

Following from the above Level 1 changes, the EU authorities' next objective is a review at Level 2 of the PD's 2004 implementing Regulation. ICMA will continue to liaise with both EU and national authorities in this respect, in particular in relation to further detailing of the forms of summary and final terms.

On 26 November, the European Commission published a consultation on its Packaged Retail Investment Products (PRIIPS) initiative (notably on the concept of a key investor information document – KIID). ICMA will likely be responding through its membership of the Joint Associations Committee on retail structured products. A general concern for ICMA is that solutions designed for the UCITS context are first transposed into the retail structured securities markets (which have their own distinct dynamics) and subsequently into the vanilla markets (which also have their own distinct dynamics) – potentially with insufficient consideration of these distinct dynamics in each case.

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Increase in the PD's €50,000 thresholds to €100,000

The PD amendments discussed in the previous article include an increase in the PD's €50,000 thresholds to €100,000 for the following reason set out in Recital 9: "The threshold of EUR 50 000 [...] no longer reflects the distinction between retail investors and professional investors in terms of investor capacity, since it appears that even retail investors have recently made investments of more than EUR 50 000 in a single transaction. For that reason it is appropriate to increase the said threshold and amend other provisions in which that threshold is mentioned accordingly."

One of the main priorities behind the creation of the PD is consumer protection. In the PD, EU authorities enacted (following intricate political negotiations) a pan EU retail regime which includes substantial retail protections that act as disincentives (together with the intrinsic multiplicity of retail tickets and challenging national consumer protection legislation) for many issuers, who do not see a countervailing pricing, liquidity or other advantage in targeting retail

Prospectus Directive review

The European Commission's proposal to amend the Prospectus Directive (covered in the October edition of the ICMA Newsletter) has been subject to initial discussion amongst Member State delegations within the European Council. Though no agreed common position for Council amendment of the proposal has been published so far, a Swedish Presidency compromise text (the latest of several) was published on 11 December. An accompanying formal memorandum from the Council's secretariat (together with a 16 December addendum on the need to account for changes consequential to the recently ratified Lisbon Treaty) notes a "broad measure of agreement" and requests that this latest (and "final") Presidency compromise text serve as the basis for negotiating an agreed position with the European Parliament.

The European Parliament's ECON Committee has appointed Dr Wolf Klinz MEP as *rappporteur* to prepare an initial report on the Commission's proposal. The report is anticipated to be presented to the ECON Committee in late January, with Parliamentary deliberation expected to continue into late April. In addition to the European Parliament, opinions are due from the ECB and the European Economic and Social Committee.

Following discussions with its members, ICMA has been working to raise awareness of concerns regarding many of the amendments to the Prospectus Directive that have been proposed. The most salient of these concerns relate to:

- requiring the summary to include "key information" on a comparable basis and with standalone liability (ie regardless of the rest of the prospectus);
- increasing the €50,000 thresholds to €100,000;
- requiring that issuer consent for third parties to use its prospectus be explicitly stated in the prospectus itself;
- further limiting the scope of final terms – notably through setting out an indicative list of items within scope;
- extending prospectus validity beyond 12 months; and granting excessive powers to the Commission to subsequently amend the Prospectus Directive.

ICMA has also expressed concerns regarding:

- ensuring that appropriate consequential amendments are made to the Transparency Directive, notably as to grandfathering; and

- exempting issues that are already admitted to trading (and subject to the Transparency and Market Abuse Directives) from the obligation to publish a prospectus.

Over the past few months ICMA representatives have met representatives of the European Commission, representatives of several Member State delegations to the European Council and several MEPs and their representatives. ICMA intends to continue such meetings as the review develops.

Pending any amendments to the Prospectus Directive regime taking effect, ICMA is further considering the complexities surrounding offers of low denomination (sub-€50,000) bonds in Prospectus Directive exempt circumstances (including the possibility of publishing some relevant considerations in this respect).

Separately, ICMA continues to participate in the Commission's *Packaged Retail Investment Products (PRIIPS) initiative* through the Joint Association Committee, which made a submission to the Commission following participation in a Commission workshop on 22 October.

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US Tax Extenders Act of 2009¹

Proposals were introduced into the US Congress in late October as the Foreign Account Tax Compliance Act of 2009 (FATCA) broadly to: (i) repeal the TEFRA exemptions relating to bonds in bearer rather than registered form (with substantial resulting fiscal sanctions, namely a 1% per annum excise tax, a 30% withholding tax and non-deductibility of interest for corporation tax); and (ii) require intermediaries effecting US source payments to enter into more substantial reporting agreements with the US Internal Revenue Service (backed by a 30% withholding tax sanction). The proposals also included some worrying ambiguities as to grandfathering in the latter case.

Following substantial industry input, including initial and follow-up submissions by ICMA, the proposals were re-introduced in amended form as part of the Tax Extenders Act of 2009 (TEA), adopted by the House of Representatives on 9 December and referred to the Senate. The Senate's diary is substantially taken up with other matters (healthcare notably), but it is anticipated the Senate will do its utmost to

¹ Previously the "Foreign Account Tax Compliance Act of 2009".

Retail structured products

There have been several recent developments concerning retail structured products, including at EU level a CESR [consultation](#) on MiFID complex and non-complex financial instruments for the purposes of the MiFID appropriateness requirements and a Commission [Communication](#) on *Packaged retail investment products* (PRIIPs). The PRIIPs Communication, *inter alia*, suggests a new “horizontal” legislative regime for retail products cutting across existing “vertical” legislation (including the Prospectus Directive) and potentially involving extension of the UCITS “key investor information/document” (KII/KID) concept to the debt securities space.

It will be interesting to see the Commission’s detailed proposals in due course – not least in relation to: (i) defining the “retail” characteristic of the new regime so that it does not disproportionately impose burdensome retail protection standards on the non-retail markets; (ii) addressing the tension between prescribing complex product disclosures to be “short and simple” whilst containing “all key information” (all in a context of differing national issuer liability regimes); and (iii) clearly and logically delineating the division of responsibilities between “manufacturer” issuers and distributors.

In this last respect, ICMA participated in the 2007 publication of [principles](#) for managing the provider-distributor relationship in the context of retail structured products. ICMA is planning to continue to follow these and other initiatives through the Joint Associations Committee, which also includes the London Investment Banking Association (LIBA), the International Swaps and Derivatives Association (ISDA) and the Securities Industry and Financial Markets Association (SIFMA) and its European Securitisation Forum (ESF).

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Asset servicing

~~An updated version of the *Market practice book* (MPB) previously covered in an article on page 15 of the [January 2009 edition](#) of this Newsletter concerning the work of the International Securities Market Advisory Group (ISMAG) has been published by the two International Central Securities Depositories (ICSDs), Euroclear and Clearstream. New material in the updated version includes *inter alia* (in Annexes 5 and 6) five template checklists intended to help ensure inclusion of relevant information when asking the ICSDs to accept issuance programmes and stand alone issues and when notifying them of rate fixings, partial redemptions and final redemptions. Excel versions of the five templates have been made available for convenience on Euroclear’s [ISMAG webpage](#) (under the “New Issues Working Group” and “Income Working Group” headings respectively), which also hosts a [naming convention](#) for final documentation e-mail attachments.~~

~~Separately, the International Capital Market Services Association (ICMSA) has published a [recommendation on payment days](#), the salient features of which are that (i) the number of included jurisdictions be minimised and (ii) the jurisdiction of the agent’s location need not be included. The recommendation is intended to apply to “open” days on which payments are to be made, rather than days contractually relating to other events (such as rate determinations).~~

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The prospects for the primary markets with Peter Eisenhardt, Principal and European Head of Origination, Bank of America Merrill Lynch and Chairman, ICMA’s Euro Commercial Paper Committee; Bertrand de Mazières, Director General Finance, European Investment Bank and Chairman, AMTE Council; Kate Craven, Director, Legal Department, Barclays Capital and Chair, ICMA’s Legal and Documentation Committee; Lachlan Burn, Partner, Linklaters LLP; Martin Egan, Global Head of Primary Markets and Securitisation, BNP Paribas and Chairman, ICMA’s Primary Market Practices Committee.