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Mr S Cubley  
HM Treasury  
Capital Markets & Governance Team  
4/22 1 Horse Guards Road  
London  
SW1A 2HQ

Your ref: 2003/71/EC

Our ref: C/lb

24 January 2005

Dear Mr Cubley

**PKF's Response to Consultation Document  
UK Implementation of the Prospectus Directive 2003/71/EC**

We have pleasure in enclosing our response to HM Treasury's Consultation Document on the UK Implementation of the Prospectus Directive.

If you wish to discuss any aspect of this, please do not hesitate to contact me.

Kind regards.

Yours sincerely



*per pro*

**Clive Brook  
Partner**

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**PKF's Response to Consultation Document**

**UK Implementation of the Prospectus  
Directive 2003/71/EC**

**January 2005**

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# **1 Introduction**

- 1.1 We set out below our responses to the specific consultation points raised in the Consultation Paper issued jointly by HM Treasury and the FSA in October 2004 under the heading "UK Implementation of the Prospectus Directive 2003/71/EC".

## 2 The Prospectus Directive

### Question 1

- 2.1 As mentioned in the document, it is clear that the definition of what constitutes an “offer to the public” is very broadly defined and, in our opinion, too broad. We note, in particular, that it makes reference to an investor deciding to “purchase or subscribe” securities. In other words, it would appear to have the possibility of covering all trades once a company is listed on a regulated market where that trade was in any way influenced by any information received by the investor. An extreme interpretation of this definition would therefore include the annual accounts and any other announcements made by the company or its advisors.
- 2.2 Clearly therefore, there is a need to provide clarity as to what communications fall outside the scope of this definition and, in our opinion, regular announcements including the publication of the financial results, should be a specific exclusion.

### Question 2

- 2.3 This question is partly dealt with in our response to Question 1. However, since we understand that the London Stock Exchange is to amend the AIM Rules to provide rules which will effectively replace the POS Regulations 1995, we believe that the definition needs not only to specify the markets to which it will apply, as set out in 4.11 of the Consultation Document, but also, as a means of easy reference, to set out other forms of offerings of public securities and the relevant regulations that will apply to those (eg. AIM Rules, OFEX Rules, etc.). If the offer is not governed by any of these particular rules, then there should be a requirement to state that fact, in our opinion.

### Question 3

- 2.4 We would envisage that the proposed revised AIM Rules will proscribe the information required for all AIM fund raisings and, as such, will cover those which fall below the €2.5 million lower threshold. Clearly, AIM accepts that for issues over €2.5 million, UKLA approval of the Prospectus will be required if none of the other exemptions are met.
- 2.5 Investor protection is important and accordingly, we would expect there to be appropriate regulations governing the issue of any document intending to raise money for companies below the €2.5 million threshold. It may be that this can be incorporated within the existing FSMA “Financial Promotions” legislation.

2.6 In answer to the specific question, we believe that there is a significant benefit to be obtained in terms of cost and time savings for fund raising at below €2.5 million, not to require UKLA approval.

#### Question 4

2.7 As mentioned in our reply under Question 3, the need for some investor protection, preferably with a light touch, but backed up with strong implementation powers, would best suit the market below the €2.5 million fund raising level.

#### Question 5

2.8 This question is particularly fraught. Nowhere is the phrase "where the offer of securities is addressed ....." defined. For the purposes of this answer, we have assumed that the issuer or his financial advisor will have to ensure that there are less than 100 numbered copies of the document in circulation at any one time, and that once a particular investor has subscribed for those shares, then that document cannot be passed on by that investor to another potential investor who then may invest, using the same document. In our view, this is unworkable. For example, a father in a family might decide to invest and pass the document to his children (assuming they are over the age of 18) and all or any of those people might choose to invest using the same document.

2.9 Another example would be where a document is circulated amongst a group of investors in an "investor club". Any attempt to provide rules preventing these types of natural actions would seem to us to become over-burdensome and we question the logic of having this limit at all. Either the document is a Prospectus which is being issued to third parties (ie. those unconnected with the company at present, who are not qualified investors – see our comments under Question 7) or not.

2.10 The problem is exacerbated by transactions "on market" after the initial fund raising has been successfully concluded. If a potential purchaser of shares within 12 months ending after the date on which the offer is first made, happens to see a copy of the Prospectus, then he or she would appear to be included within the definition of the 100 persons. As the issue of the original Prospectus has no control over later transactions, we believe this area of the proposed rules should be re-drafted.

#### Question 6

2.11 Yes.

**Question 7**

2.12 Our concern is the proposed exemption from the 100 persons rule for qualified investors. The Consultation Document does not seem to allow for the possibility of a document being sent to up to 100 natural or legal persons and also to an unspecified further number of qualified investors. We believe this is a pity since in a larger number of IPOs, this is precisely the situation that will arise, with some of the shares being offered to "retail" investors, with the balance of the money being raised from institutional investors. Our comments on the definition of what constitutes a qualified investor will follow later in this response.

**Question 8**

2.13 We agree that the Prospectus should also be available on an Issuer's website. However, we would prefer to see a continuation of the current arrangement where the Prospectus also has to be filed at Companies House. However, if it is available to everyone, how is the 100 persons restriction to be implemented?

**Question 9**

2.14 Yes.

### **3 FSA Implementation of the Prospectus Directive**

#### **Question 1**

- 3.1 The requirement for a summary should, in practice, largely depend upon the complexity of the Prospectus. In the case of a large number of small fund raising Prospectuses, and indeed Admission Documents, the "front section", normally marked Part I of the Prospectus, is in effect a useful summary. Consequently, for small issues, we are not convinced that there needs to be, in effect, a "summary of summaries". Clearly, in large complex issues (eg. the recent British Energy Prospectus), a summary is essential as the ability and willingness of investors, especially retail investors, to read a 700 page document (the length of the British Energy Prospectus) has to be questioned. We accept, however, that it is difficult to have anything other than a "one rule governs all" legislative framework.

#### **Question 2**

- 3.2 This has already been covered under Question 8 of the proposed Implementation Approach section of our response.

#### **Question 3**

- 3.3 We agree with the proposed approach on advertisements.

#### **Question 4**

- 3.4 One of the key concerns, especially for smaller listed companies, is the often low level of liquidity of trading of their stocks. The proposal that only new issues of shares should require documents to be translated into English is, we think, unlikely to assist the liquidity of other EU country stocks where the requirement for an English speaking investor to understand the company before committing his / her money is obvious. Bearing in mind that most if not all US investors and many other investors around the world speak English, we believe it would be in the interest of those companies from other EU states who wish to issue a Prospectus to ensure that an English version is available. Whether this should be incorporated into the Rules, or left to the discretion of those other companies, is a matter on which we do not have an opinion.

3.5 In one recent instance in which we are involved, the use of Welsh in a Prospectus was being discussed. It would appear that the Welsh language version probably would have no legal standing and that the FSA would only approve an English language version. Without wishing to cause upset to our Welsh colleagues, we believe this is the right approach in view of the relatively small number of Welsh speaking individuals in the UK.

**Question 5**

3.6 We see little alternative to the approach that the FSA is proposing to adopt in view of the large diversity of the original sources of the Prospectuses which will be coming forward for approval.

**Question 6**

3.7 If there are reciprocal arrangements being made by the approving authorities in each EU state, then it would seem to us imperative that all EU companies issue Prospectuses to comply with all EU states' individual requirements. This would be true for any company which believes it would benefit from a wide ownership of shares across the EU. This approach might prove a considerable disincentive if there are significant differences between the EU countries. Perhaps some discretion should be allowed where the differences are only relatively minor.

**Question 7**

3.8 We understand that the requirement for an annual information update is not negotiable, although we believe it will cause considerable additional work for very little, if any, additional benefit. Nevertheless, if one has to be produced, then our belief is that it should very definitely only be a list of the information made available by the company in order to minimise the cost implications to the company. As this information is readily available via various news services, we see no reason why companies should be obliged to do anything further unless they wish to do so voluntarily. This might apply when there is one particularly significant piece of information, or where they need to make investors aware of a subsequent change in circumstance after the announcement of a particular piece of information.

**Question 8**

3.9 See our answer to Question 7.

## Question 9

3.10 We have considerable reservations over the regime for qualified investors which is proposed. We submitted our comments on the HM Treasury Consultation on the financial promotion order and are aware that the Treasury's response has now been made public, although we have yet to review this. As mentioned in our response to the HM Treasury Consultation, we do not believe the prospective qualified investors should be certified by their solicitors or accountants as to their net worth. However, the specific criteria set out in paragraph 2.20 of the Consultation document concerning the criteria for membership of the qualified investors register are different and we agree are likely to be more verifiable. However, these do not protect against investors of a poor or fraudulent financial status becoming members of the register. Our comments on the specific tests contained in paragraph 2.20 are as follows :-

- The transaction test of ten per quarter over the previous four quarters will eliminate, in our view, the vast majority of potential investors who tend to hold their investments for medium or long-term (and indeed, the Government is seeking to encourage Business Angel type investors investing in SMEs or small listed companies) and therefore the possible requirement to "trade" some of their holdings just to meet the ten transactions per quarter test seems to be not achieving the Government's objective. However, it is accepted that it would improve the liquidity of shares in the aftermarket. Nevertheless, we believe this test should be reviewed or scrapped.
- The size of the investor's securities portfolio exceeding €0.5 million is a very much more sensible test, although it excludes information concerning any borrowings which are secured against that portfolio. Our belief is that the investor should self-certify whether or not he has borrowed any money secured against this portfolio. This is particularly important where the practice of "day trading" on bank overdraft has developed, which often leaves individual investors very financially exposed.
- The investor working for at least a year in a professional position within the financial sector which requires knowledge of securities investment will need to be much more clearly defined. Securities investments cover a very wide range of potential products and knowledge of one does not necessarily procure adequate knowledge of the others in order for them to be considered as not needing some of the protections required by the issuance of a Prospectus which has been approved by the UKLA.

**Question 10**

3.11 Our preference would be for option A which would allow the issue of securities (and presumably their advisors) access to the register at all times. This would be particularly of use when considering a "off market" placing of shares as will frequently happen with smaller companies once the "lock out" periods have elapsed. Whilst this placing market is traditionally dominated by institutions, it would be helpful to be able to spread the net wider to bring in legal persons in order to ensure a better balance and spread of the shareholding base for the company.

**4 Summary**

- 4.1 We trust that these comments are clear, but would be happy to provide any clarification required. In the initial instance, please contact Clive Brook on 0161 832 5481, or [clive.brook@uk.pkf.com](mailto:clive.brook@uk.pkf.com).
- 4.2 We thank you for giving us the opportunity of commenting on these proposals.