

ESMA Consultation Paper
**ESMA's technical advice on possible delegated
acts concerning the Prospectus Directive as
amended by the Directive 2010/73/EU**
Comments by AMAFI

Association française des marchés financiers (AMAFI) has more than 120 members representing over 10,000 professionals who operate in the cash and derivatives markets for equities, fixed-income products and commodities. Nearly one-third of the members are subsidiaries or branches of non-French institutions.

AMAFI welcomes the opportunity to comment on the Consultation paper on “ESMA’s technical advice on possible delegated acts concerning the Prospectus Directive as amended by the Directive 2010/73/EU”. However its responses hereafter will be limited to Questions 5 to 7 in respect of which it has received significant comments from its members.

ESMA questions

II.2 Prospectus disclosure requirements for convertible or exchangeable debt securities (Articles 5 to 7) – Current legal framework and ESMA’s considerations

Q5: Do you agree with ESMA’s interpretation of the current legal framework concerning prospectus disclosure requirements for convertible or exchangeable debt securities? If yes, please feel free to provide additional arguments. If not, please explain and justify your interpretation.

AMAFI’s interpretation of the Commission Regulation (EC) n° 809/2004 of 29 April 2004 (Prospectus Regulation) is that Annex III thereof relates to shares – and only to shares. Therefore it does not apply to convertible or exchangeable debt securities which, from a legal standpoint, retain the nature of bonds.

This interpretation is supported by ESMA’s finding that only a few competent authorities require the application of Annex III to such instruments.

This results logically from the fact that bonds and shares have a different legal nature which implies significant differences in terms of benefits/risks for the holder of one or the other type of instrument. It should be recalled in that respect that the holder of a convertible or exchangeable bond is free to exercise or not the option to convert / exchange its bond into shares and if it chooses not to do so, it retains a right of redemption in cash at maturity.

Therefore, AMAFI considers that ESMA’s proposal is not supported by the terms of the Prospectus Regulation.

In addition, AMAFI believes that, for the reasons set out below (see Q6), ESMA's proposal would serve no useful purpose and furthermore would create significant additional costs and constraints for the issuers with no corresponding benefits for the investors. Worse, it could lead to behaviors which would be particularly counterproductive.

Q6: Do you agree with ESMA's proposal of limiting the application of items 3.1 and 3.2 of Annex III to debt securities convertible or exchangeable into shares which are or will be issued by the issuer of the security or by an entity belonging to its group which can be converted or exchanged within 12 months since the date of their issuance? If not, please provide the reasoning behind your position.

AMAFI strongly disagrees with ESMA's proposal to require the application of item 3.1. and 3.2 of Annex III to convertible / exchangeable bonds when the conversion / exchange can occur within 12 months of the date of their issuance.

In practice, the maturity of convertible / exchangeable bonds is generally 3 to 7 years. Even if they can be converted / exchanged from the issue date, the bondholders have no interest in exercising their conversion / exchange right before the redemption date (at maturity or earlier, in the case of early redemption, which, however, does not happen – save in very exceptional circumstances – during the first year). Indeed, the market value of such an optional instrument is higher than the market value of the share, which means that until the redemption date, the bondholder would get a higher price in selling the convertible / exchangeable bond than in converting / exchanging it. This is why even if the conversion / exchange is legally possible during the first year, in practice (save in very exceptional circumstances) it never occurs during that period.

Therefore, requesting a working capital statement in respect of the 12 months following the issuance of the convertible / exchangeable bond is of no interest to the subscribers (which explains why it is not required in the Annexes to the Prospectus Regulation relating to debt securities). Furthermore, it could lead to behaviors aiming at circumventing the rules. Indeed, in order to avoid the heavy and unnecessary costs generated by such request (see Q7 below) some issuers could be tempted to issue convertible / exchangeable bonds which are convertible / exchangeable only after one year. As this type of provision would not conform to the international practice, it could raise suspicion among the potential investors as to the reasons behind it, which could in turn have a detrimental effect on the pricing of the issuance.

To circumvent this rule, it is also likely that issuers could be tempted to list their equity-linked securities on a market which is not a "regulated market" (such as Euro MTF in Luxemburg or the Open Market of the Frankfurt Stock Exchange in Germany). In that case, no prospectus would be required for the issuance of the convertible / exchangeable bond and upon conversion of such bond, the shares could be admitted on the regulated market without a prospectus on the basis of the exemption provided in Article 4.2 (g) of the Prospectus Directive. This would definitely be very counterproductive, if the aim of the proposal is to better protect the investor.

As to the request for an indebtedness and capitalization table, it is not any more useful for the subscriber, given that, for the reasons mentioned above, it is highly unlikely that it will become a shareholder before at least two years, and often longer. By the time, the bondholder starts having an interest in requesting the conversion, it will have access to publicly available financial information relating to the past years which will be far more relevant to help him decide whether or not it should request the conversion / exchange.

For all these reasons, AMAFI thinks that ESMA's proposal is inappropriate. Not only it serves no useful purpose but it would in addition be very costly for the issuers without any corresponding benefit (see Q7 below).

Furthermore, the drawing up of the capitalization table raises another issue relating to the timetable of the process and consequently of the issuance of those equity-linked products. Given that the drawing up of such a document involves a heavy process, a number of issuers are not able to prepare it at a date other than the date of the annual or half year financial statements. On the other hand, it is required that the capitalization table bear a date which is less than 90 days prior to the date of approval of the prospectus.

The consequence of these two constraints is that the "window" for an issuer to issue convertible / exchangeable bonds will be very reduced whereas the equity-linked market (just like the straight bond market) is such that companies must be able to seize any opportunity to launch a placement. This situation is also likely to lead issuers to avoid the listing of their convertible / exchangeable bonds on regulated markets and prefer instead the listing of such instruments on other recognized but less regulated markets. This again would be counterproductive if the aim of the proposal is to better protect the investor.

Q7: According to your experience, what are the costs for drawing up the working capital statement and updating information on capitalization and indebtedness, as required by items 3.1 and 3.2 of Annex III? Can you provide any data?

The drawing up of these documents is very costly for the issuer both in terms of internal costs - for the preparation of the documents which require a heavy internal process - and external costs, as such documents must be verified by the company's auditors. These costs can amount to several tens of thousands of Euros.



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