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Directorate-General for Financial Stability, Financial Services and Capital Markets Union
European Commission
1049 Bruxelles/Brussel
Belgium

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Dear Sirs,

Fostering and promoting the use of SME growth markets - Level 1

We welcome the opportunity to respond to the European Commission's consultation on its proposals to amend aspects of the Market Abuse and Prospectus Regulations, in order to foster and promote the use of SME growth markets.

We welcome the European Commission's stated objective of building a more proportionate regulatory approach to facilitate SME listings. Small and mid-size quoted companies play a vital role in driving economic growth. It is therefore essential that any legislative initiatives prioritise the needs of smaller companies ahead of their larger counterparts.

Overall, we believe that the proposed amendments go some way to reducing the administrative burden and the high compliance costs faced by SME growth market issuers.

Nonetheless, we still encourage the European Commission to consider enhancing the alleviations available to SME growth market issuers with regards to notifying the delayed disclosure of inside information and insider lists further.

The Quoted Companies Alliance *Legal* and *Primary Markets Expert Groups* have examined your proposals and advised on this response. The lists of Expert Group members are at Appendix A. We have responded to the specific proposed amendments from the point of view of our members, small and mid-size quoted companies.

If you would like to discuss our response in more detail, we would be happy to attend a meeting.

Yours faithfully,

Tim Ward
Chief Executive

I. Amendments to the Market Abuse Regulation

(a) Exemption from the market sounding regime for private placements of bonds with qualified investors

We believe that the proposal to exempt private placements from certain aspects of the market sounding regime should not be limited to private placements of bonds. The market sounding regime is also causing significant uncertainty for equity fundraising.

The attempt to reconcile the need for certainty in equity fundraising with the requirement not to deal while in possession of inside information has given birth to a new process, the so called "Accelerated Book Build".

In our experience, companies raising equity finance will make a market announcement setting out details of the proposed transaction at, say, 7am, on the morning on which the proposed transaction is expected to take place. This announcement is often referred to as a "cleansing announcement" as it will contain all the relevant inside information related to the proposed transaction which has been discussed with proposed institutional investors in the course of the prior market sounding exercise.

The cleansing announcement is then followed with a further announcement, very often within half an hour of the original cleansing announcement – and generally before the markets open on the same morning – that an "accelerated bookbuild has been successfully conducted" and that the fundraising is now complete (usually subject only to Admission of the new shares to trading on the relevant SME Growth Market).

In theory, institutional investors, to whom presentations have been made during the market sounding exercise, are not supposed to have made the decision to invest until after the information on which their decision is based is in the public domain. However in reality, a few phone calls are made confirming with those investors that they still want to proceed with their investment. The decision to invest is clearly made well before the cleansing announcement is issued.

The difficulty is that this arrangement leaves small and mid-size quoted companies with a fundamental uncertainty as to whether their fundraising is in place and that everyone on the placing list will, in fact, confirm their participation. At this stage in a proposed transaction, quoted SMEs will have spent a lot of money on, among other things, legal and accountancy fees, public relations advisers, corporate finance advisers and brokers. Yet they must bear a degree of risk that those who have said that they will invest will in fact do so.

Prior to the Market Abuse Regulation, market practice was to ensure that all investors participating in an equity placing were committed to their investment in a legally binding manner so that the SME had the comfort of knowing that the funding was in place when the market announcement was made.

We do not believe that prior market practice was inherently wrong and would welcome a discussion around whether an additional alleviation could be provided for SME growth market issues where (i) the only inside information (which would otherwise be contained in a "cleansing announcement") relates to the placing and (ii) MAR compliant wall-crossing procedures have been adhered to in communications with potential places.

(b) Liquidity Provision Contract for SME Growth Market Issuers

We are content with SME growth market issuers being given the possibility of entering into a liquidity provision contract on the condition that it is left for each individual SME growth market operator to decide whether they should be applied to its venue.

That said, if the European Commission wishes to cultivate liquidity provision contracts, it is important that any existing and new EU legislation promotes market making activities, especially in trading securities for small and mid-size quoted companies.

The Central Securities Depositories Regulation (CSDR) contains provisions, in an attempt to minimise risk in settlement, which increase the nominal minimum liquidity required to access equity capital markets. This will constrain the ability of small and mid-size quoted companies to raise the necessary capital to fund their growth. These companies tend to be issuers of low liquidity instruments and, as such, rely on their liquidity providers' support to maintain constant pricing to allow valuation.

CSDR's new settlement discipline regime will mean that trades not settled at an agreed time will face daily fines until the trade is settled. These fines will pass along the chain of settlement so that only the initial failing part of the settlement chain will pay up. For SME growth markets this will include the circumstances where fines are expected.

Logically, this will always be the liquidity provider, as they are the only type of participant permitted to naked short sell under the Short Selling Regulation. Liquidity providers are thus fined for providing liquidity in periods where demand outstrips supply. In other words: fining them for performing the specific purpose for which they exist.

Penalising formal liquidity providers for not settling trades on time will lead to those very liquidity providers reducing their activities in smaller company securities, in order to avoid these additional costs. This will lead to a further reduction in companies' liquidity, therefore reducing their access to funding on public markets.

CSDR will therefore increase market volatility by creating an environment rife for abuse. Should a trade fail to settle by a certain extended date, the trade will be arbitrarily cancelled and the difference between the original price and the current price paid to the purchaser. This creates an opportunity to ramp up the market in less liquid securities via an abusive short squeeze.

For example, if a dishonest investor tries to buy shares in a security that is tightly held by the entrepreneur that created the business, they might enter into a trade to buy shares and either expect or recognise that the trade has not or will not settle.

The dishonest investor can then buy more shares or at least express an interest in doing so. This demand pressure on liquidity providers will force them to increase prices to try and locate sellers so that they can cover their short positions to prevent large losses. The continued pressure combined with a lack of settlement means prices will increase, resulting in huge profits to the dishonest abuser, and huge losses to the market maker.

It also denies investors the opportunity to own the security they have purchased, as this is driven by the inherent lack of liquidity in the instrument rather than any deliberate act or omission by the liquidity provider.

This leads to liquidity provision and market making becoming uneconomical. As smaller liquidity providers will be unable to continue to profitably trade**,** they will withdraw their liquidity from a security / securities, which will reduce liquidity in the market for small and mid-size quoted companies. This will in turn concentrate activity on a few significant providers, which is damaging for price formation and contradicts the desire to create a healthy environment for less liquid securities.

Ultimately, this can lead to all liquidity providers withdrawing, which will lead to little or no liquidity being available for SME stocks, as there is no two-way price. Holdings cannot be valued or, worse, have no value. The European Commission should therefore remove all fines for failing to settle trades on time from securities of small and mid-size quoted companies irrespective of trading venue.

Furthermore, introducing common securities settlement standards across the EU will harm the ability of small and mid-size quoted companies to raise capital on public markets. Different SME-dedicated markets will have different levels of liquidity depending on investor interest and trading volumes and there should therefore be flexibility for different markets to set their own appropriate securities settlement standards.

(c) Justification of the delay in disclosing inside information

Although we appreciate the European Commission's intention with this proposed amendment, we question whether this would in fact achieve the desired outcome of reducing the administrative burden for small and mid-size quoted companies.

If these companies are still required to notify delayed disclosure of inside information and could also be required to provide justification by their national competent authority, they would still, ultimately, need to retain some sort of internal record in any case. Any supposed benefit of this amendment would therefore be nominal.

In our experience, National Competent Authorities (NCAS) will question regulatory news announcements regardless of whether they contain information which has been delayed, where the NCA considers there to have been a potential impact on market integrity. Companies have to contend with the issues which arise in a market integrity enquiry. The key issue is whether market integrity has been impugned; the emphasis on delay is only one factor in this analysis. We would submit that the requirement for SMEs to notify delays is placing undue emphasis on only one aspect of market abuse and is unduly burdensome for quoted SMEs with limited resources.

(d) Insider lists for SME Growth Markets

Overall, we consider the decision to replace the current alleviation provided by the Regulation to SME growth market issuers with a 'list of permanent insiders' to be a positive development.

Nonetheless, we would still encourage the European Commission to exempt SME growth market issuers from the requirement of creating and maintaining insider lists altogether, in order to take into account their limited resources. In practice SMEs can identify those involved with them who have access to inside information with relative ease, due to their generally small size. The fact that NCAs rarely rely on insider lists emphasises the lack of proportionality between the regulatory burden on SMEs and the benefit to regulators.

(e) Managers' transactions by SME Growth Market Issuers

We fully welcome the amendment that will give SME growth market issuers two extra days to disclose the transactions of a Persons Discharging Managerial Responsibilities (PMDRs) and Persons Closely Associated (PCAs) after receiving the notification themselves from the relevant PMDR or PCA.

We believe it strikes an appropriate balance between the ability of smaller companies, which have limited resources and may require sufficient lead-in time to make accurate and timely disclosures to the market in accordance with the Regulation, to provide accurate and timely information, with the practical need for the market to be notified promptly in the interests of transparency.

II. Amendment to the Prospectus Regulation

(a) Transfer Prospectus

We welcome the amendment which would create an alleviated 'transfer prospectus' for companies listed for at least three years on an SME growth market seeking admission of their securities to trading on a regulated market, or both an admission and a new offer of securities on a regulated market.

By ensuring that small and mid-size quoted companies seeking to transition from an SME growth market to a regulated market are not required to produce a full prospectus, this proportionate approach will play a key role in easing the process of transition from an SME growth market to a regulated market by removing unnecessary costs which could deter issuers from making such a transition and therefore deny them the ability to access the capital required to facilitate their continued growth which might be available on a regulated market.

APPENDIX A

Quoted Companies Alliance Legal Expert Group

Mark Taylor (Chair)	**Dorsey & Whitney**
Maegen Morrison (Co-Deputy Chair)	Hogan Lovells International LLP
Stephen Hamilton (Co-Deputy Chair)	Mills & Reeve LLP
Murdoch Currie	Bates Wells & Braithwaite LLP
Martin Kay	Blake Morgan
Paul Arathoon David Hicks	Charles Russell Speechlys LLP
Gary Thorpe Andrew Chadwick	Clyde & Co LLP
Philippa Chatterton	CMS
Kate Francis	Dorsey & Whitney
Jane Wang	Fasken Martineau LLP
Paul Cliff	Gateley Plc
Daniel Bellau	Hamlins LLP
Nicholas Narraway	Hewitson Moorhead
Jaspal Sekhon	Hill Dickinson LLP
Danette Antao	Hogan Lovells International LLP
Donald Stewart	Kepstorn
Nicola Mallett David Willbe	Lewis Silkin
Daniel Okusaga	LexisNexis
Nicholas Jennings	Locke Lord LLP
Nicholas McVeigh	Mishcon De Reya
Simon Cox Julie Keefe	Norton Rose Fulbright LLP
Jonathan King	Osborne Clarke LLP
Ashmi Bhagani	Pillsbury Winthrop Shaw Pittman LLP
Sarah Hassan	Practical Law Company Limited
Kieran Rayani	Stifel

Quoted Companies Alliance Primary Markets Expert Group

Richard Evans (Chair)	**Strand Hanson Limited**
Nick Naylor David Worlidge	Allenby Capital Ltd
Chris Hardie	Arden Partners PLC
David Coffman Tony Rawlinson	Cairn Financial Advisers LLP
Andrew Buchanan	Canaccord Genuity Ltd
David Foreman	Cantor Fitzgerald Europe
Stephen Keys	Cenkos Securities PLC
Peter Stewart	Deloitte
Stuart Andrews	finnCap
Samantha Harrison	Grant Thornton
Niall Pearson	Hybridan LLP
Richard Crawley	Liberum Capital Ltd
Tom Price	Northland Capital Partners Limited
Peter Whelan	PricewaterhouseCoopers LLP
Mark Percy	Shore Capital Group Ltd
Azhic Basirov	Smith & Williamson LLP
David Arch Stewart Wallace	Stifel
Andy Crossley	Stockdale Securities Limited
James Spinney	Strand Hanson Limited
Katy Mitchell	W H Ireland
Nicholas How	Zeus Capital