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29 January 2016

Dear Sirs,

Call for Evidence: EU Regulatory Framework for Financial Services

Introduction

We are the Quoted Companies Alliance, the independent membership organisation that champions the interests of small to mid-size quoted companies. Their individual market capitalisations tend to be below £500m.

The Quoted Companies Alliance is a founder member of European**Issuers**, which represents over 9,000 quoted companies in fourteen European countries.

Our ID number for the European Commission's register of interest representatives is 45766611524-47.

Response

We welcome the opportunity to respond to this consultation and particularly welcome the European Commission's decision to conduct this review of the EU regulatory framework for financial services in the context of the Capital Markets Union (CMU).

In our response to the CMU consultation early last year[1], we noted that it is fundamental that the Commission ensures that the regulatory framework being adopted and currently under discussion does not work against smaller issuers and the real economy and is aligned with the vision for the CMU in building a single market for capital.

We continue to believe that the Commission should conduct a thorough impact assessment on the interaction of the regulatory framework as a whole – including delegated acts and regulations – to ensure a coherent interplay of rules for a smooth functioning of the single market for finance. This is a vital assessment to identify what needs to be done towards developing and integrating capital markets. We note that, while this call for evidence is welcome, the Commission is asking for feedback only on rules adopted by co-legislators to date. We believe that assessing the rules adopted to date only, without assessing them together with the rule revisions already underway, renders the whole assessment of the EU regulatory

[1] See our submission at: www.theqca.com/qca-cmu2015

landscape moot. A definitive review of the EU regulatory framework for financial services would also take into consideration significant changes known to be currently underway.

For this reason, we believe that this call for evidence should be a continuing project, an ongoing review taking place on a regular basis (e.g. annually or biennially) and until the CMU project is completed by 2019, giving consideration to ongoing rule revisions or implementing measures.

We again state our particular concern with Level 2 measures on MiFID II, CSDr and MAR, particularly relating to investment research, delayed post trade reporting (liquidity) and SME Growth Markets. The Commission must ensure the consistency and coherence of financial services regulation with the purpose of the CMU, paying particular attention to small and mid-size quoted companies. We have addressed these concerns in our response to the questionnaire and below.

Responses to specific questions

A- Rules affecting the ability of the economy to finance itself and grow

1) Unnecessary regulatory constraints on financing: the Commission launched a consultation in July on the impact of the Capital Requirements Regulation on bank financing of the economy. In addition to the feedback provided to that consultation, please identify undue obstacles to the ability of the wider financial sector to finance the economy, with a particular focus on SME financing, long-term innovation and infrastructure projects and climate finance. Where possible, please provide quantitative estimates to support your assessment.

EXAMPLE 1

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  Other – Across EU legislation

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  A key issue affecting the ability of the economy to finance itself is the lack of promotion of public equity as a viable form of finance for companies, especially when compared to other financing options available to them. This is preventing SMEs from accessing equity finance when it could be the best option for their growth plans.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:**
  (please give references to concrete examples, reports, literature references, data, etc.)

  Over the last 10 years, the number of companies on equity markets in the EU has fallen. As pointed out in the IPO Task Force report[2], the number of IPOs in recent years is very modest, particularly for smaller companies. The report notes that, according to the exchanges, "the main factor explaining the decline of number of IPOs is the decline of smaller companies coming to the market".

[2] See http://www.europeanissuers.eu/_mdb/spotlight/44en_Final_report_IPO_Task_Force_20150323.pdf

Compounding this is a general and pronounced lack of confidence in equity markets. The QCA/BDO Small and MidCap Sentiment Index asked whether equity markets are helping or hindering a company's development in the UK. Between 2011 and 2014 there has been a marked change in sentiment. In September 2011, only 14% of companies said that equity markets were helping their company's development. In April 2014, 58% of companies held that view. The improvement correlates with the improvement of the economic climate. More importantly however, there remains a significant minority that express the view that equity markets are hindering their development (12% in 2014).

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

We believe that the European Commission should promote equity finance to SMEs through promoting increased education.

With the CMU initiative, there is momentum to help SMEs to evaluate the financing option of public equity and also help them to determine whether they would benefit from accessing a public equity market. We would welcome and support the European Commission in producing practical guides for companies considering going public (such as the 'Practical guide to going public' website, which we have supported the Commission in producing).

We are also supportive of the European Small and Mid-Cap Awards, which promote best practices and success stories on public equity markets, underscores the diversity of European capital markets and promotes stock listings. We were active in the development of these awards and we would welcome the continued visible support of the Commission.

EXAMPLE 2

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

Other – Across EU legislation

- **Please provide us with an executive/succinct summary of your example:**
(If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

Currently, tax systems throughout Europe, and specifically in the UK, are skewed to encourage companies to raise temporary debt finance rather than permanent equity. This "tax bias in favour of debt in corporate taxation" was mentioned in the Commission Staff Working Paper accompanying the CMU Green Paper as discouraging "the development of loss and shock-absorbing equity markets across the EU". [3] The recently published CMU Action Plan acknowledges that "the preferential tax treatment of debt resulting from the deductibility of interest rate payments is at the expense of other financial instruments, in particular equity".[4]

[3] See Commission Staff Working Document accompanying the Capital Markets Union Green Paper, available here http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52015SC0013&from=EN
[4] See the Commission Action Plan on Building a Capital Markets Union, available here http://ec.europa.eu/finance/capital-markets-union/docs/building-cmu-action-plan_en.pdf

For many companies, particularly those of a size to consider an IPO, temporary bank finance is not the best way to fund the capital of a business. In the UK, five clearing banks have set aside a facility of £2.5bn to form the Business Growth Fund (BGF). With regional offices to contact companies, the fund invests in businesses with revenues between £5m-£100m, both privately owned and AIM-listed. This encourages companies to recapitalise in an efficient manner. These companies are further supported by the appointment of an experienced director to the board.

The Commission should explore a pan-European version of BGF. Banks could be encouraged to do so through assigning this capital favourably under solvency ratio rules. In this way the "European Business Growth Fund", with a regional network, could accelerate a switch from reliance on temporary bank finance to permanent equity finance. It would also raise awareness of the importance and effectiveness of equity in generating growth, jobs and economic wealth throughout the European Union. The shift from debt to equity would improve the economy's risk profile in any future downturn.

We believe that the role of banks in providing long-term bank facilities to growing companies is already reduced and will continue to reduce over the next few years due to a number of factors, including changes to banking regulation. We believe that there needs to be a shift from relying on temporary bank debt finance to an ecosystem that builds on permanent equity capital. It is of the utmost importance that policymakers explore how to enable this shift and allow small and mid-size companies to access public equity markets.

Obviously, banks will continue to play a role in providing working capital to growing businesses. Therefore, it is important to ensure that any banking sector reforms do not prohibit or restrict the availability of such bank finance for SMEs.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example: (please give references to concrete examples, reports, literature references, data, etc.)**

  N/A

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  The Commission should explore creating a pan-European version of BGF.

  The European Commission and Member States should explore whether there are aspects of the European tax system that unduly favour debt/private equity/venture capital finance in comparison to public equity, as suggested in the CMU Action Plan.

2) Market liquidity: please specify whether, and to what extent, the regulatory framework has had any major positive or negative impacts on market liquidity. Please elaborate on the relative significance of such impact in comparison with the impact caused by macroeconomic or other underlying factors.

EXAMPLE 1

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  MiFID II – Lack of analyst research on quoted SMEs (Directive 2014/65/EU)

- **Please provide us with an executive/succinct summary of your example:**
(If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  Research is valued by small and mid-size quoted companies as a way to make themselves known to small cap investors. This research enhances the quality of portfolios by increasing the asset managers' ability to discover varied and different perspectives on a wider variety of companies. Research coverage increases visibility and trading in small and mid-size quoted companies' shares, thus creating liquidity and enabling growth.

  There is less research available on small and mid-size quoted companies than that which is available for large blue chip companies, which hinders their ability to attract and retain investors. As pointed out in the Commission Staff Working Document accompanying the CMU Green Paper, "there is inadequate business information on SMEs that have a listing or seek a listing. One of the reasons is that equity research analysts and business information providers are far less likely to cover SMEs with their research than large companies."[5] The lack of research on SMEs by investor analysts is also highlighted in the CMU Action Plan.[6]

  MiFID II Level 2 is trying to bring more transparency to the way research is conducted and paid for. Though the outcome of the Commission's considerations regarding its delegated acts is still uncertain, we believe that, as proposed by ESMA, these changes will fundamentally impair the ability of small and mid-size quoted companies to have research produced on them, decreasing their visibility and potentially limiting investment, thus consequentially having a negative effect on small and mid-size quoted companies' ability to raise finance, grow and create jobs.

  As a result of less research and fewer brokers involved in the small and mid-size quoted company market, the proposed rules will lead to lower liquidity, greater share price volatility and higher bid offer spreads. This will result in higher costs associated with raising finance and reduced institutional access, which could culminate in companies questioning the value of being listed on a public equity market.

  We anticipate that the costs of research will increase and the volume, quality and scope of research will fall, which will not only result in small and mid-size quoted companies finding raising capital more difficult, but will also reduce trading liquidity due to little research coverage.

  There will also be higher barriers to entry in the investment market. Smaller asset managers would be disadvantaged regarding fixed costs and access to research compared to larger competitors. According to the Peel Hunt and Extel Survey, 84% of buy-side respondents think MiFID II proposals will raise barriers to entry for new asset managers to start up and force further consolidation giving

[5] See Commission Staff Working Document accompanying the Capital Markets Union Green Paper, available here http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52015SC0013&from=EN
[6] See the Commission Action Plan on Building a Capital Markets Union, available here http://ec.europa.eu/finance/capital-markets-union/docs/building-cmu-action-plan_en.pdf

the consumer less choice. As for existing asset managers, 86% believe that there will be a greater impact on smaller asset managers compared with the larger managers.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:** (please give references to concrete examples, reports, literature references, data, etc.)

Forefactor, an independent market research organisation, conservatively estimates that 35-40% of all publicly traded companies worldwide have no sell-side analyst coverage and that small and micro cap companies suffer the most from this.[7]

In a recent survey published in 'Pulse', Issue 13 of the QCA/BDO Small and Mid-Cap Sentiment Index, we found that 21% of companies had not received any research output even from their house broker over the last two years[8].

The key reasons that small and mid-size quoted companies do not attract as much coverage include:

- Large cap companies are more likely to generate higher investment banking fees;
- Typically, greater liquidity translates into higher revenue from trading commissions; and
- Many buy-side funds are bound by market cap restrictions in their investment mandates.

All of this indicates that there is less incentive from a broker perspective to provide coverage for small and mid-size quoted companies. They simply do not gain much from covering them.

Weild and Kim (2009) also note that high quality investment research has fallen significantly in the past five years and, as a result, smaller companies have disproportionately suffered from this 'brain drain'. Weild and Kim cite research from Integrity Research that estimates that 40% of sell-side analysts lost their jobs in 2008. They also cite research from FactSet Research Systems that shows that for an eight-and-a-half month period ended in May 2009, there were 2,200 incidents of analysts dropping coverage of a company. While Weild and Kim are looking at the US economy and equity markets, these findings resonate with the declining level of research across Europe.

In order to compensate for the lack of sell-side analyst coverage, small and mid-size quoted companies can turn to independent research providers. However, this is an added cost for the company, and so, the take-up of this has not been widespread.

A recent Peel Hunt and Extel Survey[9] found that 78% of quoted companies responding see a correlation between the number of analysts writing on their company and the liquidity of their shares. Small and mid-size quoted companies need more research coverage in order to retain current investors and attract new ones, which would stimulate increased liquidity in their shares. The introduction of minimum tick sizes could be one way to create the finance to fund such research coverage.

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[7] http://www.world-exchanges.org/insight/views/small-cap-analyst-coverage-under-radar-dilemma
[8] In 'Pulse', Issue 13 of the QCA/BDO Small and Mid-Cap Sentiment Index, available here: http://www.theqca.com/article_assets/articledir_171/85657/QCABDODPULSE_Issue13Final.pdf
[9] Unintended Consequences' November 2014, available here: https://www.extelsurveys.com/Panel_Pages/PanelPagesBriefings.aspx?FileName=Peel_Hunt_Extel_Unintended_Consequences_November_2014

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  We believe that the Commission should, in its delegated directive on rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits:

  - **Introduce proportionate requirements, specific for those firms specialising in SMEs stocks' research and based on the principles of transparency, best execution and quality of research:**

    - Research on any company with a market capitalisation below EUR 200 million – either quoted on an SME Growth Market or listed on a regulated market – should be exempt from the requirements defined for investment research.

  - **Introduce a more flexible clients' agreement on cost allocation** (in lieu of the proposed research budget), ensuring that:

    - Investment firms monitor the quality of research and ensure best execution by the executing brokers (who must provide the firm with detailed information);
    - Internal administrative procedures are set up by the investment firm in order to duly assess the clients' needs for third party research;
    - Clients are informed of the criteria to deduct research charges (firms providing execution services should disclose clearly the amount of commissions of trading fees for those services).

  - **Allow investment firms to be able to agree with executing brokers that financial research could be paid by dealing commissions**, so long as:

    - It has been agreed in advance the proportion allocated to remunerate the financial research;
    - The amount of the dealing commissions reflects the quality of the research services;
    - Clear internal administrative procedures have been established to preserve the allocation criteria agreed with each client; and
    - The amount allows the firm to comply with its best execution principles (Art. 27 MiFID II).

  It is important where research exists to give more visibility to and raise awareness of its availability. Commercial initiatives to pool research output should be actively encouraged by the European Commission. We ask the Commission to take this into consideration before publishing its decision on ESMA's Technical Standards on this matter.

EXAMPLE 2

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  CSDR - Deferred publication regime and ADT bands (Regulation (EU) No 909/2014)

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

Small and mid-size quoted companies are not always taken into consideration. ADT bands and deferred publication regime in CSDR are a good example. While we agree that these measures are introduced to bring more transparency and certainty to trading in equity markets, most 'one-size-fits-all' measures will prove inadequate for smaller companies, dependent on various factors for the liquidity of trading in their stocks.

Delayed trade reporting for abnormally large trades of shares is a feature of trading which has existed for many years and facilitates the execution of large client trades without creating undue market impact and price volatility. The management of this volatility and the assurance that the DPR facility is available allows an investor to enter into a holding with confidence that they can have an expectation of divesting of it at a reasonable price. Therefore, it mitigates the liquidity risk associated with material investment, particularly for small and mid-size quoted companies' securities.

A range of delays are required to ensure that a trade receives only the most appropriate length of delay to balance the needs of the market for information with the needs of the individual investor wishing to deal in a block of shares. In effect all the costs of an insufficient DPR regime are borne by large investors such as institutions. An insufficient DPR regime will harm the primary and secondary fundraising ability of small and mid-size quoted companies, as investors will not have sufficient protection to allow them to exit such investments in an orderly manner. This will be a significant disincentive to participation in such markets for institutional funds.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example: (please give references to concrete examples, reports, literature references, data, etc.)**

  N/A

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  Following our response to its consultation paper, ESMA has reconsidered its position regarding the penalties for settlement fails, paying particular attention to trading in small and mid-size quoted companies stocks in its final report.

  ESMA's basic cash penalty rate proposal originally neglected the differences in liquidity of shares, setting penalties which would in effect disproportionately penalise small and mid-size quoted companies and the trading of their shares. After we stressed this unintended effect and provided evidence to support it, ESMA has amended the Technical Advice to the Commission in its Final Report, recommending that penalty rates should duly consider the liquidity of the instruments and significantly reducing the penalty rates for illiquid shares and SME Growth Market shares.

  The added liquidity band is a step in the right direction. We believe that the Commission should ensure that small and mid-size quoted companies and their trading liquidity is fully taken into consideration in this regard.

B - Unnecessary regulatory burdens

5) Excessive compliance costs and complexity: in response to some of the practices seen in the run-up to the crisis, EU rules have necessarily become more prescriptive. This will help to ensure that firms are held to account, but it can also increase costs and complexity, and weaken a sense of individual responsibility. Please identify and justify such burdens that, in your view, do not meet the objectives set out above efficiently and effectively. Please provide quantitative estimates to support your assessment and distinguish between direct and indirect impacts, and between one-off and recurring costs. Please identify areas where they could be simplified, to achieve more efficiently the intended regulatory objective.

EXAMPLE 1

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  Prospectus Directive (Directive 2003/71/EC)

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  As highlighted in our proposals for the reform of the Prospectus Directive[10] and our response to the European Commission consultation on the Prospectus Directive last year[11], we believe that there are several issues that merit consideration for the ability of small and mid-size quoted companies' ability to raise finance.

  A prospectus is a long and complex document that is expensive to produce and made more expensive and time consuming by having to be approved by the national competent authority (in many cases without apparent value of investor protection being added by this process). Furthermore, its usefulness as a document on which investors base their investment decision is questionable. The Study on the Impact of the Prospectus Regime on EU Financial Markets published in June 2008 stated that "unlike institutional investors, small retail investors do not, on average make use of prospectuses for their investment decisions"[12]. In addition, institutional investors will usually make an investment decision during the course of the marketing exercise carried out in the period before the prospectus is available, thus basing their decision on that exercise (where, typically, independent research is not available) and their own internal assessment. We believe it is vital to address the fact that prospectuses are not serving the original purpose intended of them – to provide meaningful information to help investors to make an informed investment decision. A less complex prospectus would mean that companies would produce clearer documents, which are more relevant to both private and institutional investors. It would also reduce the cost and time required to produce them.

  For SMEs, in most cases, the cost of producing a prospectus is simply regarded as too high in proportion to the amount of money that they typically seek to raise – up to 10% of the amount of money raised – thus making a public offer not cost effective. As a result, SMEs must stay within the available exemptions from the requirement to produce a prospectus or look for financing

[10] See www.theqca.com/PD2015
[11] See www.theqca.com/qca-pd2015
[12] See Study on the Impact of the Prospectus Regime on EU Financial Markets - Final Report, June 2008, available at http://ec.europa.eu/finance/securities/docs/prospectus/cses_report_en.pdf

elsewhere, such as debt finance from banks, which has become increasingly difficult to access. To stay within the exemptions of the Prospectus Directive to avoid these disproportionate costs, SMEs, therefore, habitually conduct limited placings with institutional shareholders, disenfranchising existing shareholders from later fundraisings and reducing the ability of SMEs to raise public equity at a time when it is sorely needed in the EU. This reduced ability to use offers to the public means that SMEs have been blocked from funding and the public has been blocked from the ability to invest and participate in SMEs' growth in value. The absence of the public clearly exacerbates a poor or nonexistent equity culture.

The ongoing review of the Prospectus Directive, therefore, represents a great opportunity to improve access for SMEs to equity financing, with all the associated benefits that this would bring for growth in the EU.

Our key proposals to amend the Prospectus Directive are designed to help small and mid-size quoted companies to raise finance more efficiently and effectively, whilst ensuring a high-level of investor protection, and include:

- Introducing separate regimes for an IPO and Secondary Public Offer in the Prospectus Directive
- Creating a Proportionate Prospectus for Secondary Public Offers on regulated markets
- Ensuring that the Proportionate Prospectus for Secondary Offers applies to all types of secondary public offer
- Addressing the process of the national competent authority (NCA) approving a prospectus
- Increasing the thresholds under which a prospectus does not have to be produced
- Exempting offers carried out under the Takeover Regime from the prospectus regime
- Creating a specific prospectus regime for SME Growth Markets

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:** (please give references to concrete examples, reports, literature references, data, etc.)

  Please see our response to the EC consultation on the review of the Prospectus Directive (May 2015).[13]

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  We welcome the publication of the Prospectus Regulation proposal by the European Commission. The European Commission's proposals are a step in the right direction in ensuring that companies throughout Europe are able to raise finance on public equity markets more efficiently. Reduced disclosure for secondary offers and SMEs, as well as allowing greater use of incorporation by reference, will reduce the administrative burdens on companies and make raising funds more cost-effective, whilst still allowing for high quality information to be available to investors.

  In principle, we welcome the increased €10,000,000 threshold in the proposal, below which a Member State can exempt companies from the need to produce a prospectus. Nonetheless, we believe that the European Commission should go further by increasing this threshold to €20,000,000. It should also increase the number of investors an offer can go to before a prospectus

[13] See our submission at www.theqca.com/qca-pd2015

needs to be produced from 150 to 500 people. This would ensure that companies are not deterred from raising equity due to the costs associated. Where a Member State sets a threshold below the maximum level, any company may choose to access finance in any other Member State which has a higher threshold.

Despite all these encouraging initiatives in the Prospectus Regulation, we think this will be a missed opportunity if the European Commission does not create a bespoke prospectus regime for companies on SME Growth Markets. It is difficult to see how the SME Growth Market category can evolve productively without the European Commission taking decisive action to outline its vision for this vital sector and reducing regulatory burdens for companies on these markets. This would be in line with the objective of strengthening the access to public markets, namely by SMEs, contained in the Capital Markets Union Action Plan. Please see Annex I of our response to the consultation [14]regarding what information should be included in such a prospectus.

We would welcome that the Prospectus Directive becomes a Regulation, provided that its drafting is sufficiently clear, allows for future flexibility and it has an overarching reach. A regulation would be directly applicable by Member States, which would be consistent with the objectives of the Capital Markets Union Action Plan. Provided that it is given the appropriate delegated authority, ESMA being in charge of drafting regulatory technical and implementing standards on most of the technical requirements would make the legislative process more flexible, allow greater consultation on proposed changes and make it easier to make any necessary changes as markets evolve.

We believe that this Regulation should expressly create separate regimes for IPO and Secondary Public Offers, as this would be the most effective way of creating a truly proportionate regime for issuers, and would be of particular benefit to small and mid-size companies due to the disproportionate burden of preparing prospectuses for smaller issues. If this is introduced, then the Commission would be able to create a truly proportionate and more effective disclosure regime for all secondary offers and SMEs, which recognises that there is already a great deal of information about quoted companies in the public domain as a result of other existing and effective European Union legislation and ongoing disclosure obligations more generally.

The new Regulation should recognise that different levels of disclosure should be required for the varying types of offers made by different types of companies (i.e. private and public companies) and that this principle should be enshrined in its articles. It is very difficult for a regulation to be clear if its object is not well defined and instead its wording is made deliberately general to encompass very distinct and differing types of offers, such as initial public offers, public offers of secondary issues and public offers by private companies – each of which require significantly different disclosure scenarios.

We welcome the creation of the Minimum Disclosure Regime for all types of Secondary Issuances. This article should establish the principle that any information that has already been disclosed to the market should not have to be repeated in a prospectus for a secondary issuance.

[14] See our submission at www.theqca.com/qca-pd2015

We would support the creation of a Minimum Disclosure Regime for SMEs. We believe that the Regulation should address one of the key issues with the current regime, which is that it applies in three different circumstances that require different levels of disclosure. These circumstances include:

o When a private company SME is conducting a public offer (which is above the Prospectus Directive exemptions);
o When a SME is doing an IPO on a public equity market; or
o When a SME is conducting an offer on a public equity market by way of a secondary issue.

It is difficult to create one set of disclosure obligations that will adequately cover what is required in all of those circumstances. In fact, the current regime has not reduced the requirements enough – most likely because it is trying to ensure it covers all the disclosures necessary in all the circumstances above. Therefore, this should be taken into consideration when determining how the new Minimum Disclosure Regime for SMEs will work in practice and the disclosure requirements should be dependent on the type of company (i.e. private or public) and type of offer (i.e. IPO or secondary offers). Consideration should also be given to the interaction between the specific disclosure items included in any minimum disclosure regime and the general duty of disclosure contained in Article 6 of the proposal.

Regarding the minimum information and format of the prospectus, we would suggest that the Regulation enshrines the principle that a prospectus should avoid duplication of information. We would welcome that the Regulation prescribes ESMA as being responsible for defining what information should be included in the different types of prospectus.

EXAMPLE 2

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  MAR – Costs of producing insider lists (Regulation No 596/2014)

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  We believe that the information required on firms to keep insider lists is far too detailed and will be burdensome for issuers to provide. The contents of such lists should be proportionate and take into the account the purpose for which insider lists are required.

  We welcomed the exemption in the Market Abuse Regulation for companies on 'SME Growth Markets' from the need to produce insider lists on an ongoing basis.

  However, it should be noted that the insider list requirements for companies on SME Growth Markets, although consisting of a specific format with a lighter regime, including optional fields, still require that there will inevitably be a need, in practice, for such issuers to have sufficient systems and procedures in place to produce such an Insider List if requested by the Competent Authority.

This may translate into issuers having to establish costly internal systems and/or processes, which in practice increases administrative burdens.

Moreover, this exemption could be further negated by the delay in the entry into force of MiFID II, as pointed out in 12), Example 1.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:** (please give references to concrete examples, reports, literature references, data, etc.)

  N/A

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  The Commission should ensure that the contents of such insider lists should be proportionate for all issuers, particularly regarding small and mid-size quoted companies, and take into the account the purpose for which insider lists are required.

  It is important that issuers on SME Growth Markets have sufficient flexibility to develop their own appropriate systems and procedures that allow them to save costs and reduce administrative burdens. The Commission should be aware of and prevent inasmuch as possible the onerous situation that small and mid-size quoted companies on growth markets will face by having to produce full insider lists before MiFID II rules enter into force, as explained in 12), Example 1.

EXAMPLE 3

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  4AMLD – Unintended effects of its application to MTFs (Directive (EU) 2015/849)

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  The 4th Anti-Money Laundering Directive (AMLD) has, in our view, failed to recognise the particular nature of small and mid-size quoted companies regarding beneficial ownership.

  Small and mid-size quoted companies are a key driver of growth in the European economy. We welcome and support changes to legislation which promote and facilitate good corporate governance. However, we are concerned with the AMLD articles on beneficial ownership and the negative effect these could have on small and mid-size quoted companies' ability to grow and create employment throughout Europe.

  We believe that placing the obligation on quoted companies to obtain and hold information on their beneficial owners, in addition to the disclosure and transparency rules that they are already subject to through national law or exchange rules, will result in significant added costs and compliance burdens for these growing businesses. This shows no consideration towards companies on growth markets and their difficulties in identifying their end owner.

The AMLD requires all companies to "obtain and hold adequate, accurate and current information on their beneficial ownership". Companies on regulated markets will be exempt from this requirement. However, companies on multilateral trading facilities (MTF) with a primary market function will have to obtain and hold information on their beneficial owners – despite the fact that these companies are publicly quoted companies subject to ongoing disclosure requirements and transparency rules similar to their counterparts on regulated markets.

These public equity markets have been designed specifically to create an environment for equity finance for growing companies, have ongoing disclosure and transparency rules, and are run by Market Operators or Recognised Investment Exchanges which are regulated by the competent authority in that country.

The EU Transparency Directive (2013/50/EU, which amends 2004/109/EC) recognises the difficulty that quoted companies face in identifying its beneficial owners as a result of ownership chains. Shares of quoted companies are often held in nominee accounts – a type of account in which a stockbroker hold shares on behalf of individual investors. Individual investors are still the legal owners of the shares but their names do not appear on the company's share register. As a result of these ownership chains, the Transparency Directive puts an obligation on the owners of significant stakes to inform companies, which then have to notify the market.

We believe that placing the obligation on quoted companies to obtain and hold information on their beneficial owners, in addition to the disclosure and transparency rules that they are already subject to through national law or exchange rules, will result in significant added costs and compliance burdens for these growing businesses.

It is not clear what benefit would arise from quoted companies having to obtain and hold information on their beneficial owners. As public companies, small and mid-size companies quoted on growth markets will have undergone comprehensive money laundering checks as part of the due diligence process of joining a public equity market and then subsequently when carrying out any secondary fundraisings.

The requirement for quoted companies to keep information on their beneficial owners could potentially create the perverse situation where small and mid-size quoted companies on growth markets would have to report more information than their larger counterparts on regulated markets. Thus, small and mid-size quoted companies on growth markets would be disproportionately burdened by this requirement.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:**
(please give references to concrete examples, reports, literature references, data, etc.)

  There are many small and mid-size companies quoted on growth markets throughout the EEA which should be able to benefit from an exemption to the requirement to obtain and hold information on their beneficial ownership. These growth markets, which are classed as MTF with a primary market function, include: Dritter Markt in Austria; Alternext in France; the Alternative

Investment Market (AIM) and the ICAP Securities and Derivatives Exchange (ISDX) in the United Kingdom; Emerging Companies Cyprus in Cyprus; Entry Standard in Germany; BETa in Hungary; Nasdaq OMX First North in the Baltic and Nordic areas; Oslo Axess in Norway; Bratislava Stock Exchange in Slovakia; Entry Market in Slovenia; the Athex Alternative Market in Greece; the Enterprise Securities Market Exchange in Ireland; AIM Italia in Italy; New Connect in Poland; and Mercado Alternativo Bursátil (MAB) in Spain.

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  We recommend that companies whose shares are trading on regulated markets or on a MTF with a primary market function are excluded from the scope of Article 30 of the 4th MLD.

C - Interactions of individual rules, inconsistencies and gaps

11) Definitions: different pieces of financial services legislation contain similar definitions, but the definitions sometimes vary (for example, the definition of SMEs). Please indicate specific areas of financial services legislation where further clarification and/or consistency of definitions would be beneficial.

EXAMPLE 1

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  Other – Across EU legislation

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  There is no single legal definition of a small and mid-size quoted company in the EU. A single definition, or asset class, is needed so that European regulations can be focused and proportionate.

  Small and mid-size quoted companies are fundamentally different from large blue chip companies - in terms of their growth potential, size, turnover, market capitalisation, job creation, percentage shareholding of investors, types of investors, etc. As such, they require a different regulatory and market ecosystem.
  As there is no one single definition, we are seeing a proliferation of definitions throughout various pieces of legislation, especially with regard to the European financial services directives. This is damaging and adds additional complexity for all market participants.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:**
  (please give references to concrete examples, reports, literature references, data, etc.)

  SME policy initiatives should not be restricted to SME Growth Markets as there are a significant number of smaller listed companies on regulated markets. For instance, out of 921 UK Listed companies on the UK Main Market, 228 (or 25%) have a market capitalisation below £100 million (the definition of SME Growth Markets is benchmarked at companies with a market capitalisation of €200 million).

The US's Jumpstart Our Business Startups (JOBS) Act aims to ease the initial public offering process and reporting requirements for growth companies. Section 101 of the Act defines an emerging growth company as a company with annual gross revenues of less than $1 000 000 000 during its most recent fiscal year as shown on the income statement presented under US GAAP. This is a much higher size threshold than any EU legislation provides for.

In Weild, Kim and Newport's report looking at US equity markets (September 2012), a small cap company is defined as a company with a market capitalisation between $500m and $2bn.[15]

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

If equity markets in the European Union are to remain internationally and domestically competitive in terms of attracting small, growth businesses, they need to provide a viable regulatory and listing regime similar to that provided in the US JOBS Act but designed to meet the needs of the EU.
We recognise that one size does not fit all. A suitable definition of small and mid-size quoted company will vary for each Member State. We need to have a single market for finance that flexes for the different types of market that are part of it and the companies that want to join the markets.

Therefore, the Commission should evaluate the creation of a SME Asset Class, so that Commissioners, policymakers, regulators and market operators can easily facilitate proportionate and appropriate policy for growing companies, and so that investors can more easily allocate funds to these companies. We believe that this definition should comprise all quoted companies with market cap below 500m EUR (being the lower level described in Weild, Kim and Newport's report mentioned above). If Member States wished to set a figure below this to suit their market they should be able to do so.

The European Commission should measure annually the economic contribution of the aggregate of companies with a market capitalisation below €200m. By raising awareness of this economic contribution, by annual tracking of such data, more political and investor interest will be created. This tracking data will help inform policy making.

12) Overlaps, duplications and inconsistencies: Please indicate specific areas of financial services legislation where there are overlapping, duplicative or inconsistent requirements.

EXAMPLE 1

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

MAR/MiFID II (Regulation No 596/2014 and Directive 2014/65/EU)

[15] Weild, David, Edward Kim and Lisa Newport. The trouble with small tick sizes: Larger tick sizes will bring back capital formation, jobs and investor confidence. Grant Thornton Capital Market Series. September 2012:
http://www.grantthornton.com/staticfiles/GTCom/Public%20companies%20and%20capital%20markets/Trouble_Small_Ticks.pdf

- **Please provide us with an executive/succinct summary of your example:**
(If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  Article 18(6) of the Market Abuse Regulation (MAR) exempts issuers on SME Growth Markets from producing an insider list. This is a measure that we welcome since we believe the requirement to produce and keep insider lists are too onerous for small and mid-size quoted companies.

  However, "SME Growth Markets" are defined in MiFID II (Directive 2014/65/EU), which does not come into effect until 3 January 2017 (and which may even be delayed beyond that).

  The direct consequence of this is that where reference made in MAR to SME Growth Markets, the relevant provisions will not apply until 3 January 2017. Since MAR will come into force on 3 July 2016, this means that companies quoted on markets which will potentially become SME Growth Markets will have to start keeping full insider lists as outlined in ESMA's technical standards from 3 July 2016 until the point at which MiFID II comes into force and these markets become a designated SME Growth Market.

  Until MIFID II applies and the application of the SME growth market definition comes into effect, the full insider list provisions will need to be met by all relevant issuers. When MIFID II comes into force, the specific provisions for the issuers on an SME growth market set out by MAR would then apply.

  By having the MiFID II requirements come into force after the entry into force of MAR, the EU has effectively removed the exemption for companies on SME Growth Markets, which means that from July this year, small and mid-size quoted companies will have to put in place systems for insider lists and be subject to rules that require the same level of information from larger companies with different resources.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:**
(please give references to concrete examples, reports, literature references, data, etc.)

  There are many small and mid-size companies quoted on growth markets throughout the EEA. These growth markets, which are classed as MTF with a primary market function, include: Dritter Markt in Austria; Alternext in France; the Alternative Investment Market (AIM) and the ICAP Securities and Derivatives Exchange (ISDX) in the United Kingdom; Emerging Companies Cyprus in Cyprus; Entry Standard in Germany; BETa in Hungary; Nasdaq OMX First North in the Baltic and Nordic areas; Oslo Axess in Norway; Bratislava Stock Exchange in Slovakia; Entry Market in Slovenia; the Athex Alternative Market in Greece; the Enterprise Securities Market Exchange in Ireland; AIM Italia in Italy; New Connect in Poland; and Mercado Alternativo Bursátil (MAB) in Spain.

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  We urge the Commission to assess how this issue can be solved through an exceptional derogation. Issuers quoted on markets which will potentially become SME Growth Markets should benefit from the more proportionate rules set out by MAR from the entry into force of this regulation in July 2016.

EXAMPLE 2

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  Other – General Level 2 implementation issues

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  We believe that there are general Level 2 implementation issues directly affecting small and mid-size quoted companies' ability to grow through accessing capital markets and raising equity finance. In this regard, we would like to point out the following:

  - The possible postponement of MiFID II implementation is causing a considerable degree of uncertainty and nervousness among small and mid-size quoted companies. The implementation of certain Level 2 measures – particularly the rules regarding investment research and SME Growth Markets – involves great technical detail and necessary preparation from the firms' side, most of which have limited resources. This is further aggravated by the fact that firms have very little indication of the Commission's direction of travel regarding taking on board, or not, ESMA's advice.

  - The delays in adopting Level 2 delegated acts and technical standards by the Commission regarding MAR translates into firms having very little knowledge of the particular technical details of a regulation they need to be fully compliant with by July this year. For example, systems and controls for keeping insider lists will have to be in place, as pointed out in 12), Example 1, and these are already being developed by firms. We are very concerned with the onerous effort that small and mid-size quoted companies will have to make, in a short amount of time and with limited resource, once the Level 2 acts are published.

  - We believe that it is essential to include more representation of smaller listed companies and associations within ESMA. This would help to ensure that policy and regulations are more fit for purpose at the right time. Also, the Commission should ensure that there is a requirement for ESMA to take into account the views of the ESMA Stakeholder Group. ESMA should be required to perform market impact assessments which specifically take into account small and mid-size quoted companies rather than look at the market as a whole. An SME Asset Class would assist this, as mentioned in 11), Example 1.

- **Please provide us with supporting relevant and verifiable empirical evidence for your example:**
  (please give references to concrete examples, reports, literature references, data, etc.)

  N/A

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  The Commission should allow firms the adequate amount of time to familiarise themselves with detailed legislation. We generally believe that, if Level 2 measures are delayed, firms should be

given a revised timeframe to comply with the rules. This timeframe should take into consideration the resources of small and mid-size quoted companies.

13) Gaps: while the recently adopted financial legislation has addressed the most pressing issues identified following the financial crisis, it is also important to consider whether they are any significant regulatory gaps. Please indicate to what extent the existing rules have met their objectives and identify any remaining gaps that should be addressed.

EXAMPLE 1

- **To which Directive(s) and/or Regulation(s) do you refer in your example?**

  Other – SME Growth Markets (Across EU legislation)

- **Please provide us with an executive/succinct summary of your example:**
  (If applicable, mention also the articles of the Directive(s) and/or Regulation(s) selected above and referred to in your example)

  The introduction of SME Growth Markets is essential in ensuring that SMEs can access capital markets in the EU and we therefore support the European Commission's and Parliament's action in this area by the creation of the SME Growth Market category in MiFID II.

  SME Growth Markets should be able to operate through the application of a number of different models. Harmonisation in this area must take into account the need for SME Growth Markets to retain flexibility as to the specific market model and eligibility criteria. It is important to highlight that harmonisation should not mean homogenisation: no one model will work for all European markets, as they all have different investment cultures. A level of flexibility must be retained at a Member State and market operator level to account for different local and market practices. This would not hinder the creation of pan-European standards, common to all SME Growth Markets across the European Union, where companies choose to access new finance outside their local market.

  SME Growth Markets are not regulated markets and to regulate them as such would remove the flexibility needed for them to provide a platform for SMEs to grow and create employment throughout the EU. Developing a pan-European market concept within a local market framework – with minimum levels of pan-European regulation which is required only for those companies choosing to access investors outside their local market – would incentivise companies and investors to look beyond their Member State boundaries as they grow.

  We note that the possible delay of the entry into force of the MiFID II rules on SME Growth Markets will cause great uncertainty to small and mid-size companies currently quoted on or looking to join growth markets. Moreover, this delay has the unintended effect of delaying the application of other rules and exemptions relating to SME Growth Markets contained in other pieces of legislation and thus possibly having the unintended effect of imposing onerous requirements to these companies which would otherwise benefit from an exemption. This was noted above regarding the specific example of the exemptions applicable to SME Growth Markets for the insider list requirements imposed by the Market Abuse Regulation in 12), Example 1.

Please provide us with supporting relevant and verifiable empirical evidence for your example: (please give references to concrete examples, reports, literature references, data, etc.)

N/A

- **If you have suggestions to remedy the issue(s) raised in your example, please make them here:**

  We urge the Commission to take into consideration the great opportunity that is being created with the introduction of SME Growth Markets and fully analyse the impact on small and mid-size quoted companies of the introduction of the rules, as a whole, applicable to such markets.

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