

<b>Title:</b> The Prospectus Regulations 2018 <b>IA No:</b> n/a <b>RPC Reference No:</b> RPC-4228(1)-HMT <b>Lead department or agency:</b> HM Treasury <b>Other departments or agencies:</b> n/a	<b>Impact Assessment (IA)</b>			
	<b>Date:</b> 13/04/2018			
	<b>Stage:</b> Final			
	<b>Source of intervention:</b> EU			
	<b>Type of measure:</b> Secondary legislation			
<b>Contact for enquiries:</b> Nye Williams-Renouf				
<b>Summary: Intervention and Options</b>				<b>RPC Opinion:</b> GREEN

Cost of Preferred (or more likely) Option				
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANDCB in 2014 prices)	One-In, Three-Out	Business Impact Target Status
£86m	£86m	-£9m	Not in scope	Qualifying provision

**What is the problem under consideration? Why is government intervention necessary?**

In June 2017 the European Parliament and Council adopted the Prospectus Regulation (PR) to replace the Prospectus Directive (PD) – the EU framework for the preparation of prospectuses, both public offers of securities and where securities are admitted to trading on a regulated market. The majority of the PR will not apply in full until 21 July 2019. However, the Government now has to update domestic law to reflect a compulsory change that will take effect in July 2018. It also has the discretion to make a further change to domestic law to reduce the burden on businesses involved in raising capital.

Both the compulsory and discretionary change concern the thresholds for an offer of securities to the public within the EU for which a Prospectus is required. This will reduce the burden and costs imposed on businesses by enabling businesses to raise greater sums of capital without being required to produce a prospectus to do so.

**What are the policy objectives and the intended effects?**

The Commission’s consultation on the PD in 2015 concluded that the regime suffered from shortcomings that were costly and burdensome for businesses, especially smaller businesses that rely more on raising smaller sums of capital but are disproportionately impacted by the high costs currently involved in doing so, particularly where a prospectus is required. The PR’s objective is to improve the prospectus regime, principally by making it cheaper and easier for smaller companies to access capital while maintaining investor protection.

As well as implementing the compulsory change to the threshold exemptions, the Government is proposing to implement the discretionary change to reduce the administrative burden on issuers and facilitate capital raising for UK business.

**What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)**

- To amend the prospectus provisions of the Financial Services and Markets Act 2000 (FSMA 2000) to comply with the requirements of the PR and implement the discretionary change that will reduce the administrative burden on issuers and facilitate capital raising for UK business by the EU deadline of 21 July 2018.
- To amend the prospectus provisions of FSMA 2000 to comply with the mandatory minimum requirements of the PR and preserve the current discretionary threshold, but not to implement the discretionary increase.
- Do nothing.

Option 1 is preferred. Option 2 would in practice have no impact on businesses’ administrative and cost burden, as the UK’s discretionary threshold for issuances of capital is already set higher than the new mandatory minimum threshold at which a prospectus becomes compulsory. Option 3 would be in breach of EU law and result in the UK’s discretionary threshold reverting to the minimum default baseline, which would have significant negative impact on business.

Option 1 will reduce the administrative burden on companies, particularly smaller companies, and facilitate capital raising.

**Will the policy be reviewed?** It will be reviewed. **If applicable, set review date:** 07/2023

Does implementation go beyond minimum EU requirements?	No			
Are any of these organisations in scope?	<b>Micro</b> Yes	<b>Small</b> Yes	<b>Medium</b> Yes	<b>Large</b> Yes
What is the CO <sub>2</sub> equivalent change in greenhouse gas emissions? (Million tonnes CO <sub>2</sub> equivalent)	<b>Traded:</b> 0		<b>Non-traded:</b> 0	

***I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.***

Signed by the responsible Minister:

John P. Glen

Date:

17 April 2018

# Summary: Analysis & Evidence

# Policy Option 1

## Description:

### FULL ECONOMIC ASSESSMENT

Price Base Year 2017	PV Base Year 2017	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: 55	High: 95	Best Estimate: 86

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	0	0	0
High	0	0	0
Best Estimate	0	0	0

#### Description and scale of key monetised costs by 'main affected groups'

These changes widen existing exemptions that have already been implemented into UK legislation. They will reduce burdens on companies, particularly SMEs, so fewer public offers will need a prospectus. No monetised costs are envisaged.

#### Other key non-monetised costs by 'main affected groups'

Non-monetised costs are expected to be negligible.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	0	£6.4 million	£55 million
High	0	£11 million	£95 million
Best Estimate	0	£10 million	£86 million

#### Description and scale of key monetised benefits by 'main affected groups'

We estimate that the potential annual benefits for companies of increasing the current exemption threshold below which there is no requirement to produce a prospectus may amount to approximately £10 million. The estimated cost of producing a prospectus ranges from 7 to 12 percent of the funds raised. For an offer of €8 million, preparing a prospectus could cost in the range of to £490,000 to £845,000. Removing this expense represents a benefit of £490,000 to £845,000 per offer, for an average of 13 public offers per year, for a total of £6.4 million to £11 million. Our best estimate is towards the higher end of this range as it is expected most issuers will take full advantage of the raised threshold to raise additional capital.

#### Other key non-monetised benefits by 'main affected groups'

Implementing this measure will allow companies more efficient access to capital. This is likely to be most significant for further fundraisings by smaller companies. The measures will enable companies to offer securities to a wider set of investors more cost-effectively and to raise capital more cost-efficiently, as they will be able to raise larger amounts of capital at a time.

#### Key assumptions/sensitivities/risks

Discount rate (%)

3.5%

We have sought views from a broad cross-section of relevant industry actors who can express more detailed opinions on the cost and benefits of the UK implementation – the Quoted Companies Alliance, Crowdcube, the UK Crowdfunding Association, the London Stock Exchange Group, and the Association for Financial Markets in Europe. Response has been overwhelmingly positive, with unanimous support for raising the threshold to €8m and no significant risks identified in doing so. Discussions held between HM Treasury and a number of organisations that represent the views of small companies and the markets on which they are admitted overwhelmingly indicate that implementing this amendment will allow companies more efficient access to capital on public markets.

### BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m: -45
Costs: 0	Benefits: 10	Net: 10	

## Evidence Base (for summary sheets)

### Specific Impact Tests: Checklist

Does this policy option/proposal have an impact on...?	Impact	IA Page Ref
<b>Legislation impacts</b> Human Rights Act Data Protection Act Freedom of Information Act	No	
<b>Economic impacts</b> Competition: <u>Competition Assessment Impact Test Guidance</u> Small and Micro-Business Assessment (SaMBA):	Yes Yes	p.5 p.5
<b>Environmental impact</b> Wider environmental issues: <u>Wider Environmental issues Impact Test Guidance</u>	No	
<b>Equality impact</b> Public Sector <u>Equality Duty Impact Test Guidance</u>	No	
<b>Social impacts</b> Health Health and safety: Family test: <u>The Family Test</u> Rural impact: <u>Rural proofing Impact Test Guidance</u> Design quality	No	
<b>Consumer focus</b>	No	
<b>Regional perspectives</b>	No	
<b>Sustainable development</b> <u>Sustainable development impact test guidance</u>	No	

### Background to the Prospectus Regulation

The EU prospectus regime has existed since 2003, when the Prospectus Directive ('PD') was adopted, and forms the EU framework for the preparation of prospectuses for public offers of securities and where securities are to be admitted to trading on a regulated market. Its objectives are to enhance investor protection and to improve the efficiency of the single market. Its key innovation is that a prospectus approved in one Member State is valid across the EU, giving issuers a 'passport' across the EU capital markets. The PD was implemented in the UK via the Prospectus Regulation 2005, which came into force on 1 July 2005 and amended the Financial Services and Markets Act 2000 (FSMA). The application of the PD was reviewed five years after its entry into force, and an Amending Directive was published that sought to improve and simplify the application of the PD, to reduce administrative burdens on issuers whilst maintaining investor protection and improving legal certainty. Since the Amending Directive was introduced, the mandatory threshold below which offers of securities to the public have been exempted from the prospectus requirement has been set at €100,000, while offers of securities to the public below €5 million have been exempt from the scope of the regime entirely, giving member states discretion to set their own domestic exemption thresholds between €100,000 and €5 million. The UK implemented these changes early and in full, exempting all offers of securities to the public below €5 million from the scope of the prospectus regime.

In 2015 the European Commission conducted a second consultation which identified further shortcomings in the Prospectus Directive regime, resulting in unnecessary costs and burdens to businesses, especially smaller ones. On 14 June 2017 the European Parliament and Council adopted Regulation (EU) 2017/1129 (the 'Prospectus Regulation', or 'PR') on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC (the 'Prospectus Directive', or 'PD'). The Prospectus Regulation entered into force on 20 July 2017, and will apply in full from 21 July 2019. However, Articles 1(3) and 3(2) will apply from 21 July 2018. These relate to offers of securities to the public with total consideration below a certain threshold. Article 1(3) exempts

from the entire scope of the regime all offers of securities to the public with a total consideration within the EU of less than €1 million, calculated over a period of 12 months. Article 3(2) permits Member States to exempt offers of securities to the public, where total consideration within the EU is less than €8 million over a period of 12 months, from the obligation to publish a prospectus.

Unlike the current Prospectus Directive, which is implemented into UK law through the FCA's Prospectus Rules and the Financial Services and Markets Act 2000 ('FSMA'), the Prospectus Regulation will be directly applicable in the UK. However, consequential amendments will need to be made to FSMA for its implementation.

The Government is proposing to implement the discretionary increase in Article 3(2) so that UK businesses can benefit from these changes. These measures will be beneficial to companies, particularly smaller companies, by reducing the administrative burden on issuers and facilitating capital raising.

### **Small and Micro-Business Assessment**

The Government is proposing to introduce the discretionary change in Article 3(2) as it will be beneficial to companies, particularly smaller companies. This change will widen an existing exemption and its effect will be to reduce the burden on businesses, in particular smaller businesses; fewer public offers will need a prospectus and more capital can be raised at lower cost. Additionally, due to the costs involved with producing a prospectus, smaller companies often choose to raise funds through institutional offers that are exempted from the prospectus requirement. However, institutional offers rather than public offers can result in dilution of the shares of existing shareholders. These changes should help to encourage smaller companies to conduct public rights issues, which will help to protect minority shareholders while enabling small businesses to raise more capital.

Discussions held between HM Treasury and a number of organisations that represent the views of small companies and the markets on which they are admitted overwhelmingly indicate that implementing this amendment will allow companies more efficient access to capital on public markets.

### **Competition Assessment**

As the Prospectus Regulation introduces incremental changes to the existing regime, they should not have a significant effect on competition. We anticipate that the implementation of these measures will not significantly alter the competitive positions of the regulated and exchange-regulated markets.

**Option 1: To amend the prospectus provisions of the Financial Services and Markets Act 2000 (FSMA 2000) to comply with the requirements of the Prospectus Regulation and implement the discretionary change that will reduce the administrative burden on issuers and facilitate capital raising for UK industry by the European deadline of 21 July 2018.**

#### *Benefits:*

Option 1 would deliver additional benefits associated with introducing the discretionary measure in the Prospectus Regulation.

Under the current Prospectus Directive, the mandatory threshold below which offers of securities to the public have been exempted from the prospectus requirement has been set at €100,000. Offers of securities to the public below €5 million have been exempt from the scope of the regime. In practice, this gave Member States the discretion to set their own exemption thresholds at which a prospectus becomes mandatory between €100,000 and €5 million. The UK implemented these changes early and in full, exempting all offers of securities to the public below €5 million from the scope of the prospectus regime.

The Prospectus Regulation introduces a mandatory change lowering the threshold for offers that are exempt from the scope of the regime entirely from €5 million to €1 million. It also gives Member States discretion to exempt from the prospectus requirement offers of securities of up to €8 million.

In practice, this means that making the necessary changes to FSMA to reflect only the mandatory change would effectively lower the threshold below which an offer of securities for which a Prospectus is required from €5 million to €1 million, which would have a significant negative impact on businesses' ability to raise capital cost effectively.

However, exercising the discretion to raise the threshold for an offer of securities to the public within the EU for which a Prospectus is required from €5 million to €8 million will allow companies more efficient access to capital on public markets. This change will widen an existing discretionary exemption which the UK exercises in full, and its effect is to lift burdens, as fewer offers will need the production of a prospectus. Introducing these measures is likely to be beneficial for UK companies in terms of competitiveness compared to other Member States which have not implemented these measures, and avoid exacerbating any competitive disadvantage compared with other Member States who do implement this discretionary measure.

Responses to the Government's 2010 Green Paper consultation *Financing a Private Sector Recovery* outlined the costs involved in producing a prospectus. Respondents estimated that the cost of producing a prospectus can range from 7 to 12 percent of the funds raised for consideration levels below £10 million, where a prospectus is required. As such, for an offer of €5 million preparing a prospectus could cost in the range of £308,000 to £528,000. For an offer of €8 million preparing a prospectus could cost in the range of to £490,000 to £845,000. These cost estimates were produced by calculating the cost in euros of producing a prospectus, using the above percentage calculations, and then applying the 2017 average EUR-GBP exchange rate of £0.88 (as recorded by Statista) to achieve a valuation in sterling.

Using data from the last six years (2012-2017) on the number of public offers on both the London Stock Exchange's Main Market and its Alternative Investment Market, 1,171 public offers benefited from the €5 million limit for the total consideration of the offer below which no prospectus is required that was introduced by the UK in 2011. The number of offers that would have benefited from a higher fundraising threshold of €8 million (i.e. those with total public issues between €5 million and €8 million between 2012-2017) is an additional 77, or approximately 13 offers per year.

Using these statistics we can estimate the benefits of increasing the fundraising threshold from €5 million to €8 million. The benefits are estimated to be in the range of £6.4 million to £11 million annually, representing a benefit of £490,000 to £845,000 per offer for 13 public offers per year.

We anticipate the benefits to be towards the higher end of the range, as it is likely that the cost of producing a prospectus has impacted upon the appeal of fundraisings below €8 million but above €5 million in the last six years. This is because once an issuer is required to produce a prospectus it is often more cost effective to undertake a higher fundraising.

The benefits are likely to be most significant in the case of further fundraisings by smaller companies. The European Commission's impact assessment for the proposals found that the evidence gathered that the preparation costs of prospectuses particularly impact upon small and medium-sized issuers, which raise capital less frequently and for smaller amounts. Small companies are likely to be able to use these exemptions to enable them to avoid production of a

prospectus. This measure will also help companies to raise capital through further issues more cost efficiently, as they will be able to raise larger amounts of capital (from €5 million to €8 million) at a time.

Due to the costs involved with producing a prospectus, smaller companies often choose to raise funds through institutional offers that are exempted from the prospectus requirement. However, institutional offers rather than public offers can result in dilution of the shares of existing shareholders. These changes should help to encourage smaller companies to conduct rights issues, which will help to protect minority shareholders.

### *Risks*

It is left to the discretion of Member States whether to introduce the discretionary higher thresholds into domestic law. As such, in the case of cross border offers issuers will need to take care when undertaking cross-border offers, as other Member States may not implement the same exemption thresholds, and the limit applies to the total consideration of the offer in the EU. For example, if an offer of €8 million is made in the UK and in another Member State that has not yet implemented the measure, the offer might not be exempt under the domestic law of the other Member State. This will not be an applicable concern where offers are made entirely in the UK. Where a prospectus is required in another Member State issuers should consider electing to have a prospectus in the UK which could then be passported into that other Member State so as to avoid the issuer infringing the laws of the other Member State. It is important that issuers have a clear understanding of this point. However, the exact same conditions currently apply to issuers making public offers between the current EU-wide minimum exemption threshold of €100,000 and the current UK discretionary exemption threshold limit of €5 million, as only nine countries have adopted the maximum discretionary limit (others have applied other exemption thresholds within that range). Nevertheless, we will work with the FCA to ensure this explanation is brought to the attention of industry.

As is the case at present, investors may always choose not to take up an offer where a prospectus is not produced. However, this is not expected to be significant, especially as issuers still have the option of producing a prospectus if they consider it necessary, and bearing in mind the continuing popularity of public offers of up to €5 million which do not currently require a prospectus.

### *Costs:*

This change widens an existing exemption and its effect is to lift burdens so that fewer offers will need a prospectus. No monetised costs are envisaged. There could be indirect costs relating to the adjustment of industry and the FCA to these changes as well as the updating of related guidance. The associated costs are expected to be negligible.

The impact assessment prepared by the European Commission to accompany the Prospectus Regulation indicated that widening these existing exemptions could have indirect costs through a possible increased risk to investor protection. This was on the basis that widening the exemption would mean a prospectus would not be required for a greater number of offers, thereby potentially reducing the information available to investors. As set out above, our analysis suggests that implementing this measure in the UK will mean issuers have the option of not producing a prospectus for approximately 13 more public offers every year. However, we consider the risk to investor protection to be minimal. Investors do not have to take up an offer where a prospectus is not produced. Some exchanges also operate their own rules on disclosure of periodic financial information.

**Option 2: To amend the prospectus provisions of FSMA 2000 to comply with the mandatory minimum requirements of the PR and preserve the current discretionary threshold, but not to implement the discretionary increase.**

*Benefits:*

Option 2 would deliver none of the benefits associated with exercising in full the discretionary measure in the Prospectus Regulation, and would potentially weaken the UK's competitive position as a destination to raise capital relative to other Member States.

As explained in Option 1, making the necessary changes to FSMA to reflect only the mandatory change would effectively lower the threshold below which an offer of securities for which a Prospectus is required from €5 million to €1 million, which would have a significant negative impact on businesses' ability to raise capital cost effectively. Exercising the discretionary power to retain the threshold for an offer of securities to the public within the EU for which a Prospectus is required at €5 million would merely preserve the status quo for business in the UK. It would have no beneficial impact on businesses' administrative and cost burden. It would also weaken the UK's competitive position as a destination to raise capital relative to other Member States that chose to exercise the discretionary exemption threshold in full.

*Costs:*

This change in effect retains the status quo, with virtually no effect on the burdens and costs incurred by businesses in making a public offer. No monetised costs are envisaged.

There could be indirect costs relating to the adjustment of industry and the FCA to these changes as well as the updating of related guidance. The associated costs are expected to be negligible.

**Option 3: Do nothing**

*Benefits:*

There are no benefits to doing nothing. Not laying a statutory instrument to meet the application date of 21 July 2018 would breach EU law. Additionally, the applicable threshold below which businesses could raise capital by offering securities to the public without requiring a prospectus to be produced would fall from €5 million to €1 million, which would be damaging to UK business – particularly SMEs.

*Costs:*

Doing nothing could result in infringement proceedings being commenced by the EU, which would involve significant costs. This change would also narrow an existing exemption by €4 million, which would significantly increase the cost of raising capital for businesses in the UK that wished to raise between €1 million and €5 million.

# Annexes

Annex 1 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

## Annex 1: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. If the policy is subject to a sunset clause, the review should be carried out sufficiently early that any renewal or amendment to legislation can be enacted before the expiry date. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

<b>Basis of the review:</b> Within 5 years of the implementation of the statutory instrument the Treasury will review the implementing regulations.
<b>Review objective:</b> To ensure that the regulations remain an appropriate method of implementing the Prospectus Regulation.
<b>Review approach and rationale:</b> Treasury officials will seek views of relevant stakeholders, such as issuers, intermediaries, investors and the FCA.
<b>Baseline:</b> n/a
<b>Success criteria:</b> The Treasury and stakeholders consider that the implementing regulations continue to satisfactorily implement the provisions of the Prospectus Regulation
<b>Monitoring information arrangements:</b> Treasury officials are in regular contact with affected stakeholders
<b>Reasons for not planning a review:</b> n/a