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COMMENTS ON THE EC PROPOSAL ON SME LISTING PACKAGE

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We welcome the opportunity to provide feedback to the Commission's proposal on the SME Listing Package. In this paper we are sharing some high-level comments on the SME Listing Package overall while also providing detailed comments on the proposed changes under the Prospectus Regulation, under the Market Abuse Regulation and for MIFID II level 2 adjustments.

We welcome the Commission's intention to adapt existing EU rules to introduce a more proportionate regulatory approach to support listing of smaller companies. We applaud the aim to boost the number of initial public offerings (IPOs), to reduce the administrative burdens and the high compliance costs faced by SME growth market issuers, and to foster the liquidity of publicly-listed SME shares. We also welcome several specific proposals. Nevertheless, overall, we believe that more ambition is needed to achieve a fully proportional environment for smaller companies and healthy and thriving European capital markets.

A definition of small and mid-cap companies – that goes alongside with the definition of SMEs – is essential to enabling focussed and proportionate regulations. Small and mid-cap companies are fundamentally different from large blue-chip companies, as well as from SMEs (in terms of their growth potential, size, turnover, job creation, percentage shareholding of investors, and types of investors, among other things). As such, they require a different regulatory and market ecosystem, along with appropriate, tailored rules for these companies' growth needs.

Therefore, we strongly believe that the SME listing package should provide a **definition of a small and mid-cap company** enshrined in EU law. In line with the US JOBS Act, we would propose an upper market capitalisation threshold of €1bn. Compared with the industry small-cap fund definitions which range from €1bn to 7bn, such a threshold is rather modest. To reflect the diversity of EU markets, certain flexibility for Member States could be permitted to adjust this threshold to local market realities. Such an approach would help to achieve a European uniform and proportionate approach towards smaller quoted companies while taking into consideration the diversity of market conditions in Member States.

The Commission SME Listing proposals are restricted to companies on SME Growth Markets only. We strongly believe that to revive EU capital markets **small and mid-cap companies on the Regulated Markets should be also subject to less stringent regulatory requirements**[1]. To ensure that such small and mid-cap companies are easily distinguishable from those subject to the full regulatory requirements, a separate market segment for small & mid-caps on the Regulated Markets could be envisaged. Consideration could be also given to setting a timeframe (e.g. five years) during which small and mid-caps on the Regulated Markets could benefit from those alleviations.

[1] See our response to EC consultation on building a proportionate regulatory environment to support SME Listing for more details http://www.europeanissuers.eu/positions/files/view/5aa6cf226b840-en

Furthermore, the proposals will be a missed opportunity for the Commission if it does not at **least review the criteria used to define SME Growth Markets for equity**. While we appreciate the intention to make corporate bond markets more attractive, we fail to understand why some of the regulatory alleviations are restricted to bond issuance / issuers only. That is contrary to the Capital Markets Union principle of attempting to remove the bias against equity finance, which we believe should be addressed in this package.

Last but not least, we would like to point out the importance of ensuring there are workable transitional arrangements in all markets allowing companies to smoothly transfer from the SME Growth Market to the Regulated Market and the other way around (from the Regulated Market to the SME Growth market). In that respect we regret that the proposals for such transitional rules that the Commission was consulting on, are not reflected in the SME Listing Package. We believe there should be an overarching principle ensuring that local market operators have appropriate transitional arrangements in place.

Flexibility must be key in setting the arrangements allowing for companies' smooth transfer between markets. Rather than introducing EU harmonised rules on voluntary transfer of listing and delisting rules, there should be an overarching principle ensuring that local market operators have appropriate arrangements in place. We have included in the annexed document our detailed comments for your consideration.

DETAILED COMMENTS

1. Proposals for changes under the Prospectus Regulation

- **Creation of a lighter 'transfer prospectus'' for SME Growth Market issuers listed for at least three years when seeking a graduation to regulated markets (changed under the Prospectus Regulation).**

We welcome this proposal, although we see further room for improvement. The period of three years could be shortened to 1 or 2 years. Also, maybe even a lighter document could be envisaged than a secondary issuance prospectus.

2. Proposals for changes under the Market Abuse Regulation

- **Adoption of a new deadline to publicly disclose managers' transactions: issuer to disclose to the public up to 2 days after receiving the PDMR/PCA notification instead of the current deadline of 3 days both for the PDMR/PCA and the company (change under MAR).**

We welcome and fully support this proposal, although we regret that such provision applies to companies on SME Growth Markets only as companies listed on Regulated Markets could also benefit from it without impairing market integrity.

- **Replacement of the current obligation to keep a list of insiders for each piece of inside information with an obligation to maintain only a list of 'permanent insiders' (change under MAR).**

We welcome and fully support this proposal. However, to avoid any legal uncertainty we suggest that the wording in the proposal concerning Article 18§6 be aligned to the wording of "permanent insiders" established in the Commission Implementing Regulation (EU) 2016/347 Article 2§2.

Nevertheless, it is also very important to exempt smaller listed companies, or at least those on SME Growth Markets, from the obligation to draw up and keep lists of persons closely associated to PDMRs (Art. 19 of MAR).

Art. 19 of MAR requires companies to gather very sensitive information from PDMRs relating to their personal life and keep this information up-to-date which is also burdensome and, we hear, unnecessary from the investors' point of view. According to the data gathered by Polish NCA there are as many as 25,200 closely related persons. In the EU there are around 13,000 publicly listed companies (both on RM and MTFs). We can estimate that each listed company has on average 10 PDMRs and each of them as on average 3 family members. That means that there are approx. 520,000 natural persons that could be toped up with approx. 100,000 legal persons that PDMRs may be associated to. While very few of those persons (ca. less than 1%) enter into transactions related to the issuer's securities. While any infringement in the procedure is subject to a fine of up to EUR 0,5 million for any person in the chain (e.g. manager and his/her family members). Considering the size of companies and earnings of managers, especially in some countries, such sanctions are highly punitive. We attach infographics developed by SEG (Polish Issuers' Association) which describe how burdensome the administrative procedures that companies must apply to comply with MAR rules regarding Managers' Transactions.

To remedy this situation, we suggest reverting to the pre-MAR situation, meaning that PMDRs would no longer be required to intermediate in transferring the information on the trades made by closely related persons to the issuer. This way, issuers would not be obliged to keep the lists of PMDRs' closely related persons.

- **Justification of delayed inside information to be made only on request (and no need to keep a disclosure record)**

SME Growth Market issuers will be still required to notify a delay to the relevant NCA but will only be obliged to provide a justification upon request. SME Growth Market issuers would be exempted from the obligation to keep the list of detailed information to justify the delay on an on-going basis.

We welcome this proposal to alleviate the administrative burden of SME Growth Market issuers. Nevertheless, we question whether this proposal will result in a substantial alleviation of burden if companies will still need to notify delayed disclosure of inside information and may be requested to provide justification on demand, and **we urge the Commission to assess whether this alleviation can be further simplified.**

Moreover, we would suggest aligning the wording of the proposal to the current wording of the Regulation, therefore, replacing "*the explanations for the decision to delay …*" **with** "*the explanation of how the conditions set out in this paragraph were met*".

- **Exemption from the market sounding regime for private placements of bonds with qualified investors**

MAR imposes very strict and burdensome requirements regarding market soundings. They include the establishment of procedures, the disclosure of standard information and an obligation to keep records. These requirements are aimed at large, relatively liquid markets and do not take into account the specifics of more local, less liquid markets such as markets specialising in small and mid-cap companies and corporate bond markets. In these markets, implementing these rules significantly restricts the willingness of potential issuers to carry out new issuances, in particular for entities that do not fall into the "frequent issuers" category.

The exemption proposed will be available when (i) the issuer seeking a private placement of bonds already has its equity or non-equity financial instruments admitted to trading on an SME Growth Market; and (ii) if an alternative wall-crossing procedure (e.g. a non-disclosure agreement) is in place, by which any potential qualified investor acknowledges the regulatory duties stemming from the access to inside information.

For the reasons outlined above, we urge the Commission to **exempt not only private placement of bonds but also other equity and bond issuance by companies on SME Growth Markets from complying with market sounding rules when investors are involved in the negotiations of the issuance**. Standard rules preventing use of privileged information will suffice to ensure markets' integrity.

- **Creation of a European regime for liquidity provision contracts for SME Growth Market equity issuers while allowing NCAs to establish Accepted Market Practices**

We welcome the Commission's initiative to propose a measure to increase liquidity and reduce volatility of SME shares. It is important to increase the attractiveness of SME Growth Markets for investors, intermediaries and exchanges.

We recognise the usefulness of liquidity contracts, which are frequently used in some countries (e.g. France). We see merits in having liquidity contracts recognised as the Accepted Market Practice. Nevertheless, we urge the Commission to recognise and support **the diversity of market making practices in the Member States where markets provide for other solutions.**

Moreover, it is important that the existing and new EU legislation does not discourage but rather promote market making activities, especially in trading securities of smaller listed companies.

For instance, The Central Securities Depositories Regulation (CSDR), that came into force in September 2014 (subject to a number of transitional provisions), raises certain concerns. It is important to note that the postponement of MiFID II to January 2018 has delayed the implementation of provisions relating to settlement discipline and interpretation provisions to 2019.

In an attempt to minimise risk in settlement the EU has increased the nominal minimum liquidity required to access equity capital markets, which will constrain the ability of small and mid-cap 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.

Under CSDR, trades not settled at an agreed time will face daily fines until the trade is settled, also in the case of SME Growth Markets, where specific fines are foreseen. These fines will pass along the chain of settlement so that only the initial failing part of the settlement chain will pay up. 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 (i.e. fining them for performing the specific purpose for which they exist).

Penalising formal liquidity providers, namely market makers, for not settling trades on time will further reduce liquidity in smaller companies' markets and reduce their access to funding on public markets.

CSDR will 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-cap 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. We would therefore urge the European Commission to remove all fines for failing to settle trades on time from securities of small and mid-cap companies irrespective of trading venue.

More broadly, we believe that introducing common securities settlement standards across the EU will harm the ability of small and mid-cap companies to raise capital on public markets. Different small cap 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.

We believe it is important to remove all fines for failing to settle trades on time from securities of all companies on SME Growth Markets and small and mid-cap companies irrespective of trading venue.

3. **Proposals for changes under MiFID II**

- **New definition of debt-only issuers**

The Commission proposes that an issuer that has no equity instrument traded on any trading venue shall be deemed an SME Growth Market issuer if the total size of its debt issuances does not exceed EUR 50 million over a period of 12 months on all SME growth markets across the Union.

While we very much support this proposal that will believe will contribute to promoting the SME Growth Markets concept and enable corporate bond issuer companies to benefit from a more proportionate regulatory framework, we regret that the criteria used to define SME Growth Markets for equity are not being reviewed.

As said above, we believe that the SME listing package should provide a **definition of a small and mid-cap company**, which is crucial to recognise the diverse nature of companies which are no longer SMEs but also very different from large blue-chip companies, and to enable focussed and proportionate rules for such companies. To facilitate healthy and thriving public capital markets, taking the example of the US

JOBS ACT, we would propose an upper market capitalisation threshold of €1bn, although some flexibility with an upper limit might need to be left to individual Member States. **All companies below this threshold should be exempted from certain EU disclosure requirements and should be allowed access to the SME Growth Markets**. Consideration also should be given to a **transitional period exempting the newly listed smaller companies from some of the requirements for five years.**

- **Minimum free-float criterion as part of the admission rules for SME Growth Market issuers**

We believe that **no rule on minimum free float should be introduced in the EU legislation**. As pointed out by the Commission, when an SME goes public, it is likely that there will be a low level of free float. Imposing free float requirements can make the listing unattractive for the company's owners. As the objective of the Commission's planned initiative is to make SME Growth Markets attractive and to facilitate SME listings, we believe it is best not to impose any EU rules on minimum free float. Such aspects will be more adequately addressed by the local markets and in discussions between investors and companies.

We note that, in the UK, the QCA-RSM Small and Mid-Cap Investors Survey 2017[2] found that a majority of institutional investors believed there should be no enforced minimum free float – either by value of company or size of shareholding floated – as it would represent an unnecessary and punitive burden on the company in question. Furthermore, after consulting a wide range of UK market participants on whether the AIM Rules for Companies should include a specific numerical or percentage threshold for free float in summer 2017, London Stock Exchange found that there was strong support that the current approach to free float strikes the right balance and that a qualitative approach is of benefit to the market. Respondents also commented that it remains of fundamental importance that a growth market has flexibility and is not hampered by numeric constraints which may result in potentially arbitrary outcomes for smaller companies.[3]

Please note that despite providing data at this stage from UK only, this concern is very much shared by all our members representing the interests of smaller issuers across the EU.

- **Analyst research**

The Directive on Markets in Financial Instruments II (MiFID II) is effective as of 3 January 2018. Small and mid-cap companies are mainly affected by the impending changes to investment research.

The MiFID research rules apply when a firm produces or arranges for the production of investment research that is intended to be disseminated to clients of the firm or to the public. This does not include where a firm distributes investment research exclusively to members of its group.

Firms must ensure the implementation of all of the MiFID measures for managing conflicts of interest in relation to the financial analysts involved in the production of investment research and other relevant persons (including corporate finance personnel and persons involved in sales and trading activities on

[2] QCA-RSM Small and Mid-Cap Investors Survey 2017, March 2017: http://www.theqca.com/article_assets/articledir_256/128121/QCA_RSM_Small_and_Mid-Cap_Investors_Survey_2017_Report.pdf

[3] Feedback Statement and Consultation: AIM Rules Review, December 2017: http://www.londonstockexchange.com/companies-and-advisors/aim/advisers/aim-notices/feedback-statement-and-consultation.pdf

behalf of clients or the firm) whose responsibilities or business interests may conflict with the interests of the persons to whom the investment research is disseminated.

Furthermore, a financial analyst should not become involved in activities other than the preparation of investment research where such involvement is inconsistent with the maintenance of the financial analyst's objectivity (for example participating in investment banking activities, participating in pitches for new business or road shows).

Independent investment research on small and mid-caps has been already very low before MiFID II (some estimated it at 30%) and it has significantly dropped since 2007 when the original MiFID was introduced. This has created a considerable informational imbalance between the professional investment community and other investors. The economics of small and mid-caps dictate that sponsorship of coverage is the only realistic means by which the market can be provided with quality investment research.

However, investment managers may only receive research when paid for either by a client-agreed research payment account, a company specifically having paid for research to be written about itself and then distributed as a marketing communication, or from an investment manager's own resources. The challenge is that the administrative burden and cost of maintaining compliance with such rules is high for small company brokers and small company investment managers in comparison to the benefits.

Markets have already noticed a drop in the production and distribution of analyst research since MiFID II coming into effect. Moreover, contrary to the intention of the Commission, MiFID II may lead to market consolidation as only the largest players will be able to finance research. We appreciate that the Commission is intending to commission a study on MiFID II impact on the provision of analyst research, but in the meantime the damage on the market may be already done and would be specifically acute for smaller companies. Therefore, **we believe that it is necessary to use the opportunity of SME Listing Package and MiFID II adjustments to:**

- Clarify that small cap research is not an inducement and can be received by fund managers free of charge;
- Allow all investment research on small and mid-cap companies to be published on a website inclusive of appropriate disclaimers;
- Not standardise price increments in the trading of securities.

These clarifications should be applicable to all companies on SME Growth Markets and small and mid-cap companies irrespective of the trading venue.

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