Fordham International Law Journal

Volume 19, *Issue* 3 1995 *Article* 4

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Abstract

This Essay gives a general overview of the EC securities regulations and their influence on the offerings of securities involving several EU markets, with a particular focus on the disclosure requirements and the registration of prospectuses. This Essay will also discuss some regulatory concerns regarding the use of licensed intermediaries and their role in organizing a multi-jurisdictional securities offering. Lastly, this Essay will examine the debate on the reconciliation of various accounting principles and disclosure standards, an issue that is presently regarded as a priority on regulators' agenda, and one which will certainly affect the accounting practices adopted by global issuers of securities.

EU CROSS-BORDER SECURITIES OFFERINGS: AN OVERVIEW

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INTRODUCTION

A cross-border offering of securities in the European Union ("EU") involves the possible application of several regulations, depending on the number of Member States that will market the securities. These laws pertain mainly to disclosure requirements and the use of authorized intermediaries. From a non-EU offeror's perspective, many of these regulations appear fairly similar across the Member States and compliance may not present a dilemma. Still, an offeror must cope with certain regulatory inconsistencies arising out of difficulties in harmonizing European legislation, and from the presence of non-regulated areas that remain within the independent jurisdiction of Member States.

This Essay gives a general overview of the EC securities regulations and their influence on the offerings of securities involving several EU markets, with a particular focus on the disclosure requirements and the registration of prospectuses. This Essay will also discuss some regulatory concerns regarding the use of licensed intermediaries and their role in organizing a multi-jurisdictional securities offering. Lastly, this Essay will examine the debate on the reconciliation of various accounting principles and disclosure standards, an issue that is presently regarded as a priority on regulators' agenda, and one which will certainly affect the accounting practices adopted by global issuers of securities.

I. *CROSS BORDER OFFERINGS*

Member States retain jurisdiction over all securities transactions occurring within their borders. As a result, cross-border securities offerings in the European Union must conform to diverse national rules and regulations. EC directives addressing the issuance and trading of securities aim to harmonize local

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laws by providing minimum standards of disclosure and by fostering cooperation among national supervisory bodies.

A. *The Impact of EC and National Laws on Cross-Border Offerings*

Unlike the United States, where the interstate sale of securities calls for the application of uniform federal laws and regulations and involves the jurisdiction of the Securities and Exchange Commission, the European Union does not have a uniform system of laws that apply generally to transactions involving the EU market as a whole. Each Member State has its own securities laws and supervisory bodies, and retains jurisdiction over any securities transaction carried out within its borders. Accordingly, EC securities regulations do not amount to a superior system for multi-state transactions, as no EU regulatory body has been created to exercise general supervision over the EU securities market.

EC rules in the securities area consist of directives that must be implemented by Member States through ad-hoc national legislation. The EC directives on securities markets form a common background of provisions that aim to harmonize local laws based on the following priorities: (1) to ensure a minimum standard of quality and information concerning the securities traded, the issuers, and the offerors involved; (2) to ensure thorough supervision of the securities markets at a local and global level, by fostering cooperation among national regulatory bodies; and (3) to make national markets accessible to issuers and intermediaries who have been admitted and are regulated in other Member States, through the elimination of regulatory barriers that are not justified by material interests and *de facto* impede the free circulation of services and products.

A non-EU cross-border offeror may choose, therefore, any Member State as the first place for registration and may subsequently be allowed to offer securities in other Member States by complying with additional local requirements. It may not, however, obtain an EC registration of its securities or file an EU prospectus with a general authority.

B. *EC Regulation of the Securities Markets*

EC directives on the securities markets cover several aspects of securities finance, including: admission to stock market list-

ing, restrictions against insider dealing, registration of prospectuses, and disclosure of significant stockholdings in listed companies. The key areas typically related to securities offerings are: (1) disclosure obligations; (2) participants in the offering; and (3) specific types of securities requiring an *ad-hoc* regime.

The disclosure requirements for public offerings focus on the securities being offered, the issuer, and the offeror(s) (if other than the issuer). Disclosure with respect to the securities and the issuer is provided through the registration of a prospectus. EC directives regulate three different types of prospectuses: (1) the prospectus for admission to stock exchange listing; (2) the prospectus for securities offered to the public that are destined for eventual stock exchange listing; and (3) the prospectus for offerings of securities not destined to admission to stock exchange listing.

The contents of prospectuses and the standard of control required on the part of local supervisors vary according to the intended use of the prospectus and the destination of the related securities. If the securities are listed on a regulated stock exchange, the issuer is required to provide additional mandatory disclosure concerning, *inter alia*, its financial condition, accounts, and business.

The rules concerning the participation of intermediaries in public offerings pertain to the intermediary's capacity to deal in securities. Such activity is subject to authorization in all the Member States, and is limited to supervised entities, such as: banks, financial intermediaries, and securities firms. The main EC directives in this field enable entities licensed in one Member State to provide financial services in other Member States on a cross-border basis. While the regulations governing the financial activities of banking entities have been progressively harmonized, non-banking intermediaries must still organize local subsidiaries in order to offer their services in particular Member States. Such is the case in Italy, where non-Italian securities firms may not place securities or collect transaction orders from investors. This situation should change when the implementation of the Financial Services Directive becomes mandatory at the end of 1996. Pursuant to this Directive, non-EU entities may offer their intermediary services in Member States where authorized, in accordance with the standards of reciprocity and quality of supervision exercised by the home-country regulatory bodies.

EC directives set out different provisions for specific types of securities, exempting certain securities transactions from the harmonization rules mentioned above. For example, differential treatment is accorded to units issued in connection with collective investment schemes ("UCITS") that are organized in the form of unit trusts, mutual funds, variable-capital-companies, and similar structures with the exception of close-end funds and other minor schemes. The UCITS Directive requires these investment entities to adopt certain organizational standards, in order to be licensed for marketing in the European Union. Once the so-called harmonized UCITS are established and registered in one Member State, they may be offered in any other Member State through a simplified recognition procedure established by local laws that have been implemented pursuant to the guidelines of the UCITS Directive. Non-EU harmonized investment entities, by contrast, may only be offered in a Member State where authorized by non-harmonized local laws.

Euro-securities that are not offered by means of general advertising campaigns or door-to-door solicitations are exempted from the application of the directives on prospectuses. Some of these special provisions are justified by the nature of the securities involved such as securities issued by international institutions.

II. *THE EUROPEAN PROSPECTUSES*

The European Union aims to foster the expansion of its securities markets through the principle of "reciprocal recognition," which allows prospectuses registered in one Member State to be easily recognized in most other Member States. The EC directives on prospectuses set forth minimum requirements for the publication of prospectuses, in an attempt to harmonize local regulations. Additionally, these directives provide several exemptions for securities that are not offered to the public at large. Despite the European Union's efforts to harmonize its securities regulations, however, inconsistencies regarding, *inter alia*, accounting principles, persist at the national level.

A. *The Purpose of the EC Directives on Prospectuses*

Securities registered for offering in a Member State or traded on a regulated stock exchange are to be admitted to mar-

keting or listing in any other Member State, as long as the registration procedure mandated by home-country regulators conforms to generally accepted standards of control and disclosure. This is, in substance, the principle of reciprocal recognition of prospectuses registered with EU Member States' regulators that has been pursued by the Commission through the adoption of the directives on prospectuses. The creation of a "passport" for registered securities by means of a harmonized prospectus, aims to foster the expansion of the securities market and the free flow of financial resources among members of the European Union.

The involvement of large numbers of prospective investors in many different countries requires the protection provided by the directives on prospectuses. These directives mandate adequate disclosure regarding the securities and their issuers, and control how supervisory bodies exert over such information. Disclosure standards maintained in all Member States ensure that regulatory diversity does not adversely affect competition among markets, nor results in potential harm for investors.

B. *The Conditions for Registration of a Prospectus*

The directives on prospectuses were adopted by the EC Commission over a period of about 15 years. The first directive, 80/390/EEC,[1] was enacted in 1980 to regulate the prospectus for issuers seeking stock market listing. The present version of this Directive is the result of subsequent amendments made in 1987 by Directive 87/345/EEC,[2] in 1990 with Directive 90/211/EEC,[3] and in 1994 by Directive 94/18/EC[4] ("Eurolist Directive"). The rules on prospectuses for public offering of securities in the absence of, at a minimum, simultaneous listing were adopted in 1989, by Directive 89/298/EEC.[5] Under these rules, a prospectus must be published in two different situations: (1) where an issuer seeks a stock exchange listing of its securities in any Member State, and (2) where securities are offered to the public in a Member State market.

The above regulatory framework is not limited to issuers in-

1. Council Directive No. 80/390, O.J. L 100/1 (1980).
2. Council Directive No. 87/345, O.J. L 185/81 (1987).
3. Council Directive No. 90/211, O.J. L 112/24 (1990).
4. Council Directive No. 94/18, O.J.L. 135/1 (1994)
5. Council Directive No. 89/298, O.J. L 124/8 (1989).

corporated in the European Union. As discussed below, non-EU entities that intend to raise capital in the European Union are required to register a prospectus in compliance with the national regulations that implement the above-mentioned directives.

Under Directive 80/390/EEC,[6] listing of a security in any Member State is conditioned upon publication of a prospectus which conforms to the minimum requirements of the Directive, with the competent national authority. The prospectus must report the information that investors and their financial advisors need to adequately evaluate the economic and financial potential of the issuer, as well as the nature of the securities.[7] It is worth noting that compliance with the requirements concerning the publication of the prospectus does not guarantee admission to listing. In fact, the Directive merely establishes the standards for information that must be given to the public; it does not regulate the requisites for admission, which are governed by national rules adopted in accordance with the general principles set forth in Directive 79/279/EEC.[8] The issuer may not be required to publish a new prospectus for additional listing in a different exchange, as the initial prospectus will be recognized by all Member States. Admission in the first Member State, however, shall not guarantee admission in other EU stock exchanges, which may still be conditioned on compliance with local regulations.

Additionally, publication of a prospectus must also occur where a public offering of "negotiable instruments" is carried out for the first time in one or more Member States and the securities involved are not already, or will not be simultaneously, listed in an EU, regulated, stock exchange. Directive 89/298/EEC[9] distinguishes between the offering of securities where such listing and the offering of securities for which such listing is not intended. For offerings of securities destined for admission to stock market listing the prospectus and control demanded by local authorities must conform substantially to the requirements set forth in Directive 80/390/EEC,[10] the Directive on prospectus

6. Council Directive No. 80/390, *supra* note 1, O.J. L 100/1 (1980).
7. *Id.*
8. Council Directive No. 79/279, O.J. L 66/21 (1979).
9. Council Directive No. 89/298, *supra* note 5, O.J. L 124/8 (1989).
10. Council Directive No. 80/390, *supra* note 1, O.J. L 100/1 (1980).

for admission to listing. For offerings that are not intended for listing, Member States may require less detailed information, so as to exempt smaller companies from excessively pervasive requirements.

The publication of a prospectus is governed by Directive 89/298/EEC.[11] This Directive sets forth three general conditions for the publication of a prospectus: (1) an instrument qualifying as security; (2) an offering to the public; and (3) the circumstance that such offering is carried out in a Member State for the first time. The Directive provides a more narrow definition of "security" than that utilized in the United States and many Member States. Under the Directive, a "security" is a share, a bond with maturity of more than one year, or any other negotiable instrument equivalent to a share or a bond that allows the purchaser to obtain a share or a bond by means of the exercise of option rights or conversion.[12] The Directive does not provide a definition of "public offering," which presents a particularly controversial issue among Member States. The Directive provides exemptions, however, that pertain to the concept of "private placement" and helps to identify, by way of contrast, the extent of the definition of public offering implied in its text.[13] Finally, by requiring that the offering first take place in a Member State, the Directive tries to reconcile the application of different regulations on prospectuses and attempts to avoid duplicative requirements for securities that are already "known" to the public.

C. *Exempted Offerings*

In examining the exemptions provided by the directives in connection with public offerings, it is worth noting, again, that these provisions do not necessarily exempt the particular transaction from local disclosure, authorization, or registration requirements. Rather, the exemptions only waive the harmonization of prospectus requirements for the particular placements. An exemption may apply when the transactions or the securities involved are already regulated by other EC directives. In such circumstances, the need to protect investors may be deemed less

11. Council Directive No. 89/298, *supra* note 5, O.J. L 124/8 (1989).
12. *Id.*
13. *Id.*

critical by the EC Commission. Also, the diversity in jurisdictional approaches to the issue has impeded the promulgation of uniform rules. As a result, a certain transaction may fall within a safe harbor in one Member State and simultaneously trigger the obligation to publish a prospectus in another.

Although Directive 89/298/EEC does not define "public offering," it does grant certain exemptions that may be used to identify its characteristics. These exemptions pertain to: (1) offerings to persons in the context of their trade, profession, or occupation; (2) offerings to a small number of investors; (3) offerings where the total value of the securities issue does not exceed ECU40,000 (roughly US$51,000); and (4) offerings where the minimum investment required for each investor amounts to at least ECU40,000.[14]

Additional exemptions are provided with regard to the types of securities offered. These exemptions are granted for: (1) securities in single denomination of at least ECU40,000; (2) securities issued, for example, by UCITS trusts and mutual funds; (3) securities issued by States or international organizations in which one or more States participate; (4) securities issued to the employees of the offeror; (5) securities acquired pursuant to the exercise of conversion or option rights; (6) securities issued by non-profit entities; (7) euro-securities that are not offered by means of a general advertising campaign or door-to-door solicitation; and (8) securities equivalent to shares that are necessary to benefit from the services rendered by building societies, industrial and provident societies and the like.[15]

As one may gather from the above, the Directive 89/298/EEC provides numerous exemptions that are supported by various rationales. The exemptions for offerings "to persons in the context of their trade, profession or occupation" use rather ambiguous language, which has been interpreted by commentators to refer to so-called accredited investors. Accredited investors, as acknowledged in several jurisdictions, should be able "to fend for themselves" since their understanding of the risks involved by the proposed investment is particularly sophisticated. A similar rationale seems to justify other exemptions, such as where the individual value of the securities offered or the minimum invest-

14. *Id.*
15. *Id.*

ment available to individual investors amount to at least ECU40,000. An example of exemptions for accredited investors is seen in Italy. In accordance with EC provisions, Italian regulators have adopted significant exemptions for accredited investors, such as banks, securities firms, mutual funds, and asset manager companies. Similar provisions are provided by most Member States.

The exemption provided for offerings to a limited number of investors is similar to the private placement safe harbor that exists in U.S. securities law. In this case, the definition of "public" already adopted by some jurisdictions such as France and the United Kingdom has served as a reference for the EC provisions. Again, the exemption contained in the Directive is not always followed by Member State securities laws. In Italy, for example, the means of solicitation employed by the offeror may lead to the application of prospectus requirements, regardless of the number of individuals solicited, as long as the offeror seeks an unrestricted search of prospective investors, rather than a face-to-face transaction proposed on the basis of personal negotiations.

The exemption provided for offerings reserved to employees, including former employees, of the issuer may sound unusual in comparison to U.S. standards. In contrast to the EC Directives, leading cases in the United States have held that because an offering is addressed solely to employees does not, by itself, exempt the offeror from public offering regulations.[16] The rationale employed by these cases maintains that employees may not possess sophisticated knowledge of the securities and of the issuer itself and, therefore, may not be able to adequately fend for themselves. At a national level, some Member States exempt offerings to employees from prospectus requirements, subject to certain conditions. In Italy, for example, this type of offering is exempted if the employees to whom the securities are offered are identified in advance and if the securities assigned to each employee may not be transferred to others if the assignee refuses to invest.

Policy reasons, rather than regulatory issues, justify the exemption available for euro-securities. Euro-securities are units for which an underwriting agreement has been entered into

16. Council Directive No. 80/390, *supra* note 1, O.J. L 100/1 (1980).

among the offeror and a pool of underwriters which includes participants from at least two Member States. Euro-securities must be initially acquired only by banks or financial institutions. The euro-securities market has developed significantly in the United Kingdom and in Luxembourg without any particular regulatory constraint. Some commentators argue that the euro-securities exemption was intended to prevent the global placements of euro-bonds from migrating to less regulated international markets.

As mentioned above, the exemption provided for units issued by UCITS is justified by the thorough regulations governing the organization and the marketing of collective investment schemes in the European Union. These entities must register a prospectus in the home jurisdiction in accordance with the standards provided by the Directive 89/298/EEC on prospectuses for public offerings.[17] A simplified registration procedure that entails the cooperation of local regulatory bodies and requires additional disclosure, allows the prospectus to be used in all Member States where the units will be marketed.

D. *The Prospectus For Admission to Multi-State Exchange Listing*

Directive 80/390/EEC,[18] as amended by the subsequent directives, regulates the disclosure obligations, the reciprocal recognition of prospectuses, the choice of first listing jurisdiction, and the exemptions available for securities sought to be admitted to official exchange listings in more than one Member State. The regulation of multi-state listings varies depending on whether the issuer requires admission to listing in several Member States simultaneously or consecutively. For simultaneous or close-in-time listings, the Directive designates the home country of the issuer, if based in the European Union, as the governing jurisdiction. Non-EU issuers may elect any Member State and publish the listing prospectus in accordance with the national laws of the chosen jurisdiction. Once the prospectus is published, all Member States will automatically recognize it as adequate for listing purposes. Special information concerning, *inter alia*, the local market and the tax implications deriving from the new listing, may still, however, be demanded by Member States.

17. Council Directive No. 89/298, *supra* note 5, O.J. L 124/8 (1989).
18. Council Directive No. 80/390, *supra* note 1, O.J. L 100/1 (1980).

The rule of reciprocal recognition also applies where listing is sought for securities already quoted in an EU securities exchange. Local jurisdictions may exempt the issuer from publication of a prospectus, where the particular securities have been traded in the original market for more than three years.[19] The same exemption may be granted where the home-country regulator certifies to the host-country agency that the issuer has consistently complied with disclosure obligations for the last three years or, if shorter, the whole period of listing.[20] These exemptions were introduced by the so-called Eurolist Directive in 1994, and have not yet been implemented by Member States.

An additional exemption is granted by Directive 90/211[21] if a prospectus was published in a Member State within three months of the application for admission to the securities market of another Member State. In this case, that first prospectus will serve as the listing prospectus in the new market, provided that additional information concerning, *inter alia*, the exchange market is added.

E. *Prospectuses For Multi-State Offering*

As mentioned above, the prospectus published in a Member State for public offerings benefits from reciprocal recognition in the other Member States. The choice of jurisdiction for offerings made simultaneously in several Member States follows the same practice required for the listing prospectus. As a general rule, the country where the EU issuer is based serves as the governing jurisdiction. If the issuer is a non-EU entity or the offering is directed toward markets outside the EU issuer's home country, the issuer may choose any of the jurisdictions that will be included in the public offering. Non-EU issuers may submit their prospectus for registration in a Member State that imposes less stringent disclosure or administrative burdens and obtain subsequent recognition of the offering materials in all the other Member States.

Similar to the Directive on listing prospectuses, the Directive on public offering prospectuses provides an exemption for securities that have a listing prospectus published in another

19. *Id.*
20. *Id.*
21. Council Directive No. 90/211, *supra* note 3, O.J. L 112/24 (1990).

Member State. The exemption is triggered if the offering is made simultaneously with the listing or within "a short time."

F. *New Issues on Mandatory Disclosure*

International organizations, including IOSCO,[22] are currently discussing the harmonization of different accounting principles and standards for auditing issuers. The outcome of these deliberations may affect issuers of securities that are subject to disclosure obligations on a continuous basis. Issuers of listed securities and issuers conducting multi-state public offerings who are required to include economic results and accounting documents in their prospectuses will be particularly concerned with the result of these debates.

These discussions stem from the diversity prevalent among internationally accepted accounting principles and audit standards. The adoption of the IV and VII Directives on Corporations concerning the publication of annual financial statements has helped to harmonize certain accounting principles in the EU market. Differences continue to persist, however, within the European Union, as well as between the EU and non-EU jurisdictions. A significant example is the timing of information. For instance, in Italy the financial statements of listed corporations are disclosed every six months, whereas the United Kingdom and the United States require quarterly reports. Additionally, other material principles lack international acceptance and formal recognition by EC Directives.

Thus, the strict disclosure policies espoused by local authorities are offset by inconsistent standards at the international level. This situation presents an especially acute problem for U.S. companies interested in raising capital in the European Union and vice-versa, due to the significant diversity existing between the respective accounting systems. Reconciling financial statements in order to comply with the requirements of each jurisdiction may have a significant impact on the costs of the proposed transactions. At present, adherence to the International Accounting Standards recommended by the International Accounting Standards Committee should save global offerors excessive harmonizing costs.

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22. International Organization of Securities Commissions.

III. *UNDERWRITING AND PLACEMENT PROCEDURES*

An offering in more than one Member State entails the participation of various financial institutions involved in the underwriting, placement, and distribution of the securities. These activities are normally conducted by banks, financial, and investment firms, which are regulated by the Second Banking Directive and the Financial Services Directive. Since the "placement" aspect of a public offering conducted in several countries is particularly important, it is advisable to address the scope of the mentioned directives and the status of their implementation.

A. *The Second Banking Directive and the Financial Services Directive*

These two Directives were adopted by the EC Commission to eliminate the national barriers impeding the offering of banking and financial services on a cross-border basis. The principle underlying the Directives is that an entity that is authorized to conduct banking or financial activities in its home-country should also be permitted to offer its services in all Member States under a "single passport." Comparable national supervision standards are fundamental to this approach. Consequently, the Directives provide license prerequisites, supervision rules, and activity regulations that must be adopted by each national jurisdiction in order to guarantee similar levels of quality and control throughout the European Union.

Mutual recognition of foreign licenses is the logical consequence of the Directives. Banking, financial, and investment services may be offered by Member State banks, financial firms, or intermediaries in other Member States through the establishment of a branch or on a cross-border basis. The implementation of the two Directives, however, has not proceeded at a desirable pace. Whereas the Second Banking Directive has been implemented in all Member States, the Financial Services Directive has a transitional period requiring implementation by the end of 1996. This delay will affect the organizational issues faced by a multi-state offeror, since some non-banking intermediaries participating in global placements may only be admitted to offer, place, or distribute securities in Member States thorough locally licensed subsidiaries.

Additionally, intermediation services offered in jurisdictions other than the home-country must comply with certain proce-

dural requirements, such as notification from the home-country authority to the host-country regulator of the intention to offer cross-border services. These obligations may place large entities, which are characterized by structures with a wide geographic distribution, in a better position than their smaller competitors.

B. *Offering Practices*

For some offering practices, EC harmonization has not been introduced. The regulation of door-to-door offerings, for instance, was omitted from the scope of the Financial Services Directive and, therefore, is governed exclusively by national rules. Many local jurisdictions permit only licensed professionals to solicit public investments door-to-door. Furthermore, a global offeror may not employ its own personnel to distribute the securities offered. Such is the case in Italy, where door-to-door solicitation may only be carried out only by licensed sales representatives employed by an Italian investment firm.

CONCLUSION

The offering of securities used to be a domestic exercise until fifteen years ago. Now international securities offerings have become the rule. The internationalization of the economy brought about a globalization of capital markets. The aim of the EC regulations is to provide a level playing field for cross-border offerings throughout Europe in order to foster further growth and access to international capital markets.