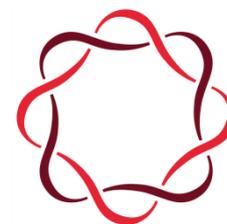


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**FINANS
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Finance Denmark's response to COM consultation: Building a proportionate regulatory environment to support SME listing

Hørings svar

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Facilitating access to finance for SMEs through all their development stages is a key element of the Commission's Capital Markets Union (CMU) initiative. This is the reason why the Commission launched a consultation on 18 December 2017 with deadline on 26 February 2018 in order to help the Commission identify ways to cut red tape and build a supportive environment for SMEs wanting to list their shares or bonds on SME Growth Markets, without jeopardising investor protection and market integrity. In short, the consultation seeks to identify how the 'SME Growth Market' concept, created by MiFID II, can be further improved. Furthermore, the aim of the consultation is also to identify areas where the administrative burden placed on listed SMEs can be lightened and where some targeted regulatory changes could help (re)build the local ecosystems surrounding SME-dedicated exchanges.

The Danish Financial Authority (Finanstilsynet) has requested input from the sector by 22 January 2018 in order to prepare a Danish response to the consultation.

Finance Denmark welcomes the consultation and presents various proposals to support increased financing of SMEs through the capital markets.

Firstly, Finance Denmark supports in general the Commission's initiatives to create improved framework for the financing of SME. Unless otherwise specified, our response includes SME financing through Initial Public Offerings (IPOs) as well as financing through corporate bonds.

In general, on the supply side, Finance Denmark primarily considers market driven barriers as obstacles for the development of more efficient SME markets. On the

demand side, the regulation constitutes an increasing obstacle for efficient SME markets.

Finance Denmark has the view that a considerable amount of potential SMEs consider the capital market as unattractive due to the high initial costs as well as running costs (see examples below).

As we do agree that efficient SME-markets may not emerge at the expense of investor protection, the potential deregulation should not compromise the quality of SME securities, but focus on easier access and distribution of the securities.

The new EU rules on packaged retail investment products (PRIIPs) and the MiFID II rules on product governance are examples of EU-regulation both increasing the costs of distribution of SME securities and limit the access to SME financing through the capital markets. The reasoning is that investment banks are imposed new obligations and risks for the production and distribution of SME-issued securities that in reality will limit the distribution to non-professional investors (retail investors).

PRIIPs has left uncertainty as to which extent corporate bonds are a PRIIP. The primary intention of PRIIPs was to ensure that packaged products produced by investment firms, fund management firms and insurance firms were subject to increased information requirements, which the industry welcomed. However, the regulation is very broad and it is our understanding that corporate issuers also are covered by PRIIPs, which has led to uncertainty when corporate issuers are also covered. This has again led to many corporate issuers feeling forced to restrict their issues of corporate bonds from the retail segment as the corporate issuers cannot handle keeping a PRIIPs KID updated. In our experience, primary and secondary SME market activity is highly interconnected. A clear statement on the use of PRIIPs on corporate bonds should be issued. In this connection, it should be recalled that complexity and being packaged are not synonyms and that investment firms still has a responsibility to handle investor protection including appropriateness test.

The new product governance requirements in MiFIDII/MiFIR make it difficult to investment firms to market and/or recommend corporate bonds and unlisted equity from SMEs. The requirement to product governance arrangements makes it difficult to market SME securities as the rules on product governance are designed to handle financial instruments issued/produced by the financial industry, which may have unintended, negative effect on the SME issuance activity.



Retail-investors are in most markets – and also in the Danish market – an important distribution channel for SME securities, which most often face a local interest and will lack adequate liquidity and size to attract interest from the professional/institutional investor segment. The reason is that the capital concentration in the institutional/professional segment hampers the ability for these investors to engage in SME investments as they operate with investments of a certain size, which most often exceeds a reasonable size of investment without becoming a (too) significant investor in a particular SME.

Another example of EU-rules, which potentially imposes SME securities unproportioned burdens, is the Market Abuse Regulation (MAR) sounding-rules. Potential unintended consequences of these rules for corporate bonds are actually identified as barriers in the *Report from the Commission Expert Group on Corporate Bonds* from November 2017 ("Improving European Corporate Bond Markets"¹).

Increased demand after SME securities can be supported by removal of such barriers and through incentives to investors to focus on SME in their investments. As an example, the capital requirements for institutional investors will normally limit the incentive to invest in SMEs. Other potential regulative adjustments can be:

- Allow exemption from the credit rating agency regulation (CRA), thereby investment banks and other financial advisors can provide internal rating and other financial advisors may perform an internal valuation of SMEs which in their startup phase cannot finance a formal rating.
- Limit the regular flow of disclosure of regulated information and the dissemination of such information to the public to a minimum – i.e to publish the annual report, inside information, information of the management trading activities. Other obligations for issuers in relation to transparency requirements are abandoned until the company reaches a certain size.
- Introduce a distinction of retail investors (investors other than institutional and financial investors and very large corporations) between sophisticated investors (e.g. private wealth clients) and other investors (e.g. consumers). The present rules applicable to distribution of securities do not allow such distinction, which in practice limit access to distribute SME securities to significant retail investor segments.

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<http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetailDoc&id=35759&no=1>



As for question 10, "key adviser requirements", such an advisory requirement will most likely imply additional burdens and responsibilities for the investment firms compared with today. The advisory functions in connection with SME issuance are subject to cooperation between issuers, investment firms, lawyers and chartered accountants, which individually are subject to professional liability. To the extent, the role as Key Advisor will change the existing division of labour for the professional advisors in connection with SME counselling, it may affect the advisors' risk profiles.

Kind Regards

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