European Commission - Fact Sheet

Frequently asked questions: Easier access to financing for smaller businesses through capital markets

Brussels, 24 May 2018

What is the Commission proposing and why?

A core aim of the Capital Markets Union is to give better access to market-based sources of financing for EU companies at each stage of their development. Newly-listed SMEs are a key motor of new investment and job creation. Recently-listed companies often outstrip privately-owned companies in terms of annual growth and job creation. For example, between 2006 and 2012, companies that listed their shares on First North Stockholm increased their workforce by 17% annually after the initial public offering (IPO), compared to an annual growth of 5% for all private companies in Sweden.

This is why the Commission is today proposing targeted amendments to EU rules for companies listed on SME Growth Markets, a recently-created category of trading venues. This is one of the numerous measures presented by the Commission since the launch of the CMU in 2015 to improve SMEs' access to market-based finance.

The proposed rules aim to reduce the administrative burden and cut red-tape faced by smaller companies, therefore fostering liquidity of these markets. However, they have been carefully calibrated to preserve the core principles of EU rules that were established to restore confidence in financial markets after the financial crisis (investor protection and market integrity).

By listing on public markets, companies can diversify their investor base, gain easier access to equity capital and debt finance, raise their public profile and increase brand recognition. Despite the benefits of stock exchange listings, EU public markets for SMEs struggle to attract new issuers. Of the 20 million SMEs in Europe, only 3,000 are listed on stock-exchanges. Currently, levels of SME initial public offerings are half of those before the financial crisis. This is partially due to high compliance costs on the one hand and insufficient liquidity on the other. Insufficient liquidity means that cost of capital is higher for SMEs, and that it is more difficult for investors to buy and sell SME shares.

Today's initiative comprises: (i) a proposed regulation which amends certain technical rules in the Market Abuse Regulation ('MAR') and the Prospectus Regulation, and (ii) envisaged technical amendments to delegated acts (also known as "level 2" measures) under the Markets in Financial Instruments Directive (MiFID II).

What are SME Growth Markets and why is the proposal limited to that type of trading venue?

SME Growth Markets are a new category of trading venue created by the Markets in Financial Instruments Directive II (MiFID II) to facilitate access to capital for smaller and medium-sized companies. They are defined as Multilateral Trading Facilities (a type of trading venue) where at least 50% of issuers are SMEs. EU rules - such as the recent Prospectus Regulation, the Central Securities Depositary Regulation and the European Venture Capital Fund Regulation - already provide SME Growth Market issuers with regulatory benefits or alleviations.

All companies listed on SME Growth Market will benefit from the regulatory alleviations. This will enable SME Growth Markets to attract both SMEs and non-SMEs, thereby fostering liquidity and profitability of this type of platforms. Applying the same set of rules to all SME Growth Market issuers will also ensure that companies are not penalised because they are growing and they are not deemed SMEs anymore.

These proposed alleviations will be limited to SME Growth Markets and will not be extended to SMEs listed on regulated markets. Otherwise, investors will be faced with a complex situation whereby companies listed on the same stock exchange are subject to two different sets of rules (alleviated requirements for SMEs, and normal requirements for all other companies). It is important that all companies listed on the main stock exchange comply with the same rules and standards.

How do the proposals fit into the Commission's work to support SME access to public markets?

Reducing dependence on bank financing and broadening access to market-based sources of financing for EU companies at each stage in their development is at the heart of the Capital Markets Union Action Plan. In this context, the Commission has already implemented a comprehensive package of measures to scale-up venture capital financing in Europe. It has also presented a proposal for a Regulation on crowdfunding services providers to improve access to this innovative form of finance for both investors and businesses.

In the Mid-term review of the CMU Action Plan, the Commission strengthened the focus on SME access to public markets. The Commission has also decided to set in motion a series of non-regulatory measures to revive public markets for SMEs. For instance, the Commission will shortly launch an external study to assess the potential impact of MiFID II rules on SME research coverage. The Commission is also exploring how EU financial support could help SME Growth Market issuers, notably at the initial public offering stage.

How will the proposals contribute to making this new type of trading venues more attractive?

Among the 40 Multilateral Trading Facilities (MTFs) with a focus on SMEs across the EU, only three have been registered as SME Growth Markets so far. This initiative will facilitate the registration of MTFs as SME Growth Markets further by amending the implementing measures (the Commission Delegated Regulation) under MiFID II:

- **Replacing the current definition of an SME issuing only bonds** by a simple 'issue size' criterion, i.e. EUR 50 million over a 12-month period. The current definition of SMEs is not suitable for companies issuing bonds. The change will facilitate the registration of trading venues (specialised in SMEs bonds or allowing both bond and share issuances) as SME Growth Markets. In turn, this will allow more listed companies to benefit from alleviations targeting SME Growth Market issuers.
- **Giving more flexibility for SME Growth Market operators on whether to impose the obligation to produce semi-annual reports on SME debt-only issuers.** Currently SME Growth Market debt-only issuers have to produce a semi-annual financial report. This is a more stringent requirement than the one applying to issuers of bonds to professional investors on regulated markets.

How is the Commission cutting red-tape?

The proposals amend MAR and the recently-adopted Prospectus Regulation by lowering the obligations placed on SME Growth Market issuers while preserving market integrity:

- **Insider lists:** The proposal limits the current obligation to produce lists of persons who have access to price-sensitive information ('insider lists'). Issuers on SME Growth Markets would only have to produce lists of a more limited group of people having regular access to inside information ('permanent insiders'). This alleviates the administrative burden on SMEs while ensuring that competent authorities preserve their ability to investigate cases of insider trading in order to ensure market integrity.
- **Managers' transactions:** The proposal will ensure that SME Growth Market issuers have sufficient time to disclose managers' transactions to the market. They will now have two days to declare the transactions to the public, counting from notification by the managers (who, in turn, will still have three days to notify their transactions to their employers);
- **Delay in disclosing inside information:**The proposal reduces the obligations currently imposed on SME Growth Market issuers when they decide to delay the publication of inside information. SME Growth Market issuers would only be held liable to justify the reasons for the delay upon the request of their National Competent Authority (instead of doing so in all circumstances). Besides, SME Growth Market issuers will be exempted from the obligation to keep records of those justifications on an ongoing basis.
- **Private placements of debt:** This is a type of funding where the funding is raised through a private offering to a small number of chosen investors, instead of an offer of bonds to the public. The proposal exempts privately-placed bonds (a) from the 'market sounding regime' if an alternative is in place. Market sounding is where information is given prior to the announcement of a transaction in order to gauge the interest of potential investors. This alleviates burdens on issuers and investors and thus facilitates private placement issuances.

What will change for SMEs when it comes to prospectus rules?

Recent rules agreed at the EU level overhauled and simplified prospectus rules to make it easier for firms to tap Europe's capital markets. But one remaining regulatory impediment for companies is the obligation to draft a full-blown prospectus when the shares are admitted to trading on a regulated market (i.e. a main stock exchange). Today's proposal goes even further than the already-agreed new rules. A new category of prospectus called a 'transfer prospectus' will allow issuers with at least three years of listing on SME Growth Markets to produce a lighter prospectus when transferring. This simplification should help growing companies listed on SME Growth Markets, very few of which actually graduate to the regulated markets. Successful companies should be encouraged to transfer from SME Growth Markets to the main stock exchange, thereby benefitting from greater liquidity and a larger investor pool.

How will this initiative contribute to the liquidity of SME shares?

Insufficient liquidity on public markets for SMEs raises the following issues:

- issuers can face higher costs for raising capital;
- investors can be reluctant to invest in SMEs if liquidity is low; and
- market intermediaries whose business models relies on liquidity (because they profit from buying and selling shares) are not incentivised to support small listed companies because it is less economically attractive for them to do so.

Today's proposals aim at ensuring a minimum level of liquidity on SME Growth Markets through two mechanisms.

First, the proposal creates a common set of rules on **liquidity contracts** for SME Growth Markets in all Member States which will co-exist with current national practices. A liquidity contract consists in an issuer entering into an agreement with a financial intermediary (a bank or an investment firm), whereby the financial intermediary buys and sells shares of and on behalf of the issuer. By so doing, the financial intermediary enhances the liquidity of the shares. Liquidity contracts are powerful instruments to ensure minimum liquidity and reduce volatility of SME shares. EU-wide rules on liquidity contracts will allow issuers in all SME Growth Markets to benefit from them.

Second, the proposed rules will require that a minimum proportion of shares of SME Growth Markets issuers are allowed to be actively traded by investors in the market. Market operators will have the flexibility to adapt those requirements to local conditions. The proposal should increase investor confidence in this asset class.

Will the proposal lower investor protection and market integrity?

Today's proposals do not change core principles of EU rules that were established to restore confidence in financial markets after the financial crisis. They have been carefully calibrated to preserve investor protection and market integrity. Investors will be able to access the same quantity and quality of information. For instance, SME Growth Markets will still be under the obligation to disclose all price-sensitive information to the public. Allowing for the possibility to exempt debt-only issuers from producing biannual reports would establish a level the playing-field with regulated markets, where this is already possible. The proposed changes to MAR would preserve the ability of national competent authorities (NCAs) to investigate or identify risks of market abuse.

The proposal at a glance

Now	**With the proposal**
SMEs must comply with high recording and disclosure obligations to prevent market abuse	More streamlined administrative burden that maintain market integrity and information to investors
Full 'prospectus' for companies wanting to move from an SME Growth Market to a regulated market	Lighter 'prospectus' more suited to SMEs that have already been listed on an SME Growth Market
Inadequate definition of debt-only issuers prevents markets to register as SME Growth Markets and use the alleviations available	New definition of SMEs in bond markets will facilitate the registration as SME Growth markets and open up these markets to more companies
Liquidity contracts cannot be used by SMEs in all Member States	New set of common rules on liquidity contracts for SME Growth Markets (in addition to potential national accepted market practice in Member States)

What preliminary work has the Commission conducted?

The proposal is the result of workshops, research and stakeholder consultations. A public consultation on building a proportionate regulatory environment to support SME listing was organised between

December 2017 and February 2018. The proposal also builds on the results of the 2015 CMU public consultation, the 2015 Call for Evidence on the regulatory framework for financial services and the 2017 CMU Mid-term review public consultation.

Four workshops were conducted in 2016 and 2017 with representatives of securities-exchanges, issuers, investors, brokers, accounting firms, credit rating agencies and public institutions. The Commission also had exchanges with Member States in November 2017 and April 2018 through the Expert Group of the European Securities Committee.

What are the next steps?

The proposal for a regulation, which brings technical amendments to the Market Abuse Regulation and the Prospectus Regulation, will now be discussed by the European Parliament and the Council.

As of today, the draft Delegated Commission Regulation is subject to a 4-week feedback period. After its adoption by the Commission, a six-month scrutiny period by the Council and the European Parliament will follow.

For more information

Press release

More information on SME listing

MEMO/18/3728

Press contacts:

Vanessa MOCK (+32 2 295 61 94)
Letizia LUPINI (+32 2 295 19 58)

General public inquiries: Europe Direct by phone 00 800 67 89 10 11 or by email