

# WHAT SECURITIES LITIGATORS NEED TO KNOW ABOUT THE NEW PROSPECTUS REGULATION

24 July 2019 | London  
Legal Briefings

---

The new [EU Prospectus Regulation](#) (EU/2017/1129) (the “**PR**”) entered into full force and effect on 21 July 2019 across EU Member States. It replaces, in its entirety, the Prospectus Directive (the “**PD**”) regime and therefore represents the most significant overhaul of European securities law since the PD came into force in 2005.

A number of the changes will have a direct impact on claims under s.90 Financial Services and Markets Act 2000 (“**FSMA**”) for liability for prospectuses and listing particulars published after the relevant change took effect (some of the PR’s provisions came into force prior to 21 July 2019). We highlight below some of the key changes introduced by the PR which are likely to be of most interest from a securities litigation perspective.

## KEY CHANGES FROM A SECURITIES LITIGATION PERSPECTIVE

### *Disclosure requirement*

The general disclosure requirement for prospectuses under the PR remains broadly the same as under the PD. It remains, fundamentally, the 'necessary information' test, but now helpfully includes an express materiality standard: “*the necessary information which is material to an investor for making an informed assessment of*” various matters including assets, liabilities, profits and losses of the issuer, the rights attaching to securities and the reasons for the issuance and its impact on the issuer (Article 6(3) PR, emphasis added).

From a litigation perspective, s.90 FSMA has been amended by the PR to import the materiality threshold in the context of such claims. In the absence of judicial guidance, it had generally been assumed that there was a materiality standard, and that a trivial omission or misstatement would not give rise to issuer liability. However, this clarification will be welcomed by issuers.

It is perhaps regrettable that the European Commission has not taken this opportunity to clarify the meaning of an 'investor'. It therefore remains the case that it is unclear what characteristics, knowledge and experience the hypothetical investor should be imbued with for the purpose of the 'necessary information' test; or whether the application of that test is affected if the prospectus was targeted at institutional investors rather than including a retail offering.

### *Risk factors*

One of the main changes brought in by the PR regime concerns the presentation of risk factors, the most relevant of which from a disputes perspective being in relation to specificity, materiality and mitigation:

- **Specificity:** Article 16(1) PR requires that risk factors in prospectuses must not be general in nature, but instead be specific to the issuer or the securities covered by the prospectus.
- **Materiality:** Article 16(1) PR further specifies that the issuer must "*assess the materiality of the risk factors based on the probability of their occurrence and expected magnitude of their negative impact...*" to allow investors to understand the relative weights which should be attached to those risks. The PR provides that the issuer has the option to rate the relevant risk as low, medium or high (although our expectation is that issuers will avoid making a qualitative assessment in this way given the obvious increase in the risk of liability).
- **Mitigation:** Article 16(4) required [ESMA to develop guidelines on risk factors](#), which contain an interesting description of the balance between overuse of mitigation at the risk of underplaying the risk (on the one hand) and underplaying the mitigants which are in place, at the risk of overstating the risks and discouraging investment (on the other).

Risk factors invariably play an important role in any subsequent litigation, particularly where risks that have been identified have come to pass after the publication of the prospectus in question. The key battleground will often be whether the risk factors were sufficiently specific to have alerted investors.

### **FOR MORE INFORMATION**

Our Capital Markets colleagues have prepared a short and helpful [webinar](#) to highlight the key changes to the PR regime, which you can access via the link. This webinar is part of a series considering the developments in this area.

If you would like more detail on any of the above, or more generally about the key changes introduced by the PR, then please see below links to six short briefings prepared by our Capital Markets team. The briefings cover:

- [Exemptions from the requirement to produce a prospectus](#);
- [Summaries and key financial information](#);
- [Risk factors](#);
- [Disclosure and format](#);
- [Approval and publication requirements](#); and
- [Advertisements and supplements](#).

## KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



**SIMON CLARKE**  
PARTNER, LONDON

+44 20 7466 2508  
Simon.Clarke@hsf.com



**HARRY EDWARDS**  
PARTNER,  
MELBOURNE

+61 3 9288 1821  
Harry.Edwards@hsf.com



**CERI MORGAN**  
PROFESSIONAL  
SUPPORT  
CONSULTANT,  
LONDON

+44 20 7466 2948  
Ceri.Morgan@hsf.com

---

# LEGAL NOTICE

The contents of this publication are for reference purposes only and may not be current as at the date of accessing this publication. They do not constitute legal advice and should not be relied upon as such. Specific legal advice about your specific circumstances should always be sought separately before taking any action based on this publication.

© Herbert Smith Freehills 2020

---

**SUBSCRIBE TO STAY UP-TO-DATE WITH LATEST THINKING, BLOGS, EVENTS, AND MORE**

Close

© HERBERT SMITH FREEHILLS LLP 2020