

# Chapter 3

## Corporate Finance and the Quality of Financial Disclosure

*The AMF lays down conduct of business rules for issuers offering securities to the public. It regulates and supervises all transactions involving financial instruments placed through public offers, including through takeover bids. The AMF also ensures that issuers make full, fair and timely disclosure of high quality information to all market participants.*

*The fields of corporate finance and financial disclosure were affected by several major regulatory and legal developments in 2005. These included a new statute transposing European financial legislation into French law, as well as the Economic Modernisation and Confidence Act, new legislation on takeover bids, and amendments to the AMF's General Regulation. In addition, the four working groups created by the AMF in 2004 completed their missions.*

*During 2005, the AMF continued working to improve market transparency through clear, fair and precise reporting and strict enforcement of accounting rules. It focused particularly on the quality of issuers' ongoing disclosures, not hesitating to litigate where necessary. It also closely monitored the quality of information provided to shareholders during takeover bids. None of the takeover bids launched in 2005 led the AMF to issue a new interpretation of the principles governing takeovers, but it did have to clarify the scope of its General Regulation in certain cases.*

### 1 Regulatory Developments

#### A The Economic Modernisation and Confidence Act

The Economic Modernisation and Confidence Act (2005-842) is designed to modernise companies' operating rules by facilitating access to bank financing and financial markets and by strengthening the confidence of investors and consumers.

The act alters the legal environment in which companies operate. It enables them to hold board meetings using modern telecommunications technologies that enable directors to be identified and participate effectively. Directors who attend meetings electronically are considered to be present for the purposes of quorum and majority requirements. However, boards of directors and supervisory boards must meet in person at least once a year to review the company's annual and consolidated financial statements. The new law also lowers quorum thresholds, making it easier to hold ordinary and extraordinary shareholders' meetings. Furthermore, it implements the European Company Statute and amends France's commercial code and labour code in order to transpose the directive intended to involve these companies' employees in labour-related decisions.

The act also sets periodic reporting requirements for issuers with financial instruments admitted to trading on a regulated market.

In accordance with the Prospectus Directive, the act stipulates that issuers for which the AMF is the competent authority for prospectus approval "shall at least annually provide a document that contains or refers to all information that they have published or made available to the public over the preceding 12 months in one or more Member States and in third countries in compliance with their obligations under Community and national laws and rules dealing with the regulation of

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securities, issuers of securities and securities markets." These provisions, which take effect immediately, were reinforced by Article 221-1-1 of the General Regulation, requiring that the document be submitted to the AMF no later than 20 days after the company publishes its provisional financial statements in the official gazette, that it be made available to the public under the same conditions as the registration document, and that it be posted on the issuer's website, if any. Moreover, this document can be incorporated into the issuer's registration document.

In accordance with the Transparency Directive, the Economic Modernisation and Confidence Act also directs the AMF to supervise the publication and filing of periodic information, i.e. the annual and half-year financial reports of French companies issuing shares or debt securities with a denomination per unit less than €1,000 that are listed on a regulated market. Issuers of debt securities with a par value greater than €1,000 that are admitted to trading on a European regulated market may choose a competent authority from among the countries in which its securities are listed. The terms of this choice are established by the AMF General Regulation in accordance with the provisions of the Transparency Directive. This framework will take effect in its entirety before 20 January 2007.

The act introduced four new major holding thresholds – 15%, 25%, 90% and 95% - to keep the market better informed. Pursuant to the Transparency Directive, in addition to shares and voting rights owned by the reporting entity, the disclosure requirements now encompass shares of which it has the life interest, as well as shares and voting rights owned by a third party with which the entity has a lending agreement. By contrast, disclosure obligations have been adjusted and relaxed for cases where a threshold is breached by an action that is in no way intended to influence a company's strategy, e.g. arbitraging and proprietary trading by investment companies for their trading book. The changes made to Articles L. 233-7 *et seq.* of the commercial code took effect immediately. The implementing provisions that are to be included in the General Regulation were put out for public consultation until 30 March 2006.

The act also alters the definition of offers of securities to the public by eliminating small offerings (less than €100,000, or between €100,000 and €2,500,000 if the financial instruments represent less than 50% of the issuer's share capital) and offerings that are reserved for qualified investors, either because the denomination per unit of the financial instruments is at least €50,000 or because of the size of the minimum investment (€50,000 per investor and per transaction). It also simplified the definition of a restricted circle of investors by limiting it to groups of persons, the number of which is below a threshold set by ministerial order.

## **B** **Tranposition of the Prospectus Directive**

In addition to the statutory amendments resulting from the Economic Modernisation and Confidence Act, Title I of Book II of the AMF General Regulation was recast following the transposition of the Prospectus Directive into French law. The new regulation was ratified by the ministerial order of 1 September 2005.

### **1** **Jurisdiction of the AMF**

The act alters the territorial jurisdiction of the AMF, which is now responsible for approving prospectuses for public offerings of equities, securities giving access to capital, or debt securities of French issuers whose denomination per unit is less than €1,000. For debt securities with a denomination per unit in excess of €1,000 or financial instruments giving access to the capital of a company other than the issuer, the competent authority may be chosen on the basis of the country where the issuer has its registered office or the country where the issue will take place. Lastly, the act stipulates the conditions under which the AMF approves prospectuses and can suspend or halt any issue subject to its approval when public disclosure does not meet the appropriate standards. The AMF still has the power to oversee promotional materials for offers of securities to the public in France.

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## **2 Content of the Prospectus**

Broadly, the existing framework has not been overhauled, but some aspects relating to the content of the prospectus have changed. In accordance with the Prospectus Directive, the Economic Modernisation and Confidence Act states that the prospectus published at the time of an offer of securities to the public must include a summary note; it also restricts the instances in which this note alone can be the basis for civil liability action.

There is no change to the form of the prospectus, which remains either a single document or a registration document accompanied by an offer document. Issuers will still be allowed to incorporate information by reference. Where a public offering is made in France, the prospectus must be written in French. However, for some types of debt security or in cases where the issuer's registered office is in another country and the offering is limited to employees of its French subsidiaries, the issuer may produce the prospectus in English and translate the summary note into French. Similarly, for issuers seeking admission to a regulated market in France, the prospectus must be either written in French or be written in English, with a French translation of the summary note.

The prospectus format must comply with the schedules and building blocks referred to in European Regulation 809/2004 of 29 April 2004, implemented directly in French law on 1 July 2005. The AMF built on this framework with the publication of Instruction 2005-11 of 13 December 2005 on disclosure requirements for offers of securities to the public. The instruction lists the documents that must be filed for examination by the AMF, along with the draft prospectus, registration document or base document, and specifies the information that must be disclosed to benefit from the waivers provided for in Articles 212-4 and 212-5 of the General Regulation.

The AMF is no longer able to include a warning when it approves a prospectus. However, promotional materials must include a statement calling readers' attention to the "risk factors" section of the prospectus, as well as a more specific warning, if requested by the AMF.

## **3 Distribution of the Prospectus**

The prospectus must now be distributed in one of the following formats<sup>1</sup>:

- published in the print media ("*nationally distributed or widely distributed publication*"); or
- available free of charge at the issuer's registered office or from the market operator; or
- posted on the issuer's website, the website of the regulated market or the websites of the financial intermediaries that are placing or dealing the financial instruments in question.

If the prospectus is made available free of charge or web-posted, the issuer must also publish a summary in the print media or issue a press release (making sure that it is fully and effectively published) explaining exactly how the prospectus may be obtained. If the prospectus is published in the print media or made available free of charge, it must also be posted online on the issuer's website if such a site exists. In any case, the prospectus must be posted on the AMF's website.

## **4 The European Passport**

Issuers may now use a prospectus approved by the competent authority in one Member State of the European Union for an offer of securities to the public in all Member States. The passport

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<sup>1</sup> Article 212-27 of the AMF General Regulation.

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mechanism requires only that the competent authority that approves the prospectus must notify the competent authority of the host Member State in which the securities will be offered. A certificate of approval will confirm that the prospectus has been produced and approved in compliance with the directive. This notification process will comply with a procedure established by the Committee of European Securities Regulators (CESR). At the same time, the prospectus must be translated into a language that is customary in the sphere of finance or accepted by the host Member State, at the issuer's discretion.

## **C Finalising the Transposition of the Market Abuse Directive**

### **1 Disclosure of Dealings in Securities by Managers and Persons Cited in Article L. 621-18-2 of the Financial and Monetary Code**

The DDAC Act (no. 2005-811, 20 July 2005) transposed various aspects of EU financial legislation into French law. It finalised the transposition of the Market Abuse Directive and set the framework for implementing the Markets in Financial Instruments Directive (MiFID).

The AMF General Regulation, published in the Official Journal of 24 November 2004, already transposed many of the directives' provisions in French regulations. However, some provisions required legislative amendments. The DDAC Act introduces several measures to enhance the quality of financial information, step up the prevention of insider dealing and introduce harsher penalties for market manipulation.

Regarding the disclosure rules for directors' dealings in their company's securities, the DDAC Act extends the reporting requirement to senior executives who have power to make management decisions regarding the company's development and strategy and who have access to inside information concerning the issuer. Moreover, directors, senior executives and persons closely connected to them are now required to report their transactions to the issuer and the AMF. The AMF is responsible for informing the public of these transactions.

Articles 222-14 and 222-15-3 of the General Regulation, ratified by a ministerial order issued on 9 March 2006 published in the Official Journal on 21 March 2006, stipulate that these disclosures must be sent to the AMF electronically within five days of the transaction. The trade confirmation must also be sent to the AMF within five days by the person filing the report or by his custodian. These reports are posted on the AMF's website.

Issuers must keep an updated list of directors and senior managers that meet the above criteria and must make it available to the AMF.

Issuers must also include a summary of these dealings in the annual report presented at the general meeting of shareholders.

AMF Instruction 2006-05 of 3 February 2006 provides a standard format for this type of declaration.

### **2 The insider List Requirement**

The DDAC Act also adds a new article to the Financial and Monetary Code. Article L. 621-18-4 requires issuers to maintain an updated list of persons working with the company and having access to inside information directly or indirectly relating to it, as well as third parties with access to such information because of their professional relationship with the company. These third parties are also responsible for drawing up their own list of persons with access to inside information.

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The AMF published a position paper<sup>2</sup> on insider lists on 18 January 2006 in order to clarify the meaning of "persons working with the company" and "third parties having access to inside information because of their professional relationship with the company". The paper coincided with the publication in the Official Journal of the ministerial order of 30 December 2005, which ratified the amendments to the General Regulation specifying how insider lists are to be kept and made available.

Articles 222-16 and 222-20 of the General Regulation specify in particular the content of insider lists and the circumstances in which they must be updated. These lists are provided to the AMF upon request and must be kept on record for five years from the date on which they were created or updated.

### **3 Regulatory Developments Involving Share Buy-backs**

The AMF has recognised two accepted market practices related to share buy-backs<sup>3</sup>: the use of liquidity agreements and the acquisition of shares for future use as consideration in acquisitions. The Market Abuse framework directive allows a company to engage in activities or practices already accepted on its market, provided they do not constitute market manipulation and they meet a list of criteria set in Directive 2004/72/EC of 29 April 2004 implementing the framework directive.

In addition, under the Economic Modernisation and Confidence Act (2005-842) of 26 July 2005, the AMF is no longer responsible for certifying offer documents for share buy-back programmes. Public disclosures are now made through a document whose content and method of distribution are determined by the AMF General Regulation<sup>4</sup>. The document, which is not required to contain as much information as a simplified prospectus, is called a "programme description" and must be published before a share buy-back programme is implemented. It is to be published in the same manner as a registration document, i.e. made available free of charge to the public and posted on the AMF's website.

The General Regulation provides issuers an exemption, under certain conditions, from publishing all or part of the programme description for the share buy-back. A partial exemption is granted where an issuer publishes a special report for its general meeting of shareholders as defined in Article L. 225-209 of the commercial code. This report contains historical data about the previous buy-back programme, so this information need not be repeated in the description of the new programme. A total exemption is granted where the issuer publishes a special report for its general meeting of shareholders that includes all the information to be included in the programme description, or if it incorporates that information into a registration document.

## **D Developments Affecting Takeover Bids**

Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids was required to be transposed by 21 May 2006 at the latest. With a view to transposing the directive in France, the finance minister commissioned Jean-François Lepetit, former chairman of

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<sup>2</sup> Available on the AMF's website under the heading Texts -> AMF Positions (*in French only*).

<sup>3</sup> Decision of 22 March 2005, whereby acquisitions of a company's own shares for future use as consideration or in exchange for other securities in an external growth transaction are recognised by the AMF as an accepted market practice. Decision of 22 March 2005, whereby the use of liquidity agreements is recognised by the AMF as an accepted market practice.

<sup>4</sup> Article 241-1 *et seq.* of the General Regulation amended by the ministerial order of 30 December 2005. As a result, modifications were made to AMF Instruction 2005-06 dealing with the information that issuers must disclose and make public when conducting a share buy-back programme and reporting schedules for transactions intended to stabilise the price of a financial instrument, and to AMF Instruction 2005-07 dealing with the terms governing an issuer's sales of its own shares acquired before 13 October 2004.

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the COB and the CMF, to examine the choices offered by the directive and the ensuing consequences. The law<sup>5</sup> passed on 31 March 2006 generally follows the Lepetit proposals.

Once the law had been enacted, the AMF was responsible for implementing the directive through its General Regulation. To this end, the AMF creating a working group in October 2005 headed by two AMF Board Members, Claire Favre and Dominique Hoenn, to draw up a draft text.

The working group's deliberations focused on the points that were the most awkward to transpose, notably where the directive offered several interpretations or options. The group also took into account the AMF's deliberations from 2005 on financial valuations and fairness opinions with respect to mergers and takeovers<sup>6</sup>. Furthermore, it issued its opinion on the conditions for implementing the mandatory declaration of intent by any person or entity preparing to launch a takeover bid.

Once this work was completed, the AMF issued a call for comments from the financial industry on a draft reform of its General Regulation in second-quarter 2006.

In addition, the Economic Modernisation and Confidence Act<sup>7</sup> stipulates that "any takeover bid [...] must, when the bid relates to a company which holds more than one third of the capital or voting rights of a French or foreign company having equity securities which are admitted to trading on a regulated market of a European Economic Area Member State or an equivalent market governed by a foreign legal system and constitute an essential asset of the company holding them, be accompanied by documents which prove that an irrevocable and fair takeover bid has been, or will be, filed for all of the controlled company's capital, or for a portion constituting an essential asset, by the opening date of the initial takeover bid at the latest". The implementation measures in the AMF General Regulation were put out for public comment until 30 September 2005. They were then written into the draft changes to the General Regulation submitted for consultation in second-quarter 2006.

## **E** Obligations of Issuers Listed on Alternext

When Euronext Paris launched Alternext<sup>8</sup> on 17 May 2005, the General Regulation was changed to reflect the specific characteristics of this exchange-regulated market.

Companies seeking an Alternext listing can choose between two procedures:

- a direct listing following a private placement of at least €5 million. In this case, companies must produce an offering circular, which is not submitted to the AMF for approval;
- an offering that effectively places at least €2.5 million in public hands. Because this qualifies as an offer of securities to the public, the company must produce a prospectus that is approved by the AMF. Under the market's rules, once their shares are admitted to trading on Alternext, all companies are subject to periodic disclosure requirements, including the release of annual and half-year accounts; they must also disclose potentially price-moving events, such as major holdings of 50% and 95%.

However, unlike companies choosing the second option, companies that list through a private placement are not subject to the requirements applicable to entities offering securities to the public, particularly as regards ongoing disclosures. In addition, the provisions of Book VI of the General Regulation on market abuse apply to transactions on Alternext.

Furthermore, the Economic Modernisation and Confidence Act amended Article L. 433-3 of the Financial and Monetary Code dealing with the requirements for filing a proposed takeover bid and

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<sup>5</sup> See Chapter 7

<sup>6</sup> See Chapter 7

<sup>7</sup> Amended by the Takeover Act of 31 March 2006.

<sup>8</sup> See Chapter 4

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empowered the AMF to arrange a standing offer on non-regulated markets. As a result, the act extends the scope of the AMF's General Regulation (Book II, Title III, on takeover bids) to standing market offers for financial instruments admitted to trading on an organised, multilateral trading facility such as Alternext.

## **F** General Principles on Warrants and Complex Debt Securities

With the implementation of the Prospectus Directive, an issuer of complex financial instruments – i.e. instruments that are index-linked or have an embedded option<sup>9</sup> – is entitled to submit its prospectus for approval to the competent authority of its choice<sup>10</sup>. If its prospectus is approved, it may then go ahead with the public offering and/or apply for the financial instrument to be listed in one or more EU countries, simply notifying the host-country competent authority of its certificate of approval. For this reason, it was important to adopt standards and a supervisory framework that would ensure equal treatment for AMF-approved and passported products.

To this end, the AMF revisited its General Principles<sup>11</sup> on warrants and complex debt securities, first published in March 2002. The main thrust of the reform was to apply the General Principles to the rules governing the marketing of these types of financial instrument, i.e. any public offering in France and/or admission to trading of these instruments on a regulated French market, regardless of the competent authority that approved the prospectus.

The aim of these reforms was to ensure that promotional materials for a complex financial instrument include key information, such as whether it offers a capital guarantee. In addition, under a "comply or explain" approach, such materials must explicitly mention non-compliance with standards for secondary market liquidity, the eligibility of the underlying instrument, the nature of the issuer, and the conditions for exercising the product. The reform also takes into consideration some of the recommendations made in the Jacques Delmas-Marsalet report on financial product marketing<sup>12</sup>, in particular the need to systematically verify that products are properly suited to investors' needs. Domestic transactions approved by the AMF and those imported under a European passport will be treated identically in terms of transparency at the distribution stage.

## **G** Appointment of a Correspondent in France by Issuers with a Registered Office Outside France

Issuers whose registered office is not located in France and whose financial instruments are admitted to trading on a French regulated market are now required to appoint a permanent correspondent in France to receive correspondence from the AMF and pass on any documents or information that the AMF deems necessary<sup>13</sup>.

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<sup>9</sup> Warrants, certificates, inflation-linked bonds, etc.

<sup>10</sup> Under the conditions established by Article L. 621-8 of the Financial and Monetary Code

<sup>11</sup> The text of these General Principles is available on the AMF's website under the heading: Texts -> Access by category of text -> AMF Positions

<sup>12</sup> AMF monthly review, issue 19, November 2005. See below Chapter 7

<sup>13</sup> Article 216-1 of the General Regulation.

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	2004	2005	change
<b>ISSUES AND LISTINGS ON A REGULATED MARKET</b>	55	54	- 1
<b>1. With pre-emptive rights</b>	29	30	+ 1
. Shares	20	21	+ 1
. Shares with warrants attached (ABSA) <sup>14</sup>	5	7	+ 2
. Shares with warrants for the acquisition of existing shares and/or subscription for new shares (ABOASA) <sup>15</sup>	0	0	0
. Bonds with redeemable warrants (OBSAR) <sup>16</sup>	1	1	0
. Subordinated bonds redeemable in shares (OSRA) <sup>17</sup>	0	0	0
. Bonds redeemable in shares (ORA) <sup>18</sup>	3	0	- 3
. Convertible bonds (OCA) <sup>19</sup>	0	1	+ 1
<b>2. Without pre-emptive rights</b>	26	24	- 2
. Shares	5	10	+ 5
. Shares with warrants attached (ABSA)	4	3	- 1
. Shares with warrants for the acquisition of existing shares and/or subscription for new shares (ABOASA)	0	0	0
. Share warrants (BSA) <sup>20</sup>	2	1	- 1
. Cooperative investment certificates (CCI) <sup>21</sup>	0	1	+ 1
. Bonds convertible into new shares or exchangeable for existing shares (OCEANE) <sup>22</sup>	7	6	- 1
. Perpetual notes redeemable in shares (TDIRA) <sup>23</sup>	0	0	0
. Convertible bonds (OCA)	3	1	- 2
. Bonds with redeemable warrants (OBSAR) <sup>24</sup>	4	1	- 3
. Bonds redeemable in shares (ORA)	0	1	+ 1
. Bonds redeemable in shares or cash (ORAN) <sup>25</sup>	0	0	0

	2004	2005	Change as a %
<b>1. Registration documents</b>	388	388	0
. post-publication review	268	302	+ 12.7
. pre-publication review	120	86	- 28.33
<b>2. Updates and corrections</b>	82	129	+ 57.3
. Corrections to registration documents (all documents)	15	14	- 6.7
. Updates of registration documents (all documents)	67	115	+ 71.6
<b>3. Offering circulars for listing on a regulated market</b>	19	24	+ 5

Source: AMF

<sup>14</sup> ABSA : action à bons de souscription d'actions.

<sup>15</sup> ABOASA : action assortie de bons à option d'acquisition d'actions existantes et/ou de souscription d'actions nouvelles.

<sup>16</sup> OBSAR : obligation à bons de souscription d'actions avec faculté de rachat des bons.

<sup>17</sup> OSRA : obligation subordonnée remboursable en actions.

<sup>18</sup> ORA : obligation remboursable en actions.

<sup>19</sup> OCA : obligation convertible en actions.

<sup>20</sup> BSA : bon de souscription d'actions.

<sup>21</sup> CCI : certificat coopératif d'investissement.

<sup>22</sup> OCEANE : obligation à option de conversion et/ou d'échange en actions nouvelles ou existantes.

<sup>23</sup> TDIRA : titre à durée indéterminée remboursable en actions.

<sup>24</sup> TDIRA : titre à durée indéterminée remboursable en actions.

<sup>25</sup> ORAN : obligation à option de remboursement en actions ou en numéraire.

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<b>TAKEOVER BIDS</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
Offers: standard procedure	13	5	14
Offers: simplified procedure	16	17	23
Mandatory buyout offers	1	4	3
Mandatory buyout offers with squeeze out	36	35	29
Share buyback offers	8	5	828
Standing offers	2	6	929
<b>TOTAL</b>	<b>76</b>	<b>72</b>	<b>86</b>