Nordic Securities Association

MEMO

NSA response to European Commission consultation on "Building a proportionate regulatory environment to support SME listing"

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The Nordic Securities Association (NSA) is a Nordic cooperation that works to promote a sound securities market primarily in the Nordic region. The NSA is formed by the Danish Securities Dealers Association (Børsmæglerforeningen), Finance Finland (Finanssiala), the Norwegian Securities Dealers Association (Verdipapirforetakenes Forbund) and the Swedish Securities Dealers Association (Svenska Fondhandlareföreningen).

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On 18 December 2017, the European Commission published a consultation paper regarding European Commission consultation on "Building a proportionate regulatory environment to support SME listing"

The deadline for the consultation is on 26 February 2018.

The NSA welcomes the initiative to consult on the question how to build a proportionate regulatory environment to support SME listing and NSA fully agrees upon the importance of SMEs as a key motor of new investment and job creation. Hence, any initiative that supports the development of SME markets is likely positive for the long-term development of the EU economy.

It is important to keep in mind that SME markets vary a lot across the EU and to a large extent they are local by nature. As put forward in the 2017 Springer-Brief report by Elert, Henreksson and Stenkula in "Institutional Reform for Innovations and Entrepreneurship, An Agenda for Europe", successful reforms in Europe to promote innovation and growth in the EU must consider country differences to be successful. They identify the existence of several different types of market structures in the EU that have evolved into complex entities held together by complementary institutions.

Therefore, it is impossible to find a regulatory solution adapted to all SME markets in the EU.

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Any regulatory framework needs to consider those differences and the overall legislative approach must be flexible. We would therefore advocate outcome-based regulations where the areas to be regulated are decided at EU level, but where the actual rules are set in each jurisdiction or market place. How to define an SME is an example at the basic level . A definition of an SME is certainly needed in each member state. That need could be defined in an EU-based framework, but how the limits should be drawn to define an SME needs to be adapted to local conditions and should therefore be done locally, meaning merely domestic scoped SMEs should continue to be subject to domestic market regulation.

There is a natural home-bias in SME investing as investors are more comfortable with the news-flow closer to the issuer. It is also difficult to participate in smaller issues for larger international investors due to size-limitations. Data from 117 different equity issues in the Norwegian market in the period 2012-2015 show clearly that in equity issues and placings below 100 million EUR, the domestic investor participation generally is in the 70-100 % range. This is not unique to Norway nor the Nordic markets, but a finding of general validity across national markets.

The Nordic SME markets differ both in size and in the stages of development. Hence, NSA's different member associations' responses to the more detailed questions sometimes differ. Nevertheless, there are several important and more fundamental areas where we have a joint opinion. One of these is to limit the administrative burden on SMEs to a strict minimum while upholding the integrity of the financial markets.

Many SMEs do not have neither the financial resources nor the manpower capacity? to handle the administrative requirements included in for example MAR. MAR is more suitable for large corporations with the resources required to establish compliance departments. At the same time, in some of the largest countries where SME markets are rather developed, an SME is probably a larger company by turnover than in the smallest member states.

Hence, an SME in one country may have larger administrative resources in some jurisdictions than in others which underline the need to define the details of those rules at a local level.

Regarding equity issuers, key advisers contribute to a sound behavior and hence fulfil a self-regulating function. The concept of a Certified Advisor (CA) was introduced ten years ago in the Nordic market when Nasdaq created First North and the general impression of the concept has been positive. The obligations of a CA are defined in the First North rulebook. The CA guides the issuer through the listing process. It ensures that the issuer complies with market standards including due diligence of the issuer, analyzing and screening of the management, the Board of Directors and principal owners. The CA is also involved in the educational process regarding the rulebook and MAR. After the market introduction the CA assumes a continuous dual role which means both monitoring and supporting the issuer. The main objective is to make sure that the issuers comply with the rules and market standards for listed companies. The CA is a guarantee of quality and has facilitated the development of a highly functional growth market. The CA has also been an important factor in the emergence of the local ecosystem surrounding the growth market.

The NSA would like to underline that it is important that such a role does not become burdensome from a regulatory perspective, as that would likely limit the willingness to take the role. Given the large differences between EU SME markets, we would advocate that this is an area where the different markets should develop rules adapted to local needs. We recommend that any Certified Advisor regime should be voluntary for the parties to choose.

The NSA also deems that financial research plays an important role when it comes to promoting investment. Investors need to get information on what they are buying. Therefore, financial research and credit information are important aspects for attracting investors. There is a risk that less research will reach out to potential investors because of MiFID II/MiFIR. As many investors will have to pay for research one could fear that the willingness to pay for SME research is limited as SME investment generally makes up a reduced part of their investment portfolios and thereby may be less worth to pay for.

In addition to this, SMEs do not have the resources to use a credit rating agency. At the same time, ratings are an important tool when investors make investment decisions. Some, larger investors may have the resources to make their own judgment, especially, if they get direct access to the management of the issuing company. But many investors do not have those resources, nor do they have access to the company management. Hence, their interest in investing in SMEs is limited to the amount of information available. At the same time, a broad investor base is a prerequisite for the long-term functioning of SME markets. To help investors get a somewhat clearer picture of the credit quality for non-rated companies, notably SMEs, several Nordic banks used to add a summary of the company's credit quality in addition to the investment analysis. The experience in the Nordic markets shows that this summary contributed to the development of the SME bond market. Furthermore, such summary may help increase investor demand – also from cross border investors.

In addition, well-functioning secondary markets underpin well-functioning primary markets. Hence, it is difficult to disregard the aspect of market liquidity and any regulatory or other measures that could hamper market liquidity should be thoroughly considered before any action is taken.