PRIVATE PLACEMENT: COMPARATIVE ANALYSIS OF LEGAL REQUIREMENTS IN THE US AND EU

by Svitlana Kuzmenko

LL.M. Capstone Thesis
Supervisor: Professor Markus Petsche
Central European University
Quellenstrasse 51-55, 1100 Vienna
Austria

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Abstract

In my capstone project, I am disclosing the topic of raising debt financing by issuing debt securities (bonds) and the legal requirements for placement bonds under EU and US law in a comparative perspective. In my opinion, this topic is quite relevant, as more and more companies are borrowing capital from investors by issuing bonds rather than through bank loans, so all of them have to choose one of the placement offerings in the end.

Depending on the type of placement, the regulation of debt securities is highly dependent and is interesting and important to understand. When there is a public offering, companies have much more documentation requirements in general and prospectuses in particular. In most cases, private placements are not listed and occur over-the-counter.

It is also important to disclose the necessary documentation and its requirements for the issue placement to occur. The main document that discloses information about the issue and makes it transparent to investors is the prospectus. But it is not always needed, especially if companies decide to place bonds using private offerings.

In general, I would like to devote most of my work to the advantages of issuing bonds and offering them via private placement and the specifics of its regulation as part of the company’s debt securities issues covered mainly by the EU Prospectus Regulation and US Securities Act 1933.

The value of this paper lies primarily in its practical orientation and the recommendations that will be made to companies after analyzing the abovementioned themes.
Introduction

The topic of the private placement was not chosen by me accidentally. How the world we live in will change and improve depends to a large extent on how the economy develops. Economic development is not possible without the development of medium and small enterprises. As stated in the Ministry of Finance report, “The private sector is the engine of growth. Successful businesses drive growth, create jobs and pay the taxes that finance services and investment”.¹ As we know, companies need funds to grow and develop. There are quite a number of methods by which companies can raise the necessary capital. These include, for example, bank loans, joint ventures with other companies, initial public offerings (“IPOs”), direct investments, or the issuance of debt securities.² Each method has its advantages and disadvantages and should therefore be evaluated by the companies separately according to their corporate strategy, objectives and possibilities. In this paper, I will elaborate on just two methods of raising money, namely loans from banks and issuance of debt securities, explaining what they have to offer and when it makes sense for a business to choose between the two.

Statistics show that the private debt markets in the US have been growing in recent years.³ More and more companies are borrowing capital from investors by issuing debt securities. This is because over time, due to the economic crisis, regulation of traditional bank

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financing has become much tighter\textsuperscript{4}, making bank lending more expensive and therefore less accessible and profitable for private businesses. Consequently, companies have had to seek alternatives and the choice has often fallen on private debt. It should be noted that debt securities occupy a special place among the set of investment instruments available to private and institutional investors. This is due to the set of unique investment characteristics of such securities. Indeed, debt financial instruments offer their holders higher guarantees of future income than, say, equities, have high liquidity, fixed amounts and terms of expected reward. Debt securities considerably expand investment opportunities, allowing the implementation of various investment strategies.

Debt securities include a wide range of financial instruments: bills of exchange, cheques, certificates, bonds, and others. As a practical component of my capstone project, I did an internship in an investment company that is focused on helping medium and small businesses raise capital through issuing bonds. Therefore, I would like to focus on bonds – the most massive debt security and disclose the legal requirements for placement of these securities in the process of raising debt financing.

The shortage of funds by companies became particularly acute with the crisis in 2020 due to the Covid-19 pandemic, which prompted business management to seek help in raising capital.\textsuperscript{5} During my internship, I came across the fact that clients are often unaware of how they can raise debt and what pitfalls may await them. As a consequence, in my paper I decided to describe the advantages and disadvantages of choosing to issue bonds, focusing on their


placement. In my opinion, this topic is quite relevant, as all of them have to choose one of the placement offerings in the end to sell their debt.

In this paper, I am describing in detail the difference between private and public offerings, what the nuances are, what company management should pay attention to, and why proper planning plays an important role. In my opinion, a private placement is preferable for small and medium-sized companies, as it takes less time and money, and has fewer disclosure requirements than a public placement, and is easier to comply with. Not all companies are ready to go public and it is particularly important for company management to correctly assess the obligations imposed on public companies. After all, if the requirements are underestimated, the benefits received may not be commensurate with the effort and risk expended.

In addition to the type of offering, the jurisdiction in which the company plans to issue the bonds and for which investors from which countries they are intended is also of great importance. A company’s management can choose the country in which it wants to issue securities. For this purpose, companies from one country may set up a special purpose vehicle (“SPV”) in the jurisdiction of their choice. And then transfer the money collected from investors under a loan agreement to the real borrowing company behind the issuer. But this is not mandatory, because it is often possible to issue bonds as a foreign issuer, i.e. being incorporated in another country. The choice of jurisdiction is extremely important because companies need to comply with relevant requirements and laws, which may impose certain restrictions as described in Chapter 2, so it is essential to think carefully and deliberately about this choice in advance.

For comparison, I have chosen two of the most popular placement jurisdictions for analyzing debt capital markets. More specifically, I have chosen the US because it is considered
to have the most developed market and regulation for debt securities,\textsuperscript{6} which are governed by specific laws, the main one being the US Securities Act 1933. The EU is considered to be the second most developed in this sense jurisdiction and has several specific features different from the US. The main sources of regulation for the EU are the EU Prospectus Regulation and the various individual rules of each stock exchange that apply to the company listing therein. In order to better understand how a private placement mechanism works and as these are the most popular jurisdictions to locate in, it will be useful to compare European and US securities statutes and regulations and highlight the advantages and disadvantages of each.

Chapter 1. Debt securities offerings: setting the scene

As I noticed before, companies often need to resort to debt financing in order to grow and scale their business. Among the many types of raise funding, in my thesis, I focus on only two of them as they are the main ones in cases where a company wants to borrow capital and without changing its organizational structure or shareholding structure. After all, when companies launch IPOs, they are subject to special stringent regulations and extensive requirements that not all companies can to meet.\textsuperscript{7} Mergers and acquisitions through a merger with a competitor or the sale of a company are also not suitable for all companies, as although shares are redeemed and exchanged for cash, there is a loss of control, which may be undesirable to the company’s founders.\textsuperscript{8}

Thus, a company may ask a bank for a loan or a credit line, or it may access the capital market. In order to enter the capital market, the company must issue debt in a bond form, which will then be bought by investors. Disposition (sale) of bonds to new owners (investors) is called a bond placement and it is the final stage in the issuance of debt securities. To exercise this option, companies need to choose the type of bond placement they will use. As will be described later in this Chapter 1, there are two main types of placement - private and public - each with its characteristics.

In the first subchapter I elaborate on why companies these days are gradually moving away from bank lending, increasingly opting for debt issuance, which companies and in what circumstances can benefit from the first or second option, and what are the advantages and disadvantages of each of these methods of raising capital. In the following I look at the specifics


\textsuperscript{8} Ibid.
of bond issuance in terms of their placement, comparing the two variants against each other and highlighting the specifics of each, as well as providing guidance to companies on what to look out for to make the right choice.

1.1. How debt issue differs from a bank loan?

Bank loans and credit lines are traditional sources of funds raising and probably the first ones that come up to mind when we are thinking about additional sources of lending capital. A Survey of ECB on the current debt capital market confirms that bank-related products remained the most important financing source for SMEs in 2020. However, the issuance of debt securities by companies has been developing at a rapid pace, particularly in recent years. I believe it is very important to keep an eye on new products and offers in order to expand business opportunities on the most favorable terms for the business.

To begin with a bank loan, its granting is usually accompanied by strict covenants, requirements and criteria that limit the freedom of action and decision-making of the company’s management. Such requirements are necessary for credit institutions to minimize the risk of their loan portfolios. In an increasingly competitive and internationalized environment, companies often aim to enter new markets, expand their product range or carry out acquisitions. To do so, they have to expand their existing credit lines and sometimes even revise their financing structures by resorting to additional financial market instruments. In such cases, due to increased risks, banks often put their clients with no alternatives on even tougher terms and companies have to accept them.

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The Covid-19 pandemic has brought new adjustments and tightened the already difficult playing field for market participants. In response to the economic fallout from the pandemics, the European Central Bank recalibrated its monetary policy\(^\text{10}\) and lowered interest rates in 2020 which provided a double benefit to issuers of securities: Against the background of declining profitability of alternative investments for investors in bank deposits, in particular, the attractiveness of investing in securities has increased. At the same time, the ECB’s low interest rates gave issuers an incentive to issue securities and borrow funds at lower interest rates.

For years the development of the bond market has been growing steadily and last year the market boomed while a study by the European Central Bank showed a declining trend in the demand for bank loans in the first 9 months of 2020 compared to the same period last year.\(^\text{11}\)

For the placement of securities, transparency of the Issuer is a prerequisite. In particular, information on possible risks should be provided as well as information on the strategy and financial indicators for a broad and diversified audience. In addition, information in the format of the prospectus must be passed to the stock exchange at the offering stage. The prospectus is typically comprehensive and contains basic information that is published in the annual report. In addition to the regular reports, the company issuing the bond must also issue an annual report containing information that could affect the creditworthiness of the debtor. The specific terms depend on many parameters such as the creditworthiness of the debtors and the frequency of placements. Large companies which can afford to offer bonds often are able to borrow at lower interest rates than smaller companies with a low frequency of offerings.


As capital market financing is less collateral based than bank financing, great importance is placed on the ability of the issuer to generate constant and stable cash flow. A decisive factor for a credit rating is, for example, how comfortably the interest burden of the issuer can be covered by earnings before interest and taxes (EBIT). Companies whose EBIT does not exceed at least twice their interest burden do not stand a good chance of placing a product on the capital market.

The main advantage of the loan over bank financing is that no collateral is needed. The company has the opportunity to address a wide range of investors – creditors – as potential buyers of these securities, i.e. apart from funds from credit institutions, also funds from insurance and investment companies, pension and investment funds, individuals, foreign investors.

In addition to concerns regarding information disclosure, market participants frequently succeed in exploiting the publicity effect for marketing purposes. In this case, companies manage to arouse public interest as well as to increase the visibility and the number of potential customers.

1.2. Public offering vs private offering: when is it beneficial for companies to use a private placement of bonds?

The most common purpose for which bond issues are used is to raise funds to finance the operations of a company or its group to scale the business. However, this is not the only reason, there may be a variety, all depending on the plans of the company’s management that decided to issue debt securities. For example, companies may issue debt as an additional source of funds or to refinance debts and close loans, as well as for specific projects. The fundraising
company may choose or to act as an issuer itself or create a separate capital raising company – an SPV (special purpose vehicle) for bond issuance purposes only.

There are two main types of offerings that exist – private and public ones. In order to understand which type of securities placement is best suited for a specific company, I am going to compare them in detail. I would like to begin with private placement or as is also called a non-public offering. A private placement is a means of raising funds by which securities are offered to a limited number of selected investors. Participants in a private placement typically include large banks, insurance companies, asset managers, funds and institutional (professional) investors.\(^{12}\)

An important aspect in choosing the type of offering is the particulars of its regulation. If we are talking about private placements, things are simpler in comparison with a public offering. Private placements are relatively unregulated compared to sales of securities on the open market.\(^{13}\) First, the requirements for issuers and their information disclosure are minimal, which simplifies and greatly speeds up the entire process. For example, companies typically do not need to comply with an annual or quarterly disclosure requirement, although they do need to provide information to investors on the company’s financial position and material changes, but need not do so publicly.

Secondly, it becomes easier to comply with the standards and regulations for issuance documentation. For example, a non-public offering in the US does not require registration with the Securities and Exchange Commission (“SEC”).\(^{14}\) This means that the issuer is exempt from


additional financial disclosure and the drafting of a private placement memorandum. The exemption from registration is enshrined in Regulation D of the Securities Act 1933.\textsuperscript{15} That is, the sale of securities may only be made to accredited investors, who may be individuals or legal entities. This rule is established to reduce the risk of an adverse investment, as investors must assess all risks themselves and carry out due diligence on the issuer and the issue of the securities. Thus, more sophisticated investor protection is established, because in order to become a qualified (accredited) investor one must meet certain criteria contained in the Securities Act 1933. It should also be noted that the minimum denomination of a bond is $100,000.

The advantages of a private placement include: 1) minimum standards for disclosure, which limits access to it by competitors; 2) the ability to choose investors who share the company’s values and can provide assistance to the business; 3) reduced time and costs for additional documentation and registration, which will allow funds to turn over faster; 4) no need to provide a credit rating; 5) flexibility for the issuer in setting parameters and size of securities and for investors securities are likely to yield higher than the average price on the market. It is for these reasons that private placements have become more common in the last few years.

However, in addition to the advantages, the disadvantages facing companies that have opted for a private placement programme must also be mentioned. As noted above, the securities can only be offered to a certain circle of investors who qualify for accreditation. Not only does this significantly reduce the number of potential investors, but it also reduces access to the market for issued bonds. This can then have a negative impact on the long-term value of the business, as investors are less interested in buying securities with low liquidity, which can

be difficult to sell. Again, low liquidity is provided by a limited range of investors. However, the illiquidity of bonds is usually covered by a higher interest rate in a private placement.

A public offering involves the sale of securities to an unlimited number of investors with a listing on a stock exchange. An open subscription method is used. In the case of a public offering, the company must go through a number of legally required procedures to register the bond issue. One of the most important requirements in a public offering is the registration of the prospectus, which discloses all necessary information about the issuer, the issue, and its financing, while in a private placement the potential investor must conduct due diligence on its own. For example, placement or distribution of securities in the US usually requires a registration statement, whereas in the EU there is a requirement for a prospectus to comply with a prospectus regulation, as discussed in more detail in Chapter 2.

The main advantages of a public offering include 1) the possibility of raising a large sum of money as it is offered to an unlimited number of people; 2) investors’ confidence in the stock exchange and this type of offering is an indication of the company’s integrity and its desire to have transparent relations with investors and that it has nothing to hide; 3) as a result of the previous point, the company earns a positive reputation; 4) the bonds have high liquidity as compared to a private placement.

As for the disadvantages, they mainly correlate with the advantages of a private placement. That is, they include the complexity of organization, time-consuming and high cost of public offerings, as they require the assistance of many professionals, including lawyers, marketing experts, business consultants, etc. Otherwise, a company will be subject to fines for failing to comply with any public offering requirements. Also, companies placing publicly need to disclose their financial position and material changes on an ongoing basis, which eliminates any privacy and provides access to information for competitors that can be avoided in a private
placement. That is why, it is strongly recommended for issuers before listing with the Securities Exchange Commission or any stock exchange to check the availability and sufficiency of its financial reports with auditors, otherwise the process of debt issuance can dramatically increase.

Overall, both types of placement have positive and negative aspects. When deciding on an offering, companies must weigh the potential advantages and disadvantages inherent in each type and weigh these against their issuance objectives, risk management policies and potential beneficiaries. According to Scott Crist, companies should make a careful analysis that considers the anticipated interest rates for each option, along with the anticipated costs of issuance and any customization required in the financing structure to meet the company’s specific project needs.16

I believe that private placements are a good opportunity for start-ups, small and medium-sized companies to raise funds. They are more suitable for short and medium-term securities with maturities from 1 to 10 years and an issue size of up to $500 million because they are faster and carry fewer expenses in terms of arranging the placement. Under the same conditions, it is difficult to raise more capital in a private placement than in a public placement. Public offerings, from my point of view, would benefit larger companies with longer maturities and larger issuance size because they would be available to a larger number of investors and therefore the capital could be raised more easily. They also disclose more information and investors may be more willing to invest in them.

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Chapter 2. Legal framework of debt securities offerings in the European Union and the United States

In this chapter, I look specifically at the regulation of private placements in two of the most widely used jurisdictions. I have chosen to focus on private placements because they are growing rapidly and from my perspective are more suited to the small and medium-sized companies that I focus on in this paper. Both US and European private placement regulations have a number of different features which are important for a company's management to consider in order to make a proper decision on the jurisdiction of the placement. This decision depends primarily on, but is not limited to, the company's strategy, objectives, capabilities and the investors it seeks to target. In order to do so, it will be helpful to compare European and US securities regulations and highlight the particularities inherent in each.

My aim is to point out to companies the requirements and challenges they may face, and to provide guidance to management on how they can overcome them, what the exceptions are, etc. Overall, I would like to advise companies on what to look out for when choosing a jurisdiction for a private placement and outline the rather complex and extensive regulation in the most relevant aspects in the simplest possible words. I will start with the regulation of the offer and sale of securities under US law, which is considered somewhat complicated and may initially appear “overwhelming to an issuer accessing the US capital markets for the first time”. I will take into account the federal level of regulation without the peculiarities of separate states (Blue Sky laws) and continue with a description of European Union regulation, mainly but not exclusively at the directive level.

2.1. Regulation and exemptions applicable for private placement in the US

In connection with the chosen topic of the thesis, I will look at a few primary federal statutes which are the main ones in the regulation of securities. The offer and sale of securities are regulated mainly by the Securities Act of 1933 (the “Securities Act”). Everything which occurs after the primary sale and concerns the secondary market, the trading of securities, reporting obligations, the activities of public companies which go public, as well as persons and institutions involved in the securities industry is regulated by the Securities Exchange Act of 1934 (the “Exchange Act”). It also established the Securities and Exchange Commission (“SEC”).

The Securities Act sets out a relatively broad definition of ‘security’ which, among other things, includes such debt securities as bonds (Section 2(a)(1)). Pursuant to Section 4(a)(1) of the Act any transaction carried out by an issuer requires registration with the SEC. Under Section 5(a)(1) it is stated that “unless a registration statement is in effect as to security, it shall be unlawful ... to sell such security through the use or medium of any prospectus or otherwise”. However, there is no rule that to issue security in the US, the company should be incorporated in the US only, and the foreign issuers also have an access to the US debt market. The Securities Act also specifies the content of the prospectus and registration statement in detail.

The complication of US securities legislation, in my view, is that it is over-regulated. There are many requirements to pay attention to at the same time and they are not easy to understand. However, in this way, the “weakest” party in a bond deal – the investors – is afforded the most protection. And the more potential purchasers a company targets, the more information it will have to disclose. Although it seems to me that there is some bias towards investors, which can probably be explained by previous financial crises. After all, crises are
known to be followed by active reforms and new laws, as was the case, for example, with the financial crisis of 2008.

The US law, however, allows a waiver from the obligation to file a registration statement in the case of “transactions by an issuer not involving any public offering” (Section 4(a)(2)). And this is a positive aspect, as exemptions allow companies to maneuver and grow. However, it is important to note that there are many exemptions (or safe harbors) relating to private placements. In addition to Section 4(a)(2), these include Rule 144A, which allows sales only to US qualified institutional buyers (“QIBs”)\(^{18}\), Regulation S regulates sales to non-US investors (offshore transactions)\(^{19}\), Rule 701 governs sales to the issuer’s employees\(^{20}\) and Securities Act Regulation D.\(^{21}\) Therefore, in my paper, I will only address the most frequently used exceptions.

As per Section 4(a)(2), it is important to note that the term ‘public offering’ itself is not defined in the Act. This section permits an issuer to sell securities in a “private placement” without registration under the Securities Act. Such unregistered transactions are considered to be less demanding in comparison with registered ones because apart from not being required to register with the SEC, companies are also exempt from detailed disclosure and financial data.\(^{22}\)

A company’s ability to benefit from the exemption under Section 4(a)(2) is influenced by a number of factors which have been crystallized using case law and market practice. Thus, the attitude of the issuer and the offeree, their number and ability to negotiate with the issuer, the size and denomination of the issue are all taken into account.\(^{23}\) All of these are aimed at

\(^{19}\) Ibid. para. 230.901-905.
\(^{20}\) Ibid. para. 230.701.
determining whether or not offerees need Securities Act protection. Companies therefore often require potential investors to confirm that they have obtained all the necessary information and assurances as to their sophistication in order to ensure compliance with this exemption. Various ‘investor questionnaires’ are often used for this purpose.

Since the “boundaries” for section 4(a)(2) exemption could not be clearly defined, Regulation D was adopted to bring clarity and legal certainty. Thus, Regulation D is considered safe harbor because, if the conditions are met, a transaction to buy or sell bonds would not be considered a public offer under section 4(a)(2). Regulation D provides three exemptions, including Rule 504, Rule 505 and Rule 506, but the latter is the most widely used because it does not impose limits on the size of the issue or the number of ‘accredited investors’ and allows for an offer up to 35 non-accredited investors. Accredited investors include banks, broker-dealers, insurance companies, funds and the like, HNWI of $1,000,000+ or annual income of $200,000+ and directors and executive officers of the issuer. However, under Reg. D there are restrictions on direct sale attempts (general solicitation and advertising), which can only be used to offer or sell securities in certain cases set out in Rule 506(c).

Regulation S should also be mentioned. It is used if offers are made outside the US, i.e. if the buyers (investors) are not located in the US. This exemption prohibits any efforts on direct sales of securities to US investors. ‘Directed selling efforts’ are defined broadly enough

24 SEC v. Ralston Purina Co., 346 US 119,125 (1953) (“the applicability of the [exemption] should turn on whether the particular class of persons affected needs the protection”).
27 Securities Act 1933 Rule 501(a).
28 Securities Act 1933 Rule 901.
and mean prohibition of the distribution or forwarding of bond offers, interviews or advertisements in the US about the offer and sale of the securities.\textsuperscript{29} The requirements under Reg. S are categorized into 3 categories from basic to most restrictive and must be strictly adhered to or investors can cancel the purchase of securities.\textsuperscript{30}

Rule 144A deals with the securities that were issued in a private placement and later resold on a public trading market (only to QIBs in the US). A ‘qualified institutional buyer’ defined generally as a large institution with an owned or managed portfolio of securities valued at $100+ million or a bank that has $25+ million net worth or invests $100+ million in securities or broker-dealer with securities for $10+ million in ownership or under management.\textsuperscript{31} This exemption is advantageous in cases where bonds need to be issued and sold quickly. The issuer also benefits from the fact on a private offering it essentially gains access to the secondary market, albeit in the form of institutional investors, thereby significantly increasing the liquidity of the bond, which in private placements is lower than in public offerings, as discussed in Subchapter 1.2. Rule 144 is often used together with Regulation S. The reason for that is that the compilation of the two rules is used simultaneously, it will broaden the investor pool, increase the recognition of the issuer in the US market and create additional legal certainty in the area of documentation.\textsuperscript{32}

To sum up, there is a general logic to the laws governing securities and the exemptions that exist for private placements. US legislation gradually became increasingly complex as the


\textsuperscript{30} Securities Act 1933 Section 12(a).

\textsuperscript{31} Ibid.

\textsuperscript{32} Adam B. Farlow, Charles Farnsworth, Andrew J Brown, ‘144A vs Reg. S Only – Considerations in High Yield Offerings’ (Baker McKenzie, 28 December 2020) <https://insightplus.bakermckenzie.com/bm/attachment_dw.action?attkey=FRbANEucS95NMLRN47z%2BeeOgEFCt8EGQJisWjCH2WAXW59W9rh3JQT7yD3BEI9GGJ&nav=FRbANEucS95NMLRN47z%2BeeOgEFCt8EGQbuwypnZjc4%3D&attidocparam=p7HEsg%2FZ312Bk80OlqOIH1c%2BY4beLEaER6Y7D%2B%2BUuHY%3D&fromContentView=1> accessed 29 June 2021.
market grew and needed to be regulated. To support the market (and the economy as a whole), a number of laws were passed to protect the “weaker” and more numerous parties, i.e. the buyers of the securities, in order to avoid them being defrauded and causing the market to collapse. However, in cases where buyers are “professional” investors and understand the risk they are taking, they do not need to be protected and thus fall under various exemptions. Such investors have far fewer rights than those involved in public offerings, for example, in the event of “a material misstatement or omission”. Under Rule 10b-5 of the Exchange Act, however, purchasers of a private placement can still sue under the general anti-fraud provision applicable to all securities transactions, but they will also need to prove “scienter, reliance and causation” in cases of a material misstatement or omission.

2.2. Regulation of private placement in the EU

European regulation does not remain at a standstill either. Recent reforms have introduced changes to the regulation of capital markets, including the entry into force of the Prospectus Regulation (EU) 2017/1129 (“PR”), which is applicable and directly binding in all MS. It replaced the former Prospectus Directive 2003/71/EC (“PD”), which remains subject to “grandfathering” arrangements. It has continued to implement a plan for the development of European companies by expanding the sources of funding alternatives to bank loans. The directive is supplemented by Commission Delegated Regulation (EU) 2019/980 and

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34 Ibid.
Commission Delegated Regulation (EU) 2019/979, which set standards for the documentation of offers and sales of securities to the public.

As for the private placement, a prospectus under the rules contained in the aforementioned directives is not required, provided that debt securities are to be issued in denomination of €100,000+ and there is no listing on a regulated market.\textsuperscript{37} In my opinion, such a denomination is too high, as most companies would simply increase the denomination of their securities to be exempt from the requirements, as there are still many institutional investors who can buy such bonds and in this case, retail investors would suffer. From a long-term perspective, it could lead to the development of solely qualified investor markets in the EU\textsuperscript{38} and deepen the problem of illiquidity on the retail secondary markets.\textsuperscript{39}

Although in a private placement companies cannot list their securities to the general public, it should be noted that it is still possible to do on unregulated markets, i.e. on multilateral trading facilities (“MTF”) such as the Euro MTF in Luxembourg, Vienna MTF in Austria or the International Securities Market that operates as an MTF in the UK. Each of them has different requirements, but almost everywhere one or two years of audited financial statements are required, so this is not suitable for start-ups or newly incorporated companies that are less than a year old.

A safe harbor from ‘public offer’ exists under Article 1(4) of PR where the exemptions from the obligation to publish a prospectus are listed. Among others, it includes offerings that


\textsuperscript{38} R.S. Panasar et al., “The new prospectus regulation – the story so far”, Clearly Gottlieb Alert Memorandum 7.03.2019, pp. 3-4.

are proposed to qualified investors only or fewer than 150 non-qualified investors.\textsuperscript{40} This echoes somewhat the US Reg. D Rule 506, which does not impose a limit on the number of accredited investors to whom securities may be sold, but the number of permitted non-accredited investors is significantly lower (35).

It should be noted that PR does not use such notions as a private placement or private offering. Article 2(d) contains only the definition of a public offer, which in effect places private offerings within the term of the public offer. This removes the dualistic private-public system and brings harmonization within the EU, however, this may subsequently lead to uncertainty between MS and their disability to define what constitutes a private placement under their national law.\textsuperscript{41} This is reminiscent of the US exception under Section 4(a)(2) of the Securities Act where “transactions by an issuer not involving any public offering” are exempt from filing a registration statement with the SEC.

It is also important to take into account whether the issue will be a cross-border or domestic one, as it depends on national law whether the Member States can exempt domestic issues entirely or set minimum disclosure requirements. For example, in Luxembourg by adopting the New Prospectus Act a threshold of up to €8 million and from 1 year has been set for an offering to be exempt from providing a prospectus.\textsuperscript{42}

PR is continuing the reforms initiated by PD to develop European capital markets by attracting small and medium-sized enterprises which are not focused on regulated markets. For


them, under the “EU Growth prospectus” there are simplified disclosure rules as long as the issues are no more than €20 million. Such a regime seems more attractive because it would be universal for all EEA Member States. This is in my view a really good initiative that could interest companies wishing to issue debt securities to pay more attention to the European market. It is too early to tell how it has performed because it is a relatively short time and the year 2020 was marked by the crisis that occurred in connection with the Covid-19 pandemic. As a consequence, there was a small outflow of money from the debt capital markets last year, but this is now slowly recovering.

Overall, speaking of the differences between US and European placements, the European offerings have significantly smaller issue sizes and are less likely to be listed or rated. US placements usually offer longer maturities and it is not required to enter into a confidentiality agreement to cover the disclosure as disclosure is only made to a limited group of investors. Interestingly, in 2017 the Commission conducted a study in which it assessed the growth potential of private capital markets in the EU and the obstacles for their development. The study found that not all private placement markets have been able to reach their full potential, revealing a wide gap between old and new member states. The most promising countries were identified as Italy, the Netherlands and Spain. In addition, it was noted that the European private placement market is significantly behind the US market in terms of depth and size.

Conclusion

Since the basis for writing this paper was my internship and the various assignments I undertook during it, my main task was to guide clients (SMEs) through the complex regulatory hurdles that accompany the issuance and placement of bonds in various jurisdictions. The bias of this paper is therefore more of a practical nature and therefore it is important to analyze the information available, telling the complexities as simply as possible.

To summarize, though bank lending is still quite popular among SMEs, it makes sense to pay attention to debt securities issues as this area has been actively developing lately and as compared to banks, this type of raising capital has a number of undeniable advantages, including no ties to banks, possibility to choose investors, securities circulate in the debt market, higher liquidity, debt body is payable at maturity, can be unsecured, fixed interest rate, etc. Of course, there are also disadvantages and each company has to be evaluated individually to arrive at a final decision as to what is beneficial for it at a particular time.

Regarding the choice of private or public placement, I tend to think that for SMEs private placements are more suitable because they are less expensive, simpler and quicker to implement, contain minimal disclosure requirements and carry less liability risk. However, the decision to choose the type of placement should be carefully considered by the company’s management and analyzed in terms of the company’s objectives, expectations and capabilities.

Last but not least is the choice of jurisdiction and here everything is trickier. As has been shown, US debt capital markets are much broader and more developed than European ones but regulation is also quite complex. For SME’s I would advise choosing the country based on the investors who will be offered the securities and the jurisdiction of the issuer itself. There are exemptions to facilitate issues in both jurisdictions and some of them even overlap, so the choice will depend on the individual company’s characteristics and desires of its management.
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