The Regulation of Private Placements in France (Updated)

This memorandum discusses the current state of law concerning private placements in France, including the impact of a recently adopted Ordinance¹ (the “Reform Act”) and amendments to the General Regulations (the “General Regulations”) of the French securities regulator, the Autorité des marchés financiers (the “AMF”). These amendments are intended to improve the competitiveness of the French financial market and to harmonize the French regulatory definition of a public offering with the European definition under the Prospectus Directive.²

The Reform Act and amended regulations became effective as of April 1, 2009.

1. Public Offering of Securities

In France, every issuer that makes a public offering of equity or debt securities must file a prospectus with the AMF.³ In compliance with the Prospectus Directive’s definition of “offers of securities to the public,” the Reform Act redefines a public offering to mean:⁴

(1) a communication to persons in any form and by any means, presenting sufficient information on the terms of the offer and the securities to be offered, so as to enable an investor to decide to purchase or subscribe to these securities; or

(2) the placing of securities through financial intermediaries.

The former definition specifically referred to certain means of communication to the public such as solicitation (“démarchage”) and advertising while the new definition uses more general terms and refers to any kind of communication. However, neither the Prospectus Directive, the Reform Act nor the AMF General Regulations have defined the word “communication,” and its scope remains unclear.

³ Article L.412-1 of the French Monetary and Financial Code (the “MFC”).
⁴ Article L.411-1 of the MFC.
The Committee of European Securities Regulators (CESR)\(^5\) has provided a certain number of clarifications in response to questions by market participants. For instance, in response to a question as to whether free offers fall under the definition of a public offering, the CESR replied that, since the Prospectus Directive refers to a communication containing sufficient information to enable an investor to decide to purchase or subscribe for securities and no decision is made by the recipient of free securities, such an allocation would fall outside the scope of the Prospectus Directive.\(^6\)

The CESR also discussed whether a communication made by a custodian bank to its clients in one member state concerning pre-emption rights in relation to a public offering of new shares in another member state constituted an offer of securities subject to the provisions of the Prospectus Directive. The CESR considered that such a communication would constitute a public offering only if (1) the custodian bank communicates to shareholders the terms and conditions of the offering to enable them to decide whether to subscribe the shares and (2) the custodian bank acts on behalf of the offeror or issuer when making such a communication.

Those two examples indicate that there is no public offering under the Prospectus Directive where no decision is required from the recipient of the securities.

Under previous French rules, issuers that had once made a public offering acquired a special status ("statut d'émetteur faisant appel public à l'épargne") and became subject to a number of additional disclosure obligations, separate from those of the exchange on which their securities were offered. This status no longer exists under the new regulations. Instead, issuers are subject only to the disclosure obligations that are required by the regulations applicable to the market on which their securities are listed.

The minimum capital requirements to make a public offering have been amended and lowered from €225,000 to €37,000.\(^7\) Stock exchange operators, such as Euronext, will need to set specific capital requirements, if any, for issuers listed on the various exchanges it operates.

2. The Private Placement Exemption

Unlike the United States, France had no private placement exemptions from prospectus requirements prior to 1998.\(^8\) In 1998, France implemented the original EU Prospectus Directive,\(^9\) creating a private placement exemption for the issuance or sale of securities to "qualified investors" or a "restricted group of investors" acting in each case for their own account.

\(^{5}\) The CESR’s role is to improve co-ordination among securities regulators and ensure more consistent and timely day-to-day implementation of community legislation in the European Union.
\(^{7}\) Ordinance N° 2009-80 dated January 22, 2009; Article L.224-2 of the French Commercial Code
\(^{8}\) In the United States, private placements are regulated by Section 4(2) of the Securities Act of 1933, 15 USCA § 78d(2), and by SEC Regulation D (Rules 501 to 508), 17 C.F.R. §§ 230.501 – 230.508.
Scope of the Private Placement Exemption

The Prospectus Directive expanded the definition of “qualified investors” and simplified the definition of a “restricted group of investors.”

(i) Qualified Investors

"Qualified investors" are defined as individuals and legal entities that possess the necessary competence and means to appreciate the risks inherent in transactions relating to financial instruments.\(^{10}\)

There are two categories of qualified investors.

Certain investors are automatically treated as qualified investors.\(^{11}\) This category includes, for instance, large companies; i.e., legal entities which, according to their last annual or consolidated accounts, meet two of the following criteria: (a) an average of more than 250 employees during the financial year; (b) a total balance sheet exceeding € 43 million; and (c) an annual net turnover exceeding € 50 million.\(^{12}\)

Certain investors can elect to be treated as qualified investors. This category includes small and medium-sized companies that expressly choose qualified investor status. Small and medium-sized companies are defined as those which, according to their last annual or consolidated accounts, meet at least two of the following criteria: an average of less than 250 employees during the financial year, a total balance sheet not exceeding €43 million and an annual net turnover not exceeding €50 million.\(^{13}\) It also includes certain individuals who meet at least two of the following criteria: (i) the investor has carried out transactions in financial instruments of an amount exceeding €600 per transaction at an average frequency of at least 10 per quarter over the previous four quarters; (ii) the size of the investor’s securities portfolio exceeds €500,000; and (iii) the investor works or has worked for at least one year in the financial sector in a professional position that requires knowledge of securities investment.\(^{14}\)

Qualified investors that elect to be so treated must declare themselves to the AMF which maintains a special registry of this category of qualified investors.\(^{15}\) This registry is not accessible to the public. Investors registered as qualified investors may opt out at any time.\(^{16}\)

(ii) Restricted Group of Investors

Since the adoption of the Prospectus Directive, a prospectus is no longer required for a public offering of securities addressed to fewer than 100 individuals or legal entities per Member State, not counting qualified investors.\(^{17}\)

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\(^{10}\) Article L.411-2 II of the MFC.
\(^{11}\) D. 411-1 I list of 15 investors.
\(^{12}\) Article 2.1.e.iii of the Prospectus Directive and Article D. 411-1 I 15° of the MFC.
\(^{13}\) Article 2.1.e.v of the Prospectus Directive and Article D. 411-1 II 1° of the MFC.
\(^{14}\) Article 2.1.f. of the Prospectus Directive and Article D. 411-1 II 2° of the MFC.
\(^{15}\) Article D. 411-3 of the MFC and 211-2-1 of the AMF GR.
\(^{16}\) Article 211-2-1 of the AMF GR.
\(^{17}\) Articles L.411-2 II in fine and D 411-4 of the MFC.
(iii) Acting for Its Own Account

The "acting for its own account" requirement is a restrictive condition that applies to both the exemption for qualified investors and for members of a "restricted group." The concept is not defined by law or regulation. Reading this condition as an anti-avoidance mechanism would imply that qualified investors cannot purchase privately placed securities on behalf of non-qualified investors. However, it is unclear whether a financial institution buying securities for a qualified investor's account is ineligible for the exemption and whether qualified investors qualify for the exemption if they act on behalf of other qualified investors. Furthermore, if this condition is to function as an anti-avoidance mechanism, it becomes necessary to determine whether qualified investors can purchase privately placed securities for their own account with the intent to later resell them to unqualified investors. As discussed further below, the AMF partially clarified this latter issue by adopting a rather flexible approach with respect to the resale of securities acquired by qualified investors.

**Financial Intermediaries**

A US issuer intending to place its securities with French residents must act through a financial intermediary qualified to conduct business in France.

In order to conduct a placement of securities in France, a financial intermediary must be an authorized French "investment service provider" (*prestataire de services d'investissement*), or an equivalent entity in an EU Member State that benefits from the EU Single Passport system. French investment service providers must be approved by the Comité des établissements de crédit et des entreprises d'Investissements ("CECEI").

The marketing activities of qualified financial intermediaries must be structured carefully to avoid losing the benefits of the private placement exemption. In general, brokers' research reports and circulars may be distributed to professional and institutional investors acting for their own account in a private placement. However, if such documents are distributed after there has been a public announcement or solicitation with respect to the offering (e.g., after the publication of a press release or the general distribution of a preliminary prospectus), these reports and circulars could be deemed "public offering documents" and hence render the placement subject to registration requirements.

Similarly, road shows in France must be conducted in such a manner as to ensure that certain rules are respected: no more than 100 investors other than "qualified investors" can be invited, and all forms of public advertising should be avoided.

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18 Article L. 411-2 II 4° b) of the MFC.
19 US financial intermediaries might be able to argue that a private placement does not constitute a "placement" within the meaning of Article L.321-1 of the MFC, and that brokerage activities in connection with such a private placement are therefore not restricted to authorized investment services providers. This interpretation, however, is contrary to the AMF’s position, as expressed to us verbally.
20 Article L. 532-16 of the MFC.
21 Article L.532-1 of the MFC.
Resale of Securities issued under the Private Placement Exemption

In 1998, the former French securities regulator (the “COB”) suggested, though did not formally require, that purchasers of securities issued in a private placement should purchase with the intent to hold the securities. However, the AMF failed to state any specific or indicative holding period, either by regulation or other official statements.

By contrast, in the US, when investors acquire restricted securities through private placement offerings, they must benefit from an exemption from the SEC's registration requirements to resell them in the marketplace. Rule 144, for instance, allows public resale of restricted securities if, among other conditions, they are held for certain holding periods. If the company that issued the securities is subject to the reporting requirements of the Securities Exchange Act of 1934, then the investor must hold the securities for at least six months. If the issuer of the securities is not subject to the reporting requirements, then the investor must hold the securities for at least one year.

Similarly, equity securities placed offshore by US issuers under Regulation S (the safe harbor from the registration requirements of the Securities Act for offshore offers and sales of securities) are also classified as "restricted securities," so that resales of these securities without registration or an exemption from registration are also restricted. Under Regulation S, investors are subject to certain "distribution compliance periods" to ensure that during the offering period and in the subsequent aftermarket trading that takes place offshore, the persons complying with the safe harbor (issuers, distributors and their affiliates) are not engaged in an unregistered, non-exempt distribution of securities into the United States capital markets.

In the absence of equivalent bright-line rules governing resale, securities acquired in French private placements could prove less attractive to foreign investors. Nevertheless, following the launch by NYSE Euronext Paris of a stock exchange called Alternext, the AMF has alleviated those concerns. In a press release dated October 15, 2007, the AMF stated that the issuance of securities by issuers on Alternext to qualified investors under the private placement exemption does not prevent non-qualified investors from acquiring them later on the secondary market. The AMF did not set any minimum holding period. However, if a broker receives an order from a non-qualified investor to acquire such a security, the broker must carry out the necessary due diligence to ascertain whether the non-qualified investor is fully appraised of the specific risks associated with the applicable security. Furthermore, the AMF stated that both investment service providers and qualified investors on an exchange-regulated market (such as

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23 In a No-Action Letter dated March 16, 2007, the SEC stated that it would “not object if the reference to the Bourse de Paris in Rule 902(b) under the Securities Act of 1933 is deemed to be a reference to the Eurolist Market and the Alternext Market” (emphasis added). Accordingly, Alternext qualifies as a “Designated Offshore Securities Market” and an offer or sale of securities executed in, on or through the facilities of Alternext can qualify for the “offshore transaction” exemption under Regulation S.
Alternext) must refrain from targeting non-qualified investors through marketing, particularly through advertising or solicitation.\(^{24}\)

The resale of securities on the "professional" segment of Euronext Paris, set up in December 2007 to allow companies to list securities issued to qualified investors under the private placement exemption, raises similar issues.\(^{25}\) The AMF has amended its General Regulations to specifically provide that a non-qualified investor can acquire securities from qualified investors on the professional segment of Euronext provided that (i) the non-qualified investor decides to invest without any kind of solicitation or advertising and that (ii) such non-qualified investor has been duly informed by its investment service provider of the risks associated with acquiring such securities.\(^{26}\)

The above AMF press release and regulations point towards a more relaxed approach by the AMF when reviewing the resale of securities issued in a private placement to non-qualified investors: such resale is possible in principle, provided that the specified conditions are met.\(^{27}\) Nevertheless, any such resale should be reviewed carefully by the issuer, as a resale by means of solicitation or other forms of communication could be deemed a public offering, and the same criteria will apply to determine whether the prospectus regulations are triggered.\(^{28}\) Consequently, a company that issues securities to qualified investors pursuant to the private placement exemption might be deemed to have conducted a "passive" public offering if such investors resell them to over 100 non-qualified investors by means of solicitation or other forms of communication subject to public offering rules.\(^{29}\)

3. Other Exemptions from Public Offerings

French law provides two other types of exemptions for share offers that are not deemed to be public offerings, and as such are not subject to prospectus requirements. One concerns offerings to investment service providers performing asset management for third parties.\(^{30}\) The other exemption, for "local" offerings, is intended to facilitate start-up financing.

Under the local offering exemption,\(^{31}\) an offering does not require a prospectus if it falls into one of the following categories:

- offers for a total consideration of less than € 100,000, or the equivalent in another currency, calculated over a 12 month period following the first transaction;

\(^{24}\) AMF Press release, October 15, 2007. Article 314-43 et seq. of the AMF GR. These regulations aim to ensure that the non-qualified investor understands the specific risks attached to the applicable security.

\(^{25}\) This segment was set up to primarily attract institutional investors that operate in English in order to facilitate listing for foreign companies, particularly from emerging markets.

\(^{26}\) Articles 516-18 and 516-19 of the AMF GR.

\(^{27}\) AMF Press Release October 15, 2007, and Articles 516-18 and 516-19 of the AMF GR.

\(^{28}\) This is in line with Article 3(2) of the Prospectus Directive, which provides that any subsequent resale of securities which were previously the subject to a private offering shall be regarded as a separate offer and the definition for a public offering shall apply for the purpose of deciding whether that resale is an offer of securities to the public.

\(^{29}\) For reasons that remain unclear, certain issuers first admitted on Alternext by private placement later started filing a prospectus (GENFIT for instance).

\(^{30}\) Article L.411-2 II 4° of the MFC.

\(^{31}\) Article L.411-2 II 1°, 2° and 3° of the MFC. Article 211-2 of the AMF GR.
offers for a total consideration between € 100,000 and € 2,500,000, or the equivalent in another currency, calculated over a 12-month period following the first transaction, when the securities issued represent less than 50% of the capital stock of the issuer;

· offers for a consideration exceeding € 50,000, or the equivalent in another currency, per investor, for each separate transaction;

· offers of securities having a per unit price of at least € 50,000, or the equivalent in another currency.

4. The Marketing of Financial Products in France

The benefit of the private placement exemption in France is limited by restrictions on the canvassing of securities ("démarchage") that overlap with and in some cases contradict French public offering rules. The implementation of the Prospectus Directive into French law created new discrepancies between the two regimes, as transactions that are exempted from public offering regulations by the Prospectus Directive may still fall within the ambit of the démarchage regulations. Despite these discrepancies, the Reform Act failed to amend démarchage regulations.

Démarchage in connection with the offer of financial instruments is defined in the French regulations quite broadly, as (a) any unrequested solicitation of a specific individual or legal entity, by any means, for the purpose of obtaining his/her consent to realize a transaction involving financial instruments or to provide any investment services or activities; or (b) visiting persons at their homes, places of work or in any other place where such financial instruments are not supposed to be marketed, for the same purpose.32

For instance, sending letters, circulars or other marketing materials and making telephone calls to customers for such purposes are included within the definition of démarchage, whether these activities are carried out from within France or from abroad. The distribution of investment research materials for marketing purposes and the solicitation of potential clients to participate in brokerage activities such as roadshows, would also be considered démarchage under the MFC.

Where démarchage rules are deemed to apply, various consumer protection laws are triggered. Under the MFC, démarchage may be carried out only by (1) French credit institutions authorized by the CECEI; (2) registered French investment service providers; (3) French insurance companies; (4) venture capital companies ("sociétés de capital-risque") for distributions of their own shares or (5) equivalent entities in EU Member States that benefit from the EU single passport system, i.e., those authorized to conduct démarchage activities in their home states. Démarchage may also be carried out in France by (6) companies offering shares to their employees pursuant to certain profit-sharing plans and (7) financial investment advisors.33

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32 Article L. 341-1 of the MFC.
33 Article L 341-3 of the MFC.
Entities conducting *démarchage* must be licensed by the AMF, which maintains a central registry of *démarcheurs*.\(^{34}\) Furthermore, entities conducting *démarchage* must maintain professional insurance;\(^ {35}\) register with market regulators; obtain a personal *démarchage* card;\(^ {36}\) and provide potential investors a form to use if they decide to withdraw their offers.\(^ {37}\) Violation of the *démarchage* rules may be sanctioned by imprisonment and a €7,500 fine.\(^ {38}\)

The *démarchage* provisions do not apply to solicitation of “qualified investors.”\(^ {39}\) However, private placements targeting a "restricted group" of investors remain subject, on the face of the regulations, to *démarchage* rules, and thus require an information memorandum. Such information memorandum need not be approved by the AMF, but would be distributed under the sole responsibility of the *démarcheur*. The same is true for offers having a total consideration of less than €100,000, or for offers of between €100,000 and €2,500,000 which do not represent more than 50% of the outstanding capital of the issuer. These offers are exempt from formal prospectus requirements, but may fall within the scope of the *démarchage* regulations.

Placements to employees under qualified profit sharing plans are also exempt from the *démarchage* rules.\(^ {40}\) The exempt plans include *plans d'épargne d'entreprise* ("PEE"), under which companies and employees make contributions to reserved share accounts that hold stock of the employing company or shares of a mutual fund.\(^ {41}\)

The MFC prohibits the solicitation of investors in France for the purchase of securities that are not admitted to trading on a French regulated market or on a recognized foreign market.\(^ {42}\) The recognition of foreign securities markets is regulated by Article D. 423-1 and seq. of the MFC which empowers the Ministry of Finance, acting on the AMF's recommendation, to certify foreign securities markets as having sufficient levels of regulatory oversight and investor protection. For the US, the current list of approved markets includes primarily commodities and derivatives exchanges, such as the Chicago Mercantile
Exchange, the Chicago Board of Trade, the Amex, the New York Futures Exchange and the New York Mercantile Exchange.\textsuperscript{43}

Companies listed solely on non-approved foreign exchanges can privately offer their securities in France only under the "qualified investor" exemption,\textsuperscript{44} or pursuant to a profit sharing program of the type discussed above.\textsuperscript{45} French investors can also purchase securities traded on non-approved foreign exchanges on their own volition.

\textbf{Conclusion}

According to data from the CESR regarding the distribution of prospectuses approved by Member States, between July 2005 and June 2007, France, with 3\% of the total, had one of the lowest number of prospectuses approved in the EU since the Prospectus Directive came into force, in contrast with jurisdictions such as Ireland, with 26\% of the European total. Feedback from interviews conducted by the Centre for strategy and Evaluation Services suggest that some issuers use private placements to bypass EU Member States where the regulator has imposed restrictions and obligations that were additional to the minimum required under the Prospectus Regime.

In light of these shortcomings, France recently amended its public offering regime to further harmonize it with the Prospectus Directive and make the French financial market more attractive to foreign issuers.

Despite these recent amendments, new changes may be forthcoming. On January 9, 2009, the EU Commission launched a new consultation to revise the Prospectus Directive to reduce the burden and cost for companies and intermediaries. Such proposal would include amendments to the definition of qualified investors, the scope of exempt offers (such as employee share schemes) and certain thresholds under the Directive. These proposals will most likely lead to several amendments to the Prospectus Directive that will once again impact private placements in France.

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\textsuperscript{43} AMF Annual Report 2007, Exhibit 1.
\textsuperscript{44} The law does not define the term "public" within the meaning of Article L.423-1 of the MFC, prohibiting solicitation of the public in France for financial transactions performed on a non-recognized market. In our view, this term should not include qualified investors.
\textsuperscript{45} The AMF has verbally indicated to us that the prohibition of Article L.423-1 of the MFC applies only to financial intermediaries and not to issuers.
If you have any questions about the contents of this memorandum, please call your regular Fried Frank contact or any of the attorneys listed below.

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