Danny Busch and Matthias Lehmann*

Uniform Prospectus Liability Rules for Europe

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Abstract: In this contribution, we make the case for the introduction of uniform rules on liability for incorrect or incomplete prospectuses relating to financial instruments offered in the European Union (EU). We set out the reasons for such uniformisation, in particular the need to complete the Capital Markets Union, the insoluble conflict-of-laws problems created by prospectus liability, and the discriminatory treatment of investors resulting from the application of different national laws to the issue. We show that uniform rules are possible, drawing a parallel to the recently adopted Markets in Crypto-Assets Regulation (MiCAR) and other EU texts. We also demonstrate that the EU has the competence to adopt such rules, and that concerns about subsidiarity and proportionality are unfounded.

I Introduction

In the European Union, capital markets law is to a large extent harmonised, either by way of directives that provide for maximum harmonisation and which require transposition into national law, or, increasingly, by way of regulations with direct effect. Examples of the latter are the Market Abuse Regulation (MAR), the Prospectus Regulation, the Crowdfunding Regulation, the Sustainable Finance Disclosure Regulation (SFDR) and the MiCAR.[1]

1 Regulation (EU) No 596/2014 of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC [2014] Official Journal of the European Union (OJ) L 173/1 (MAR); Regulation (EU) 2017/1129 of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC [2017] OJ L 168/12 (Prospectus Regulation); Regulation (EU) 2020/1503 of 7 October 2020 on European

***Corresponding authors: Danny Busch,** Professor of Financial Law and Founding Director of the Financial Law Centre at Radboud University Nijmegen and a Senior Research Fellow at Harris Manchester College, University of Oxford, E-Mail: danny.busch@ru.nl
Matthias Lehmann, Professor of Private, Private International and Comparative Law at the University of Vienna and Rotating Professor of European and Comparative Business Law at Radboud University Nijmegen, E-Mail: matthias.lehmann@univie.ac.at

However, EU capital markets law does not traditionally feature uniform liability rules. A pertinent example is the Prospectus Regulation. If a company offers securities (such as transferable shares and bonds) to the investing public, this company must first publish an information document (prospectus) that complies with the detailed information requirements under the Prospectus Regulation and which requires prior approval by the competent financial regulator. The prospectus that must be published before securities are offered to the public is intended to provide interested investors with the information they need to decide whether or not to purchase them. Once the prospectus has been approved, it serves as a 'European passport'. This means that the securities to which the prospectus relates may be offered to the public on the basis of the approval by one national financial regulator throughout all Member States of the EU and the European Economic Area.

The Prospectus Regulation is primarily regarded as an instrument of EU financial supervision law. Information duties under the Regulation are part of administrative law. Compliance is monitored by the competent national financial regulator. In the event of non-compliance, it will use administrative measures of enforcement, for example by imposing a fine on the issuer.

II Reasons for adopting uniform prospectus liability rules

If the prospectus contains inaccurate or incomplete information that has affected the value of the securities offered, this may lead to civil liability of the company and the advising banks involved under applicable national liability law (prospectus liability). The Prospectus Regulation does not feature uniform prospectus liability rules, but instead calls on Member States to ensure that their laws, regulations and administrative provisions on civil liability apply to those persons responsible for the information given in a prospectus.[2] It provides some limits to liability, in particular with regard to the summary of the prospectus and the registration document.[3] Yet it does not set out any parameters for such liability, leaving open even funda-

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crowdfunding service providers for business, and amending Regulation (EU) 2017/1129 and Directive (EU) 2019/1937 [2020] L 347/1 (Crowdfunding Regulation); Regulation (EU) 2019/2088 of 27 November 2019 on sustainability – related disclosures in the financial services sector [2019] OJ L 317/1 (SFDR); Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets, [2023] OJ L 150/40 (MiCAR).

2 Art 11(2) subpara 1 Prospectus Regulation.

3 Art 11(2) subparas 2 and 3 Prospectus Regulation.

mental questions, such as the violations on which liability is based, the requirement of causation, the standard of culpability or the available civil remedies.[4]

These issues are currently governed by the applicable national liability rules, which vary from one Member State to another.[5] This is problematic for several reasons.

First of all, the law governing prospectus liability is highly uncertain. The conflict-of-laws principles of EU law refer primarily to the place of damage.[6] This place is virtually impossible to determine in the case of financial loss.[7]

Currently, the Court of Justice of the European Union (CJEU) takes the habitual residence of the investor – combined with the place of the bank account – as a proxy for the place of damage, but only under the condition that 'the other specific circumstances of that situation also contribute to attributing jurisdiction to those courts'.[8] This formula requires an assessment of the individual circumstances of each case, which is time consuming and produces highly uncertain outcomes. Uniform prospectus liability rules would eliminate such intricate conflict-of-laws questions that regularly arise in prospectus liability cases.

Moreover, the approach of the CJEU results in different prospectus liability standards for investors in the same securities. Depending on their habitual residence and the place of establishment of the bank managing their accounts, some investors will recoup more for the same violations than others. Such distinctions are unfair, discriminatory and counterproductive.[9] Following such a view would permit investors who are residents of certain States to raid the coffers of issuers. It may be asked why a habitual resident, for example, of the Netherlands, should be better protected than, for example, a domiciliary of Italy, even when both invest in the same stock traded on the same exchange. Another downside of this approach is that it makes the applicable liability regime unforeseeable for the issuer.

4 See further eg *D Busch*, The influence of the EU prospectus rules on private law, Capital Markets Law Journal 2021/1, 3.

5 That there exist important differences among the prospectus liability regimes in the EU is, for example, evident from the national reports in *D Busch/G Ferrarini/JP Franx* (eds), Prospectus Regulation and Prospectus Liability (2020) (featuring national reports on France, Germany, Italy, Luxembourg, Spain and The Netherlands).

6 See art 4(1) Rome II Regulation (Regulation [EC] 864/2007 of 11 July 2007 on the law applicable to non-contractual obligations [Rome II], [2007] OJ L 199/40).

7 See eg *M Lehmann*, Where Does Economic Loss Occur? 7 (2011) Journal of Private International Law (JPIL) 527–550.

8 CJEU 28.1.2015, C-375/13, *Kolassa v Barclays Bank plc*, ECLI:EU:C:2015:37, para 57; CJEU 12.9.2018, C-304/17, *Helga Löber v Barclays Bank plc*, ECLI:EU:C:2018:701, para 36.

9 *M Lehmann*, Prospectus Liability and Private International Law – Assessing the Landscape after the CJEU's Kolassa Ruling (C-375/13), 12 (2016) JPIL 318, 338.

These problems could to a large extent be eliminated if the EU were to adopt uniform prospectus liability rules. Moreover, a uniform legal regime in this area would also benefit the completion of the internal market. As the experience in other parts of the world teaches, prospectus liability is absolutely crucial as an enforcement mechanism for capital markets law. In the United States, it was harmonised as early as 1934 by the Securities and Exchange Act.[10] Interestingly, this is a regulatory act, which bears more than some resemblances with the EU Prospectus Regulation. Yet in contrast to the latter, it contains a fully-fledged private liability regime. That is no coincidence, but a consequence of the fact that private causes of action are an important enforcement mechanism for public law.[11] The private individual who sues an issuer or financial intermediary is seen in the US as not only self-serving, but also as furthering the public interest of safeguarding the honesty, transparency and reliability of financial markets, which is why such a litigant is sometimes likened to a 'private attorney general'.[12] This does have the important advantage of reducing the need for administrative personnel of the financial regulator, who is freed for other tasks. In addition, the claim brought by private individuals is arguably also a far more effective deterrent than the prospect of the imposition of a fine by the competent financial regulator.

In the EU, we are still in the pre-1934 state in comparison to US law. Clearly the EU is not a federal state, but if it is serious about building an effective and integrated market that can compete with that on the other side of the Atlantic, it cannot afford to ignore some hard lessons. Prospectus liability is not some accidental matter that can be left to the discretion of national legislators. Instead, it is an essential building block of capital markets law. The fact that the relevant rules in the EU vary from one Member State to another significantly distorts the level playing field for companies.

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10 See sec 18(a) Securities Exchange Act 1934 (15 US Code § 78r) ('Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this title or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsec [d] of sec 15 of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person [not knowing that such statement was false or misleading] who, in reliance upon such statement shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. … '). On this topic, see the contribution by *Marc I Steinberg* below.

11 See on this *W Kip Viscusi*, Regulation through Litigation (2004).

12 See *WB Rubenstein*, On What a Private Attorney General Is – And Why It Matters, Vanderbilt Law Review (57) 2004, 2129; *BG Garth/IH Nagel/S Plager*, The Institution of the Private Attorney General: Perspectives from an Empirical Study of Class Action Litigation, Southern California Law Review (61) 1988, 353.

Furthermore, it is also detrimental to the interests of investors, who will find it difficult to enforce their claims. In particular, they will encounter obstacles in joining collective actions because the applicable law in the EU is fragmented for the same class of investors. This does not allow the necessary economies of scope that are necessary to make such a collective action attractive to be achieved. The recently adopted Directive on representative actions[13] does not change this because it does not feature harmonised conflict-of-laws rules.[14]

Especially with a view to the completion of the internal market and the ambition of fully integrated European capital markets (the Capital Markets Union (CMU) Action Plan[15]), further harmonisation in Europe is absolutely crucial, also with regard to prospectus liability. Fast progress on these long-running projects is now more important than ever. The EU will only be able to maintain its autonomy in an ever-changing and uncertain world if it can effectively counterbalance superpowers such as China and the United States. The bloody war that Russia initiated against Ukraine on 24 February 2022 has made most of us realise that an autonomous and resilient Europe in all respects is also literally of vital importance. Such geopolitical considerations are now more than ever at the forefront of the European Commission's thinking.

Harmonisation of private law has always been a sensitive topic in Europe. It is therefore inevitable to face the question of whether the adoption of uniform prospectus liability rules is at all feasible. To provide a beginning of an answer, we would like to point to the following considerations, trends and developments.

III The EU has the competence to harmonise prospectus liability rules

First of all, there can hardly be any doubt that the EU has the competence to harmonise the rules on prospectus liability. Article 114 of the Treaty on the Functioning of

13 Directive (EU) 2020/1828 of 25 November 2020 on representative actions for the protection of the collective interests of consumers [2020] OJ L 409/1.

14 See its Recital 21.

15 See European Commission, Green Paper 'Building a Capital Markets Union', COM(2015) 63 final. For the latest version of the CMU Action Plan, see *European Commission*, Communication to the European Parliament, the Council, the European Economic and Social Committee, and the Committee of the Regions, 'A Capital Markets Union for people and businesses-new action plan', COM(2020) 590 final and <https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/capital-markets-union/capital-markets-union-2020-action-plan_en>.

the European Union (TFEU) empowers the EU to adopt measures for the approximation of laws of the Member States, inter alia by Regulation, with such Regulation having as its object the establishment and functioning of the internal market. We have already shown that harmonisation is crucial for the internal market. Article 114 TFEU is also not limited to the harmonisation of public law, but encompasses private law as well, with the EU being generally blind to the distinction between the two.

Fears that this would result in a general harmonisation of private law, which many Member States view with a sceptical eye, would not be justified. The topic is sufficiently specific and specialised to be dealt with by Union rules without any risk of depriving national codifications of private law of their value. The principle of subsidiarity[16] is also complied with: the intricate and infinite conflict-of-laws problems as well as the discrimination of investors clearly demonstrate that the objective of the rules can be better achieved by Union law than at the local or regional level. One must also not worry that the EU would not be able to supply the necessary content and certainty with regard to the application of such private rules. The Court of Justice has demonstrated in the past its ability to interpret and develop rules of private law, from the Unfair Terms Directive to the Consumer Rights Directive. There is no reason to think that it would not be able to also shape appropriate liability for defective prospectuses.

IV Substantive liability rules in EU capital markets law

Second, it is apparent from the more recent pieces of EU capital markets law that the EU no longer shies away from providing substantive liability rules, albeit in a piecemeal manner. EU capital markets law, for instance, features special liability rules for (i) credit rating agencies; (ii) investment fund depositaries, (iii) manufacturers of packaged retail and insurance-based investment products (PRIIPs); (iv) providers of Pan-European Personal Pension Products (PEPPs); and, in the near future, (v) parties offering crypto-assets to the public; and (vi) the use of artificial intelligence, which are intended to apply more broadly beyond the financial services industry.[17]

16 See art 5(3) TFEU.

17 Art 35a Credit Rating Agency Regulation (Regulation [EC] No 1060/2009 of 16 September 2009 on credit rating agencies [2009] OJ L 302/1, as amended); art 21 Alternative Investment Fund Managers Directive (Directive 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers and amend-

In the current context, the European liability regime applicable to parties offering crypto-assets to the public is of particular interest, due to the similarities with the activity of offering securities to the public. To stress these similarities, the offerings of crypto-assets to the public are in practice also referred to as initial coin offerings (ICOs), in parallel to initial public offerings (IPOs) of securities, which in the EU are subject to the Prospectus Regulation. For a better understanding of this point, it is necessary to zoom out for a moment.

The recently adopted MiCAR regulates the issuance of crypto-assets and related services. MiCAR excludes from its scope crypto-assets that qualify as securities.[18] These fall under the Prospectus Regulation.[19] The offering of crypto-assets that are not securities to the public is not subject to the rules of the Prospectus Regulation, so no prospectus needs to be published. It is, however, common practice to publish a so-called 'white paper' containing information about the crypto-assets on offer. MiCAR regulates this as follows.

To begin with, MiCAR distinguishes between asset-referenced tokens, e-money tokens and the other crypto-assets covered by MiCAR. For all three types of crypto-assets, prior to offering them to the public, a white paper must be published that meets the information requirements set by MiCAR, these requirements differing depending on the type of crypto-assets being offered.[20] For offerings of asset-referenced tokens, the competent financial regulator must approve the white paper in advance.[21] For other crypto-assets covered by MiCAR, including e-money tokens,

ing Directives 2003/41/EC and 2009/65/EC and Regulations [EC] No 1060/2009 and [EU] No 1095/2010 [2011] OJ L 174/1); art 24 and 79 Undertakings for Collective Investment in Transferable Securities (UCITS) Directive (Directive 2009/65/EC of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities [UCITS] [recast] [2009] OJ L 302/32, as amended); art 11 Packaged Retail Investment Products Regulation (Regulation [EU] No 1286/2014 of 26 November 2014 on key information documents for packaged retail and insurance-based investment products [PRIIPs] [2014] OJ L 352/1); arts 31 and 55 Pan-European Personal Pension Product Regulation (Regulation [EU] 2019/1238 of 20 June 2019 on a Pan-European Personal Pension Product [PEPP] [2019] OJ L 198/1); art 15 MiCAR (crypto-assets other than asset-referenced tokens and e-money tokens), art 26 MiCAR (asset-referenced tokens); art 52 MiCAR (e-money tokens). See finally the proposal for the Artificial Intelligence Liability Directive dated 28 September 2022 (COM(2022) 496 final).

18 Art 2(4)(a) MiCAR.

19 Art 2(a) Prospectus Regulation in conjunction with art 4(1) point (44) MiFID II (Directive 2014/65/EU of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU [recast] [2014] OJ L 173/349).

20 The content of the white paper is set out in art 6 in conjunction with Annex I MiCAR (crypto-assets other than asset-referenced tokens and e-money tokens); art 19 in conjunction with Annex II MiCAR (asset-referenced tokens); art 51 in conjunction with Annex III MiCAR (e-money tokens).

this is not required, but the white paper must still be sent in advance to the financial regulator for information purposes only.[22]

The three types of crypto-assets that MiCAR distinguishes are subject to distinct liability regimes when offered to the public.[23] However, these liability regimes have a similar structure that boils down to the following. Purchasers of crypto-assets have a damages claim against the offeror (and sometimes against other parties involved as well) if (i) the white paper infringes the requirements set by MiCAR, by providing information that is incomplete or unclear, or by providing misleading information; and (ii) the holder of the crypto-assets has suffered damage as a result of the infringement. A contractual provision limiting or excluding such liability shall have no legal effect ('shall be deprived of any legal effect'). The holder of the crypto-assets must prove that (1) the white paper infringes the requirements set by MiCAR; and (2) that this infringement had an impact on his or her decision to buy, sell or exchange the crypto-assets. The white paper should also always include a summary. However, liability of the provider (and possibly others involved) for the summary alone is excluded, although they can be held liable on the basis of the summary read in conjunction with other parts of the white paper. Liability based on MiCAR does not affect liability claims based on national law.

If it is feasible to agree on European rules on 'white paper liability', it should, in our view, also be possible to agree on uniform prospectus liability rules in Europe.

Admittedly, the European rules for white paper liability are still relatively rudimentary. They raise many questions and it is often necessary to include national liability law and national procedural and evidentiary law in the analysis. For now, European law is simply not a fully-fledged legal system capable of operating completely autonomously from national law. Since, for the time being, national courts have jurisdiction to take cognisance of liability issues of this kind, one can only hope that they will apply these liability rules with due regard to their European origins,

21 See art 17(1)(a) MiCAR for credit institutions. Other issuers require an authorisation, for which the white paper will be examined, see art 21(1) 2 MiCAR.

22 Art 8 MiCAR (crypto-assets other than asset-referenced tokens and e-money tokens); art 51(11) MiCAR (e-money tokens).

23 Art 15 MiCAR (crypto-assets other than asset-referenced tokens and e-money tokens), art 26 MiCAR (asset-referenced tokens); art 52 MiCAR (e-money tokens). Incidentally, art 75(8) MiCAR also contains a liability regime for 'crypto-asset service providers that are authorised for the custody and administration of crypto-assets on behalf of third parties' regarding loss of crypto-assets. Finally, see art 94(7) MiCAR: 'A person making information available to the competent authority in accordance with this Regulation shall not be considered to be infringing any restriction on disclosure of information imposed by contract or by any legislative, regulatory or administrative provision, and shall not be subject to liability of any kind related to such notification.' We will leave art 75(8) and art 94(7) MiCAR here because they are not relevant for this contribution.

and that they will be prepared to submit preliminary questions to the CJEU if that is indicated.

V Revival of the idea of a European codification

Third, Europe could also take a more ambitious, less fragmented, course. Not that long ago, a whole generation of civil lawyers argued assiduously for a European civil code, and when that proved impossible, a European sales law. That too never materialised.[24] Subsequently, a long silence reigned from this corner of academia.

Since Brexit, this has changed. French and German academics in particular have revived the idea of a European codification but in a different form. Namely, they are no longer aiming for a European civil code, but are rather focusing on topics that are closer to the home of EU legislation. The French Association Henri Capitant, for instance, is in the process of drafting a European Business Code (*Code Européen des Affaires*), including one book on banking law (*Droit Bancaire*) and another on financial markets law (*Droit des Marchés Financiers*).[25] Whether this project will suffer the same fate as once did the European Civil Code Project remains to be seen.

In any case, the world has changed significantly in the meantime. Indeed, as discussed, besides the argument of a level playing field and the completion of the internal market and achieving the goal of the CMU plans, geopolitical arguments now argue in favour of more harmonisation in Europe. Common lawyers are traditionally less keen on codifications, but now that the UK has left the EU, little effective opposition is to be expected from that quarter in any case. Seen in this light, a codification project might now perhaps be less complicated, provided that Ireland (after all, also a common law jurisdiction) can live with it, although Ireland will in any case carry less weight than the UK. On the other hand, nationalist forces are at work in several Member States that might be less happy with a European Business Code. It remains to be seen which influences will ultimately prevail.

24 See in this regard, eg, *N Jansen*/*R Zimmermann* (eds), Commentaries on European Contract Laws (2018); *MW Hesselink*, Justifying Contract in Europe (2021).

25 See <https://www.henricapitant.org/actions-category/travaux-europeens/>; <https://www.henricapitant.org/actions/avant-projet-relatif-au-droit-bancaire-et-des-marches-financiers-2021/>. For a discussion, see *M Lehmann*, EU Law-Making 2.0: The Prospect of a European Business Code (2020) European Review of Private Law 73–106.

VI The way forward

In view of all of the above, harmonisation of the prospectus liability rules in Europe may actually be feasible and should urgently be put on the legislative CMU agenda of the European Commission. The rules could be included in a future version of the Prospectus Regulation, or, if these plans come to fruition, in a European Business Code.

In any event, we have already taken the initiative of setting up an international working group for the purpose of drafting possible rules for a European prospectus liability regime. This group will not only consist of academics and practitioners from Europe, but also from the US to inform the work of the group. Through a comparative investigation into the laws of several European countries and the law of the US with its decade-long experience in the area, we aim to show that such uniformisation is both necessary and feasible.

VII The content of this special issue

The special session on Prospectus Liability that we had the honour of organising on 14 April 2023, as part of the 22nd Annual Conference on European Tort Law in Vienna, established the first step in our comparative law investigation. This special issue of the Journal of European Tort Law contains the reworked presentations of the speakers.

The first article, by Marc I Steinberg (Dallas, USA), addresses prospectus liability in the US. The key statutes and Securities and Exchange Commission rules and regulations are addressed in conjunction with an analysis of the causes of action and defences that are applicable. While the US prospectus framework is thorough, substantial gaps exist that should be remedied. The article accordingly focuses on principal aspects of US prospectus liability exposure and proffers recommendations for improving the overall framework.

The second article, by Paola Lucantoni (Rome, Italy) focuses on the relevant breach of duties under art 11 of the Prospectus Regulation, which provides only few elements of the private enforcement model, leaving the specific choices of the civil liability regime to the Member States. The main purpose of this paper is to underline the contradiction that exists between (i) a rigid formalism in the Prospectus Regulation and the extensive administrative rulebook and related soft law, which imposes binding formats and contents of prospectuses in order to enhance maximum harmonised investor protection and reduce issuers' costs in Europe, and (ii) the existing different prospectus liability regimes among the EU Member States, which undermine the effectiveness of Union law on prospectuses. In order to highlight this contradiction, the contribution analyses the different legal bases of prospectus liability provided in a sample of Member States, focusing on the different (and sometimes conflicting) methods of defining, from the defendant's side, the persons responsible and liable for the incompleteness or the incorrectness of the prospectus, and, from the plaintiff's side, the persons who can sue for damages.

The third article, by Arnoud Pijls (Rotterdam, The Netherlands) concentrates on prospectus liability and causation. When establishing causation, it is the factual basis of the claim and the corresponding line of argumentation that determines the perspective that should be taken as a starting point. The author argues that there are basically two factual bases that can be distinguished. For the first factual basis of causation, the reliance of the investor on the prospectus is irrelevant. For the second factual basis, reliance is, however, relevant. In its *World Online* decision, the Dutch Supreme Court adopted a presumption of reliance for both factual bases of causation. This presumption of reliance is based on art 11(2) of the Prospectus Regulation. In the opinion of the author, this provision does not provide a convincing basis for the adoption of such a presumption. Article 11a(1) of the Unfair Commercial Practices Directive[26] provides a much more convincing basis.

26 Directive 2005/29/EC of the European Parliament and of the Council of 11 May 2005 concerning unfair business-to-consumer commercial practices in the internal market, [2005] OJ L 149/22.