



## **3L3 Consultation Paper**

# **Guidelines for the prudential assessment of Mergers and Acquisitions**

**Jo Swyngedouw**

**3L3 Public Hearing, CEBS offices, 19 September 2008**



## Outline

1. **Opening remarks**
2. **Changes implied by the five assessment criteria**
3. **Practicalities of the cooperation process**
4. **Assessment of an acquisition: list of information required**



## 1. Opening remarks

- **The role of the 3L3 Committees**
- **The current state of play for prudential assessment of mergers and acquisitions**
- **The Consultation Paper**
- **The Public Hearing**



## The role of the 3L3 Committees

- Established in 2001 (CESR) and 2003 (CEBS, CEIOPS)
- High level representatives from the supervisory authorities of the 3 financial sectors
- 27 Member States + Observers
- Chairs: Kerstin af Jochnick (CEBS), Eddy Wymeersch (CESR), Thomas Steffen (CEIOPS)



## The role of the 3L3 Committees

### Objectives:

Promote efficient and effective supervision and the safety and soundness of the EU financial system through:

- Good supervisory practices
- Efficient and cost-effective approaches to supervision of cross-border groups
- Effective regulation
- Level playing field and proportionality

### Main tasks:

- Give advice to the Commission
- Promote consistent implementation/application of the EU legislation and enhance convergence of supervisory practices
- Exchange information and enhance supervisory cooperation
- Alert on financial stability



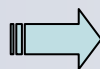
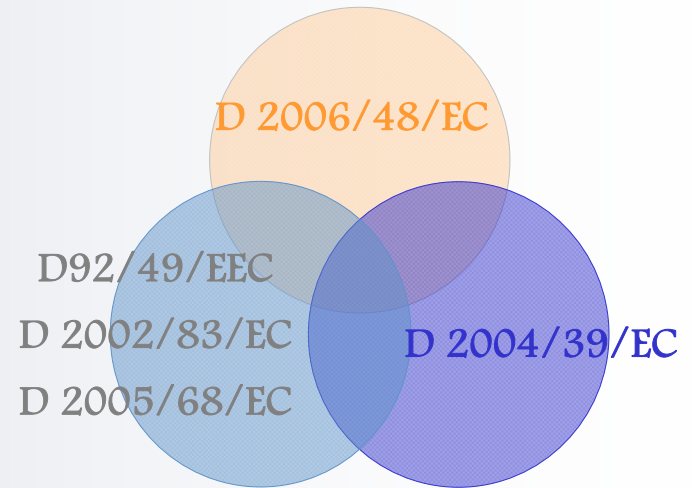
## The role of the 3L3 Committees

- Joint Protocol (Nov 2005)
- Impact of the Lamfalussy process
- 3L3 Annual and medium-term work programmes
- Joint work on financial conglomerates, anti-money laundering, commodities, internal governance, delegation, etc...

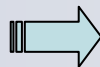


# The foundations for prudential assessment of mergers and acquisitions

The  
sectoral  
directives



*Minimum harmonization*



*Commonalities in F&P requirements*





## Directive 2007/44/EC of 5 September 2007

- cross sector perspective
    - 1) Procedural rules
    - 2) Evaluation criteria
  - maximum harmonization
  - proportionality
  - transposition by 21 March 2009
- ⇒ **Need for 3L3 guidance**

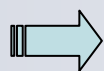




## The 3L3 Cross border Mergers and Acquisitions Task Force



- Established in January 2008
- Chair: Jo Swyngedouw (CBFA)
- 24 members from 20 countries
- Follow-up of CEBS' work
- 3 meetings, 2 telcos



**Consultation Paper (July 2008)**



# The Consultation Paper

## Objectives

1. Reach a common understanding on the five assessment criteria
2. Define appropriate cooperation arrangements
3. Establish an exhaustive and harmonised list of information requirements



# The Consultation Paper

## General Principles

1. No interpretation of D. 2007/44/EC
2. Proportionality applies to the information required and the assessment procedures
3. Scope : in the event of acquisition or increase in a qualifying holding (limited number of thresholds)



## Notification requirement

- **Who?**
  - A proposed acquirer (direct or indirect)
  - All persons acting in concert
  
- **When?**
  - As soon as the decision to acquire, increase or reduce a qualifying holding is taken
  - In the case of an involuntary crossing of a threshold (both ways)
  
- **What?**
  - ~ All the information required, but possibility to exempt certain pieces of information



## Assessment timeline for the supervisor of the target institution

1. Reception of notification + all required information

2 working days

2. Written acknowledgment of reception + deadline for the assessment

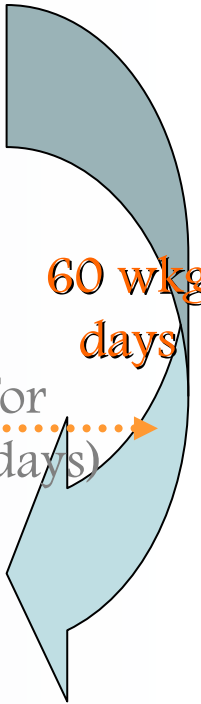
60 wkg days

Interruption possible for additional info (max 20 days)

4. If negative decision, written notification

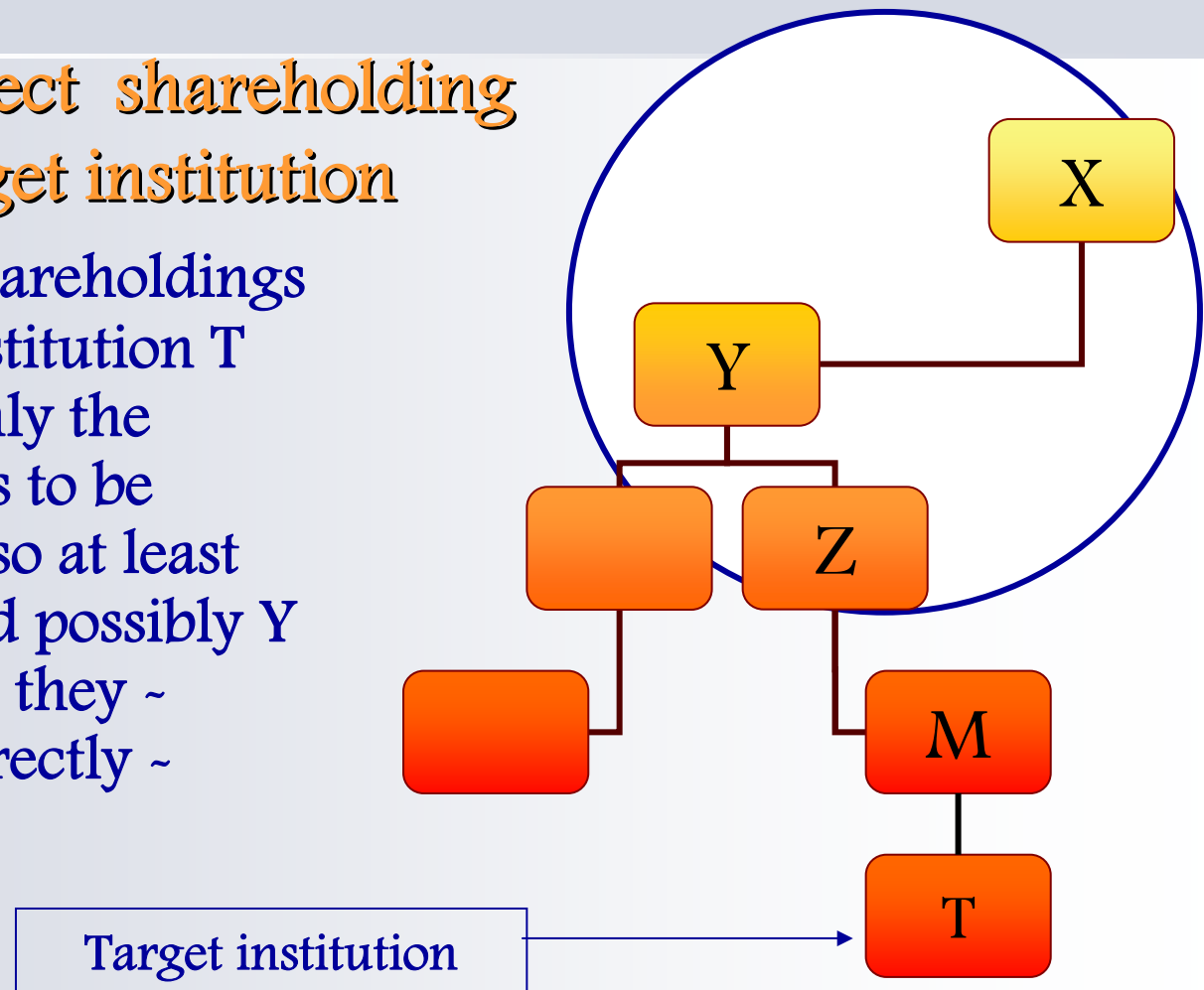
2 wkg days

3. Decision



## Case of indirect shareholding of the target institution

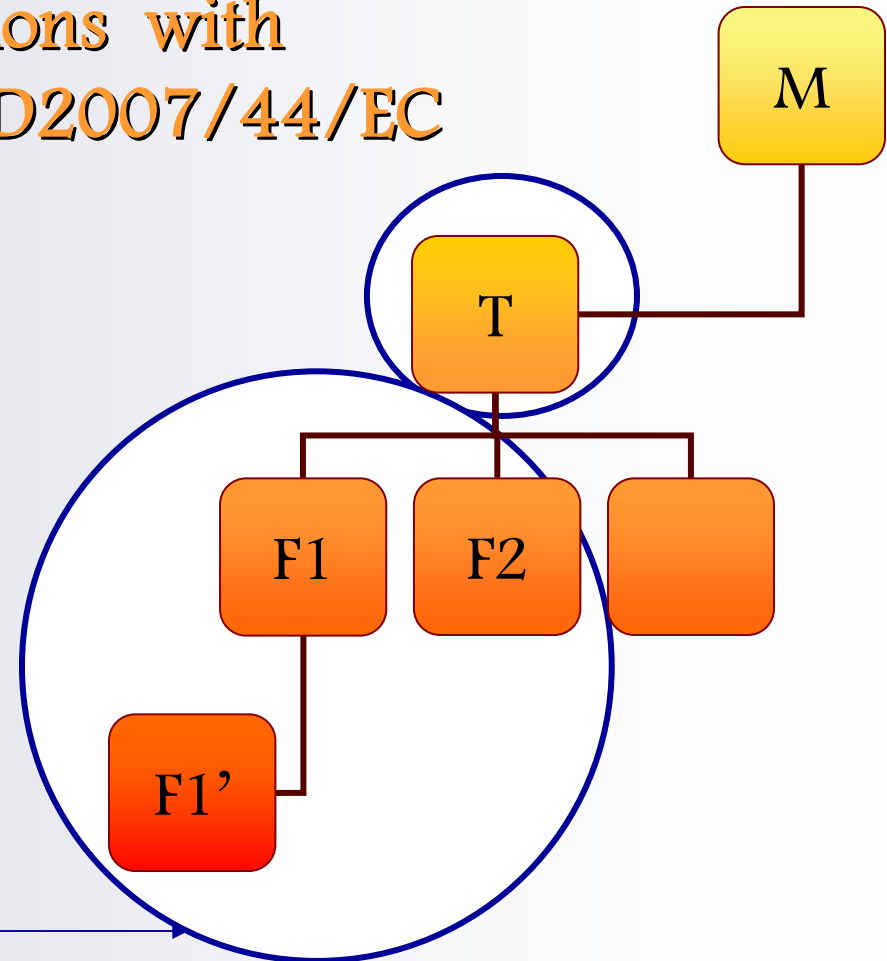
If significant shareholdings of the target institution T are held, not only the company M has to be assessed, but also at least company X, and possibly Y and Z (as far as they ~ directly or indirectly ~ control M)





## Case of a target institutions with subsidiaries subject to D2007/44/EC

If the target institution directly or indirectly controls financial institutions supervised in the EEA, each of these (F1, F1' and F2) are also considered as 'target financial institutions'.



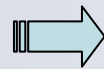
EEA financial institutions





## Competent supervisory authority

- The responsibility for the decision remains with the authority responsible for the supervision of the target institution
- In the case of a target institution with controlled subsidiaries supervised in the EEA: a decision is also required from each authority responsible for the supervision of the target institution's subsidiaries



**Coordination is key**



## The Consultation process

- Open to all interested parties
- 11 July – 3 October 2008
- Public hearing on 19 September 2008
- Written responses and related feedback from 3L3 TF to be posted on the 3L3 Committees' websites



## Outline

1. **Opening remarks**
2. **Changes implied by the five assessment criteria (*Alessandra Dealdisio*)**
3. **Practicalities of the cooperation process**
4. **Assessment of an acquisition: list of information required**



## Directive 2007/44/CE

In order to ensure the **sound and prudent management** of the credit institution in which an acquisition is proposed, and having regard to the **likely influence** of the proposed acquirer on the credit institution, the competent authorities shall appraise the **suitability** of the proposed acquirer and the **financial soundness** of the proposed acquisition against a **list of criteria**



## Changes implied by the five assessment criteria

### ■ Main changes

- ~ Reputation of the proposed acquirer, incl. AML (C1 & 5)
- ~ Financial soundness of the proposed acquirer & future compliance of the target institution (C3 & 4)
- If the proposed acquisition involves the appointment of new directors or managers:
  - ~ Reputation of the persons who will direct the business at the target institution (C2)



## Reputation of the proposed acquirer (C1), including AML (C5)



- ~ What? Assumption of good repute if no negative records
- ~ Who? Proposed acquirer and possibly connected persons
- ~ Proportionality does not apply

- ~ management & technical
- ~ persons who direct the business + legal person
- ~ Proportionality applies



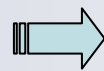
## Reputation of the proposed acquirer (C1), including AML (C5)

1. How to determine the existence of "any doubts about the integrity and professional competence" of the proposed acquirer?
2. How to determine the existence of "reasonable grounds" to suspect ML or TF in connection with the proposed acquisition?





## Reputation of the proposed acquirer (C1)

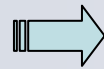


### Integrity

- Criminal records: not only convictions for any relevant criminal offence but also any criminal offences currently being tried or having been tried in the past
- Investigations and/or enforcement actions or the imposition of administrative sanction
- Correctness in past business dealings: situations which may cast doubts on the integrity of the acquirer



## Reputation of the proposed acquirer (C1)



### Professional competence

- Management competence: experience in acquiring and managing holding
- Technical competence: experience in operating and managing financial firms

Proportionality: the need for technical competence will be greater when the influence on the management is strong



## Suspicion of money laundering or terrorist financing (C5)

- The circumstances surrounding the acquisition would lead a reasonable person to suspect that the transaction involves the proceeds of criminal activity
- The context of the acquisition is not completely clear
- The acquisition would increase the risk of ML/TF

Proportionality does not apply



## Financial soundness of the proposed acquirer (C3)

Capacity to finance the proposed acquisition & to maintain a sound financial structure for the foreseeable future

- Identify any financial difficulties or conflict of interest
- Proportionality applies with respect to:
  - ~ *the nature of the proposed acquirer* (legal/natural person? supervised or not? In the EEA or equivalent countries?...)
  - ~ *the nature of the acquisition* (change of control? Involvement of the proposed acquirer in the management of the target?...)



## Future compliance of the target institution with the prudential requirements (C4)

- Compliance with all the prudential requirements including requirements related to governance arrangements, internal control, risk management, compliance
- The group structure resulting from the acquisition: effective supervision, exchange of information, clear responsibilities

⇒ *Clear link between C3 & C4*

The prospective soundness of the target institution presupposes the financial soundness of the acquirer

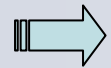


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*(James Borley)*
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## Practicalities of the cooperation process

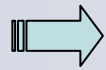


**Various *practical consequences* as a result of the guidelines in relation to criteria 1, 3 and 5.**





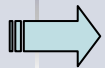
## First criterion: Reputation of the proposed acquirer (integrity and professional competence)



**Scenario 1: Acquirer is supervised by the same competent supervisor in the same country or in another Member State**

**Generally met if acquirer is:**

- Considered to be “of good repute”;
- [Natural person] holding a post (manager etc) supervised by the same competent supervisor / supervisor of same MS / or other MS;
- [Legal person] regulated and supervised as a financial institution by the same competent supervisor / supervisor of same MS / or other MS.



## **Scenario 2: Acquirer is supervised by a competent supervisor in a third country**

**Assessment or integrity may be based on substantial equivalence of the regulations concerning integrity requirements in a third country, facilitated by cooperation, if acquirer is:**

- **Considered to be “of good repute”;**
- **[Natural person] holding post (manager etc) supervised by third country;**
- **[Legal person] regulated and supervised as financial institution in third country.**



## Third criterion: Financial soundness of the proposed acquirer

**The cooperation will depend on the nature and location of the acquirer:**

- **If a supervised entity in another Member State, the assessment of the financial soundness will rely heavily on the assessment made by the acquirer supervisor which will have all relevant information available.**
- **If in a third country considered ‘equivalent’, the assessment may be facilitated by cooperation with that competent supervisor.**



## Fifth criterion: Suspicion of Money laundering or terrorist financing

### *Owners*

- 'Reasonable grounds' important
- Missing, incomplete, insufficient, information or information otherwise liable to give rise to suspicion should trigger increased supervisory diligence and requests for further information from the acquirer supervisor.

### *Funds*

- Funds used for the acquisition are channelled through chains of financial institutions subject to supervision by competent authorities in the EEA or equivalent third countries.
- History of the business activities of the acquirer and on the financing scheme should be consistent with the value of the deal.
- an uninterrupted paper trail back to their origins, or other information to alleviate all doubt as to their legal origin.



## Guidance to facilitate coordination and exchange of information between supervisory authorities

**The directive sets a tight timeframe for the authorities (60 days); needs prompt and efficient cooperation between authorities. Facilitated by:**

- **Use of e-mail – immediacy and security**
- **Preliminary dialogue**
- **Limited number of persons – efficiency and security**
- **Standardised formats for communication – model template**



## Practical Concerns

### 1. Initiation

- **Target supervisor to inform acquirer supervisor as soon as possible of:**
  - **identity of acquirer**
  - **identity of target**
  - **description of the proposed transaction, including:**
    - **the size of the intended holding (change in control or qualifying holding);**
    - **information on the current stage in the planned acquisition process;**
  - **contact details for those at the target supervisor dealing with the proposed acquisition; and**
  - **a list of other supervisors that could be involved in the assessment process.**



## **2. Need for cooperation?**

- **As soon as possible, upon receipt and analysis of formal notification, the target supervisor to determine need for and scope of cooperation with other supervisors and the subject matter for such cooperation.**
- **The target supervisor should then re-contact the acquirer supervisor(s) promptly re exchange of information and cooperation between supervisors.**

## **3. Information exchange**

- **the shareholding structure;**
- **the most recent assessments of:**
  - **suitability;**
  - **financial soundness,**
  - **quality of the management structure**
- **any other views or concerns**





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## List of information required

- The Directive requires a fixed list  
⇒ all information required to launch the assessment process.
- The information requirement must be proportionate to the particularities of each proposed acquisition.
- The list of information is divided into **two sections**.
  - General information requirements: all information normally requested by the target supervisor concerning
    - the nature of the proposed acquirer
    - and the proposed acquisition,regardless of percentage of capital or voting rights that the acquirer will have in the target financial institution
  - Specific information required on the basis of the proportionality principle, distinguishing between two cases:
    - Case 1) When the acquisition will result in a change in control over the financial institution,
    - Case 2) When acquirer will not gain control over the target financial institution but will acquire a qualifying holding.



### Case 1- Change in control:

- In this case the proposed acquirer need to provide a business plan to the target supervisor.

### Case 2 - Acquisition of a qualifying shareholding:

- Information required should be proportionate to the presumed degree of involvement of the acquirer in the management of the target financial institution.
- The Supervisor should have the possibility to verify the information.
- The target Supervisor may exempt from providing some information : on a case by case basis



# **I. General information requirements**

## **1. Identity of the proposed acquirer**

In the case of

- a) a natural person,
- b) a legal person or
- c) a trust

## **2. Additional Information on the Acquirer**

concerns issues such as : criminal record, investigations, authorisations, previous assessments financial position and strength ratings financial and non-financial interests. Further list of persons who direct, any companies in the acquirers group

## **3. Information on the Acquisition itself – identification of the target institution**

## **4. Information on the financing of the institution**



## **II. Specific information proportionate to the level of the shareholding to be acquired.**

### **A. Change in Control (as defined by sector directives)**

**Requires a business plan containing information on the contemplated strategic development plan justifying the acquisition, prospective data, and details on principal modifications or changes in the target institution envisaged by the proposed acquirer:**

- I. Strategic development plan**
- II. Estimated financial Statements of the target financial institution, solo and consolidated for 3 yrs**
- III. Impact of the acquisition on the corporate governance and general organisational structure**



## **B. Qualifying shareholding without change in control**

The proposed Acquirer should provide a strategy document- in accordance with the proportionality principle - the level of information to be provided will vary depending on the level of influence on the management and activities of the target institution.

- **Qualified holding less than 20 %**
  - Policy of the acquirer regarding the acquisition
  - Intentions of the acquirer towards target institution
  - Information of the intentions of the acquirer towards the target institution (intention to act)
  
- **Qualified holding between 20 and 50 %**
  - Same as below 20 % but in more detail
  - Detail on the influence the acquirer intends to exercise on the financial position (including dividend policy), strategic development, allocation of resources of the target institution
  - Description of the acquirer's intentions and expectation in the medium term covering the elements of the business plan.



### *Control*

- The notion of ‘control’ of the target financial institution shall be understood as defined in the sectoral directives, i.e. "*the relationship between a parent undertaking and a subsidiary, as defined in Article 1 of Directive 83/349/EEC or a similar relationship between any natural or legal person and an undertaking*".

### *Qualifying holding*

- ‘Qualifying holding’, as defined in Directives 2002/83/EC, 2004/39/EC, 2005/68/EC, and 2006/48/EC, means a direct or indirect holding in an undertaking which represents 10% or more of the capital or the voting rights of an undertaking or which makes it possible to exercise a significant influence over the management of the undertaking. In the case of ‘*indirect qualifying holders*’, such as cascading holdings that span different Member States, the immediate acquiring institution must notify each of the jurisdictions, while (as stipulated in the Directive) the responsibility for the final decision regarding the prudential assessment remains with the competent supervisor of the entity in which the acquisition is proposed.





**Deadline for sending responses to the  
consultation paper:**

**3 October 2008**

**to**

**[m&a@c-ebs.org](mailto:m&a@c-ebs.org)**

**(Earlier welcome too!)**