	Comments Template on EBA, EIOPA and ESMA's Joint Consultation Paper (JC CP 2012 01) on its proposed response to the European Commission Call for Advice on the fundamental Review of the Financial Conglomerates Directive	**Deadline: 13.08.2012 cob**
Stakeholder:	European Private Equity and Venture Capital Association (EVCA) Bastion Tower, Place du Champ de Mars 5, B-1050 Brussels - BELGIUM	

The question numbers below correspond to Joint Consultation Paper JC CP 2012 01

Please follow the instructions for filling in the template:

- Do **not** change the numbering in column "Question".
- Please fill in your comment in the relevant row. If you have no comment on a question, keep the row empty.
- There are in total 10 questions. Please restrict responses in the row "General comment" only to material which is not covered by these 10 questions.
  - If your comment refers to multiple questions, please insert your comment at the first relevant question and mention in your comment to which other questions this also applies.
  - If your comment refers to parts of a question, please indicate this in the comment itself.

Please send the completed template to joint-committee@eba.europa.eu, jointcommittee@eiopa.europa.eu, and joint.committee@esma.europa.eu**, in MSWord Format.**

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CFA Questions	Comments
General Comments	The European Private Equity and Venture Capital Association (“EVCA”) welcomes the opportunity given by the European Banking Authority (“EBA”), the European Insurance and Occupational Pension Authority (“EIOPA”) and the European Securities and Markets Authority (“ESMA”) in their Joint Consultation Paper[1] (“the Consultation paper”) to provide comments on the matters raised in the Consultation paper, and, more generally, on the review of Directive 2002/87[2] (“FCD”). Rather than answering the questions of the Consultation paper, EVCA’s response will provide specific comments and remarks on the Consultation paper, focusing on the areas of key relevance for the private equity and venture capital industry (PE), regarding the scope of the FCD, supervisory powers and the adoption of Guidelines on waivers. EVCA would like to draw the attention of the ESAs and the Commission to the need to take into account the specificities of the PE industry and ensure sufficient tailoring in connection with the Fundamental review. **1) The scope of the FCD and the perimeter of supervision** EVCA welcomes the efforts made to ensure the sound regulation of financial conglomerates and of their banking, insurance and investment firm activities. To the extent that mixed banking/investment services and insurance groups subject to the FCD act as AIFMs, EVCA acknowledges that it is appropriate to include such activities in the scope of supplementary supervision. As stated by the Hungarian Presidency of the Council of the EU during the 2011 review, monitoring is justified where an AIFM is owned by a financial conglomerate.

[1] JC/CP/2012/01.

[2] Directive 2002/87 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate.

	However, EVCA has always understood that the FCD neither intends nor should result in PE groups being identified as financial conglomerates solely by virtue of the fact that they make investments in the financial sector.[3] While EVCA agrees that supplementary supervision should capture financial activities that pose a risk to financial conglomerates, it is concerned with the ESAs' suggestions regarding the treatment of holding companies, which appear to go significantly beyond the definition of financial conglomerates in the Directive and potentially imply a further change in the scope of the FCD. In particular, the ESAs refer to "large complex groups",[4] i.e. groups which provide financial services to clients and markets but do not qualify as financial conglomerates and indicate that supervisors should be able to monitor such groups, with a focus on their financial activities. Such a change could result in **unintended consequences**: EVCA submits that simply because a group includes a wide range of activities, such as a PE group, is not a justification for treating it as a financial conglomerate. Annex E also reinforces our concerns about the interpretation of the Directive and its scope; in particular, the third graph of Annex E (on page 78) is not aligned with the definition of financial conglomerate and the requirement that a conglomerate must have both banking/investment firm **and** insurance activities. EVCA contends that such changes and unintended consequences should be avoided, for the following reasons: -Firstly, PE groups are not cross-sectoral financial conglomerates. Under Article 3 (2) FCD, the relative size of both the balance sheet and the solvency requirements of entities within the various financial sectors are assessed in order to determine whether the group is sufficiently cross-sectoral to constitute a financial conglomerate. But the intent of the legislator was never for PE

[3] It should be noted that for the private equity industry, in 2011, financial services represented globally 7 to 8% of the volume of buyout investment and 4% of the invested companies.

[4] Cf. para. 50 of the Consultation paper.

	groups to be caught within the scope of the FCD merely because they have invested in both banking and insurance companies. PE groups typically include portfolio companies in a wide range of businesses. Imposing supplementary supervision over the whole group because of (potentially quite limited) activities in the banking/investment firm and insurance/reinsurance businesses would risk catching a large number of companies in completely different businesses for which such supervision would be inappropriate. -Secondly, the FCD is meant to regulate financial conglomerates and to address a number of specific issues (such as multiple-gearing, group risks and systemic risk), none of which are relevant in the context of the PE industry: • Given the characteristics of the PE model, the risk of multiple-gearing of the same funds for separate banking and insurance entities in which an AIFM has invested is non-existent: PE investments are made through separate vehicles and are carefully siloed, separated from one another, so that investments may be monitored and managed on an individual basis by the AIFM. • None of the "group risks"[5] addressed by the FCD arise in PE groups: there is no concentration of risk, and conflicts of interest are strictly avoided, AIFMs' activities being regulated under the AIFM Directive. Investments made by AIFMs backed by long-term commitments from their investors and their funds are siloed, using transparent and separate management structures. There is therefore no contagion risk. • As recognised in the De Larosière Report, the PE industry does not create systemic risk, and given the characteristics of PE investments as outlined above, additional prudential supervision of AIFMs as financial conglomerates would serve no purpose. **Therefore, EVCA urges the ESAs and the European Commission to carefully assess the impact of any modification to the scope of the FCD and to be mindful that the Fundamental review does not inadvertently characterize PE groups as financial conglomerates. It also strongly encourages them to confirm, as was the case in 2011, that PE groups should not be covered as such, but only where an AIFM is owned by a financial conglomerate.**

[5] Cf. below under Point 3 for further explanations regarding the absence of "group risks" in PE groups.

2) Supervisory powers and enforcement under the FCD

The Consultation paper also provides a number of suggestions regarding the powers of supervisors in the European Union. Various solutions are examined by the ESAs in the Consultation paper: a tool kit designed to help competent authorities efficiently supervise Mixed Activity Holding Companies (MAHCs) and Mixed Activity Insurance Holding Companies (MAIHCs), as well as Mixed Financial Holding Companies (MFHCs), strengthening current requirements, using preventive measures and/or corrective measures, producing guidelines and harmonised standards.

EVCA considers that additional powers on top of existing supervisory powers should be **limited to what is necessary to capture financial risks within financial conglomerates, and should not extend supervision towards non-financial activities.** The tools and measures considered in the Consultation paper appear problematic for the following reasons:

First, the **supervisory tools** suggested in the Consultation paper include the following: (i) requiring an intra-group restructuring to create an intermediate financial holding heading all the entities carrying out financial activities subject to supplementary supervision, (ii) designating a specific department, team or Board member of the ultimate parent entity of the non-financial group, and/or (iii) designating one of the regulated entities in the financial conglomerate, rather than the ultimate parent or an intermediate non-regulated holding, as the supervisors' "single point of entry" under FICOD).[6]

Even though EVCA understands the reason for the proposal to identify an "ultimate responsible entity", such tools are not appropriate to PE groups. Besides the difficulties that may arise in its enforcement, Tool 1 appears disproportionate in view of its objectives. The inclusion of MAHCs and MAIHCs is supposedly considered for very limited purposes only, namely for providing the relevant supervisory information and for internal governance requirements. Requiring an intra-group restructuring is the least proportionate of the three tools, and would entail a concentration of financial activities and of risks. The autonomous choices of groups with respect to their internal structure and governance must be protected, as long as it is not used to circumvent the rules.

[6] Cf. paras. 6, 61 ss of the Consultation paper.

In addition, given the details provided in the Consultation paper, it is not clear how tools 2 and 3 would apply in a PE context and how useful it would eventually prove for the supervisor; the information needed should preferably be sought at sectoral level (with the help of the competent authorities) rather than at group level, when possible.

Second, the Consultation paper examines measures which may be taken against holding companies or group structures where they are considered inappropriate to effectively control financial risks (by requiring a transfer of ownership, change in governance, withdrawal of a declaration of non-objection). Preventive measures must be favoured over corrective measures, in particular for non-financial groups such as PE groups.

Third, regarding supplementary supervision, the ESAs suggest strengthening capital requirements so that funds would only count towards a conglomerate's capital requirements if they are effectively transferable and available among the various conglomerate members (cf. paras. 120-121). This requirement would arguably be inconsistent with the European Commission's intention to impose strict limits on movements of capital between banks in the proposed crisis management framework directive. Furthermore, such transferability, if relied upon, could reinforce systemic risk. Indeed, the siloed nature of PE investments is an important reason why PE groups do not raise systemic risks.

Last, and even though EVCA agrees with the importance of having a harmonised set of sanctions at EU level so as to avoid discrepancies between the national frameworks and in the implementation of the FCD, it is important to ensure that these sanctions remain adequate and proportionate, taking into account the sectoral requirements and sanctions which already exist.

Therefore, the EVCA calls upon the Commission to exercise great caution when undertaking the Fundamental review, to carefully assess the powers entrusted to supervisors, and to favour the interaction and exchange of information between sectoral competent authorities whenever possible, rather than imposing an additional layer of group-wide requirements on PE groups, which are already appropriately regulated.

	3) Waivers In their advice,[7] the ESAs refer to Article 3 (8) FCD which, following the FICOD 1 review, includes an obligation of the ESAs to issue, through the Joint Committee of the ESAs, guidelines aimed at the convergence of supervisory practices with regard to the application of the waivers. This task has not yet been developed by the Joint Committee. The objectives of supplementary supervision are to supervise "group risks" in groups composed of various financial institutions active in different financial sectors, and as such aimed primarily at large and complex financial institutions, such as Allianz or Crédit Agricole.[8] Group risks include risks of contagion (i.e., where risks spread from one end of the group to another), risk concentration, potential conflicts of interest, the complexity of managing many different legal entities, and the multiple use of capital. Unlike in a typical financial conglomerate of the kind contemplated by the FCD, PE structures present none of the "group risks" that supplementary supervision would seek to address: • PE funds buy individual portfolio companies as investments, which then continue to be **managed as separate companies**, with the ultimate goal of selling these investments in the medium-term. In other words, unlike a traditional "strategic" financial institution buyer, a PE fund generally does not acquire a financial institution with a view to integrating it in a broader group. There is **no group-wide management** and there are no group-wide operations (and hence no complex governance framework to align a group-wide management and organization with individual legal entities). On the contrary, each portfolio company is managed separately and has independent management. • There is **no risk of contagion**, because each portfolio company is independently managed and portfolio companies do not enter into cross-guarantees, loans, cost-sharing arrangements, retrocession operations or other transactions with other portfolio companies that could give rise to cross-liabilities.

[7] Cf. paras. 47-49 of the Consultation paper.

[8] Cf. Identification of financial conglomerates, EBA, EIOPA and ESMA, published 20 July 2012.

	• Each portfolio company is independently capitalized through equity contributions made with the proceeds of capital calls made on the ultimate limited partners of the PE fund under their respective capital commitments. Accordingly, there is **no multiple use of capital** through multiple-gearing of own funds instruments or otherwise. • Potential conflicts of interest are strictly monitored and dealt with under a stringent framework of regulatory restrictions applicable to the AIFM (cf. the AIFM Directive). Supplementary supervision should only be applied to financial conglomerates to the extent to which they are exposed to group risk. **Therefore, EVCA calls upon the Joint Committee not to postpone any further the adoption of the guidelines but to proceed and to ensure a risk-based application of waivers duly taking into account the objectives of the FCD (i.e. addressing loopholes in sectoral legislation and additional prudential risks to ensure sound supervisory arrangements with regard to financial groups with cross-sectoral financial activities), as well as the characteristics of private equity groups outlined above**.
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Annex H Questions	
General Comments	
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