bvca The voice of long-term investment

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Neil Guthrie
Carbon Reduction Commitment Technical Adviser
The Environment Agency
By email (neil.guthrie@environment-agency.gov.uk)

Re: CRC Energy Efficiency Scheme: CRC Registry

Dear Mr Guthrie

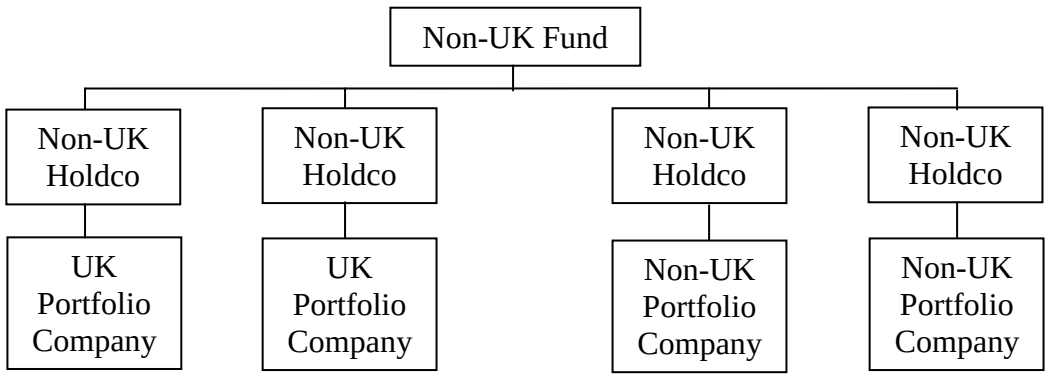
The BVCA is the representative body for private equity and venture capital in the UK. Our 450 members cover the whole investment spectrum, from venture capital firms investing into high growth technology start-ups, to the largest global buyout funds turning around and growing mature companies.

As you will know, several of our member firms and their portfolio companies are required to register for the CRC Energy Efficiency Scheme. We understand from a number of our members that their technical queries on CRC registration have been referred to you.

You may be aware that the British Private Equity & Venture Capital Association (BVCA) Legal & Technical Committee, of which I am Chairman, has raised a number of important issues with Dr Mark Toal of the Department of Energy and Climate Change. In case it is not possible to address these larger issues in advance of Phase 2, the BVCA would like to raise with you a number of specific practical difficulties in relation to the online registration system that might quickly be resolved as an interim measure.

<u>Identifying the "highest UK parent"</u>

The structure of a number of private equity funds is broadly similar to that shown below:



In this structure, the 'highest parent undertaking' (as defined in Schedule 4 to the CRC Order) is often the Non-UK Fund (or, in some cases, its general partner).

Assuming that the group is required to register as a CRC participant, under Article 73 of the CRC Order, Non-UK Fund must nominate a UK member of the group to act as the compliance account holder for the group. Some funds have elected to incorporate a special purpose UK company to act as compliance account holder. Others have elected to nominate one of the UK Portfolio Companies. In either case, the two entities that are relevant for the purposes of the CRC Order are Non-UK Fund, as the highest parent undertaking, and the UK entity nominated as the compliance account holder.

However, when registering as a CRC participant, the first piece of information to be entered into the system is details of the "highest UK parent". In the above structure, the two UK Portfolio Companies are linked by a common overseas parent, but there is no common UK parent, and consequently no 'highest UK parent". Even if a special purpose company is incorporated to act as the compliance account holder, this will be a subsidiary of Non-UK Fund (and so part of the CRC group), but it will not be a parent undertaking of either UK Portfolio Company.

This has caused a significant amount of confusion on registration, as it is necessary to provide this information in order to move on to the next step. In many cases, firms are inserting the details of whichever UK entity is to be nominated as the compliance account holder, but there is concern that this inaccurately suggests that company identified as the highest UK parent is, in fact, the parent undertaking of the other UK entities within the group.

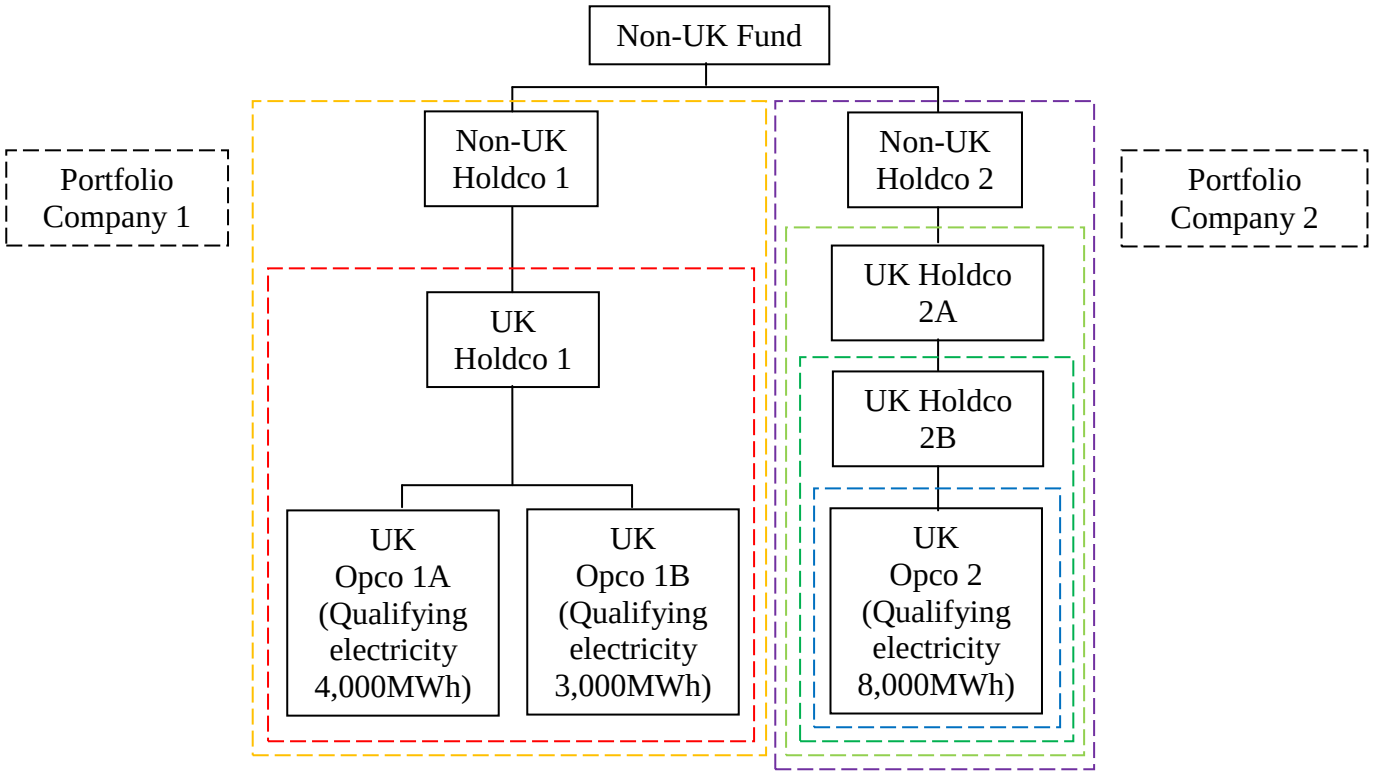
The subsequent question "are you acting as a UK parent for an overseas organisation?" is also causing confusion for the same reasons.

The term 'highest UK parent' is not defined in the CRC Order, so we cannot see a specific reason for requiring this information. We would suggest that for Phase 2, the registration form should simply require details of the highest parent undertaking (whether UK or non-UK), followed by details of the UK compliance account holder (or primary member).

On a related point, there is also some confusion as to which entity should apply for a Government Gateway ID on behalf of the group, assuming that the highest parent undertaking is an overseas entity. Some legal advisers have advised that the application should be made by the group company with the most substantial UK operations, but guidance on this point would be useful (even if only to indicate that it does not matter for CRC purposes which group company holds the Government Gateway ID, provided that the registration information is correctly entered).

Disaggregation

An individual "portfolio company" is likely, in fact, to consist of a number of different companies, often with a complex holding structure. An example structure is shown below (although some structures may, in fact, be significantly more complex than this):



Applying the definitions in Schedule 4 of the CRC Order, there are six significant group undertakings in this group:

1. Non-UK Holdco 1 + UK Holdco 1 + UK Opco 1A + UK Opco 1B
2. UK Holdco 1 + UK Opco 1A + UK Opco 1B
3. Non-UK Holdco 2 + UK Holdco 2A + UK Holdco 2B + UK Opco 2
4. UK Holdco 2A + UK Holdco 2B + UK Opco 2
5. UK Holdco 2B + UK Opco 2
6. UK Opco 2

This is the case because, if any of these sub-groups existed independently of the wider group, that sub-group would be required to register as a CRC participant under either Article 23 or

Article 26 of the CRC Order. This approach is consistent with the guidance in Annex A to the Government Response and Policy Decisions to the Consultation on the Draft Order to Implement the Carbon Reduction Commitment dated 7 October 2009.

On this basis, members have been advised to identify each of these SGUs in their registration applications; in some cases, this has required them to enter details of eight or nine entities per portfolio company. However, the online registration system takes a different approach, which appears to be inconsistent with the CRC Order.

First, we understand that it is not possible to enter details of a non-UK company into the system, as a Companies House registration number is required in each case. Consequently, the SGUs numbered 1 and 3 in the list above cannot be identified. We understand that firms have generally taken this as an indication that information about such non-UK entities is not required by the Environment Agency.

Second, as became apparent when members attempted to start the disaggregation process, the system indicates that only the SGUs numbered 2, 4 and 6 in the list above can be disaggregated. We understand this is on the basis that the Environment Agency considers that only (i) the highest possible UK parent; or (ii) an individual company whose qualifying electricity consumption is independently over the 6,000MWh threshold is capable of disaggregation under the CRC Order. However, we are of the view that all the SGUs in the list above satisfy the requirements of Article 25 of the CRC Order, and are therefore capable of disaggregation, subject to the Environment Agency's agreement.

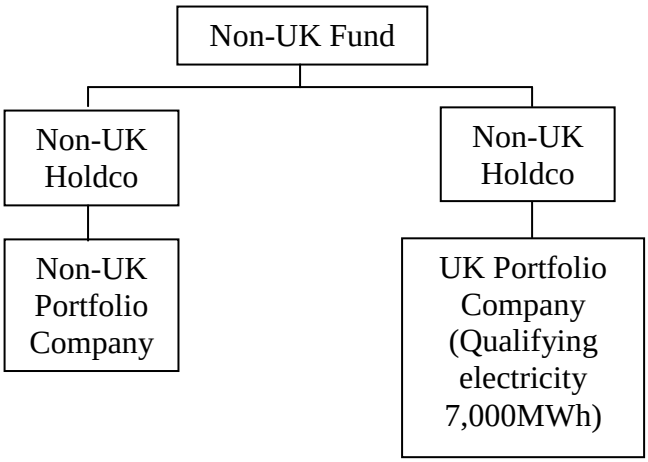
In the example above, if Non-UK Fund wishes to disaggregate Portfolio Company 2, there may well be good commercial and operational reasons for the disaggregation to take place at the level of UK Holdco 2B, rather than at the level of UK Holdco 2A, or UK Opco 2. (It is less likely to be of practical importance to be able to disaggregate at the level of the Non-UK Holdcos, although in some cases this may be desirable.)

We would suggest that for Phase 2, the details required to be entered into the system are details of the highest parent undertaking of any SGU that the parent group actually proposes to disaggregate (whether this is a UK entity or a non-UK entity). Details of the UK company that will act as the compliance account holder of the disaggregated SGU would then be entered as part of the SGU's own registration. This would be a welcome simplification.

In addition, we understand that the parent group is required to enter a significant amount of information about the SGU to be disaggregated before the initial disaggregation becomes effective in the system; for example, details of the SGU's primary and secondary contacts. In practice, the parent group may not have this information readily available, so it would be much simpler administratively if the entry of this information were to be deferred to the SGU's own registration application.

Participants with no UK entities within the group

It is highly likely that some CRC participants will cease to have any UK operations midway through a Phase. For example, take the following structure:



If Non-UK Fund sells UK Portfolio Company, applying Schedule 6 of the CRC Order (changes to participants), UK Portfolio Company will either be required to register as a participant in its own right, or will join another group.

The residual group will no longer contain any UK companies (or, indeed, have any UK energy consumption), but it will be required to remain as a participant for the rest of the phase. This gives rise to two practical issues:

First, the residual group is required to nominate a new compliance account holder, but there is no UK company to perform this role. We understand that the Environment Agency's current position is that Non-UK Fund should incorporate a new UK company expressly for the purposes of acting as compliance account holder. This seems wholly disproportionate. We would suggest instead that it should be possible for a non-UK entity within the group to act as compliance account holder for so long as the group contains no UK entities.

Second, the residual group is required to continue to report in accordance with the CRC Order. The reporting requirements are complex, and it is likely that the relevant expertise will have left the group with the UK Portfolio Company. We would therefore suggest that organisations that no longer have any UK operations should be able to file a very basic 'nil return' each year, simply confirming that the group contains no UK entities and has no UK operations.

It is also possible that CRC participants will have no part of their corporate structure incorporated in the UK, but may directly own assets in the UK with qualifying electricity consumption. In such cases, there is no "highest parent undertaking of the group with its principal place of activity in the United Kingdom" for the purposes of Article 73(1) of the CRC Order and Article 73(2) of the CRC Order requires the highest parent undertaking of the

group to appoint a representative with a principal place of activity in the United Kingdom as the account holder. This is fine in theory, but the Registry does not allow this in practice. Before appointing an agent, the undertaking must itself register and as part of this process is required to provide a Companies House registration number and a registered office in the UK, and to state in which part of the UK its parent undertaking is located. An overseas undertaking clearly cannot provide this information. We understand that the Environment Agency's advice is that the address of the location of one of the undertaking's MPANs should be given as the registered office, the question "Are you acting as UK parent for an overseas organisation?" should be answered "Yes" and the undertaking's actual overseas registered office be supplied in the next screen. The information provided is therefore factually incorrect, but there is no other way for such an entity to register. We would suggest that it should be possible to enter the details of an overseas undertaking in the Registry where there is no UK entity within the corporate structure.

In conclusion, we would emphasise that these practical difficulties are generating very significant costs for businesses, both in terms of management time and in external advisory and consultancy costs. We appreciate that the Environment Agency's resources are likely to be fully focussed on the initial registration round at present, but it would be extremely beneficial if some of these teething problems could be addressed in advance of registration for Phase 2. We would be very happy to discuss the issues by telephone or in a meeting if that would be useful.

Yours sincerely,

SIMON WITNEY
Chairman, BVCA Legal and Technical Committee

cc:
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