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# Five Things to Know About Espirito Santo International

ByMargot Patrick



Reuters

One surprise in Banco Espirito Santo SA's collapse this month is how parent company Espirito Santo International was able to operate for decades with minimal oversight despite its web of transactions and intragroup funding with the Portuguese bank.

Espirito Santo International was set up in Luxembourg in 1975 to hold investments of the Espirito Santo family. It has two main holdings: a 49% stake in Espirito Santo Financial Group SA and a 100% stake in Rio Forte Investments SA. Through these companies, it held a 25% stake in Banco Espirito Santo as of early July.

After Banco Espirito Santo's exposure to ESI and other group companies wiped out its capital buffer last month, Portugal's central bank late Sunday said [Banco Espirito Santo will be rescued with billions of euros in state aid](#). It will be carved up into a good bank with retail deposits and a bad bank with toxic loans including all of its exposure to Espirito Santo group companies.

Here are five things to know about ESI:

**Supervision:** There was none. Portugal's central bank has oversight over Banco Espirito Santo and Espirito Santo Financial Group SA, a publicly-traded Luxembourg company that holds ESI's Banco Espirito Santo stake. Luxembourg's CSSF supervised a Banco Espirito Santo branch in the country but not its holding companies.

"This is a sprawling conglomerate, which was family-controlled until very recently. Unless you're an auditor or maybe a ratings agency it's very hard to discern the level of oversight and regulation," said Robert Montague, a senior investment analyst at ECM Asset Management.

**Audit:** ESI's accounts were signed off by Francisco Machado da Cruz, who was a director at ESI until he became its official accountant in 2011. He continued to be a director at other group entities including Rio Forte, and an official at Eurofin Holding SA, whose ties with Espirito Santo were detailed by The Wall Street Journal Monday.

Mr. Machado da Cruz signed the accounts as a "commissaire aux comptes," an unregulated function that Luxembourg accounting experts said can be performed by anyone and is typically used by small companies that don't need or can't afford an external audit. At the end of 2012, ESI reported €4.27 billion in assets and €184.3 million in revenue, made up of dividend and interest income as well as payments from a subsidiary for management services.

London Business School accounting professor Chris Higson said ESI raises the "timeless problem of opaque accounting and a lack of accounting for family businesses." He said ESI's 2012 accounts look like a financial summary, "certainly not a complete set of financial statements."

**Intragroup funding:** BES's exposure to ESI and other group companies was around €1.57 billion at the end of June, according to its first-half results Wednesday. Its customers are owed another €3.1 billion.

**Commercial paper:** ESI set up a €2 billion commercial paper program in 2012. The paper was unrated and wasn't registered on a stock exchange. It did receive a STEP label, however, giving it some respectability as part of a protocol supported by the European Central Bank to help standardize and encourage liquidity in European commercial paper. But getting the label requires an independent audit, and a STEP market spokesman on Monday said it will now contact ESI for clarification.

**Legal issues:** ESI is now under gestion contr lee, or managed control, by a Luxembourg court. Alain Rukavina, a lawyer, and Paul Laplume, an expert accountant, have been appointed to assess ESI's prospects for restructuring its debts and expect to report back in October. The two men are well known in Luxembourg restructuring circles for their roles in the liquidations of Luxembourg-registered investment funds linked to [Bernard Madoff](#).

ESI's two holdings, Espirito Santo Financial Group and Rio Forte are also under Luxembourg court protection.

In addition, public prosecutors in Luxembourg are investigating ESI for potential criminal breaches of company law, while Portuguese prosecutors are investigating ESI and its entities for "suspected abuse of privileged information and abuse of trust."

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