Consultation on Member State discretions in the European Markets Infrastructure Regulation (EMIR) No 648/2012

Submission from the Irish Association of Corporate Treasurers

14th March 2014

Dear Sir/Madam,

The Irish Association of Corporate Treasurers (IACT) welcomes the Department of Finance's invitation to participate in this important public consultation.

The IACT was founded in 1986 with the aim of promoting the practice of corporate treasury management in Ireland. It is a not for profit organisation that provides a forum in which corporate treasurers can meet and exchange information.

The IACT currently has in excess of 400 members including practicing treasurers from major Irish public companies, multinationals and commercial state entities, as well as a significant number of smaller and medium-sized enterprises (SMEs). We have engaged with our members on the Department's consultation paper and as practitioners our members have expressed a number of significant concerns relating to the proposals.

The Role of the Treasurer in Derivatives Markets

The role of a corporate treasurer is to manage financial risks on behalf of their company, their board and ultimately their shareholders. The treasurer typically manages funding risk, liquidity risk, foreign exchange risk, interest rate risk, counterparty risk and operational risks. Treasurers use financial derivatives to remove risk from their business. Typical hedges include FX forward contracts and interest rate swaps. We believe corporate treasurers use derivatives prudently, sustainably and productively as:

- The tenor and size of the derivatives are tailored to match measurable business exposures
- Shareholders, management and consumers are aligned in benefitting from the removal of risk
- The individual executing the hedge is carrying out company strategy/policy and is not inappropriately motivated by short term reward
- Most corporate treasury departments are acting as cost centres and are not actively looking to take risk to make a gain
- The most straight forward derivative that adequately hedges the exposure is sought
- In many transactions both parties can be confident they broadly understand why the other is entering the deal.

This role in the market explains why corporate treasury activity did not contribute to the latest financial crisis. It is also in recognition of the prudent and real world nature of this activity, that EMIR regulations set no limit on unmargined derivative hedging positions for Non Financial Counterparties (NFCs).

Corporate treasury in Ireland is vibrant and central to traditional and online commerce, capital investment, mergers, acquisitions as well as aircraft and other leasing activities. Treasury and OTC derivatives are also likely to be intrinsic to some industry sectors that Ireland may wish to attract in future. The OTC derivative market provides suitably tailored hedges which treasurers arrange with their

banks to mitigate the financial risks the business is exposed to. This segment of the market works and EMIR does not propose to obstruct it or to add unnecessary administrative burden.

Ireland's response to the crisis

In this formal engagement with the Department of Finance, the IACT would like to acknowledge the leadership that the Department, along with other state bodies, has provided in response to Ireland's financial crisis. Many Irish corporate treasurers experienced adverse funding conditions in recent years. The improved fiscal position and the steadying of the domestic bank sector have improved the business environment and Ireland's reputation internationally. The crisis measures taken in both Ireland and Europe have reduced uncertainty in Europe's banking system and the currency union. Corporate treasurers welcome these successes and measures such as the Single Resolution Mechanism developed by the Irish Presidency last year.

Specific comments on the consultation

We believe the IACT and the Department of Finance's interests are aligned in the implementation of EMIR. The consultation emphasises (as ESMA has done) the importance of the harmonious implementation of EMIR at member state level. In crafting EMIR, policymakers have recognised that NFC hedging activity is not an area of significant systemic risk that requires mandatory clearing. We believe that it may be acutely damaging for important sectors of the Irish economy if prudent hedging activity was stigmatised or made much more onerous in Ireland than in other member states. EMIR's treatment of the NFC who operates below the clearing thresholds should not be undermined.

As practitioners impacted by the implementation of EMIR, we believe it is not in Ireland's interest that onerous compliance measures or sanctions extend into corporate treasury hedging activity.

Our specific comments on the proposal in the consultation are as follows:

1. In its letter of 14 February 2014 ESMA publicly signalled that, if it was legally possible, National Competent Authorities should not apply EMIR to certain FX forwards and certain commodity contracts. Given ESMA's clear effort to harmonise the scope of EMIR on a European-wide basis, we believe the Department of Finance and the Central Bank of Ireland (Central Bank) should provide public assurance that they will follow ESMA's approach and not apply EMIR to these contracts unless ESMA's approach is modified by the European Commission. We note that in this respect, the position taken by the Department that all FX forward transactions with a settlement date beyond the spot date, even if entered into for commercial hedging purposes, are to be considered as within the definition of a derivative under EMIR goes against ESMA's recommendation. We believe these contracts should be taken out of scope for now as any stricter Irish interpretation than ESMA's approach would disadvantage Irish business and discourage international companies from considering Ireland as a location for their European treasury headquarters. This is particularly important given so many Irish companies survive on trade with the UK; making FX forwards a vital part of their business.

2. We have found no example of another member state where imprisonment sanctions or indeed any form of criminal law proceedings are available to regulators as sanctions for non-compliance with EMIR. As described above, corporate treasurers reduce risk on behalf of their companies in arms length agreements with willing market participants. This is a necessary and simple component of commercial trade and bears no resemblance to nefarious activities such as, money laundering, fraud, inappropriate use of client funds, market manipulation or insider trading, for which financial regulators may utilise imprisonment sanctions. The maximum sentence of 3 years proposed by the Department of Finance for EMIR is (according to a recent ESMA study) equivalent to the heaviest sentence imposed for insider trading under the Market Abuse Directive in any member state[1]. Based on this we find the proposed criminal sanctions for EMIR to be inappropriately excessive and out of line with EMIR implementation in other member states. The proposal that the sanctions regime would include the ability to take criminal law proceedings, especially proceedings that could result in imprisonment, risks making Ireland an unacceptable location for corporate treasury activity.

3. Providing the Central Bank with the power to "*direct an entity to take or refrain from taking or to prohibit actions, including entering into derivatives contracts*" is an extraordinary proposal and goes far beyond the scope of EMIR. This proposal implies a form of licensing regime not mandated by the G-20 meeting at Pittsburgh, by the Dodd-Frank Act or by EMIR. The power to prohibit transactions, or oblige an entity to enter into derivatives contracts, is of significant concern to corporate treasurers. To our knowledge no NFC in any other Member State will be exposed to this risk.

4. No rationale is made for the requirement for a Statement of Compliance (including a third party validation) which is not a feature of EMIR. We note that there is no requirement to confirm compliance with many other laws and regulations. This onerous requirement contrasts with the Companies Bill 2012, which is focussed on certifying that policies and structures are in place in respect of compliance, rather than stating that the company has actually complied with each requirement of an enactment. In this respect we note that;
    a. The range of offences addressed in the Companies Bill could reasonably be considered more serious than EMIR non-compliance for hedging transactions
    b. It is not clear if an assessment has been carried out on the additional burden of compliance costs for the Statement of Compliance.

5. We understand that the "Skilled Persons Report" is used for regulated financial services providers and in that industry the Central Bank may only require a report where it is for the purposes of the proper and effective regulation of those financial service providers. It must have regard to the cost implications of providing the report, the resources available to the reviewee and the benefit to the reviewee of providing the report. It must also consider whether it has other powers which are more appropriate to use. It would be important to understand what condition must be met for the CBI to require a report. For example, must the Central Bank of Ireland have reason to suspect that a contravention of EMIR has occurred? In addition, it is not clear why it is necessary that the power to require a report should extend to NFCs, where the Central Bank proposes to have the power to use the "assessor model" for an NFC and where

[1] 'Actual use of sanctioning powers under MAD', ESMA (April 2012)

a certification regime is proposed. As the Skilled Persons Report model is sourced from the UK financial services regime, it would be useful to understand if the UK National Competent Authority elected to extend this to NFCs when they implemented EMIR. If the UK did not extend it to NFCs, it would be useful to understand why the Department of Finance believe the approach in Ireland should be different.

6. We note that the proposal references Article 22 of EMIR for the authority to grade "investigatory and supervisory powers" however it appears Article 22 applies only in the case of supervising Central Counterparties (CCPs).

7. Intra-group trades pose even less systemic risk than other NFC trades and therefore should be explicitly taken out of scope from intrusive surveillance and sanctions.

8. The proposed carve out mechanism for SMEs introduces an additional level of categorisation that does not exist in EMIR and it is not apparent whether many companies will be able to utilise this exemption. The requirement to delegate reporting is particularly difficult given it is usually not possible to delegate the reporting of inter-company transactions.

We have also requested the clarifications outlined in the Appendix

Conclusion

The IACT has been involved in preparation for EMIR since 2012. We support the harmonious implementation of EMIR in Ireland. However the Department's proposals have far reaching and unexpected consequences for treasury practitioners in Ireland and Irish business.

We ask that the Department reconsiders the proposal given the concerns listed above and we request a meeting to discuss EMIR implementation in Ireland.

Treasury practitioners from the following companies support this submission and would like to attend such a meeting;

CRH PLC
Electricity Supply Board
Espirito Santo Investment PLC
Musgrave Group
Paddy Power PLC
Pfizer Dublin Treasury Centre
Securitas Treasury Ireland Limited
Smurfit Kappa Group
Xerox

Yours Sincerely,

Colm Moriarty
IACT President

Appendix

Clarifications sought:

1. Is the Statement of Compliance mandatory and repeating, or required upon request from the Central Bank?
2. In the exemption from the Statement of Compliance, is the requirement to have less than 100 outstanding contracts at any specific point in time (calendar year-end or reporting date) or is it a continuous requirement?
3. Does delegating reporting to the counterparty bank (who is not ordinarily considered a third party) meet the requirement for delegating to a third party?