Response to the European Commission's Public Consultation on Building a Capital Markets Union

8 May 2015

The European Association of Corporate Treasurers (EACT)

The EACT is a grouping of national associations representing treasury and finance professionals in 18 countries of the European Union. We bring together about 12,000 members representing 6,500 groups/companies located in the EU. We comment to the European authorities, national governments, regulators and standard-setters on issues faced by treasury and finance professionals across Europe.

We seek to encourage the profession of treasury, corporate finance and risk management, promoting the value of treasury skills through best practice and education.

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Introductory remarks

The EACT welcomes the European Commission's aim to create a Capital Markets Union and appreciates the opportunity to comment on this Green Paper consultation.

The EACT is naturally in favour of all initiatives that aim to relaunch and support the European economy.

We view the Capital Markets Union as an opportunity for the EU to move beyond a post-crisis financial regulation agenda and re-focus financial regulation, putting the needs of the real economy at the centre of policy initiatives. The wave of financial

regulation since 2009 has concentrated on ensuring financial stability and on reducing the likelihood of a similar crisis recurring. Whilst this was necessary, these measures have had some serious negative consequences and constraints on non-financials companies' ability to fund themselves, manage their risks and handle their liquidity.

For us the central objective of this project must be the funding of the real economy; this should be supported by a framework of financial regulation in the EU creating a financial system that helps companies to conduct their business. This cannot be achieved without a holistic approach to all financial regulation: embracing legislative initiatives already taken, those that are currently being discussed and those that will be proposed in the future and affecting both funding of industrial and commercial firms and associated risk management.

The shortage of capital market funding is not (by far) the only structural issue non-financial companies are suffering from today in terms of the current environment. As we further detail in our response to question 32, many aspects of past legislation and the initiatives currently under discussion are detrimental to the real economy and create unnecessary burdens on businesses without contributing in any way to financial stability. These should be tackled simultaneously with this initiative so as to improve overall the way in which the financial system supports the real economy.

We believe that it is important for European companies that funding sources are diversified and that generally speaking Europe should seek better to supplement bank funding with non-bank sources. The end objective should be that more European companies have choice of and access to different and varied funding sources such that the real economy is less dependent on the health of the banking sector.

Responses to questions posed in the Green Paper

1) Beyond the five priority areas identified for short term action, what other areas should be prioritised?

We generally support action in the priority areas identified by the Green Paper and would like to make the following comments:

- We support the encouragement for **securitisation** as it is a source of funding, creates liquidity, and widens and deepens financial markets. However,

regulatory oversight is particularly important in view of the recent crisis, specifically with respect to the quality of assets or receivables that are subject to securitisation and subsequent investor information.

It is of great importance that companies retain the ability to negotiate non-assignment clauses in respect of their transactions with banks. Managing the exposure to financial institutions is a key part of good corporate treasury practice; there is a threat of concentration of bank exposures in case of assignment from one bank to another. Furthermore, for fast-growing firms or for weaker credits, the relationship with banks can be formalised in "incomplete contracts" – both sides expecting that in case of temporary problems or new opportunities, the lender will show some understanding and (prudent) flexibility. Assignment to an unsympathetic bank or to a securitisation scheme with no ability to review, consider, and adjust can cause major problems, even failure of the firm.

- We also very much welcome the review of the **Prospectus Directive;** we would point out that in our experience prospectuses were more easily readable before the review that took place in 2010. Complex and costly prospectuses have the negative impact of both restricting the access of certain companies to finance, as the cost of producing a prospectus can be too high compared to the other advantages. This cost factor (including the internal costs of management time, etc.) is particularly relevant for SMEs and smaller mid-sized firms. More complexity decreases prospectuses' relevance and meaningfulness to investors, which goes against the Directive's initial purpose. Broadly speaking we would encourage the following enhancements to the current Directive:

    - There is a need to make the prospectus process more efficient and cost effective by removing the requirements to duplicate information that is already in the public domain. This includes documents which have already been published or filed under the Transparency Directive as well as regularly-published quarterly, half-yearly and/or annual financial statements. The filing of prospectus supplements to incorporate such publicly-available financial statements into the prospectus is duplicative and costly and does not offer any additional benefit to investors as the information is already available. Automatic or presumed incorporation of documents which were already published/ filed and made publicly available by issuers could be facilitated by creation of one central depositary (a single, integrated EU filing system) where investors could

access a 'one-stop-shop' to source prospectuses for those issuers in whose securities such investors may be interested in reviewing. This would also prove beneficial to investors investing from different EU jurisdictions and has worked well in other jurisdictions (e.g. the USA). Investors should also be able to link to certain information housed on the issuer's website, such as the issuer's financial statement, for themselves (in the spirit of caveat emptor); this would make it much easier to incorporate information by reference whilst still ensuring that the investor is able to make an informed decision.

- Increasing the thresholds above which a prospectus needs to be produced for a public offer – the main thresholds being the fundraising threshold and the number of persons. Furthermore, the limit on the number of persons should be clarified so that it is clear that it applies per Member State and is not an aggregate limit across all Member States.

- The Directive should be amended to create two distinct regimes with different levels of required information: one for a prospectus for a public offer that is part of an IPO and one related to a secondary offer. Shortening and making a secondary offer document more relevant and focused on the main terms of an offer will also benefit investors as the most important aspects of the offer will be more easily recognisable. Of, course, once a company is admitted to trading on a market it has on-going disclosure requirements and an obligation to publish any price sensitive information. This ensures that investors and potential investors are kept duly informed about the company.

- The scope of the Directive should not be enlarged beyond transferable securities

We would encourage the Commission to consider an additional item in the short-term actions: **FX transactions undertaken for commercial purposes** by non-financial companies should **not be understood as financial instruments** under MiFID. This issue has been raised as part of the difficulties linked to the reporting obligation under EMIR but no solution has been proposed so far. There are different interpretations in Member States as to the definition of an FX forward and whether an FX transaction carried out for commercial purposes is a financial instrument. This unharmonised approach at EU level is not helpful for companies and we would encourage the Commission to take the necessary steps to clarify this point as soon as possible.

For non-financial companies the need for managing foreign exchange exposures arises from their commercial transactions and the conduct of daily business, including purchases from suppliers or vendors, sales to customers in other countries and currencies and changes in commodity prices. FX transactions are commonly used by non-financial companies of all sizes for purposes that are linked to the underlying business and not for investment or speculation. Such transactions promote rather than threaten financial stability; obliging non-financial companies to report their transactions does not in our view help to reduce systemic risk but instead puts a significant compliance burden on non-financial actors. A clarification that these transactions, when undertaken for commercial purposes, are not classified as financial instruments under MiFID would help to reduce the regulatory burden on non-financial companies and allow them to focus on the core aim of promoting jobs and growth across Europe.

In the same area, the deletion of exemption 2(k) for commodity dealers under MiFID and the contemplated introduction of a cumulative capital and trading test – which we understand will be set at extremely low thresholds – to simply be authorised to enter into a commodity-related derivative without requiring a license to operate as an investment service provider (which will require regulatory capital and other prudential requirements) does not seem appropriate nor relevant for corporate groups whose economic activity results in the conduct of commodity-related transactions without any threat to financial stability. Consequently, we strongly encourage the Commission to adopt a more flexible and reasonable approach when setting out the parameters which will define the capital and trading tests.

2) What further steps around the availability and standardisation of SME credit information could support a deeper market in SME and start-up finance and a wider investor base?

The EACT is in favour of improving the quality and availability of SME credit information, however we consider that an imposed harmonisation of SME credit information as envisaged by the Commission would not necessarily achieve the desired goals.

The objective of having companies harmonise, publish and communicate information is a laudable one but we would encourage the Commission to keep the following aspects in mind:

- Financial disclosure: we believe that disclosure of statutory accounts of all companies benefiting from 'limited liability status' (and its equivalent under the jurisdictions of all Member States) should be mandatory

- Accounting standards: the EACT does not see added value in creating a new accounting standard (for SMEs); generally, the adoption of IFRS should be a priority, bearing in mind however that IFR standards cannot realistically be applied in a full version by small or mid-cap companies (a lighter version of IFRS could therefore be explored);

- Credit analysis: the EACT notes that credit rating agencies have a relatively low appetite to rate SMEs. “Credit scoring” based on historical financial statements can be helpful for stable and low-growth firms, but, importantly in the context of encouraging economic growth, for growing firms in changing industries and those in new fields in high-tech or bio-tech, historical figures are a very poor guide to the future.

4) Is any action by the EU needed to support the development of private placement markets other than supporting market-led efforts to agree common standards?

In our view the conditions and the framework for the development of a pan-European private placement market are already identified and able to be put in place at the Member State level. We do not see any major legal or operational obstacles and would therefore not favour any legislative action from the Commission in this respect, with one small exception.

The main challenge we see at this point is whether investors will have enough appetite to invest in this type of market. From this point of view, it would be beneficial for the development of a pan-European private placement market if restrictions to invest in this market were lifted – both in terms of existing restrictions to crossborder investment (we understand that for instance certain regional banks in Europe are not allowed to invest in foreign assets) and in terms of the capital charges imposed especially on institutional investors (Solvency II).

The EACT would like to highlight that the use of standard documentation can play a crucial role in facilitating private placement markets. We would encourage the Commission and all other relevant institutions to recognise this in their future actions.

5) What further measures could help to increase access to funding and channelling of funds to those who need them?

1. The commercial paper markets can be a source of funding at interesting rates and we believe that more companies could benefit from issuance in this market. An appropriately regulated and transparent market, encouraged by the EC, would be welcomed. Any moves to stimulate investor interest from outside the EU would also be helpful.

2. Whilst we do not believe that the following action will be materially helpful in achieving the objectives of CMU, the legislators could encourage the removal of any national barriers to corporate to corporate lending.

6) Should measures be taken to promote greater liquidity in corporate bond markets, such as standardisation? If so, which measures are needed and can these be achieved by the market, or is regulatory action required?

We are concerned at suggestions on the part of the asset management community that it would be beneficial to impose standardised maturities and coupon dates on corporate bond issuance. Whilst this may be attractive for investors, such an approach would not reflect issuers' underlying funding requirements, which are not susceptible to such regimentation.

Standardisation of the mechanics of issue and some of the "boiler plate" in documentation is already substantial and increments in this can be left to capital markets participants to identify and agree as good practice over time. It goes without saying that standardisation of conditions – covenants, etc. – would be wholly inappropriate as contingencies vary greatly from issuer to issuer and from issue to issue.

We would welcome any initiative that encourages commercial paper and bond brokers to further develop electronic trading platforms, in particular multi broker trading platforms, such as those seen on the Foreign Exchange market. This would provide greater liquidity in the commercial paper and bond market and reduce transaction costs.

9) Are there barriers to the development of appropriately regulated crowdfunding or peer to peer platforms including on a cross border basis? If so, how should they be addressed?

We welcome and encourage any project that brings competition to traditional banking services and additional sources of funding to companies; we therefore support the development of crowdfunding and peer to peer platforms. At this stage the EU should not legislatively intervene other than monitoring that excessive risks are not being created or accumulated. A priori such risks are at present highly unlikely to be on a scale threatening financial stability but there can be retail investor information and protection issues and these are mostly dealt with at Member State levels.

15) How can the EU further develop private equity and venture capital as an alternative source of finance for the economy? In particular, what measures could boost the scale of venture capital funds and enhance the exit opportunities for venture capital investors?

We view the private equity and venture capital sectors as best driven by the market. Direct intervention is therefore not seen as a priority.

19) What policy measures could increase retail investment? What else could be done to empower and protect EU citizens accessing capital markets?

We believe that measures should be taken in order to direct more private savings to invest in companies. Different actions could be considered and the general aim of any reform should be to give private investors the choice between investing in companies directly, via collective funds or through private savings plans:

- In general, using the tax system to encourage investment in equities and other corporate assets to help protect individuals' long-term savings
- In the area of corporate governance and corporate law where certain requirements for issuers should be reviewed and eased, for instance the requirements regarding prospectuses (see our response to question 1)
- Seeking to achieve harmonisation (preferably abolition) of withholding tax
- Seeking to remove any restrictions on the inclusion of corporate bonds, equity issued by a company located in another Member State and other relevant products in private saving plans which benefit from favourable tax treatment

21) Are there additional actions in the field of financial services regulation that could be taken ensure that the EU is internationally competitive and an attractive place in which to invest?

We believe the single most important action is to abandon the Financial Transaction Tax proposal as it represents a major potential obstacle to attract investment in the EU. Since the beginning of the FTT discussion the EACT has expressed its concerns on the tax, which in our view would essentially be a tax on the real economy, on pensions and on savings. We strongly believe that the FTT will not deliver its objectives of making the banking sector contribute to the cost of the crisis and creating disincentives for certain financial activities that may be viewed as not bringing an added value to the overall economy. It will on the contrary add further difficulties to the struggling European economy. The FTT will cause serious damage to companies, pension funds and individuals as users of financial services, by directly and indirectly burdening them with additional costs. The FTT will not in the end fall solely on the financial sector and force it to make a fair contribution to the costs of the financial crisis but will do just the opposite. It will fall on companies in the real economy and compound the negative effects of the financial crisis that businesses have already experienced. In the current economic context this outcome is the opposite of what EU policy should be seeking to achieve. Furthermore, as other major jurisdictions have not and are not planning to implement an FTT, the tax would put EU companies in a competitive disadvantage and would discourage investment, compounding the problem.

The FTT is particularly in contradiction with the aim of creating a well-functioning Capital Market Union. It would increase the cost of funding and tighten credit conditions for EU companies. Issuers of corporate debt would have to offer higher returns to investors due to FTT eroding investors' returns, thereby raising the overall cost of capital. Liquidity in secondary markets would also be likely to be reduced, putting further upward pressure on the cost of capital. Managing the risks associated with funding (and with basic business transactions) would be more costly and difficult given the impact on derivatives used for these purposes.

We believe that the Commission and the 11 Member States participating in the enhanced cooperation procedure should withdraw the FTT proposal from the table immediately and concentrate on other areas of taxation that would be less harmful to the economy and could bring more societal benefits. Whilst banks should be sanctioned for any demonstrated misconduct or market manipulation, it is not beneficial or forward-looking for the European economy to impose such a tax with the misguided objective to make banks contribute to the costs of the crisis –

crippling the future because of past problems. We understand the political sensitivity of the matter due to the perception that the public opinion would "demand" such measures imposed on banks but we firmly believe that any public policy should first and foremost consider the broad economic and societal impact ahead of considerations of transient political popularity.

22) What measures can be taken to facilitate the access of EU firms to investors and capital markets in third countries?

Negotiation of favourable withholding tax and double taxation treaties in order to encourage EU firms' access to third countries.

23) Are there mechanisms to improve the functioning and efficiency of markets not covered in this paper, particularly in the areas of equity and bond market functioning and liquidity?

1. We would favour moves to increase issuers' ability to identify their bond holders, thereby facilitating the process of launching a tender on a company's own bonds.

2. Due to the fact that bonds are held through various central custodians, there are currently multiple circuits for issuing and settling bonds. The situation is different in the US where all bonds are held through a single custodian (DTCC). Therefore it might be beneficial to have one single central custodian for all bond issuances in the EU with the aim to have lower transaction costs, better liquidity and higher market efficiency.

25) Do you think that the powers of the ESAs to ensure consistent supervision are sufficient? What additional measures relating to EU level supervision would materially contribute to developing a capital markets union?

We recognise that the ESAs – or any future authority to be created in the area of capital markets – will have an important role and impact on the manner in which different measures relating to the CMU will be implemented. The level 2 measures are more than often of critical importance from the practitioners' point of view, and it is important to ensure their quality.

As a general remark, we would like to point out that in order to take on any new responsibilities and in order to carry out any new tasks, the funding and resourcing of the ESAs should be considerably strengthened.

In the recent years our members have been impacted by numerous measures drafted by the ESAs (especially ESMA) and we have been actively engaging as a stakeholder in particular through public consultations. We have generally felt disappointment in some aspects of the functioning of ESMA: we have found little interest or understanding of the non-financial sector and its specificities as an end-user of the financial system. However, the ESAs regulate on issues that deal with and impact actors both in the financial and non-financial sectors, and therefore we would expect the authorities to have an understanding of both and to consider both as serious stakeholders.

We believe that the following aspects would bring substantial benefit to end-users and are necessary in order to achieve a meaningful contribution from the ESAs:

1. The ESAs should take into account also the public policy aspects of financial regulation in their work, and not only purely technical aspects. We do understand and appreciate that it is not in the mandate of the ESAs to develop public policy, but we consider it very important that the ESAs have a respect for the underlying policy objectives or regulation, and more importantly that the ESAs adhere to the spirit and the letter of the level 1 texts.

2. The ESAs should be serious about having adequate representation of all stakeholder groups impacted by regulation in their stakeholder groups. Currently there is a complete absence of transparency and accountability on ESMA's part and appointments appear to be driven by what can best be described as political and academic correctness, as opposed to seeking to identify the best and most relevant people in terms of skills, experience and real rather than nominal stakeholder representation. We are particularly disappointed by ESMA's repeated failure to appoint corporate treasury representatives to the stakeholder groups and have filed an official complaint to the EU Ombudsman on the latest appointment of ESMA's main stakeholder group, the Securities and Markets Stakeholder Group (SMSG). In our view the representation of the ESMA SMSG is unbalanced as it does not include any recognised representatives from the users of financial markets within non-financial companies. These companies are a key segment of end-users of financial services; they have been and will continue to be heavily impacted by financial services legislation. Indeed a large part of the social

role of the financial services sector is support of real economy firms and that must not be ignored.

27) What measures could be taken to improve the cross-border flow of collateral? Should work be undertaken to improve the legal enforceability of collateral and close-out netting arrangements cross-border?

Clear rules should be in place concerning the ownership of collateral in case of re-hypothecation.

Furthermore, market participants should have the option to agree on a contract-by-contract basis either to prohibit or allow:

i) Broad/flexible types of collateral including in the form of a pledge rather than a transfer of title, as it would help to prevent price distortions of high quality collateral in the market due to artificial demand to fulfill regulatory requirements.

ii) Limited re-hypothecation of initial margin, to balance the risks of allowing re-hypothecation against the extensive costs to non-financial and non-bank financial counterparties in purchasing collateral and safely storing counterparty collateral, which ties up working capital that otherwise could be put towards growth in the wider economy.

iii) Netting between the parties.

Segregation of collaterals into silos by currency should not be required as it is expected to lead to operational complexities which could further expose non-financial and non-bank financial counterparties to additional currency exposure.

30) What barriers are there around taxation that should be looked at as a matter of priority to contribute to more integrated capital markets within the EU and a more robust funding structure at company level and through which instruments?

With regard to taxation, we would like to make the following suggestions that, implemented, would greatly encourage natural development of a capital markets union:

- The tax treatment of the difference sources of financing should be as neutral as possible to avoid distortion of investment decisions. Equity financed investment decisions remain significantly hampered in many EU countries by a corporate income tax system that presents a strong bias towards debt over equity financed investments. The efforts to remove distortions between the fiscal treatment of debt and equity should however focus on improving the fiscal treatment of equity rather than impairing the fiscal treatment of interest costs.

- Any form of fiscal discrimination between residents and non-residents (or national and non-national) should be abolished. In order to fully reap the benefits of the Capital Markets Union and to generally attract investment in EU companies, Member States must accept more flexibility in the taxation of capital.

- The EU should move towards the harmonization of tax regimes, for instance dividend withholding tax. We would favour an exemption from withholding tax in all Member States.

- Additionally, Member States should develop tax regimes that are supportive of long-term investment aims in Europe by being predictable and globally competitive. This will require Member States to have a clear consensus on their policy objectives as well as consultation with tax collectors and tax payers on the efficient means of achieving these policy objectives.

31) How can the EU best support the development by the market of new technologies and business models, to the benefit of integrated and efficient capital markets?

Seeking to nurture whenever possible developments relying on new technologies and business models, with intervention only when these innovations put non-professional users at risk or threaten financial stability.

32) Are there other issues, not identified in this Green Paper, which in your view require action to achieve a Capital Markets Union? If so, what are they and what form could such action take?

As mentioned in the introduction, we firmly believe that the Capital Markets Union should also consider reviewing some of the recent years' legislative measures due to their negative impact on the economy and what we consider a fundamental failure to understand and take account of financial regulation's impact beyond the financial system. Below we would like to give an overview of these impacts and suggest changes going forward.

How has the real economy been impacted by financial regulation in the recent years?

Non-financial companies depend on the financial system to provide essential services for conducting their business. These can vary from deposit-taking, payment services, working capital finance, risk management services, provision of debt finance, assistance with access to other markets, investing excess cash and advisory services across the whole range of financial management. Therefore the non-financial sector has been both directly and indirectly impacted by the regulatory changes that have and are still taking place in financial services:

- **Access to and conditions for financing**: the impact of Basel III / CRD IV on bank lending is a commonly accepted fact – if banks are required to increase their capital and liquidity levels they are inclined to do this by deleveraging rather than raising fresh capital. In general, banks' behaviour in terms of lending seems to be much more directed by the necessity to fulfil different regulatory ratios and requirements rather than by economic needs.

- **Risk management:** non-financial companies use OTC derivatives as they are best suited to hedge companies' financial risks. As opposed to centrally cleared and exchange-traded derivatives, non-cleared OTC derivatives can be tailor-made to cover most efficiently the specific financial risk a company is facing, and they do not expose non-financial companies to the unmanageable liquidity risk that margin calls would represent. We wish to highlight that this use of OTC derivatives is made for business and commercial purposes and not for speculation, and it is economically beneficial as it helps to reduce volatility in the real economy.

  The recent years' regulatory agenda has sought to push as much trading as possible to central clearing and on exchanges, which for a large part of the

market, intra-financial services, is surely justified. The current regulatory framework (EMIR) partially exempts non-financial companies' hedging transactions from such obligations, but it imposes other significant obligations that unduly burden non-financial companies for little or no benefit to the supervisors. This is especially so as non-financial companies collectively represent a tiny proportion of the OTC markets and inter-connectedness among non-financials is much less than among financial firms while granularity is higher.

We also stress that continued pressure on the use OTC derivatives (e.g. bank structural reform, CRD IV CVA risk capital calculation) is a source of uncertainty and detrimental to the pricing and conditions that non-financial companies will have on their transactions and has seen reductions in the number of banks happy to supply these services in the required volumes.

We believe that public authorities should consider how different financial reforms will impact the overall market for and prices and availability of derivatives and therefore also non-financial companies' hedging actions. If companies as a whole were to be pushed to reduce their hedging volumes or stop hedging altogether, their operational risks would materially increase. This outcome would inevitably threaten financial, employment and growth as well as directly increasing risk for their lending banks.

- **Cumulative impact of regulation:** The accumulation of all the post-crisis financial regulation since 2008 brings with it – in implementation – a real risk of inconsistent outcomes and unintended consequences. It is important therefore to look critically at the case for each incremental piece of new regulation and its real impact given all the pre-existing regulation.

- **Global convergence:** the impact and cost of regulatory change is amplified for companies operating internationally faced with inconsistent rules globally and the obligation to comply with different legal frameworks. Coherence and consistency of regulation at G20 level should be one of the main objectives of the legislator. Regulators at the global level should of course also have in mind the effects of regulation on real economy firms.

How should the existing legislation or legislative measures in the pipeline be amended?

Regulation must be well adapted to support the growth agenda; we believe the following changes are needed in order to achieve this:

I. EMIR

The burden on non-financial companies that use OTC derivatives to hedge their underlying commercial and financial risks should be considerably reduced and simplified. Non-financial companies have invested and continue to invest considerable funds in the implementation and on-going compliance with EMIR, particularly in reporting. However, we very strongly feel that this investment does not contribute to greater financial stability – as non-financial counterparties do not have the same systemic relevance as financial counterparties - but it drains funds from more productive investment.

The balance sheets of non-Financial corporates above the clearing threshold (NFC+) are likely to be significantly hit through the tying up of liquid assets with the future EMIR margining requirements. We believe that EMIR should require the central clearing of only the asset class in which an NFC is above the clearing threshold, and should not apply to all asset classes as is currently required. Imposing variation margin on hedging transactions below the clearing thresholds will expose NFC+s to daily volatility up to the settlement date of the underlying commercial transaction and will entail higher levels of working capital. This will tie up liquidity which could otherwise be invested in the real economy.

We therefore consider that two main changes are needed to the current EMIR regime:

- One-sided reporting: we see absolutely no added value in reporting the same transaction twice, both by the financial and the non-financial counterparty. The EU should adopt one-sided reporting (as is already done in the US under Dodd Frank) as this would not compromise the supervisors' ability to monitor systemic risk but would greatly ease the burden on companies.

- Exempting non-financials' intra-group transactions from the reporting requirement. Non-financial companies centralise risk management for the purposes of efficiency and cost saving. External derivative transactions (usually of net but sometimes of gross exposures) are often undertaken by a

central unit and these are then mirrored appropriately as intra-group transactions with the part of the group where the underlying business risk has arisen. While it significantly increases the reporting burden on companies, reporting the intra-group transactions does not bring any additional value to the supervisor, as the related external trades have already indirectly been reported by the counterparties (as well as, under current requirements, by the companies as an external transaction – see previous bullet point).

We believe that these improvements to EMIR would also be helpful to the supervisor as they would decrease the number of reported transactions that bear no systemic significance, and would therefore allow the supervisor to better monitor real systemic risk concentrations within the financial system.

II. CRD IV

a. Capital and liquidity requirements

Whilst the EACT of course recognises the need to ensure correct levels of bank capital, we would encourage the decision-makers to review whether or not some aspects of the capital and liquidity requirements in place are excessive in relation to risks to bank capital. We believe that the EU banking system must be able to continue to play its role in the economy of maturity transformation and funding and risk management of companies – we see a fundamental problem in the system if banks are only able to perform these tasks on a severely reduced scale.

b. CVA

The economic importance of non-financial companies hedging their risks by using OTC derivatives was recognised in CRD IV, in exempting non-financial counterparties from the Credit Valuation Adjustment (CVA) risk capital charge calculation. This exemption is instrumental in giving European companies access to more reasonably priced risk management products, but it has been challenged both at international level (the Basel Committee) and at EU level (by the EBA in its technical advice to the Commission published on 26 February). We found it extremely frustrating that the EBA as a supervisory authority seeks to modify the essence of a policy principle that has been agreed by the legislators in the level 1 text. As we underline in our response

to question 25, the ESAs should understand and respect the policy goals and principles of the level 1 text.

We advocate the maintenance of the EU exemption and would encourage the Basel Committee to take the views of and impact on the real economy end-users into account in formulating changes to CVA as part of their work in this area.

III. Bank structural separation

We are not convinced of the need to introduce a fundamental separation of banking activities as proposed by the Commission. Given the plethora of ways in which a bank can work with a company it is inherently difficult to argue, from the perspective of the real economy, that there would be major benefits from legislatively imposed separation of certain activities within a bank. On the contrary there are evident benefits from institutional size and diversification, provided that the management processes are prudent, based on sound controls, with good governance effectively monitored by stakeholders.

If however a separation is put in place, the Regulation needs to be framed around a much narrower trading entity and a broader deposit entity, allowing the latter to offer the services that non-financial companies require from their banks. Many of the activities that the Commission is proposing to separate to a trading unit are necessary and have value to the wider economy; they should not be under-valued by being assumed to be inherently risky and undesirable, in an overzealous attempt to reduce bank size. The following two aspects should specifically be addressed:

- Capital market activity such as market-making should not be subject to separation as it benefits the real economy in that it supports the issuance of equity and bonds by non-financial companies with vital immediate liquidity. Its proposed separation to a trading unit would therefore completely go against the aims of the Capital Market Union, as such a separation could substantially limit the ability of financial institutions to underwrite and make markets for corporate bond issuance.

- The prohibition on the core institution to offer non-centrally cleared OTC derivatives to their non-financial clients should be deleted in order to preserve the ability of companies to manage their financial and market risk exposures.

IV. Money Market Fund Regulation

MMFs are an important cash management tool and are buyers of short-term commercial paper. From an investor perspective, MMFs offer a highly liquid and secure alternative to bank deposits and a way to diversify cash deposits. For non-financial companies it is important that the continued existence of both Constant Net Asset Value (CNAV) and Variable Net Asset Value (VNAV) funds is ensured. This is all the more important in a context where bank deposits are at the same time becoming more risky from corporates' perspective (possibility of a bail-in) and corporate short-term deposits may be undesirable from the banks' point of view (Basel III / CRD IV). Providing companies with the necessary cash management tools is increasingly important in such a context.

Furthermore, any implementation of a ban on ratings of MMFs would effectively destroy the market for all those (other than banks) who rely on the provision of sound ratings to guide investment. The combination of the threats to MMFs contained within the proposed Regulation would, if implemented, perversely lead to an increase in systemic financial risk, as a result of a forced concentration of liquidity in a small number of well rated 'national champion' banks.

V. Financial Transaction Tax

As mentioned in our response to question 21, we believe that the FTT project should be abandoned.

VI. Benchmark Regulation

The Commission's proposal for regulating financial benchmarks is an understandable initiative given the many cases of benchmark manipulation over the recent years. However, we believe that the legislator should be very careful not to over-regulate in this area. Firstly, if the scope of the Regulation is too large or inappropriately calibrated and/or if the administrative and compliance burden are too great, certain important benchmarks might cease to be published. Alternatively, contributors might choose to retire from panels (where membership is not made mandatory), in fact making benchmarks more volatile and unrepresentative of the underlying market and perhaps eventually making publication of the benchmark impossible.

Secondly, the Regulation should not lead to the unavailability of third country benchmarks. The Commission proposal would have the effect of seriously restricting the availability of non-EU benchmarks, which would unduly restrict access to

appropriate financial instruments. Furthermore, the legal, contractual and practical consequences of discontinuation of important benchmarks should be taken seriously and necessary provisions should be foreseen (e.g. “grandfathering” clauses) in the legislation.

The legislators should ensure that benchmark administrators have proportionate, sound governance processes in place and that appropriate sanctions exists in case of market abuse and manipulation, while keeping in mind that the legislation should not lead to a significant reduction in the availability of benchmarks in the market.

VII. Credit Rating Agencies Regulation

Credit ratings are important in a well-functioning capital market as we believe that credit ratings are an important mechanism for providing good quality analysis to the markets.

Non-financial companies make use of credit ratings in a variety of ways, for instance to support funding from financial markets and to assess the risk of exposures with financial counterparties

Having in mind the possible review in 2016 – which in our view is not necessary at this point due to the thorough review of the legal framework in the recent years - we would like to highlight the following aspects:

- Reducing over-reliance on credit ratings : whilst we understand the objective, we would like to stress that this objective must not lead to banning the use of credit ratings, at least where such a ban could have serious consequences on end-users. The reduction of over-reliance to credit ratings should come from sustained market encouragement not to rely solely on credit ratings.

- Mandatory rotation of CRAs: the idea of a mandatory rotation on corporate ratings should be abandoned as this would seriously impact the efficiency of funding markets for the real economy. Corporates should be allowed to use an agency with suitable expertise and knowledge of the corporate, and a recognised (international) reputation.

- Issuer pays / Investor pays model : from the perspective of corporate issuers the ‘issuer pays’ business model has proven to be the most practical and suitable for both issuers and investors. Any eventual move to the ‘investor pays’ model is likely to result in reduced coverage of companies – especially

of sub-investment grade and of mid-sized and smaller companies. This would go completely against the aim to create a Capital Markets Union and would be counterproductive.

How the decision-makers can better recognise end-user impacts in the future?

Better regulation is one of the key concerns of the new Commission – we believe that in terms of financial regulation this should translate into recognition and minimisation of the impact on end-users. We consider that the following changes are needed:

- ***Assessment of the impact of legislative measures on the real economy and early engagement*** between policy-makers, legislators and representatives of non-financial companies. Corporate treasurers deal with financial institutions, products and services on a daily basis and their voice should be heard when these are being regulated – because changes in the financial system also have fundamental impacts on the users. The impacts on end-users of financial services can be hard to perceive in advance as they are at the end of the financial industry's implementations of regulations and the financial firms' behavioural adaptations. Accordingly, there must be a willingness suitably to amend legislation, regulation and rules after experience with their effects and the consequential multi-stage behavioural changes become apparent.

- ***Non-financial companies should not be assumed by default to be the same as financial companies*** when financial regulation is being developed. In many ways the business of financial services is about regulation and they are organised accordingly – but non-financial services companies are about making widgets or servicing them. At the very least companies in the real economy do not have the same systemic importance, being more numerous, less correlated, less leveraged, and so on. Imposing financial sector obligations on non-financial companies is neither meaningful nor appropriate.
  The compliance burden for such non-added value activity is considerable and legislators need to consider carefully whether the legislation being contemplated has true importance to the reduction of systemic risk and increase in financial stability or may, in the end, do more harm than good after all the effects are worked through.

Where corporates are caught by such regulations, it is important that sufficient time is allocated for compliance, recognising that lead in time is likely to be longer for NFCs than for FCs.

- There should be ***a more structured and sustained dialogue with non-financial companies – and in general, the real economy***. This could be done by more effective and timely consultation with representatives of non-financial companies and in general organisations other than those lobbying for the interests of the financial sector. There is also an urgent and continuing need for a more balanced composition of stakeholder groups such as the ESMA Securities and Markets Stakeholder Group (SMSG) – where there is currently no non-financial company representative.

- ***Flexibility should be built in to legislation where possible and appropriate***, so that modifications after experience is gained are relatively easily achieved and not grand projects themselves. The consequences of financial regulation for end-users are hard to predict and may emerge only after rules come into effect, sometimes being realised only later in economic cycles.

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