EUROPEAN ASSOCIATION
OF CORPORATE TREASURERS

7 November 2011

Financial regulatory policy: the need for dialogue with the real economy

Open letter to the Commissioners of the European Union

In January 2010 more than 160 European companies supported the EACT's letter to the European Union Commissioners, in which we highlighted the risks to economic and financial stability, employment and growth in the initial proposals for regulation of OTC derivatives. Since then we and others have continued to engage with the Commission, Parliament and Council; our overall objective was to ensure that the final regulatory approach took proper account of its impact on the 'real economy', where non-financial end users need access to derivatives on economically realistic terms in order that underlying risk in their businesses can be mitigated.

The approach now embodied in EMIR and in Dodd-Frank in the US includes workable principles that, when translated into rules by ESMA and by the CFTC (and other US regulators), will allow the great majority of companies to continue to use cost effective derivatives to reduce risk. We have welcomed this outcome, which reflects a more developed appreciation of the consequences of regulatory action than we saw at the beginning of the discussion of EMIR.

The EACT and the 188 companies whose names are attached to this letter are writing because, notwithstanding the outcome on EMIR, there is grave concern across Europe over how the European institutions take proper account of the real economy in their development of regulatory proposals. We start from the widely held view that the financial sector has a loud and established voice in debate in Brussels. Representation of the real economy is by contrast much more diverse. We strongly believe that as a result there is a poor recognition of the impact of proposals on the non-financial sector in the European economy, with a consequentially negative influence on employment, economic recovery and growth.

The next stage in financial regulatory action by the European Union poses significant threats both to the success of the EMIR proposals and to the cost and availability of funding for both SMEs and the larger companies in Europe. It is therefore particularly important that the Commission, Parliament and Council recognise these risks and commit to an effective dialogue with the real economy.

The proposed regulatory changes will affect the provision of financial services across industry and commerce. In the US, the Chairman of the Federal Reserve and the Acting Comptroller of the Currency have acknowledged that they cannot know the overall effect on the real economy of all the changes that are being made. We see no reason to expect the position in Europe to be very different.

Our immediate concerns focus on the Commission's proposal to replace the current Capital Requirements Directives with a Directive and a Regulation (CRD IV and CRR) and on the proposed new Markets in Financial Instruments Directive (MiFID) and Regulation (MiFIR).

The CRD IV / CRR proposals include principles that (consistently with the content of Basel III) would materially increase the costs for the real economy of hedging with bilateral OTC derivatives. This approach threatens the value of the EMIR exemption. Implementation of CRD IV / CRR in its current form will trigger many if not all of the seriously adverse consequences (reduced hedging of risk, more cash tied up in collateral arrangements, greater business uncertainty) that we and others sought to avoid by proposing and obtaining the exemptions within EMIR. There is no evidence to suggest that this aspect of CRD IV / CRR can be justified by any associated reduction in systemic risk.

Responses to the earlier MiFID consultation urged the Commission not to include wording that would force OTC derivatives trading onto exchanges; there is uncertainty in the MiFID / MiFIR drafting that could still effectively invalidate the exemption provided for non-financial end users within EMIR (and Dodd-Frank).

We urge the Commissioners, at a time of great uncertainty in the European economy, to ensure that in the general development of financial regulatory policy there is a proper dialogue with end users of financial services; this group is profoundly impacted by the way Europe and the rest of the world address the need for reform within the financial sector. Given the exceptional level of uncertainty and the clear risk of an economic double dip, companies across Europe look to the European Union to focus on regulatory initiatives that are properly justified, are consistent in their development and avoid penalisation through unnecessary regulatory burdens.

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This letter is supported by the member associations of the EACT and has been signed by the following companies:

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