

CFD Requirements Consultation
Asset Management Supervision Division
Central Bank of Ireland
New Wapping Street
North Wall Quay
Dublin

29th May 2017

To whom it concerns,

Merrion Stockbrokers Ltd. appreciates the opportunity to respond to the Consultation on the Protection of Retail Investors in relation to the distribution of CFDs.

The following are our considered responses to the questions posed:

1. Which of the options outlined in this paper do you consider will most effectively and proportionately address the investor protection risks associated with the sale or distribution of CFDs to retail clients?

We consider Option 2 is the more reasonable and proportionate of the two options presented in Consultation Paper 107 (CP107).

We understand the CBI's objective is to limit losses for retail investors and believe that most of the proposals in option 2 are constructive in this regard. Indeed, we believe that our current Suitability & Appropriateness processes substantially achieve this investor protection objective.

In Summary, we believe that Option 1, a wholesale ban, would be excessive and counterproductive for those clients who are suitable to trade CFDs. Furthermore, it may steer investors towards unregulated firms outside the CBI's jurisdiction. CFDs, if used in the appropriate manner, are advantageous for investors' risk management for the following reasons: -

- CFDs allow exposure to an investment instrument efficiently without incurring the full foreign exchange risk.
- CFDs are less expensive than trading direct equities, particularly in relation to Irish and UK stamp duty and overseas dealing charges.
- CFDs allow clients to hedge their portfolios by 'going short'.
- CFDs are more tax efficient in their treatment of 'dividends' compared to investing in direct equities.
- Crystallisation of CFD gains is more tax efficient than exit tax on disposal of unitised funds.

There is a greater probability that investors will become clients of unregulated firms in other jurisdictions and be allowed to trade equities as CFDs without under-going an appropriate risk assessment, without advice and with large leverage capability if a blanket ban is put in place.

2. In relation to Option 2 please see supporting comments below.

a) Do you agree with the proposal to restrict leverage to 25:1 for retail clients trading CFDs?

Merrion have no difficulty with the proposed maximum leverage of 25:1. We believe that a leverage restriction per asset class would be more common sense and perhaps add extra protection. Merrion advisory CFD service restricts its CFD offering to equities, E.T.F.s, E.T.C.s, commodities and indices, i.e. Merrion do not include currencies and bonds in our advisory offering. Merrion consider 25:1 as an exceptionally highly leveraged account and typically advise no more than five times leverage.

b) Do you agree with the proposal that retail clients trading CFDs should not be at risk of potentially limitless losses and that firms offering CFDs should be required to put in place negative balance protection on a per position basis?

Merrion agree with the principal with respect to the measure of limiting losses. Nevertheless, we believe it is more practical to implement a 'per account' loss limit level rather than a 'per position' loss limit level. This measure would ensure that the client and advisor are considering the risk of each position in question before this position is taken. This option would facilitate the continued hedging of a portfolio without the hedge being closed out in the circumstance that this hedge is a losing position hedging profitable positions. In summary, Merrion's view is that limiting account/portfolio losses is more practical and more appropriate than limiting position losses.

Merrion agrees with the practice of tiering leverage lower in relation to the size of a position, especially with respect to CFD positions in equities which are less liquid.

The above conditions with respect to the question of leverage, allied with robust internal monitoring of client accounts, will further help protect clients that Merrion allow to trade CFDs.

c) Do you agree with the proposal to prohibit all bonus promotions and trading incentives in relation to CFD client accounts?

Merrion strongly agrees with these proposals.

d) Do you agree with the proposal to require firms offering CFDs to retail consumers to provide a standardised risk warning to clients disclosing the percentage of active retail CFD clients who suffered a loss of equity during the previous quarter and over the previous 12-month period?

Merrion agrees with this proposal.

3. Are there further measures which the Central Bank should consider as part of its analysis? Please give reasons for your answer.

We believe the implementation of the Option 2 proposals goes a long way to de-risk the environment for retail investors. Perhaps a review of the effectiveness of these measures after 12-18 months is appropriate.

4. In relation to the options outlined in this paper, are there any detrimental effects on investors or the markets or unintended consequences that you consider should be taken into account by the Central Bank?

An outright ban would ensure that many clients will access this class of offering from unregulated offshore firms exposing investors to a litany of unscrupulous practices. Research indicates that clients will seek leverage elsewhere if not offered by their regulated provider. This inevitable movement of clients to other jurisdictions could only be judged as a clear negative from a consumer protection perspective, i.e. there would be no regulatory supervision.

5. What do you consider will be the likely effect of the options outlined in this paper on investors and market participants who may hold, use or benefit from CFDs?

Merrion agrees with the measures proposed in Option 2 of CP107. Please see as follows a summary of the effects of **both options** on investors and market participants who may hold, use or benefit from CFDs.

Option 1: The Prohibition of the Sale or Distribution of CFDs to Retail Clients

The likely effect of an outright ban would ensure that many clients will access CFD products from distributors of unregulated offshore firms exposing investors to a litany of unscrupulous practices. As stated in Answer 4, research evidences that clients will seek leverage elsewhere if not offered by their current provider. This inevitable movement of clients to other jurisdictions could only be judged as a clear negative from a consumer protection perspective, i.e. there would be no regulatory supervision. It could also take employment from the financial services sector out of this regulator's jurisdiction.

Option 2: Enhanced Investor Protection Measures

The likely effect of Option 2 would be a healthy tightening of attitudes to risk in this space. Merrion view these measures as sensible investor protection initiatives with the effect of further protecting clients by:

- limiting losses to no greater than the sum deposited.
- further ensuring that the client is comfortable both with the risk of each position taken and the over-all exposure of the CFD account.

Merrion's view is that if these Enhanced Investor Protection Measures are introduced, it will result in a higher awareness of the risks created by CFDs.

Merrion see no negative impact to business if the financial instruments offered to clients with CFD accounts (equities, E.T.F.s etc....) are subject to the conditions that the leverage is limited on both a 'per account' and 'per asset class' perspective and the negative balance protection is applied per account.

We appreciate the opportunity to respond to this consultation paper and wish to convey our willingness to meet with the CBI to discuss further. We trust that you find this response useful.

Yours faithfully,

Patrick O'Neill

CEO Merrion Capital Group