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IN BRIEF

The Bank of England's **asset purchase facility** to provide companies with funding has started operation, initially buying investment-grade sterling commercial paper. In the first three weeks of its operation, the Bank has built up a holding of £985m in corporate CP. Any investment-grade issuer that makes a material contribution to the UK economy can gain access to this funding at very attractive rates well below Libor. The Bank is also keen to move on to further lending support mechanisms for UK business by buying corporate bonds and syndicated loans.

Guidance on **the going concern basis for smaller companies** has been published by the Financial Reporting Council. Assessing whether a company is still a going concern is a requirement under the financial reporting standard for smaller entities even though many can opt out of an audit. Directors should have regard to their business plan, including cashflow forecasts, and regularly update and discuss this plan with their bankers and other lenders to check if it is reasonable to assume that loans and/or overdrafts will continue to be available. The FRC says: "The absence of confirmations, particularly in the current environment where banks are having to deal with a significant increase in workload, does not of itself necessarily cast significant doubt on the ability of a company to continue as a going concern."

The **Banking Act 2009** came into force on 21 February 2009, replacing the emergency legislation that brought Northern Rock into public ownership. The Act creates a permanent special resolution regime to protect financial stability in the event of a bank or building society failing. HM Treasury has issued a code of practice on how it, the FSA and the Bank of England will use the three stabilisation options, the bank insolvency procedure, and the bank administration procedure.

A legal briefing on **debt buyback** has been published by Clifford Chance. It describes various techniques and addresses the legal issues, including open market purchases, tender offers and market abuse and price-sensitive information obligations. Topically, it also covers consent solicitations to obtain a waiver or amendment where covenants are becoming tight; voting incentives; and exchange offers to buy in one set of bonds and reissue with an extended maturity. The briefing is freely available at: **www.tiny.cc/ccliabilitymanagement**

INTRODUCTION

By Martin O'Donovan
ACT assistant director, policy and technical

I received an email headed "Gutta cavat lapidem," from my counterpart at the Italian ACT equivalent but my Latin was not as good as his. Looking up the full quote (Gutta cavat lapidem, non vi, sed saepe cadendo), I found it means: "The drop hollows out the stone by repetition, not by force." Working on behalf of all treasurers, the ACT policy and technical team try to influence the world of regulation, standards and markets. Timescales can be extended, but persistence often wins in the end.

So we were delighted to see that submissions from the ACT and LMA over the excessive administration and delays in getting treaty clearance to pay interest gross have prompted a review by HMRC. This will take yet more time, but little by little we can hope to see improvements here and in other fields. On other things the pace is more rapid and we commend the Bank of England for moving swiftly to implement the asset purchase facility to inject funding into corporates.

Boost for treaty clearance

HM Revenue and Customs has launched a consultation on the treaty clearance processes by which non-resident lenders can be paid interest by UK companies without withholding tax deducted.

This welcome move seems to be the result of a joint initiative by the ACT and the Loan Market Association (LMA) last autumn when we approached HMRC with ideas to modernise the treaty clearance procedure for syndicated loans.

HMRC now recognises that the arrangements for obtaining treaty relief have not been running as efficiently as it had hoped and is looking for ways to improve the service while still monitoring and addressing tax compliance risks.

The UK generally imposes a 20% withholding tax on interest payments by UK borrowers to any non-resident lender that does not lend through a UK permanent establishment. Where a double-tax treaty exists – and the UK has an extensive network of such treaties – gross payments may be made once the foreign lender has applied to its home tax authority, which in turn has to apply to HMRC, which will check eligibility and give a direction to the borrower. Only then may payments be made gross and previously withheld tax recovered. This time-consuming process has to be repeated for each loan the lender is party to.

There was an attempt to streamline the process with the provisional treaty relief scheme and changes in the 2007 Budget theoretically allowed a syndicate manager to make a composite treaty application to HMRC on behalf of the syndicate. But for a variety of reasons, including agent reluctance to take on this sort of role, scheme take-up has been disappointing.

The ideas already put forward by the ACT and LMA are for a form of treaty passport. Rather than a lender making a separate application for each loan it grants, it would be awarded a passport that would apply to all loans it made to unconnected third-party borrowers.

The lender would make an application to HMRC for a passport clearance, including a certification of residence by the lender's home tax authority, much as under the present procedure. Assuming passport status was granted, there would then need to be suitable mechanism for borrowers to determine that their lenders were covered by a treaty passport, possibly via the HMRC website. Additional procedures might be required for borrowers to notify HMRC when interest payments are first made to the lender under the passport, and to cover withdrawal of passport status and liability for withholdings.

The review is also looking at the provisional treaty scheme and the arrangements for obtaining a compensating adjustment where interest is disallowed as an expense (for example, on thin-capitalisation grounds) so that withholding tax becomes payable.

HMRC is seeking comments on treaty clearance by 17 April 2009 and appears keen to hear about any difficulties that borrowers have been having with the current arrangements. ■

www.worldwidewords.org
Not a treasury-related site this month, but one for those who enjoy derivations and weird words and phrases. There are no ACT warranties as to accuracy and a US slant is apparent, but it's good fun.

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ACT investment guidance

The ACT has issued two new guidance notes on the corporate investment of liquid funds and bank counterparty credit assessment for companies.

The financial strategy for liquid funds, the initial cash forecasting and analysis, the governance and processes, the risks and returns and countless other considerations could fill a book. But given the current market conditions a quick checklist can help ensure the the major issues are being covered in your company. Some of the ideas in the notes are outlined here.

Surplus funds can be used in the first instance to repay external debt. For external investments the old textbook mantra is security, liquidity, yield – in that order – or SLY for short. The past year has made abundantly clear that SLY is not merely a textbook concept; the counterparty's ability to repay an investment, on time and in full is absolutely fundamental.

Generally, the approach to investment security is not designed to be event-free under all circumstances but to make it unlikely, systemic failure apart, that a credit event, while damaging, unwelcome and embarrassing, will be catastrophic.

The counterparty limit set for a bank will usually, and subject to a maximum exposure limit, be derived from an approach that starts with the credit ratings of the banks. The limit may vary with the maturities of the exposures.

But credit standings can change very quickly. Subscribing (rather than relying on the freely available abbreviated ratings) gives access to the ratings report written by the analysts that provide more nuanced information and the opportunity to talk to the analysts about the report. It also helps in staying up to date rather than relying on out-of-date rating opinions. It is very important to pay attention to the outlook indicated by the rating agency for the obligor and for the government (domestic and foreign currency).

Ratings do not pretend to be updated in anything like real-time. On the other hand, model-driven or market-implied ratings or a combination of the two are available. These may be updated much more frequently than analyst-driven ratings, but may engender volatility and false signals.

Other indicators can give false signals but it is always better to be cautious. You can read the financial newspapers and set Google alerts, and Reuters and Bloomberg feeds to pick up news stories and comments from all over the world about your counterparties. You can monitor share prices, bond and CDS spreads.

Limits can be set where other connectedness between counterparties exists, such as for banks within one banking group or one jurisdiction.

At times of uncertainty, credit limits tend to be reduced, portfolio diversification increased and attention given to credit support for material exposures (including collateralisation and so on for contingent exposures). Using liquid money-market funds can help diversification.

Liquidity is the ability of the investor to realise the value of the investment prior to its maturity if the need should arise. The desired liquidity profile of investments will be influenced by the company's strategy and its expected cashflows and potential cashflow volatility, and the availability of alternative liquidity; it will also factor in the higher credit uncertainty with longer maturities and from lower liquidity.

Yield comes last in the treasurer's priorities.

The full guidance notes are available at: **www.treasurers.org/investingcash** ■

FSA brings forward CFD disclosures

Disclosure of long positions in contracts for differences (CFDs) will be required from 1 June 2009 rather than September as previously announced.

The Financial Services Authority (FSA) has left unchanged the rule that holdings of CFDs should be aggregated with shares, and the initial disclosure threshold will be set at 3%.

The scope of disclosure will extend beyond the existing categories of shares and qualifying financial instruments and take in any financial instruments having similar economic effect to a qualifying financial instrument. As a result, options, whether settled in shares or cash, will be included.

The FSA has also decided that disclosures will be on a delta-adjusted basis rather than purely nominal. The delta of an equity derivative represents how the pay-off from that derivative changes in relation to a change in the price of the underlying equity. A CFD, for example, would normally have a delta of 1 as it perfectly mirrors the change in the underlying share price.

On options, the delta is representative of the number of shares the person writing the derivative would need to hold to hedge perfectly its exposure under the derivative.

The delta will vary continuously, so there will be added admin from the extra notifications required. In the light of this there is a transitional period of seven months from implementation.

IN BRIEF

▸ **Corporate Financing in Troubled Times** is a briefing from Slaughter and May covering some of the processes and legal issues for corporates trying to raise finance in difficult circumstances or facing a breach of covenant. As trading for many corporates deteriorates, technical defaults are likely to become common at a time when banks are trying to de-risk their own balance sheets. The briefing contains commercial advice on possible approaches along with the serious legal issues and directors' duties if insolvency is a possibility. The briefing is freely available at: **www.tiny.cc/SandMfinancing**

▸ The Quoted Companies Alliance has released a guidebook to assist **smaller quoted companies** in the proper running of their audit committees. It includes coverage of audit committee membership and organisation; oversight of the accounts cycle; external auditors, reporting, and risk management and internal controls.

▸ The EU's de Larosière expert group has reported on the **future of European financial supervision**. Key among the proposals is the establishment of a pan-European supervisory body, the European Systemic Risk Council. Its role will be to gather information on all macro-prudential risks in the EU.

A further significant proposal is to improve co-operation between the current banking, insurance and securities committees with new European authorities for these sectors by 2011/12. The three new authorities will set regulatory standards and supervise national authorities. National supervisory authorities should continue to be fully responsible for the day-to-day supervision of firms, but the new authorities would have added powers including legally binding mediation between national supervisors, adoption of binding supervisory standards, oversight and co-ordination of colleges of supervisors, and the licensing and supervision of specific EU-wide institutions (such as credit rating agencies, and post-trading infrastructures). The group falls short of suggesting a single pan-European regulator, which will hearten some national regulators.

▸ Recommendations on **loan syndication timeline** are included in new guidelines for mandated lead arrangers from the Loan Market Association. They include the decisions on the closing of syndication and allocation, declaring a transaction free to trade, and the exercise of flex, along with the issue of frontrunning.