IN BRIEF

The US Securities and Exchange Commission (SEC) has delayed a decision on global accounting standards until sometime this year, saying it needs more time to decide on convergence. The SEC's original deadline to decide on IFRS was the end of 2011. Both Hans Hoogervorst, chairman of IFRS body the IASB, and Leslie Seidman, chairman of the US Financial Accounting Standards Board (FASB), have acknowledged that the original aim of complete convergence of IFRS and US GAAP is increasingly remote.

In a move to protect liquid assets, 42% of corporate treasurers in developed markets made changes to their banking or counterparty relationships in 2011, according to a recent Fitch Ratings survey. This compares with 36% in the 2010 survey. A flight to quality is also evident in emerging markets, where 56% of corporates targeted a minimum rating of A- for their counterparties in 2011, compared with just 19% in 2008 and 48% in 2010. Fitch surveyed 181 corporate issuers, mainly from EMEA and Asia-Pacific.

HM Treasury has announced plans to take action against excessive surcharges on card payments. Following a super-complaint by consumer organisation Which? about the application of surcharges when cards are used to pay for transport and the response of the Office of Fair Trading (OFT) to it, the Treasury has decided to take strong action. It will consult on legislation that will apply to most retail sectors (not just transport) and ban excessive surcharges on all forms of payment, not just cards. Businesses will be able to make a small charge to cover their costs for supporting card payments. The Treasury wants measures in place by the end of 2012, and so will plan for early implementation of the Consumer Rights Directive.

The aggregate deficit of the 6,533 defined benefit schemes in the Pension Protection Fund (PPF) 7800 index is estimated to have increased to £255.2bn at the end of December 2011, from a deficit of £222.1bn at the end of November. The position has worsened since the end of December 2010, when a surplus of £21.7bn was recorded. It should be noted, though, that the comparison with a year earlier is affected by the changes in assumptions for s179 valuation, which raised liabilities by 3.6%.

INTRODUCTION

By Michelle Price

Associate policy and technical director

As we go to print the media is anticipating that unless Greece can restructure its debt it will default, with a possible exit from the euro zone. With euro contingency planning still on everyone's agenda we have highlighted what is at risk in the article on page 09 and provided a link to our exceptionally popular euro contingency planning briefing note – the link to this document on the ACT's website had more than 1,500 hits in its first month.

The threat of pension funds having to hold additional capital, as do insurance companies under Solvency II, has also been on the policy and technical department's agenda and is covered in the story below. As ever there is no shortage of new emerging risks for us all to cope with.

EU death threat for UK pensions

All credit to pensions minister Steve Webb, who has been vocal in rejecting EU proposals to introduce Solvency II-style requirements to make pension funds hold additional capital buffers – in other words, to overfund. The minister puts the cost to UK companies at £100bn while analysts have produced figures up to £600bn.

Rather more surprising is that treasurers have been relatively quiet on this issue, although they may be voting with their feet as companies close down their defined benefit schemes.

The fundamental principle behind the EU thinking is that the Solvency II directive will require insurance companies to hold a prudent level of capital reserves, and since insurance companies provide pensions then occupational pension schemes should do the same. The UK government quite rightly rejects that comparison. Holding extra capital is a safety buffer for insurance companies to help ensure they can deliver on the pension commitments they have made and sold as commercial products. Occupational pension schemes are ultimately backed by their sponsor, so there is not the same need to prefund them with additional capital.

The European Commission is at the stage of thinking about which provisions in Solvency II could form the heart of a directive for occupational schemes and the adjustments that might be needed to make those rules applicable for the different circumstances of pension funds. The Commission has asked for advice from the European Insurance and Occupational Pensions Authority (EIOPA), which has in turn formulated some ideas and asked for public comment.

The ACT has responded to EIOPA, arguing that pushing pension schemes and insurance into the same regulation is utterly inappropriate, and that introducing excessive requirements for pension schemes to make them safer for members is sure to backfire. Far from protecting employees, such a regulation would make defined benefit schemes unaffordable for employers, so individuals would end up with defined contribution-style savings schemes, which carry a huge investment risk.

The EIOPA consultation (all 500 pages of it) goes into some detail on how to arrive at an assessment of the funding level required. The concept of calculating a holistic balance sheet is introduced to record:

- the pension liabilities calculated on something like a buyout valuation;
- the fund assets;
- the value of any contingent assets provided; and
- an allowance for the sponsor covenant and any pension protection schemes.

The required fund assets will then be set so as to provide an excess of assets over liabilities plus a risk buffer.

Defined benefit schemes may be in terminal decline but even closed schemes will be materially impacted, so companies should be vocal in explaining the implications of any new legislation. If your company does have strong views or has already been vocal, please let us at the ACT know at: **technical@treasurers.org** ■

Prepare the business for a euro breakup

With the euro zone crisis showing little sign of easing, many of the risks arising from any sort of breakup may be routine treasury management issues but ones that are taken to the extreme.

A number of spread betting markets and media outlets are indicating a 30–35% prediction that the euro will be restructured by the end of 2012. While it is widely recognised that any fragmentation of the currency would have devastating economic consequences, planning ahead can minimise certain risks.

The ACT and Deloitte have produced a briefing paper on contingency planning for the euro. The following list is an example of what is at risk.

Sales and purchases

- While your company may not have huge exposure to the euro zone either financially or operationally, your customers may. They may not be able to pay you when invoices are due and may even default on their liabilities.
- The same is true of your suppliers.
- Future sales may be reduced as changes to FX rates make exports too expensive for some markets. For example, if Greece leaves the euro zone and Italy doesn't, then Greek olive oil will be cheaper than Italian. The Italian olive oil industry may then lose sales as contracts shift to Greek olive oil (priced in a new, devalued currency).

Commercial and financial contracts

- If a country leaves the euro it won't be easy to determine whether contracts with businesses in that country will remain in euro or be redenominated to the new currency. Each contract would need to be assessed individually for contractual and jurisdictional law, place of payment, contractual intention, etc.

Cash and cash management

- A country leaving the euro may well implement exchange controls. Cross-border euro payments may be illegal, which could complicate the repatriation of euro assets held in that country by non-residents. Conversely the euro zone may place trade restrictions on the departing country.
- Trapped cash issues can have a knock-on impact on cross-border euro pooling structures, resulting in a need for greater credit lines.

Credit risk

- Irrespective of any impact on the euro, sovereign and commercial debt write-downs and a continued or elevated bank funding squeeze could result in bank defaults. The items at risk include loss of cash and bank deposits, cancellation of debt facilities, and loss of in-the-money value and protection from derivatives.

Debt and credit facilities

- In addition to bank credit drying up, other sources of funding may be impacted. In the past year the bond markets have shut temporarily on a number of occasions. This may happen again.
- For borrowers in affected countries, euro debt located outside the country may stay denominated in euro whereas assets may convert to a weaker new currency.

Foreign exchange and derivatives

- Euro positions currently deemed hedged may become unhedged if the counterparty is in a potentially seceding euro country or if euro derivatives are redenominated or unenforceable. The resultant mismatch of assets and liabilities by currency could lead to a material FX gain or loss.

Reputational risk

- Breaches of new rules introduced by countries, such as trade restrictions or exchange controls on fund transfers, could result in prosecutions and penalties, damaging reputation and brand.

The ACT/Deloitte briefing paper has been designed as a checklist of aspects to review and consider. For a copy of the briefing paper go to: **www.treasurers.org/contingencyplanning/euro**
Also see Fasten Your Seatbelts, page 28 ■

How the City grew
For those with an interest in financial history the Financial Services Club has been running a series on how the City developed from Roman times to the present. **http://bit.ly/weV306**

IN BRIEF

▸ **Oil company Shell is to close its final salary pension scheme to new staff**. This decision by the last FTSE 100 company that was still offering a guaranteed retirement pension regardless of life expectancy or the equity performance of the pension scheme will be effective from the first quarter of 2013. Only 20 years ago almost all large private employers offered final salary-linked pensions as the norm.

▸ **The Payments Council has issued its revised UK National Payments Plan.** The council's goal is to help consumers and businesses by delivering innovation, enhancing inclusion and ensuring integrity in the way we make payments. Key actions identified include helping increase customer confidence in making electronic payments and reviewing ways to allow customers to elect someone to make payments on their behalf.

▸ **EU internal market commissioner** Michel Barnier has welcomed agreement that 1 February 2014 will be the end date for full migration of retail payments in the Single Euro Payment Area (SEPA) for euro members. This is the deadline in the euro area for existing national euro credit transfer and direct debit schemes to be replaced by the SEPA credit transfer and direct debit schemes developed by the European Payments Council.

▸ **Foreign exchange options** are increasingly being used by corporates to hedge FX risk, according to Misys. The volume of FX options matched through its Confirmation Matching Service (CMS) more than doubled in the year to September 2011. The analysis was based on the activity of 130 of Misys' global clients. The increase in currency market volatility and the uncertainty in the euro zone have led many corporate treasurers to update their FX hedging strategies.

▸ **Following the Davies report**, 27% of FTSE 100 board appointments between 1 March 2011 and January 2012 were women. This brings the proportion of FTSE 100 female directors to 14.9%, up from 12.5% at the start of 2011, but still well short of the Davies target of 25% for 2015. FTSE 250 companies have started from a lower position and while 25% of appointments to FTSE 250 boards since 1 March 2011 have been women, the total proportion now stands at only 9.2%.