THIS MONTH

EUROZONE TOPS THE AGENDA

The troubles of Greece and the eurozone are enduring headline news. So, unsurprisingly, the ACT's briefing note on euro contingency planning remains popular. Although most companies have minimal direct exposure to Greece, the wider risks to the European economy are not so easily avoided. I remind readers below about the ACT's note on contingency planning for a downturn in the economy, issued some time back, but now becoming increasingly relevant again.

Martin O'Donovan is ACT deputy policy and technical director @MartinODonovan1

{ IN DEPTH }

PLANNING FOR A DOWNTURN IN THE ECONOMY

The threat of a Greek exit from the euro and financial contagion spreading through the eurozone mean the European economy is at risk of downturn once more.

In May 2008, the ACT issued a briefing note on contingency planning for a downturn, which is worth revisiting given recent events. Here is a summary of some key elements.

Cash and working capital management

In a downturn it is even more important there are no pockets of idle cash around the group. Liquidity becomes critical, so ensure that no 'draw stops' in loan agreements can be used to deny access to vital credit lines. Understand your current supplier and customer terms, and where there may be opportunity to flex them to benefit working capital.

Credit standing

The relative stability of credit rating/standing may make all the difference to availability of funding. Companies perceived as more likely to suffer may encounter problems even before they actually start to feel the direct effects of the downturn. If the company's credit rating was significantly affected during a past downturn, find good reasons to explain why it may be different this time and communicate early with lenders (and other investors).

Funding

Keep close to your lenders and assess where they are coming from and the pressures they might be under. Think about whether your current financing includes any potential pitfalls and make sure you understand the detail. Pitfalls could include:

- 'Draw stops', for example, the need to repeat warranties on a drawing or rollover of revolving credit lines.
- 'Material adverse change' clauses, which could prevent you drawing otherwise committed credit lines.
- Covenants that might be triggered by downturn-inspired changes in accounting ratios.
- Restrictions that might affect how the company responds to a downturn, for example, restrictions on disposals or uses of alternative financing.
- Automatic repayments required by changes in your credit ratings.

Depending on your funding headroom, should you now be thinking about raising more medium- and long-term finance? Beware of delaying funding in the hope of better conditions; for they may actually get worse.

Business plans

Operational and financial flexibility become much more important in a downturn, so review plans with a newly critical eye.

- Use standard tools such as SWOT, Porter and PEST to assess strategic issues. There may be chances to make opportunistic or defensive acquisitions, for example, to stop a firm falling into the hands of a competitor.
- Are there under-used assets or an under-performing division that could be disposed of?
- Will you be subject to new competitors coming into your markets in response to declines in their existing markets?
- In a downturn, the company is likely to be less able to withstand events it previously could just absorb. So, update the risk register, or equivalent; update risk management practices; and review those risks the company is retaining/managing and consider laying off/avoiding/hedging more than when the company was stronger.

A treasurer's checklist is available at www.treasurers.org/contingencyplanning

YOUR SHOUT

Which regulatory developments concern you most right now? Are important changes coming down the line that you think treasurers are not sufficiently aware of? Tell the ACT policy and technical team. Email: modonovan@treasurers.org or mprice@treasurers.org

{ INTERNATIONAL }

EU PARLIAMENT ADOPTS FTT

The European Parliament has resolved to go ahead with a financial transactions tax (FTT) even if only some member states opt for it. Parliament accepted the Commission's proposed timetable of a 31 December 2013 deadline for member states to legislate and 31 December 2014 for entry. But a taxation measure like this cannot be forced upon any member state without unanimous approval from all 27 members.

While the UK does not intend to implement an FTT, the EU Parliament has adopted an 'issuance principle' that was not in the Commission proposal. Under this principle, financial institutions located outside the EU would be obliged to pay the FTT if they traded securities originally issued within the EU. For example, the tax would be liable if a Hong Kong institution and a US institution traded shares in Siemens that were originally issued in Germany.

Parliament also ruled that:

- The tax rates proposed by the Commission (0.1% for shares and bonds and 0.01% for derivatives) are suitable and pension funds should be the only sector exempted from the tax.
- The 'residence principle' remains, which would catch shares issued outside the EU but subsequently traded by at least one institution inside the EU.
- The payment of the FTT will be linked to the acquisition of legal ownership rights.
- Transactions made on the primary market (ie purchasing of securities from the issuer when such securities are first placed on the market) will be exempted.

NEW ON THE WEB

View the following technical updates and policy submissions at: www.treasurers.org/technical

ACT response to IOSCO on Money Market Funds reform

Euro contingency planning

20 issues on the increasing significance of corporate treasury

Collateral requirements for OTC derivatives: ACT submission to ESMA

Clearing requirements for OTC derivatives: ACT submission to ESMA

{ WATCH THIS SPACE }

EC IS LESS RADICAL ON CREDIT RATING REGULATION

The European Council has adopted a slightly less radical position on regulating credit rating agencies (CRAs) compared with the EU Parliament, but agreement is still some way off:

- Mandatory rotation is limited to ratings of structured finance products with underlying re-securitised assets.
- An outgoing CRA would not be allowed to rate re-securitised products of the same issuer for a period equal to the duration of the expired contract, though not exceeding four years.
- Issuers of rated securitised instruments would have to engage at least two different CRAs.
- Mandatory rotation would not apply to small CRAs, or to issuers employing at least four CRAs, each rating more than 10% of the total number of outstanding rated structured finance instruments.
- Investors or issuers could claim damages from a CRA if they suffered a loss due to an infringement committed by the agency intentionally or with gross negligence, and the reverse burden of proof concept is removed.
- Sovereign ratings would have to be reviewed at least every six months (rather than 12, as currently applicable under general rules).

{ TECHNICAL ROUND-UP }

REFORM AND REGULATION

Pay Your Way is the Payments Council's consumer campaign to give impartial information on the speed, cost and security of different payments. Its website, www.payyourway.org.uk, has recently flagged a banking fraud where people are telephoned by fraudsters and duped into revealing their PIN and handing over their bank card to a courier.

The IASB has appointed a new board member – Martin Edelmann. He served as a member of the German Accounting Standards Board (GASB) from 2006 until 2011, and is a former head of group reporting at Deutsche Bank AG.

A recent High Court case (*Jayesh Shah* v *HSBC Private Bank*) has established that banks will not be liable to customers for delays in processing transactions while waiting for clearance under UK anti-money laundering legislation.

Ideas for reform of money market funds (MMFs) have been put forward by the International Organization of Securities Commissions (IOSCO). Regulators are concerned over systemic risk arising from MMFs and the potential for dangerous runs on their funds. Suggestions include liquidity controls, redemption restrictions and possibly moving all funds to a variable net asset valuation basis. In its submission to IOSCO, the ACT recognises that the constant net asset value (CNAV) label is potentially misleading, but argues that this is insufficient reason to change fund structures, effectively removing a very popular instrument from investors.

Swap termination rules have been interpreted in a Court of Appeal judgment (*Lomas & Others* v *Firth Rixson & Others*). Several companies that bought interest rate swaps from Lehman Brothers had decided, based on their interpretation of the 'Section 2' clause within the International Swaps and Derivatives Association master agreement, not to terminate their contracts as they would have had to pay out to the defunct bank. It was ruled that Section 2(a)(iii) suspends rather than extinguishes the relevant payment obligations of a non-defaulting party until the default is cured.