Pact to widen legal certainty for swaps

Lawmakers from the US Senate and House of Representatives recently struck a ground-breaking agreement on modernising US derivatives legislation that, if passed, will broaden the legal certainty for swaps.

The agreement offers the OTC derivative industry the broadest legal certainty for swaps yet, as it excludes all banking products from the Commodity Futures Trading Commission's jurisdiction. The Gramm-Leach-Bliley Act, passed last year, already contains a provision that prohibits the SEC from regulating swaps or any banking products. The recent deal is expected to be enshrined in a new version of the Commodity Futures Modernisation Bill.

A clause stating that circuit court will not give either the CFTC or the Fed deference in any future hearing on grounds that either agency has expertise in the area will be included in the redraft. Typically, the court pays attention to one agency over another on this basis.

If the bill passes the House in its current form, the Senate is expected to simply pick up the House version and schedule it for a vote before session adjourns. The entire modernisation push is aimed at re-authorising the CFTC, securing legal certainty for OTC derivatives, as well as repealing the 18-year ban on single stock futures.

US banking lobby groups had written to House of Representatives majority leader Dick Armey urging a compromise over the recent amendment to the bill that would exempt swaps and options from the prospect of being categorised as futures – and from possible regulation by the CFTC.

The banking committee tacked on an amendment to the Commodity Futures Modernisation Bill that would provide a regulatory framework for the sale of OTC derivatives to retail counterparties such as small businesses and individuals.

It has been a hard grind this year to get the various committees with some derivatives oversight in the House and Senate, and key regulators, to reach a consensus on legal exemption for swaps, streamlined futures regulation, and an end to the 18-year ban on single stock futures.

That is now threatened by the clause effectively to open up a market for retail use of OTC derivatives.

Trade groups said they would be happy to participate in a further review of the bill, and suggested a compromise where the threshold for eligible OTC derivative participants would be established at $5m, if the transaction was to be used for hedging purposes. IFR

US tax changes may help investors

Retail investors in Europe have never quite taken to global bonds. Registered securities have always gone against the grain in the Eurobond market, which has thrived for almost 40 years on the back of thin regulation and the tax-efficiency of bearer securities.

Ironically, new US tax rules coming into effect in January will result generally in more onerous withholding tax requirements on US securities purchases made through foreign intermediaries. But European retail will, for the first time, be able to gain formal anonymity from US tax authorities.

This should make global bond offerings more appealing. If underwriters have a direct relationship with investors, they can pool assets according to tax eligibility without providing the IRS with details of specific investors.

This could open the door to a whole new asset class for retail investors and further the US agencies and other benchmark US issuers' efforts to generate the fabled pricing tension and value efficiencies with regard to the US domestic market. IFR

These extracts are from IFR (International Financing Review). For further details, please contact Lara Bull on 020 7369 7984 (tel) or 020 7369 7397 (fax).
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Investment banks learn relationships

Investment banks are starting to get a taste of life in the clubby world of syndicated lending. The value proposition is simple: you stump up huge volumes of cheap money to maintain a cosy relationship with the borrower in the hope of getting some ancillary business.

Relationship lending has always been anathema to investment banks, because only a few can ever get a share of what ancillary business is on offer. But borrowers – and lenders – know full well that the opportunity cost of not playing the game is too high.

However, things may be changing. News that a trio of Wall Street's most distinguished have had the audacity to turn down Vodafone and Deutsche Telekom's invitations to support their vanilla loans was a memorable moment. They were reported to have declined the €12bn and £3.5bn financing for Deutsche Telekom. Vodafone received just one decline from the 40 banks invited to join its $15bn self-arranged CP backstop financing – from an investment bank.

Profitable

Resentful at the investment banks' ability to originate high-profile and highly profitable M&A advisory and capital markets business without having to endure loss-leading balance sheet lending, the commercial banks and new financial supermarkets see the incidents as a turning point.

European borrowers have until now accepted that investment banks have only chased high-yielding financings. DT and Vodafone have put paid to that. Other borrowers are expected to follow suit and ask investment banks to stump up hard cash.

In the US, requiring investment banks to enter vanilla facilities has been a source of conflict between the two groups of banks for years. Ford's request this summer that its investment banks extend substantial CP backstop commitments was heralded by commercial banks as a triumph. IFR