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A ring fence will not save the UK from exposure

Richard Tice, Chairman of the Global Britain Business Group, has described as “worthless and complacent” Chancellor George Osborne’s assurance that UK taxpayers’ money being used to underwrite a third Greek bailout will be protected by an “impregnable ringfence” arrangement.

Commenting on the failure by the government to prevent any UK financial exposure from the EU’s attempt to solve the Greek debt crisis Richard Tice commented:

“Global Britain is releasing today research conducted by respected City international finance consultant Bob Lyddon that exposes the truth about a bailout using EFSM funds, and that is that the debt will be the joint and several liability of all EU member states. In short, this means that the UK liability cannot be limited to its 14 per cent membership share of the loan if Greece defaults (estimated to be £850 million) but will also be liable for a share of Greece’s own EU membership fee that it will not be able to pay – and could be liable for up to 100 per cent of the loan if every other member failed to contribute.

“While the worst case scenario of being liable for all of the Greek bailout is unlikely the risk of contagion from a Greek default is high and that would mean other countries such as Portugal, Italy, Spain and even France could be drawn into the crisis. Any inability of another country to contribute to the Greek default would then leave the UK with far larger bills to pick up than George Osborne is prepared to admit. No ring fence can prevent this.

“The truth must be that just as the 2010 agreement to leave the UK out of any future Eurozone bailouts has been found to be worthless, so too must any ringfencing be worthless and complacent to pretend otherwise. Calling it impregnable is an attempt to mask the truth.

“Bob Lyddon is an expert in the field and his paper lays bare the real arrangements for the EU’s international debt finance, supported by rating reports of Standard&Poor and Moodys. Whatever assurances are given the legal arrangements are defined by EU treaties and not by some face-saving Commission assurances that can be broken when it suits the EU.

“This whole episode emphasises just why any EU reforms are worthless without treaty change and that our politicians and the EU cannot be trusted to act in good faith.”

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Editor's notes:
The *Global Britain* briefing paper by Bob Lyddon is in full below:

The UK's risk to Greece is greater than we realise

The proposal to revive the EFSM (European Financial Stabilisation Mechanism) to provide funds for Greece is what many have feared for some time: that the EU authorities will try to engage non-Eurozone states in the Greek salvage operation either through the undrawn portion of the EFSM (which is about EUR12 billion) or the Balance of Payments Facility of EUR50 billion (which is substantially undrawn).

The risks to the UK from the EFSM seem to be misunderstood in two ways.

Firstly, this is not a bridging loan or temporary assistance. The precedent is with Ireland and Portugal. The EFSM funds were publicised in 2010 as "available for 3 years", which one could assume meant that the countries could draw the money but then had to pay it back by 2013. At least the countries should not be able to exit the bailout mode without repaying the bailout money.

Instead, successive meetings of the Council of Ministers approved EFSM loan maturities for Ireland and Portugal going out to 30 years, such that "available for 3 years" really meant "available for *drawing* for 3 years", and both countries were able to exit bailout without repaying the bailout funds: an absurdity.

Secondly, is the question of the amount of risk for the UK. This is put about as being 14 per cent of the EFSM loans because the UK's normal percentage of the EU budget is 14 per cent.

This not the worst case, though. The funds for the EFSM are first borrowed by the legal person The European Community via issuance international bonds. Then the European Community on-lends the bond proceeds back-to-back to the EFSM, which then makes its loans back-to-back to the bailout countries. If a bailout country defaults or only repays with a haircut, the loss is booked in the EFSM first of all but then made good out of the European Community budget.

Then the European Community budget is increased by the amount of the loss to be borne, and, in the first instance, parcelled out at 14 per cent for UK, x per cent for Germany, y per cent for Slovenia and so on – and n per cent for Greece. But Greece has defaulted, hasn't it? It cannot pay its EU budget contribution. In consequence the contributions of the other member states are increased, and they can be increased to a point where one member has to pay everything – the last-man-standing principle.

The bond prospectus for the bonds that the European Community issues to fund the EFSM explains the mechanism. Bonds issued by the European Community are the *joint and several liability* of all member states. The rating reports of Standard&Poor and Moodys on the European Community explain this as well. That's why international investors favour the bonds of the European Community over EIB (European Investment Bank), EFSF (European Financial Stability Facility) and ESM (European Stability Mechanism).

The European Community is the best quality borrower of all the European institutions because:
- It can make a call for money on all EU member states and not the Eurozone ones alone;
- The call on member states is joint and several, meaning unlimited up to 100 per cent of the amount on any one member state, whereas the calls on the European Investment Bank and on the EFSF and ESM are capped: they are several but not joint, meaning there is a ceiling to the call that can be made on any one member state.

So all loans out of the EFSM are 100 per cent at the risk of the UK, not the 14 per cent that is the UK's normal EU budget contribution. That is why the EFSM – and the Balance of Payments Facility – are so dangerous for the UK.

Bob Lyddon, of Lyddon Consulting, for Global Britain