

Currency options – the Polish aspect of the global financial crisis | BY DOMINIK GAŁKOWSKI

The global financial crisis that began last year, so far has been relatively gentle on the Polish economy. According to the current data published by Eurostat, only Poland and Cyprus have recorded positive GDP growth out of the EU member states that have communicated their results. However, despite the relatively good shape of Polish businesses, a significant weakening of the Polish currency in relation to the Euro has taken place since August 2008. To illustrate this phenomenon, it is sufficient to indicate the PLN/EUR exchange rate on 31 July 2008 was PLN 3.20 per 1 EUR, compared to PLN 4.89 per 1 EUR on 18 July 2009. The exchange rate currently oscillates around PLN 4.5 per 1 EUR. Such substantial weakening of the Polish currency has caused unexpected yet significant problems for many Polish businesses that relied on asymmetrical currency options not just as means of securing the exchange rate but for speculative purposes as well. In mid 2008 it was common to conclude asymmetrical zero-cost options whereby put-call options were concluded in which the call option nominal for the bank exceeded the put option nominal for the business owner.

Indirectly, Polish business owners' problems could have a negative impact on the Polish banking sector due to conclusion by Polish banks of back-to-back hedging transactions with foreign banks as means of securing options. In such a situation, the loss incurred by the business owner is similar to the bank's loss for a back-to-back transaction and as such, in the event of the client's insolvency, the bank will not have the means to cover the loss that it will suffer due to the securing of the option.

To date, Poland has still not adopted Directive 2004/39/CE on MiFID – Markets in Financial Instruments Directive – nor Directive 2006/73/CE which alongside significant facilitation of access to the market by investment companies introduces regulations increasing the level of protection of investor rights (the date by which this was to take place passed on 31 January 2007). One of three Polish acts that were to implement MiFID (the act on amendment of the act on financial instrument trading) was referred by the President of the Polish Republic to the Constitutional Tribunal for examination of its compliance with the Polish Constitution. At the same time, executive orders for the MiFID are in force as of 1 November 2007 in the form of EC Commission regulation 1287/2006 that give executive powers to directive 2004/39/CE of the European Parliament and Council concerning the obligations of investment companies regarding the maintenance of registers, transaction reports, market transparency, allowance of financial instruments for trading as well as terms defined for the purposes of the directive. However, since the provisions of the above regulations have a direct application, there is currently some uncertainty concerning the legal status regulating the rules of provision of investment services on the Polish market.

A potential direct result of the directive on MiFID will be limited to the vertical aspect (individual-state relationship) although there will be a lack of horizontal effectiveness. This will additionally mean that it will not be possible to apply some provisions of regulation 1287/2006 currently in force due to their relationship with the relevant provisions

of the non-implemented directive.

The above legal status and above all the lack of full implementation of the directive on MiFID are the reason for the serious problems experienced by business owners who concluded the above-mentioned asymmetrical currency option agreements. As a result of the sudden change in the EUR/PLN exchange rate to the Polish currency's disadvantage, businesses have suffered significant losses and increase in debt. The magnitude of the problem could be illustrated by the statistical data published by the Polish Financial Supervisory Authority from which it emerges that the current combined negative valuation of option transactions could even reach PLN 15bn.

Ill-judged investments have led to the insolvency of not just small and medium-sized enterprises but also large companies listed on the stock exchange which have been forced to lodge motions for the declaration of bankruptcy. In turn, it was impossible for such a state of affairs not to have been noticed by government, which has offered help for the affected business owners in the form of free legal aid. However, some politicians have gone even further by submitting a package of special bills to the parliament aimed at not only the introduction of appropriate protective measures against dishonest practices of financial institutions in the scope of trading of some complex financial instruments, but foremost at the protection of businesses from the unfavourable results of concluded currency option agreements. The bills foresee above all: (i) the possibility of suspending the execution of concluded asymmetrical currency option agreements; (ii) the obligation of the parties to the agreement to conduct negotiations on changing the agreement provisions; and also – most importantly (iii) give the parties (and in practice the interested business owners that have suffered damage) the right to withdraw from the concluded agreement. Moreover, business owners will gain a series of privileges that they could exercise as a means of protection against banks' claims in court. The bills are currently awaiting examination by the parliament hence it is not possible to foresee at the moment whether they will become a binding law. Nonetheless, according to the latest information, the bill authors have categorically announced that they will fight for the fastest possible implementation of the bills.

Regardless of the mode of implementation of the regulations on the protection of the interests of clients of financial institutions, which – and it should be emphasised – are compatible with the solutions offered by the directive on MiFID, they can with all certainty be positively assessed as they constitute a step towards the harmonisation of Polish law with European standards. However, we should be a lot more careful when it comes to such profound interference by the legislator in contractual relations between private law subjects as the one described above. Particularly since such interference will have retrospective force. Firstly, we should ask how such interference will influence Poland's attractiveness as an investment destination. Doubtlessly, some foreign investors could feel discouraged from investing their capital in Poland precisely fearing that their investments may become the object of such top-down interference. Secondly, it cannot be entertained that the law ►►

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is sufficiently flexible as to provide business owners with appropriate instruments which they may use as defence against unfair banking practices. The implementation of the described solutions could hence constitute a dangerous precedent for which politicians will reach increasingly more often in the future, thus destabilising the market. However, even worse is that there is no certainty that the actions proposed by the politicians will help to solve the problem. For it should be supposed that banks will not so easily let go of the money that businesses owe them and most definitely they will demand an inquiry into the compatibility of the enacted laws with the Constitution.

Hence, regardless of how the problem will be solved, a hope remains that on the one hand Polish business owners will reach an understanding with the banks that will enable them to avoid bankruptcy, and on the other hand, that the actions of decision-makers aimed at the rescue of the affected businesses will not have a negative impact on Poland's attractiveness for investors as well as its international credibility as a business partner. ■

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