

about Canada at the moment, Canada could be seen as a safe haven and experience (temporary) capital inflows and an appreciating currency against Europe.

5.2 Canadian Trade and Financial Markets

There will be a number of technical issues for Canadian foreign trade and financial market participants as they deal in a new currency, and, over the transition period, relating the euro to the predecessor currencies.¹¹

Contracts

One major issue will be the legitimacy of long-term contracts set for payment in predecessor currencies which will no longer exist after 2002. Europe is aiming to make the euro the legal successor currency to national currencies of EMU participants, and it is likely that UK jurisdictions will adopt the same approach even if the UK stays out of EMU. However, many swap contracts are subject to New York jurisdiction and the litigious and unpredictable nature of USA courts is a worry. It is possible that swap contract parties could, taking advantage of the legal confusion, successfully argue that force majeure existed and so unwind the swap contract prior to its maturity under standard clauses in swap contracts.

Another issue is whether the accounting profession and tax authorities would require realization of gains and losses (and associated tax liabilities) of assets converted to euro. The issue will revolve around whether the restated assets and liabilities are the same as the old or whether they are new ones which replace the old.

International trade practices

Tendering and trade invoicing may undergo some revision. At present the practice is to quote bids and invoice largely in US funds, which requires non-US bidders to hedge against exchange risk if they feel overexposed. Over time, some invoicing might move to euros, as might quotes for commodities such as oil, gold, and base metals. There is no particular economic need to do so, however, as long as exchange markets are liquid and unrestricted and the cost of hedging remains low.

¹¹Such issues may appear trivial (ie just multiply everything by the locked exchange rate). However, the issue of reciprocal conversion factors has received considerable attention. The EMI is recommending outlawing the use of reciprocal conversion factors because rounding-induced discrepancies will produce different "round-trip" amounts. Therefore to convert back to the original currency, one should divide by the published exchange factor rather than multiply by its reciprocal. This is one example of the issues Canadian business should be aware of.