EC PARENT

Subsidiary directive

The European Council has made some changes to the Parent-Subsidiary Directive to extend the scope of the existing rules, which prevent double taxation of parents in respect of the profits of their subsidiaries, and which eliminate withholding taxes on dividends paid between group companies which are located in different member States. The Directive progressively reduces the ownership thresholds required to qualify from the current 25% down to 10% from 2009, and will additionally include the new 'European Company' and the 'European Cooperative Society' within its scope. ■

The Treasurer's Handbook 2004

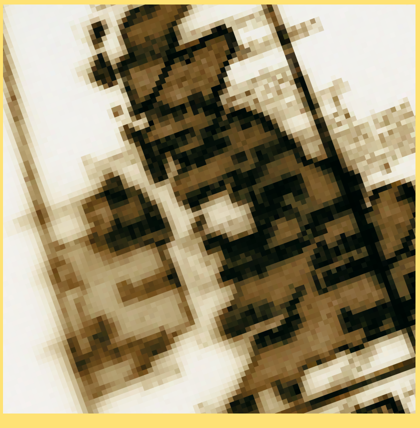
The 2004 edition was published in February. ACT members who have not received their copy should email **amcgee@treasurers.co.uk**.

The following contributors were not acknowledged in the Handbook, and we would like to thank them along with the other contributors:

- Treasury Systems and the Internet, p223 – Jonathan Hodgson of adsatis, www.adsatis.com, tel +44 (0)20 7663 0815 (co-author with Ken Lillie of SunGard Treasury Systems).
- US Country Guide, p511 – Susan Skerritt of Treasury Strategies Inc, www.TreasuryStrategies.com, tel +1 212-785-5653. ■

FSA

Review of the UK Listing regime



The December 2003 edition of *The Treasurer* summarised proposals from the Financial Services Authority (FSA) concerning the reform of the Listing regime. The FSA was seeking views on their objective to simplify and modernise the Listing regime and at the same time to accommodate the impact of changes being proposed to the European regulatory framework.

The consultation paper covered overall policy and any detailed rule changes will be published in the third quarter of 2004 in the form of a further consultation paper. Finalised rules should then be published in spring 2005 for implementation that summer.

Given the implications for companies engaged in debt or equity issues or subject to the continuing requirements of being listed, the ACT has made a formal response to the FSA. (For full response see www.treasurers.org/technical)

The Association of Corporate Treasurers (ACT) was generally supportive of the purpose and general direction of the proposals to simplify and modernise the Listing regime, whilst at the same time not detracting from the reputation of the London markets through diluting the effectiveness of regulation here.

The ACT supported an introduction of overarching principles which would provide a substance-over-form approach that would supplement the detailed rules. Other significant changes proposed that were specifically supported were:

- Relaxation to the requirement for a working capital statement on equity issues so that full cover of forecast cash needs was not essential and instead the issuer could explain how it proposed to cover any shortfalls.
- Removal of a need for any working capital statement for non-specialist debt issues
- Dropping the two-year track record required for specialist bond issues and instead changing to 'two years or since start of operations if shorter'.
- Maintaining the requirements for approval of Class 1 transactions by shareholders.
- Extending the scope of Class 1 transactions to include other types of transactions where the shareholders' investments are to be significantly changed or diluted, eg certain securitisations.
- A new requirement for shareholder approval prior to delisting.
- A proposal to enable issuers to publish additional and unaudited financial information, as long as this is clearly indicated and it is capable of subsequent comparison to actual published results.

On certain other points the FSA was open in seeking views on various options.

The representations made by the ACT were to support the following:

- Retention of the requirement on equity issues and Class 1 transactions to have a sponsor.
- Retention of the need to include a significant change statement in Class 1 circulars even if companies move on to a quarterly reporting schedule.

On just a few points the ACT took a slightly different stance from the FSA proposals or felt it necessary to extend its comments beyond the specifics raised by them, including:

- The belief that if the reporting requirements on Prospective Financial Information were to be relaxed there was still a real need for a form of audit reasonableness test to avoid such statements becoming merely wish lists.
- A strong view that there was a need to amend the listing rules to allow the disclosure of price-sensitive information to credit rating agencies under a confidentiality agreement, notwithstanding that the FSA recognises that this is already an accepted practice in the market.
- A recommendation that further consideration be given to the distinction between specialist and non-specialist debt issues and the rules applicable to each. This is needed because additional rules are being introduced to distinguish wholesale and non wholesale debt issues under the Prospectus Directive and in any case the UK rules for non-specialist debt are so onerous that these retail type issues are rarely made in the London market. ■

PRE-BUDGET REPORT

ACT responds to pre-budget consultations

The Inland Revenue's pre-budget report in December 2003 included numerous consultation papers on possible forthcoming changes to taxation. The ACT has submitted responses on those of particular relevance to treasurers.

The ACT supported the standardisation of the tax regime for property derivatives, but expressed concern if there was to be a mismatch between the taxation of the derivative and the underlying asset. In particular, if unrealised gains on the derivative were to be taxed year-by-year then there should be the right to carry back capital losses on the underlying asset to provide the offset. This offset should be capable of crossing from one group company to another. The extension of similar rules to equity derivatives was not felt to be appropriate since there were wider implications that would need to be dealt with.

There was another consultation on the meaning of UK source for payments of interest and royalties where the ACT was pleased that a statutory definition would be introduced in order to provide clarity and certainty. However it was not thought sensible to define as UK source, interest paid by non-resident landlords in respect of property situated in the UK. Were this to happen the non-resident landlord would be required to deduct income tax from interest payments.

The Revenue was also consulting on the giving of tax relief on membership subscriptions to encourage organisations which promote the development and education of the workforce. As an organisation where members do receive this tax relief, the ACT supported the continuation of this arrangement, and made the point for extending the relief to the costs of membership exams and training. ■

SHARE-BASED PAYMENTS (PART 1)

Big change under IFRS 2

Before International Financial Reporting Standard 2 (IFRS 2), there was no international accounting standard covering the recognition or measurement of share-based payment, according to the International Accounting Standards Board (IASB). But the importance of high-quality financial statements that provide neutral, transparent and comparable information is key, given the increasing use of such payment methods in recent years, and given the spate of recent corporate failures where accounting irregularities came to light. (See p14 for key points).

In particular, the omission of expenses arising from share-based payment transactions with employees has been highlighted by investors, other users of financial statements and other commentators, as causing economic distortions and corporate governance concerns, says the IASB. IFRS 2 fills this gap in international standards.

The objective of IFRS 2 is to specify the financial reporting by an entity when it undertakes a share-based payment transaction. In particular, the IFRS requires an entity to reflect in its profit or loss and financial position the effects of share-based payment transactions, including expenses associated with transactions in which share options are granted to employees.

Sir David Tweedie, IASB Chairman, explains: "This standard addresses an area of accounting that has been a concern to users of financial statements for some time. Recently, those concerns increased substantially when major corporate failures demonstrated the importance of transparent, unbiased and complete financial statements.

"The objective of IFRS 2 is to require that, no matter what form of remuneration is used, the entity recognises the associated expenses."

He adds: "In this way, IFRS 2 will improve the quality of financial reporting by giving a clearer and more complete picture of an entity's activities, which will assist investors and other users of financial statements to make informed economic decisions."

Previously under IFRS, only the nature and terms of share arrangements had to be disclosed and recognition was voluntary so there was rarely a charge in the income statement.

Commenting on the launch of IFRS 2, Ian Wright, Global Corporate Reporting Leader at PricewaterhouseCoopers, remarked: "The first concern for companies with share-option schemes will be to understand the scope of the standard and to determine the data requirements. Implementation will be especially complex for senior executives' share-option awards that contain individual performance criteria."

He says the next steps will be to collect the information and carry out the required valuations. "But the most important step – getting the outside world to understand the charge to the income statement – is a crucial one that management should address early," he adds.

"The publication of IFRS 2 is an important step in completing the final platform of standards for all companies adopting IFRS in 2005 and brings the capital markets closer to having one global language of financial reporting."

www.iasb.org.
www.pwcglobal.com ■

Simultaneously the ASB announced its intention to issue an accounting standard on share option schemes and other share-based payments and to bring that standard into effect for accounting periods beginning on or after 1 January 2005 for listed entities and 1 January 2006 for all other entities. FRS 20 'Share-based Payment' will be identical to IFRS 2 'Share-based Payment', save for the deferred implementation date for unlisted companies.

BUDGET

Tax focus for 2004 budget

There was good news for corporate treasurers in the 2004 Budget with corporation tax unchanged and favourable amendments to tax rules for companies making the transition to International Financial Accounting Standards in 2005. But the government came down heavily on tax avoidance while also tightening the rules on transfer pricing.

For corporate treasurers, one of the most positive pieces of news was that companies adopting International Financial Reporting Standards (IFRS) as of 1 January 2005 will qualify for the same tax treatment as companies continuing to use UK GAAP (Generally Accepted Accounting Principles). This dispelled concerns that companies adopting IFRS next year will be penalised immediately on gains and losses made from derivative transactions.

"The specific measure announced today will allow fair value gains or losses on certain hedging transactions to be deferred for tax purposes until the gain or loss on the underlying hedge item is realised," commented Gillian Wild, Tax Director at PricewaterhouseCoopers. "We were aware that this was an area causing significant concern in the corporate sector and this does represent a measure of transitional relief that will be very valuable."

At the same time, corporates managing investment business were given a boost with the decision that they will now all qualify for tax relief on expenses accrued from managing investments – regardless of whether or not they qualify as investment companies.

However, on the downside, Chancellor Brown's Budget came down heavily on tax schemes and arrangements. Under the new rules, promoters of schemes must provide the Inland Revenue with details of the arrangements involved as soon as a sale is made. This will provide the IR with information about potential tax avoidance schemes much earlier than at present, enabling more immediate investigation.

The 2004 Budget also brought new requirements for transfer pricing between the subsidiary companies of a group within the UK as of 1 April 2004, one major aspect of which is the obligation that inter-company loans be made at market interest rates. This move is expected to bring increased administration and new systems needs and costs for corporate treasurers. ■ *The Treasurer will be taking a more detailed look at the 2004 Budget and the implications of its announcements for corporate treasurers in its May issue.*

SHARE-BASED PAYMENTS (PART 2)

Key points of IFRS 2

In principle, transactions in which goods or services are received as consideration for equity instruments of the entity should be measured at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity is required to measure the transaction by reference to the fair value of the equity instruments granted.

For transactions with employees and others providing similar services, the entity is required to measure the fair value of the equity instruments granted, because it is typically not possible to estimate reliably the fair value of employee services received. The fair value of the equity instruments granted is measured at grant date.

For transactions with other parties (ie other than employees and those providing similar services), there is a rebuttable presumption that the fair value of the goods or services received can be estimated reliably. That fair value is measured at the date the entity obtains the goods or the counterparty renders service. In rare cases, if the presumption is rebutted, the transaction is measured by reference to the fair value of the equity instruments granted, measured at the date the entity obtains the goods or the counterparty renders service.

For goods or services measured by reference to the fair value of the equity instruments granted, the International Financial Reporting Standards (IFRS) specifies that, in general, vesting conditions are not taken into account when estimating the fair value of the shares or options at the relevant measurement date (as specified above). Instead, vesting conditions are taken into account by adjusting the number of equity instruments included in the measurement of the transaction amount so that, ultimately, the amount recognised for goods or services received as consideration for the equity instruments granted is based on the number of equity instruments that eventually vest.

The IFRS requires the fair value of equity instruments granted to be based on market prices, if available, and to take into account the terms and conditions upon which those equity instruments were granted. In the absence of market prices, fair value is estimated, using a valuation technique to estimate what the price of those equity instruments would have been on the measurement date in an arm's length transaction between knowledgeable, willing parties.

The IFRS also sets out requirements if the terms and conditions of an option or share grant are modified (eg an option is repriced) or if a grant is cancelled, repurchased or replaced with another grant of equity instruments.

For cash-settled share-based payment transactions, the IFRS requires an entity to measure the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, the entity is required to remeasure the fair value of the liability at each reporting date and at the date of settlement, with any changes in value recognised in profit or loss for the period.

The IFRS also sets out requirements for share-based payment transactions in which the terms of the arrangement provide either the entity or the supplier of goods or services with a choice of whether the entity settles the transaction in cash or by issuing equity instruments.

The IFRS prescribes various disclosure requirements to enable users of financial statements to understand:

- the nature and extent of share-based payment arrangements that existed during the period;
- how the fair value of the goods or services received, or the fair value of the equity instruments granted, during the period was determined; and
- the effect of share-based payment transactions on the entity's profit or loss for the period and on its financial position. ■

BASEL II

Tiner voices concern

In a recent interview John Tiner, Chief Executive of the Financial Services Authority (FSA), expressed concerns over the drafting of the new Basel II capital adequacy rules for banks. At a conference in London, he was critical of how securities regulators were not consulted before the drafting of the Accord. In an article in the *Financial Times*, Tiner was reported as saying: "It is clearly unsatisfactory that the banking regulators alone should set standards for capital adequacy that then need to be adopted by securities regulators."

Super-regulators, such as the FSA, have worked alongside the Basel Committee and central bankers in drafting Basel II, but the big concern is that in the US, only bank regulators such as the Federal Reserve and the Controller of the Currency were involved. In particular, the absence of the Securities and Exchange Commission (SEC) could cause headaches. The SEC is introducing new capital adequacy rules aimed at broker/dealers, which differ in a number of key areas, most notably as the SEC rules may allow long-term non-subordinated debt to count as capital. "If permitted this would clearly set a substantially lower standard for available capital than applies under Basel," said Tiner. **www.fsa.gov.uk** ■

COMPLIANCE

The Sarbanes -Oxley catalyst

Although the Sarbanes-Oxley Act has received much attention, technology and its role in helping financial institutions meet compliance requirements has received little regard, according to new research from TowerGroup. The group says that financial institutions should view the Act as a catalyst for long-delayed business transformation. **www.towergroup.com** ■

EU UPDATE

SME support needs more work

The EU has released its fourth Implementation Report of the European Charter for Small Enterprises, showing that results have been seen in improving the environment for small businesses, but it remains crucial that Member States continue to take action in line with the Charter's recommendations.

Erkki Liikanen, EU Enterprise and Information Society Commissioner, said the combination of benchmarking, monitoring progress and sharing good practice has proved successful in the Charter context. "The Member States are increasingly drawing inspiration from measures developed in other countries and from recommendations of the Commission's projects to improve the business environment. This is real progress and the best way to bridge performance gaps in the EU."

One priority area is that of consulting SMEs on development projects. But, according to the report, while a number of countries have well-established systems in place to consult SMEs, differences between the Member States still exist. Constant pressure for improving regular and systematic consultation is needed.

In addition, many SMEs still encounter significant problems to improve their innovation performance. Measures to facilitate technology transfer, clusters and inter-company networking are needed, said the report. **http://europa.eu.int/comm/enterprise/enterprise_policy/charter/reports.htm.** ■

Transferring offices

The European Commission has launched an Internet consultation on the planned Directive on the right of limited companies to transfer their registered office from one Member State to another. Comments can be registered by 15 April 2004 at **http://europa.eu.int/yourvoice/consultation.** ■

IN BRIEF

■ The US Clearing House Interbank Payment System (CHIPS) will begin accepting large value payment transactions via SWIFTNet in addition to accepting them over its private TCP/IP Network. This will allow CHIPS customers to benefit from communications flexibility and efficiency, while the industry will benefit from improved resiliency of the global payments infrastructure, according to CHIPS. **www.chips.org**

■ JMH Demica has launched Citadel Factor, a software solution that aims to automate the factoring and invoice discounting process whilst providing a platform for invoice securitisation. **www.demica.com**

■ S1 Corporation has released S1 Trade Finance 2.2, an updated version of its internet-based solution for managing international trade finance operations. The new release offers administrative, customer service and real-time reporting features and enables institutions to expedite trade cycles, reduce processing costs and offer competitive services to gain new customers, according to S1. **www.s1.com**

■ SunGard Trading & Risk Systems is unifying its existing systems for buy-side and sell-side institutions under a single technology framework, called Adaptiv. The group says Adaptiv will help customers implement technology tailored to their specific needs using a modular, building-block approach. It can be configured to provide real-time, straight-through trading, portfolio analysis, desk-level risk management and processing, as well as enterprise-wide credit and market risk management. **www.risk.sungard.com**

■ SuperDerivatives is releasing a new risk management system, SDRM, which provides options risk management for front and middle offices of trading and treasury operations in banks and large corporations. **www.superderivatives.com**

■ Trema has bought the assets of Alterna Technologies and will use the Canadian group's Auros technology as an integrated cash management, payment factory and in-house banking module within the Trema product suite. The repackaged software is expected to be available from Q2 2004.

The group has also announced the launch of NAV Monitor, used for the real-time calculation and reporting of Net Asset Value (NAV). **www.trema.com**

PERCENTAGES

CENTRALISING CASH

Regional centralisation of cash balances is expected to grow over coming months, according to a survey by BDRC on behalf of ABN AMRO's Working Capital group. According to the research, 66% of corporate treasurers already concentrate cash balances with a single bank, while seven out of 10 treasurers are interested in using multi-bank cash concentration services. The research noted that Europe-wide centralisation of cash balances is now accepted best practice, with 48% of respondents already centralising cash balances across the region.

In another survey released just prior to this one, ABN found that the difficulty of cashflow forecasting and the unpredictability of cash balances is a major challenge for corporate treasurers in managing working capital requirements. While 82% of respondents said cashflows could be predicted with reasonable accuracy up to two to three days ahead, this fell to 72% for a week's horizon, says the group. **www.abnamro.com**. ■

DISCOUNTING FORERUNNER

The invoice finance industry has seen a five-fold increase in turnover during the last decade, according to the Factors & Discounters Association (FDA), with FDA members' client turnover growing from £18.9bn to £117.1bn. In addition, nearly three-quarters of companies chose invoice discounting as opposed to factoring. **www.factors.org.uk**. ■ *bfinance*

EQUIPMENT FINANCE

Demand for commercial equipment finance has increased by 15% over the past year, according to new figures from the Finance & Leasing Association (FLA). Overall, new finance provided to businesses to fund capital investment increased by 8% compared with January 2003 to £1,254m; £816m of which was used to fund new machinery, plant and truck equipment. **www.fla.org.uk**. ■ *bfinance*

LOAN MARKET

Good time to borrow

It is a good time to borrow, according to a report by Lloyds TSB. The bank says, in its review of loan market prospects for 2004, that with bank liquidity currently exceeding demand, conditions are perfect for borrowing. But how long this will last is the central issue for both borrowers and bankers.

Despite the easing of much of the uncertainty over the global economy and equity markets, volumes in the UK loan market have continued to decline for the third year in succession, according to Lloyd's, and the latter part of 2003 has not seen expected growth.

This lack of market dealflow has, to a certain extent, been balanced by ongoing banking consolidation which will continue to impact general market liquidity, says the group, and there is a sense that if transaction volumes increase substantially, then the market may be affected by shortfalls in supply.

However, the underlying trends of the last three years have remained unchanged. Global economic recovery is now underway, but the lack of corporate investment and M&A activity has depressed loan market volumes. This is evident in that European and UK markets show the trend of declining transaction numbers in Europe and the UK and declining volumes in the UK, according to Lloyd's. All of which indicates that it is a good time to borrow, but for how long is unclear. **www.marketplace.lloydstsb.com** ■

ASSET FINANCE

Tax reforms hurt

Reforms of the taxation of asset finance could hit UK corporate investment hard, according to a report published today by the Finance & Leasing Association (FLA). The FLA report examines the economic impact of the government's corporation tax proposals and assesses the Inland Revenue's proposal for the treatment of finance leases.

According to the FLA report, corporation tax proposals would increase the cost of finance leasing, decreasing its use, and excluding temporarily unprofitable, but potentially successful companies (perhaps 15-20 percent of the total at any point in time), from the benefit of capital allowances. Martin Hall, Director General of the FLA, said: "This research demonstrates that any ill-considered changes in the tax treatment of asset finance would do considerable damage to the UK economy, not least to capital investment by SMEs and in infrastructure." **www.fla.org.uk** ■ *bfinance*

FORTHCOMING EVENTS

REGIONAL GROUPS

For more information, contact Anna McGee
amcgee@treasurers.co.uk
020 7213 0719. Or visit our website at
www.treasurers.org/membership/rgoevents.cfm

Midlands Group: Treasury Fraud – Managing the risks.
05 April 2004. Location: Deloitte & Touche, Birmingham

Midlands Group: Economics update from the RBS Chief Economist.
07 June 2004. Location: TBC

Central London Group event: Kim Holdsworth (BAA Treasury) presents on CAPEX Funding.
22nd April 2004. Location: BAA Corporate Offices, 130 Wilton Road, LONDON SW1. Evening starts at 6pm. Limited places available.
To register attendance for the event email
Bansishah99@hotmail.com

SOURCES • • **The News section was compiled by Denise Bedell • Press releases should be addressed to mhenigan@treasurers.co.uk.**