

The world of finance is littered with thousands of acronyms but what do they actually mean? It pays for treasurers to be in the know.



Systems analysis

THE SYSTEMS available to treasury departments are so varied these days, there is something for everyone – from the one-person treasury using a single bank, to the multi-national, multi-banked integrated treasury. Treasurers and their suppliers love acronyms, some of which are familiar and some less so, and the purpose of this article is to act as an introduction to both the familiar and unfamiliar.

The treasury management system (TMS)

Not every treasury can justify the expense and resource requirements of a separate TMS, although the simple alternative of a combination of spreadsheets and word processing is so limited and vulnerable to error and interference, providing no security support, which is important in even the most basic treasury.

The TMS is at the centre of most larger treasury departments. In its basic form, it records and manages all the main treasury transactions with external and internal parties. Activities such as money market (MM) and foreign exchange (FX) transactions are recorded on the TMS when agreed with the bank and a confirmation of the transaction is sent back to the bank. The system will also hold details of counterparty (bank) limits and record outstanding transactions with authorised counterparties to check that the limits are not exceeded, and also give notice when the settlement of a transaction is due.

The TMS will usually collect bank information for cash and liquidity management, and may also generate payment instructions. It will be able to value outstanding transactions against up-to-date market prices, generate a wide range of management reports, offer risk analysis to help with decision-making including value at risk (VAR) calculations. It will usually link with the main company accounting system to avoid having to re-input details of treasury transactions. Other types of functionality include liquidity and debt management, cash forecasting and planning, bank facility details and letters of credit and guarantee.

In the early days of TMS, some firms developed their own systems, but due to the need for frequent updating because of the complexity of new products few such systems still survive. These days, systems are supplied by all kinds of software houses, from the large and multi-functional, to the small and specialist.

The TMS software is frequently operated on a separate server within the company, to which the various users of the system will link. In recent years, an alternative method of operation has been offered by some of the suppliers, whereby the TMS can be retained and operated by the supplier, with the company accessing it remotely – usually through the internet. This is known as an application services provider (ASP) system and it meets the increasing preference of some companies to outsource their systems management. The cost of ASP systems is competitive, but there are still concerns about outsourcing highly sensitive corporate data, possibly to different parts of the world.



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Enterprise resource planning (ERP)

An ERP system generally provides all of the systems software for a company: accounts receivable, accounts payable, general ledger and sometimes human resource (HR) management. The principle is that there is just one key financial system in the entire firm that ensures common systems standards throughout, thereby lowering overall costs. The main problem, however, is that while some ERP systems provide treasury functionality, it is not as well developed as a separate TMS.

ERPs are often different in structure from a standalone TMS, with the treasury functionality spread over the system as a whole, as opposed to being concentrated in one area. There are only a small number of comprehensive ERP systems available – and a smaller number with real ERP treasury capability – while others are little more than a device to input treasury transactions into the accounting system. TMS suppliers are able to provide adequate interfaces with the main ERP systems.

Information systems

The main information systems available for corporate treasury departments are Reuters and Bloomberg. At one time, Reuters had an almost complete monopoly of the provision of a FX and MM information from a range of banks on a single screen, but Bloomberg's introduction of live broadcast information provided welcome competition. Both Bloomberg and Reuters offer market data that, as well as providing the latest information about the various market movements, can be imported into the TMS for valuations and analysis. Both provide news and research, and analytical tools for decision support.

The expensive and inflexible supply contracts from the information providers has always been an issue for companies, but the increased competition has improved the situation. Meanwhile, the internet has proved a good alternative source of inexpensive financial information and immediate market prices, especially for smaller companies.

Electronic funds transfer (EFT)

EFT is the electronic transmission of payment instructions between the company and its bank. Initially, it was just a more secure method of sending payment instructions to a bank, but it is now often used to deliver instructions directly into the various payment systems, such as BACS, Chaps, Target, Chips and FedWire (see Glossary).

Such straight-through processing (STP) means that, for routine payments, there is no bank intervention, so costs are reduced significantly. All of the main banks have provided EFT for the past 20 years and, although the technology has altered, the overall structure has changed very little.

TRUE MEANINGS

In addition to the main acronyms described in the panels, the following relate to the various payment systems

- **The Association for Payment Clearing Services (APACS)** The organisation that is owned by all of the main banks operating in the UK which is responsible for money transmission and payment clearing activities.
- **Bankers Automated Clearing System (BACS)** The UK's low-cost, low-value electronic batch payment system.
- **Clearing House Automated Payment System (Chaps)** The UK RTGS same-day electronic system for individual payments.
- **Real-Time Gross Settlement (RTGS)** A system that processes payments individually and continuously during the day, in real-time.
- **Clearing House Inter-Bank Payment System (Chips)** One of the two major US systems which is provided by the New York Clearing House. Chips is not RTGS, but its members agree net settlement at the end of each day.
- **FedWire** The RTGS payment system provided by the US Federal Reserve Offices.
- **Straight-through processing (STP)** The processing of electronic payments under strict controls so that no manual intervention is required between the authorisation and transmission of a payment and the transfer to the clearing system, to minimise costs. The latest technology has enabled the term to be extended to the entire process, from striking the original transaction right through to settlement. >>>

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■ **Society for Worldwide Interbank Funds Transfer (SWIFT)** The international system owned and used by the international banks to advise each other of payments.

■ **Trans-European Automated Real-Time Gross Settlement (Target)** One of the main RTGS systems for transferring euro payments.

■ **The Treasury Workstation Integration Standards Team (Twist)** is promoted by Shell to encourage integration between the different EFX and TMS systems used by treasurers, so that they can connect with each other.

■ **Value at risk (VAR)** is a technique to measure and manage the risk associated with investment returns. It is used mainly by banks, financial institutions and the larger corporate treasuries.

When EFT was first introduced, there was some concern about the security of payments and vulnerability to hackers. In practice there is little evidence of any successful fraudulent activity and it is generally accepted that EFT is secure. If there is any risk of fraud, it is prior to authorisation of payment at the corporate, or after it has been received by the bank.

The concern about fraud has led to the banks developing tight controls around EFT, including message encryption, compression and sequencing. More recently, web-based EFT systems have been created that use many of the same security techniques. Web-based payment systems have been introduced by many banks for private individuals, but there has been some reluctance on the part of some companies to migrate to this technology because of the large amounts involved in electronic transfer.

Electronic foreign exchange dealing systems (EFX)

Following the general theme of avoiding manual (human) intervention in financial transactions, systems have been developed to automate routine FX sales and purchases. They provide quotes from and transactions with single banks and can also cater for multiple competing banks.

The two systems are different. The single bank systems are aimed at smaller companies that are not obtaining particularly competitive quotations, and typically offer prices in spot, forward FX and occasionally MM deposits and loans. The benefit to the company is that the rates provided are at least the same and are probably more competitive than would be available by speaking to the bank direct. In addition, the confirmation and settlement processes are automated, reducing the risk of error and fraud.

The multiple bank systems confine themselves to FX-based products – spot, forwards, swaps, options aimed at corporates, money managers, hedge funds, central banks and other institutional clients – and deal in much larger amounts than the single bank systems.

Both types of system offer vast amounts of research material. ■

ELECTRONIC BANKING

Electronic banking provides two main types of service: balance and transaction reporting (BTR) and electronic funds transfer (EFT). It also sometimes provides other functions such as creation of simple letters of credit.

BTR does what its name suggests. Most corporates and public organisations need up-to-date information about their banking balances and individual transactions, and BTR is the fastest and most accurate way of receiving that information, although it is not cheap.

In the UK, the clearing banks provide two types of balance information, the cleared or closing balance for the previous day, and the predictive information for the end of the day on which the information is received. The cleared information is accurate and reliable. The predictive information is

only based on the information that the bank has at the time of the report, so is based on:

- The cleared balance;
- cheques that will have cleared and have been credited to the account;
- cheques that have been issued, and will be debited from the account;
- automated debits, such as Bankers Automated Clearing Services (Bacs) payments, direct debits and other standing order payments;
- automated credits, such as direct debits collected from other accounts and Bacs transactions received.

The predictive information does not include:

- Clearing House Automated Payments Service (Chaps) debits or credits,

including foreign exchange (FX) and money market transactions;

- specially cleared cheques, which may be presented at the banking branch where the bank account is located; and
- cash movements taken from or paid into the branch where the account is located.

The predictive information relies on the integrated nature of the UK banking system, which is not repeated in other countries because the breakdown of transactions can be very different – both more or less automated. As a result, while historic BTR information is a fairly standard product throughout the world, predictive information is much more variable and less reliable.