This month's Hotline focuses on two major issues on which the ACT's Technical Committee has its eye.

The most pressing one is IAS 39, where corporates are urged to let the IASB know directly, as well as through the ACT, of their strength of feeling over the effects of the Exposure Draft as it stands – see p11, opposite.

As you can see from the column on the right, the other major issue is the FSA's reforms of the Listing Regime. As ever, your feedback is welcome at *technical@treasurers.co.uk*. ■

BOND MARKET

Consultation on standards

In early October a group of 25 major investors published a consultation document, *Improving standards in the sterling and European fixed Income credit markets*, and specifically seeking views from the ACT and the Euro-Associations of Corporate Treasurers (EACT). The Technical Committee has set up a working group in order to submit a response by mid-December – if you want to make an input to the ACT comments or see the draft, please email technical@treasurers.co.uk.

The document encourages bondholders and issuers to develop an ongoing dialogue and relationship.

As reported in the November edition (*Hotline*, p11), the document lists a number of market and documentation practices which it wishes to change. No doubt the market will resolve these issues differently according to supply and demand. The proposals, relating to credit rating, types of subordination, disposals, and event risk (such as following the acquisition of the issuer) would, for affected issuers, change the nature of the Euro-markets.

For example the investors are looking for standard minimum covenants such as an investor right to repayment on a change of control and rating downgrade, and a negative pledge that restricts a group from permitting more than 20% of its group indebtedness from ranking ahead of its senior unsecured debt. ■

The consultation document (and the ACT response when issued) can be found on the ACT's website. If you or your company are commenting separately, and you are willing to let the ACT see your comments, please let us know at technical@treasurers.co.uk.

UK LISTINGS REGIME

Consultations on FSA reform

The FSA has published a consultation paper containing wide-ranging and radical proposals for reforming the Listing Regime for equity, debt and financial products.

The review aims 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. Its implications cross the boundaries into the legal, company secretarial, and financial accounting disciplines, but also impinge on the treasurer's capital raising process in the debt and equity markets.

The timetable for eventual implementation runs through to summer 2005, but to achieve this the FSA is seeking responses by 31 January 2004. The Technical Committee will be making a submission and, as usual, views from members are being sought to feed into this. Please send any comments to technical@treasurers.co.uk. If your company is itself submitting a response and you are able to share this with the ACT, this would be appreciated.

The key areas for change are:

- To introduce a set of high level Listing Principles which will inform the making and understanding of the rules and be enforceable like other rules.
- To restructure the listing sourcebook so that it is consistent in format and style with the rest of the FSA Handbook, and to re-organise it into the categories of Equity, Debt and Financial Products.
- To consult on the importance of retaining super-equivalent (meaning requiring higher standards than are required by European legislation) eligibility requirements for equity issuers such as a three-year 'track record' and a 'clean' working capital statement.
- To consult on retaining super-equivalent eligibility requirements in relation to debt issues, including the requirement for an authorised adviser.
- To require overseas issuers with a primary listing to conform to the same standards as UK issuers. Secondary listed issuers would be required to comply with the standards set by the EU's Financial Services Action Plan Directives.

Non-UK EU issuers would be able to obtain a secondary listing in the UK based on a prospectus approved by another EU competent authority (provided they also satisfy Consolidated Admissions and Reporting Directive requirements for listing). Alternatively, a non-UK EU issuer could opt for a primary listing in the UK, but would be expected to satisfy the same standards as UK issuers.

- To recommend that all listed issuers comply with the Operating and Financial Review (OFR) regulations, so that listed issuers are at the forefront of good market practice in this area.
- To retain our super-equivalent continuing obligations requirements on UK companies, such as our class test regime (subject to minor amendments) requiring equity issuers to obtain shareholder approval for major transactions.
- To introduce a new requirement for companies to obtain shareholder approval where an issuer intends to delist.
- To streamline the Model Code once the Market Abuse Directive (MAD) implementation measures have been finalised to reduce duplication.
- To implement a more flexible approach to the presentation of financial information, so that companies may include both audited and non-audited figures, provided they disclose the source of information. It is also proposed to remove the requirements for prospective financial information such as profit forecasts to be 'reported on', except where such information is contained in a prospectus.
- To consult on the options of either retaining the obligation to have a sponsor for new issues and major transactions or abolishing the mandatory requirement to have a sponsor in these circumstances and leaving issuers the choice of whether or not to retain a sponsor. The FSA intend to clarify the regime (whether compulsory or voluntary) and strengthen enforcement against those that fall short of the required standards. ■

The full text of the paper can be found on ***www.fsa.gov.uk/pubs/cp/cp203****.*

It is worth noting that at this stage the consultation paper is seeking views on Policy. The proposals for detailed changes will not be presented until 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.

As usual if you or your company are commenting directly to the FSA, we would appreciate seeing a copy. ***(technical@treasurers.co.uk)***

ACCOUNTING STANDARDS

IAS 39: Last chance for corporates

If your company has not yet started planning for IAS 32-39 to come into effect for 2005 you are leaving it very late, and as yet there are rough edges to IAS 39 which unless removed will have serious consequences for non-financial corporates.

The numbers of emails, letters and meetings reached a frantic level at the time of writing as organisations representative of corporates in the UK and Europe co-ordinated their feedback to the IASB in time for the mid-November deadline for comments on the Exposure Draft (ED) covering amendments to IAS 39 on fair value accounting for a portfolio hedge of interest rate risk. The ACT, and EACT, which groups euro-zone treasurers' associations, have been prominent in this exercise.

SERIOUS CONCERNS. The opportunity was used to reiterate the Associations' support for IAS 39 generally, but to repeat the serious concerns that we have been expressing to the IASB since the early days of IAS 39.

Our objective remains that normal commercial hedging carried out as standard treasury best practice should not be caught out by the rules and fail to qualify as hedges. We do not wish the accounts to give a misleading picture of routine treasury activity, nor do we wish to see the accounting process introduce excessive administration or costs. Worst of all we would not wish to find that corporates are actually changing their hedging policies to their commercial detriment simply on account of the accounting presentation, or finding work-arounds by 'quaint' transactions with banks or involving non-consolidating special purpose vehicles (SPVs).

The ACT has concentrated on three main points which are all ones where the IASB is proposing to diverge from US GAAP. This will put companies accounting on a European basis at a disadvantage to those operating under FAS 133, either in the range of treasury dealing they are prepared to do or in the excessive administrative and cost burden that they will have to bear in order to be compliant. The specific points made covered:

- treasury centre netting of foreign currency;
- prospective effectiveness testing bands; and
- short cut method for interest rate swaps.

SMALL CHANGES, MAJOR IMPACT. Only small changes are needed but they would have a major impact on non-financial corporates. As things currently stand, where a central treasury does internal deals with its subsidiaries and then lays off the net position in the external market, it will run into problems. It will not be allowed to designate the net of its internal contracts as the hedged item. It would need to identify sufficient exposures in each of its various subsidiaries and designate each of those exposures on a one to one basis with its external contract, up to the amount of its external contract. The balance of the subsidiary exposures will not qualify for hedge accounting at the consolidated level.

The ACT has been arguing that this prohibition must be deleted so as to cater for perfectly normal and proper treasury activity, and that this commercial activity should not be discouraged by the accounting treatment. The danger is that either the accounts will not fairly show the FX activity as hedging or alternatively groups will have to start dealing gross, on an entity by entity basis with all the administrative, cost and control implications that this could have. In the extreme case the use of unconsolidated SPV's may become compelling, which is surely a retrograde step.

There are two further points where relatively small drafting changes are being sought but which would make the implementation of the standard massively easier and its effect more representative.

When testing effectiveness on a prospective basis, IAS 39 requires the outcome to be "highly effective" without specifying the bands, whereas on a retrospective basis it applies the 80% to 125% bands familiar from FAS 133. Given the use of the words "almost full offset" for the prospective test, the worry is that interpretation of highly effective will be set nearer 95% to 105% which for some hedges, for example in the commodity field, will be impossible to meet. At their July Board meeting the IASB agreed to change to the 80% to 125% band for the prospective test, but this decisions was reversed at the October Board.

The final point is to seek an extension of the short cut method to hedging with interest rate swaps. The concept is allowed under US GAAP and means that no periodic effectiveness testing is required where the hedge and the hedged item meet certain conditions designed to demonstrate that they are perfectly matched and that there is no chance of any real ineffectiveness.

The ED was proposing very welcome changes to make macro hedging of interest rates of a portfolio more workable in practice. Most crucially the amendments provide that "in a fair value hedge of the interest rate exposure of a portfolio of financial assets and /or financial liabilities, the portion hedged may be designated in terms of an amount of currency rather than as individual assets or liabilities". The hedge will be subject to effectiveness testing as normal.

The ED has been used as a chance to bring together the three related remaining key points which have all been made to the IASB on previous occasions. The drafting changes needed would be relatively minor and could be incorporated without the need for a further ED, but the benefits in practical terms would be immense. While the IASB does not enter into dialogue it has been prepared to hold meetings and to give us a hearing. The ED indicates that it has been prepared to react to external pressure but at the time of writing it is unclear whether the latest round of inputs will result in the developments non-financial corporates need.

NOT TOO LATE. Even by the time of publication in December it should still be possible for readers to show the strength of feeling from corporates by writing to urge the IASB to move to a more user friendly standard prior to IAS 39 becoming cast in stone next March in time for the 2005 EU adoption of IAS.

If you do write to the ASB, please could you copy your comments to the ACT – technical@treasurers.co.uk. ■

Full details of our submissions are available at ***www.treasurers.org/technical/papers***

CORPORATION TAX

Response on reform

The ACT has made a limited response to the Inland Revenue consultation paper on Corporation tax reform, confining our comments to hedging gains and losses and leasing. Our concerns have been to ensure that non financial-sector corporates are not taxed by reference to short-term movements in the values of financial derivatives which are held for the long term as part of a genuine commercial hedging policy. The fear is that this could become a more significant issue because of the need to fair value derivative contracts and the very restricted definition of hedge accounting in IAS 39.

HM Treasury is considering changing the way capital allowances for leased items are dealt with. We believe the incentive to invest provided by capital allowances should be available to companies with no taxable profits. Leasing structures are able to achieve this and that to remove this ability would be a retrograde step. ■

See ***www.treasurers.org/technical/index.cfm*** *for the full HM Treasury paper and ACT response.*

TREASURY SHARES

Loose ends

The new laws allowing the purchase and sale of one's own shares came into force on 1 December 2003, but several loose ends are still being tied up. The ACT has replied to HM Treasury consultation on proposed changes to the Regulated Activities Order, indicating its support, not least to the new exclusion that would ensure that if a corporate engages in frequent transactions, it will not be treated as carrying out a regulated activity that would require FSA consent or the use of an authorised person. See **www.treasurers.org/technical/index.cfm** for our response.

UITF Abstract 37 confirms the ASB's accounting treatment. This requires a company's holdings of its own shares to be accounted for as a deduction in arriving at shareholders' funds, rather than to be recorded as assets. Purchases and sales of own shares should be shown as changes in shareholders' funds. Profits or losses should not be recognised in respect of dealings in a company's own shares. The Abstract applies for accounting periods ending on or after 23 December 2003. ■

IN BRIEF

- **Bolero.net** will be now be integrated with JPMorgan Treasury Services' global trade supply chain solution, TradeDoc. Through this, international trade clients can prepare and transmit secure, authenticated trade documents. **www.bolero.net www.jpmorgan.com/ts**

- **Coface UK** is to offer a factoring service beginning in 2004. The service will be made available through a Coface subsidiary, London Bridge Finance. **www.cofaceuk.com.** *bfinance*

- **Deutsche Bank Global Cash Management** has launched Multi-Option Investment Sweep, a corporate US dollar investment sweep mechanism for partial pooling of subsidiary assets within a pooling arrangement. Corporate clients can use various overnight investment sweep options and allocate funds from a subsidiary participating in a cash pooling arrangement into separate investments outside the pool. The group has also launched its db-cheque service in Europe, for outsourced management of corporate cheque dispatch and payment processes. **www.db.com**

REVENUE RECOGNITION

New rules

The ASB has issued new requirements on revenue recognition, in the form of an Application Note to FRS 5 *Reporting the Substance of Transactions*. Given the importance of the revenue line as a key indicator of a company's performance, and recent reports of questionable practices, there was a need for this standard, which will be consistent with international standard IAS 18.

The Application Note sets out the basic principles of revenue recognition, and specifically addresses five types of arrangement which give rise to turnover and have been subject to differing interpretations in practice:

- long-term contractual performance;
- separation and linking of contractual arrangements;
- bill and hold arrangements;
- sales with right of return; and
- presentation of turnover as principal or as agent.

www.fsa.gov.uk ■

FSA GUIDELINES

Conflicts of interest

The Financial Services Authority (FSA) has released a paper outlining standards to increase analyst independence and avoid conflict of interest issues with other operating businesses.

Under the proposed policies, regulated firms who publish research would be required to publish a policy explaining how they manage conflicts of interests in their business. Without this in place, firms would not be allowed to suggest that they were producing objective, unconflicted research.

The policy, according to the FSA, would apply to all research on designated investments, including shares, fixed income and derivatives. In addition, senior managers of regulated firms would be responsible for developing and implementing appropriate conflict management policies. These management policies would be subject to certain core standards outlined by the FSA. The standards would also outline and limit the situations in which firms can deal ahead of publishing investment research.

www.fsa.gov.uk ■

IN BRIEF

- **EBS**'s Prime Broker service is now live with a number of counterparties. The service should help drive down FX costs for corporates and improve pricing across the market by giving FX banks with limited counterparty credit the ability to trade on better EBS spot prices using the credit of an EBS Prime Broker Bank. **www.ebs.com/products/primebroker**

- Real-time matching and messaging will now be available to **FXall** asset management clients through its Settlement Center. The service is designed for asset managers planning to use the CLS third-party setttlement services. **www.fxall.com**

- **Integrity Treasury Solutions** has launched integra-T cash plus, a turnkey solution offering full cash management functionality and implementation support and services at a guaranteed price to help companies to stream-line their cash processing and control costs. **www.integra-t.com**

- **JPMorgan Treasury** has launched a multi-currency notional pooling service to give customers the option of combining long and short balances in US dollars and euros without the limitations of early cut-off times or the need to perform FX swaps. The group has also announced that it will now offer internet banking services in China and India. JPMorgan received approval for five products: JPMorgan ACCESSSM; Trade Information Exchange (TIE); Trade Origination Process (TOP); eServe; and EC Gateway. **www.jpmorgan.com/ts**

- **Nordic Financial Systems** (NFS), the provider of technical and business integration knowledge, has introduced a new upgrade methodology, which will enable multinational corporations to benefit from quicker and more cost effective upgrades to their treasury management systems (TMS). The methodology, developed by NFS, can be applied to any TMS and reduces time and cost issues related to data or script conversion, inherent with projects of this kind. **www.nfs.se**

- **Oracle Treasury** solution has been upgraded with functionality for regulatory compliance and improved visibility. The new version has improved regulatory compliance, including additional validation levels for payment processing and more pre-configured business roles to help enforce common separation of duties, says the group. **www.oracle.com**

CREDIT RATINGS

Treasury effect on ratings

Fitch Ratings has issued a report claiming that the treasury management practices of corporates have important implications for their credit ratings and therefore how much they pay for funding. The group looked at companies operating in the power and gas sectors in the US and found that credit issues affecting subsidiaries caused 50% of recent rating actions. The group says internal cash management and money pool criteria can affect these ratings. Corporates with centralised treasuries and therefore centralised funding and cash management could be at a disadvantage, while those with a decentralised treasury, as is common within public utilities, have shared money pools which can crucially reduce a group's costs and outside borrowing levels but, argues the report, still preserve distinction in the credit of the participants for rating purposes.

Sharon Bonelli, Senior Director, Fitch Ratings, says 51% of all US utility rating actions in 2001 were caused by credit issues affecting affiliated companies: "Shared money pools are common for public utilities, while complete centralisation of funding and cash management is common for affiliated groups in other non-regulated industries." **www.fitchratings.com**

ACT NEWS

New faces

The ACT Council elections have taken place. Six candidates stood for four places and the new members of Council are announced on page 60.

TECHNICAL TEAM BOOSTED. Martin O'Donovan (pictured), formerly Group Treasurer of National Grid, has joined the ACT's technical team, and will be working closely with John Grout, Technical Director, the Technical Committee and the various ACT Working Groups. Martin's role will involve contributing to the technical excellence of the ACT's range of activities, including the education programme, publications, events and website; and the ACT's influence on the practice of corporate finance and treasury in corporations and the legal/regulatory and market environments for that practice.

BASEL II

Conflicting views

Ratings firm Moody's Investors Service, in a recent report, has said that new Basel Capital Accord should add more clarity and safety to the industry.

The report says that it is of little consequence if finalising of the Accord is delayed several months, because it is now at the point of no return. The agency said this brings more certainty to the entire process, and outlined what the group sees as the main effects of Basel II – namely a marked improvement to regulatory philosophy and in the framework for risk measurement, management, and controls.

Ratings agency Standard & Poor's, on the other hand, released a conflicting message – in its response to the Basel Committee on Bank Supervision's third consultative paper – voicing its "ongoing concerns" over the potential impact of certain aspects of Basel II.

"While we support Basel II's efforts to improve banks' sensitivity to risk and encourage banks to improve their risk assessment and measurement, changes in the availability of credit arising from incentives created by the accord could have far-reaching effects on bank funding, the continued development of international capital markets, and the global economy," said Barbara Ridpath, Managing Director and Chief Criteria Officer at Standard & Poor's Europe.

The report pointed out inconsistencies in Basel II's calibration of risk – especially regarding lenient approaches to mortgage and consumer lending, and rather severe treatment of securitised debt. **www.moodys.com**. **www.standardandpoors.com**

IN BRIEF

Raft International will partner with SunGard to offer an operational risk management solution combining project delivery methodology through SunGard's EnFORM Consulting unit with Raft's Radar software for qualitative and quantitative operational risk measurement, management and control, says the group. **www.raft.dk www.sungard.com**

SimCorp has launched its latest version of the IT/2 corporate treasury management system. The latest release has added functionality for corporates with smaller treasury departments, and has added cash management process and risk scenario analysis functionalities, along with new hedge accounting and internet banking features. **www.simcorp.com**

Standard & Poor's has established the European Corporate Securitisation group to coordinate the group's analytical and rating work for corporate securitisations – described by S&P as hybrid financings (sometimes known as corporate entity or whole business securitisations) that fall between classical securitisations and unsecured straight corporate bonds. **www.standardandpoors.com**

SunGard eProcess Intelligence has upgraded its STeP (straight-through exception processing) platform to integrate intelliMATCH, its automated reconciliation solution. The group says this will create a comprehensive enterprise edition solution for transaction event management. **www.epic.sungard.com**

The programme for **The Treasurers' Conference,** organised by the ACT, has been announced. The conference will run at Celtic Manor from 22-24 March 2004. Visit **www.treasurersconference.com** or see p34 for further details.

ENTERPRISE ACT

Big impact

The Enterprise Act, which took effect a few weeks ago, brings big changes to the UK's bank-friendly insolvency procedure. The goal of the legislation is to create a corporate rescue culture, helping companies to manage the insolvency process and come out intact, rather than split into small pieces during the hostile receivership process now in place.

Under the new legislation, which is also intended to deliver better returns for creditors, banks will no longer be able to appoint a receiver to act in their interests, and will no longer retain the favoured status they once held. The interest of all creditors – including banks and bondholders – will be considered by the administrator that manages the insolvency. The only exception will be that of LBO creditors, in which case the banks will maintain their senior status. The legislation is much closer to that seen in the US under Chapter 11 reorganisation proceedings. **www.hmso.gov.uk**

PERCENTAGES

FULL DISCLOSURE
According to new research by the Risk Advisory Group, one in four mergers and acquisition transactions collapse or are modified significantly after due diligence has been conducted, highlighting the need for integrity and full disclosure during the deal-making process. The study showed companies pull out of one in ten mergers or acquisitions (10.3%) as a result of information uncovered during background checks on the other party. Risk Advisory Group looked at more than 250 such investigations conducted over the last 12 months. **www.riskadvisory.net**

NEW TREASURY ROLE
According to a new survey of senior financial executives conducted by the US Association for Financial Professionals (AFP), heightened levels of scrutiny in the area of financial accounting are creating broader roles for corporate treasury professionals in the areas of SEC compliance and strategic financial planning. In the wake of Sarbanes-Oxley, the corporate treasury department is being asked to play a far more strategic role in the corporation, moving beyond its traditional responsibilities of bank relationships and cash management. **www.afponline.org**

SURPRISE
Firm Watson Wyatt says share options could have unintended effects on remuneration. The group has released new research on share options identifying anomalies in the approach of the UK Accounting Standards Board (ASB) and the International Accounting Standards Board (IASB), which could have surprising results on the design of executive remuneration packages. **www.watsonwyatt.com**

NO SURPRISE
Hedging activity will suffer in the aftermath of hedge accounting compliance, according to a survey conducted jointly by GTNews and JMH Treasury. FAS 133 and IAS 39 are especially problematic, according to respondents, if standards go ahead as they currently exist. **www.gtnews.com www.jmhfs.com**

GETTING INTEGRATED
Asset managers would like fully integrated IT solutions, but few have them, according to research by Trema. Less than 40% of asset managers have fully integrated solutions, despite more than 60% identifying these as desirable according to a global asset management market survey commissioned by the Scandinavian firm. **www.trema.com**

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

South West: Networking Meeting - Case Studies
3 December 2003, 18.30. Venue: BP Plc, Wakefield House, Pipers Way, Swindon, Wiltshire SN3 1RE.

Foreign Multinationals The discreet role of the English Law Trustee
Speaker: Stephen Norton, Law Debenture.
3 December 2003, 18.00 Venue: The Law Debenture Trust Corporation plc, Fifth Floor, 100 Wood Street, London EC2V 7EX (nearest tube station St Paul's)

Midlands
10 December 2003. 18.30.
Venue: Wragge & Co, 55 Colmore Row, Birmingham B3 2AS

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