

Hotline

Welcome to the July/August Hotline. The Association of Corporate Treasurers (ACT) is hosting a half-day update for treasurers focusing on the new UK regime for treasury shares. The event, which is sponsored by Cazenove, is on 17 September 2003 and is open to both members and non-members. For more details, visit the Events area of the ACT website or contact mrahman@treasurers.co.uk. To whet the appetite, Treasury Practice this month includes an article by Peter Elwin on some of the implications for treasurers of the new treasury shares arrangements (p28). If you have any comments on any of the topics covered in Hotline, please contact technical@treasurers.co.uk. ■ *Sheelagh Killen, Technical Editor. skillen@treasurers.co.uk.*

DERIVATIVES ACCOUNTING

ACT continues to lobby on IAS 39

The ACT continues to be concerned about several details of IAS 39 - which are stopping us giving the support we would like to give to the principles and the draft Standard generally. We continue to make representations.

Our principal concern is about the treatment of hedging achieved by netting - where only the net exposure is laid off into the market. This is the main point being raised by many treasury associations in Europe. The presentation by Mark Morris of Rolls Royce at our recent conference in Brighton illustrated some of the major issues which can arise - focused at Rolls Royce on hedging multiple, multi-currency long-term cashflows. Not all companies

are affected, of course, and some have reasonable work arounds, but some are heavily affected and do not have such work arounds.

There are a number of other points on the draft which are being pursued through various channels.

This continued uncertainty is worrying as unless there is strong support for the IASB developing a principles-based approach, there is always the threat of extension of rules-based approaches. Ironically, IAS 39 is one of the most rules-based IAS standards and our issues arise in the detailed "rules", not with the key principles. ■ *Richard Raeburn, ACT Chief Executive; John Grout, Technical Director*

INTERNATIONAL TREASURY

Trading places

On 4 March 2003, the Organisation for Economic and Cultural Development (OECD) published two further discussion papers on the attribution of profits relating to overseas activities from transactions in financial instruments.

These could potentially have a significant effect on sophisticated corporate treasury departments. Sometimes they operate as an in-house bank and with large groups who often have treasury activities in more than one country. Also, it is important that corporate treasurers understand the factors driving the banks and financial institutions with whom they deal so they are in a better negotiating position.

The good news for treasurers who carry out financial transactions overseas is the existence of guidelines that can now be used to help them think through the issues surrounding risk and reward, capital allocation and profit attribution. Treasurers can ensure they adopt a method of profit attribution that does not create any problems under the OECD guidelines.

The bad news for companies is that it is necessary to allocate capital to branches to support the risks the overseas operations assume related to the local functions carried on. This may directly impact some companies' tax positions and will generally put pressure on bank margins which will create pressure on prices.

The OECD papers are discussed in more detail in an article from PricewaterhouseCoopers on the ACT's website at www.treasurers.org. ■



This update was provided for Hotline by Richard Clarke, tax partner at PricewaterhouseCoopers (PWC), and Lisa McGinty AMCT, who is a Manager

at the same firm. Both are members of the PWC Finance & Treasury Network. richard.d.clarke@uk.pwc.com; lisa.mcginty@uk.pwc.com, www.pwcglobal.com

TAXATION

Relationship counselling

The Chartered Institute of Taxation (CIOT) has issued a guidance note to help finance professionals understand the Inland Revenue's approach to the treatment of

loan relationships deemed to be made for unallowable purposes (para. 13 Sch.9 FA 1996).

The Note is based on discussions which the CIOT has conducted with the Inland Revenue and is structured as annotations to the text of the Inland Revenue Corporate Finance Manual. The guidance note is available at www.tax.org.uk (Technical Committee Newsdesk section) and in the June edition of the *Tax Adviser* journal. ■

CORPORATE GOVERNANCE

Fool's gold

The Department of Trade & Industry (DTI) has announced that it will be carrying out a consultative exercise into the issue of executive pay, with particular focus on so-called "golden parachute" severance packages.

The consultative document is entitled *Rewards for Failure* and comes hot on the heels of the controversial shareholder vote at GlaxoSmithKline which recommended that the company look again at arrangements which would reward Chief Executive Jean-Pierre Garnier even if he was asked to leave his position. Whilst recognising that directors' pay is principally a matter for companies and shareholders, the DTI review will consider whether an adequate framework is available for shareholders to influence how business leaders are rewarded.

In addition, the consultation will examine the potential effectiveness of best practice or legislative measures to ensure that executive compensation properly reflects performance.

Trade and Industry Secretary Patricia Hewitt explained the rationale for the review, commenting: "We have no problems with big rewards for big success but shareholders are rightly concerned when directors leave failing companies and walk away with excessive payouts."

The consultation will continue until 30 September 2003. Any treasurer wishing to express a view on this issue should contact Hotline at technical@treasurers.co.uk. www.dti.gov.uk. ■

COMPLIANCE

First principles

The Non-Investment Products (NIPS) Code which governs best practice in London foreign exchange and wholesale money market dealing has been updated.

The changes involve additional requirements in respect of transactions with undisclosed principals and therefore should have limited impact for corporate treasurers. The fund management industry will be most affected. ■

Copies of the revised Code can be downloaded at www.bankofengland.co.uk/markets/nipscode.pdf.

LETTER

ISDA 2002 master agreement

Gary Walker's article (*Master class in ISDA*, May 2003, p17) asks whether a shift to the 2002 Master Agreement is really necessary for a UK end-user of routine derivative products (such as interest swaps in sterling or other major currencies). The point is well made. The new definition of "close-out amount" is an elaborate of the old "loss" method, and more imprecise than the old "market quotation" method which was invariably chosen for routine contracts because of its transparent, objective methodology. The main protection an end-user has with the new definition is that the calculation must be done "in good faith and on a

commercially reasonable basis". In a straightforward case there may be little room for doubt about what the "right" answer is – and treasurers are likely to hear this argument put forward by banks suggesting a switch – but they will also be aware that, just as there can be more than one "true and fair view" of a transaction for accounting purposes, similarly there is scope to have more than one "commercially reasonable" result.

Yours Sincerely

MARK DALEY
Partner, Berwin Leighton

ENTREPRENEURSHIP

Small wonder

The DTI's Small Business Service has launched a new website providing information and practical support which is aimed specifically at small and medium sized firms. The website aims to help smaller firms boost profits, productivity and performance by providing access to 'real-life' documentary video case studies, an extensive resource library and clear self-assessment methodologies. The site can be found at www.connectbestpractice.com. ■

FINANCIAL ACCOUNTING

Coming clean

The Urgent Issues Task Force (UITF) has issued a draft Abstract setting out proposed UK GAAP guidance on accounting for transactions in greenhouse gas emission rights.

As part of initiatives by a number of governments to limit environmentally harmful emissions, schemes are in operation whereby companies accept a cap on their emissions and receive allowances to emit pollutants up to this cap. These emission allowances (which may be obtained either free of charge or for payment) can then be traded on a secondary market. The UK's Emissions Trading Scheme was launched in 2002 and an EU-wide scheme is due to start in 2005.

The consultation document (Information Sheet 61) suggests that emission allowances

would be treated as an asset, with a corresponding liability for those allowances against which emissions are expected to be produced. Where emission allowances are allocated by government at below market value, this would be accounted for as a government grant under SSAP 4. The draft Abstract is closely aligned to the text of equivalent proposals from the International Accounting Standards Board's International Financial Reporting Interpretations Committee which are also under consultation. ■

Copies of the draft Abstract can be downloaded free of charge from the ASB website at www.asb.org.uk/publications/publication417.html.

For comments on Hotline or news, please contact Sheelagh Killen at technical@treasurers.co.uk.

RATINGS

Credibility on credit

The US Securities and Exchange Commission (SEC) has now published its concept release on the role and function of credit rating agencies.

The release, which was published on 4 June 2003, comes in response to a requirement in the Sarbanes-Oxley Act 2002 and follows on from the Interim Report issued earlier this year (see John Grout's article, *Redefining the Credit Rating Role*, March 2003, p17). It seeks comments from market-users on a number of issues including:

- Whether the designation of credit rating agencies in the US as nationally recognised statistical rating organisations (NRSROs) should continue.
- What, if any, alternative approaches could be adopted by the SEC in ensuring that high standards are met by ratings service providers, for

example, in respect of accreditation, oversight, access to rating agency records etc.

- The suitability of internal credit models as an alternative to external rating bandings for computing capital adequacy requirements for US regulated broker-dealers.
- How ratings service providers should deal with potential conflicts of interest.
- Whether anti-competitive practices exist within the credit ratings industry.
- How the transparency of the credit ratings process might be enhanced.

The full text of the concept release can be accessed via the SEC website at www.sec.gov/rules/concept/33-8236.htm or through the link from www.treasurers.org/technical/papers/index.cfm#ratings. Comments are invited by 28 July 2003. The ACT will be preparing a response to the paper and invites all treasury professionals who are interested in contributing a view to contact technical@treasurers.co.uk.

News

EU TAXATION

Measures against harmful competition

A new tax package, just adopted by the European Council (EC), should help tackle harmful tax competition, according to the EC. The tax package includes a Code of Conduct for business taxation and a Council Directive to eliminate withholding taxes on payments of interest and royalties made between associated companies of different Member States. The package was agreed by Member States in 1997 to help reduce continuing distortions in the Internal Market, prevent excessive losses of tax revenue and re-structure tax systems in a more employment-friendly direction.

Criteria for identifying potentially harmful measures include: an effective tax level which is significantly lower than the general level of taxation in the country concerned; tax benefits reserved for non-residents; tax incentives for activities which are isolated from the domestic economy and therefore have no impact on the national tax base; granting of tax advantages even in the absence of any real economic activity; instances where the basis of profit determination for companies in a multinational group departs from internationally accepted rules – in particular those approved by the OECD (see Hotline); and lack of transparency. <http://europa.eu.int/>. ■

CASH MANAGEMENT

Insight into global practice

This July sees the launch of the 2003 ACT/JPMorgan Fleming International Cash Management Survey.

The highly-regarded survey, now in its fifth year, seeks to enhance understanding of cash management practice across the globe and allows both treasurers and providers to benchmark their approach to cash and liquidity management. For more information, please refer to the article on p16. ■

In brief...

Alterna Technologies has launched the auros2004 Extended Liquidity Suite (ELS) to provide a single-window view of a company's global cash position. According to Alterna, the latest version offers flexible reporting and the ability to rapidly deploy the auros global bank Connection Library. It also includes configurable and reusable PC transport interfaces with urgent/high value payments and intra-day reporting in 89 countries, says the group. www.alterna.com. ■

The Bank of New York can now process correspondent banks' euro trade transactions through its new euro reimbursement service. The service is delivered through a link to the inter-bank Target funds transfer system from the bank's Frankfurt branch. It was designed to meet the growing importance of euro-denominated trade flows, says the bank, and users will be offered pre-debit notification of reimbursement claims, value-added reporting on euro-denominated transactions and timely transaction execution through a central processing hub. www.bankofny.com. ■

Online treasury and financial information provider **Bobsguide** will now offer a matching service for request for proposals (RFP) or request for information (RFI). Free to members, the service lets entities submit secure requests online, after which it is reviewed by bobsguide.com and then distributed to all applicable software vendors or IT consultants. www.bobsguide.com. ■

City Networks and **Trema** have partnered to offer CityNet Confirmation Matching module through Trema's Finance KIT. The module performs three-way matching of confirmations and manages CLS trades. A standard interface will automate a two-way connection between the two systems to better enable straight-through-processing of trades. www.citynetworks.com. www.trema.com. ■

The Clearing House, part of the Chicago Mercantile Exchange, and **The Chicago Clearing House Association** have signed a letter of intent to merge. The merger will further the US banking industry's need to rationalise infrastructure and for clearing houses and check exchanges to adopt common rules, common settlement, and common governance. www.cme.com/risk_management/clearing_house/index.cfm. www.chgo.org/ccha/mainhome2.htm. ■

Currenex and **XRT** have set up a partnership to integrate systems. XRT clients will now be able to use Currenex's FXtrades service to execute trades online and import deals directly into their treasury management system. www.currenex.com. www.xrt.com. ■

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SHAREHOLDINGS

Court rules against UK's golden shares

In a recent decision, the European Court of Justice has ruled against the Spanish and United Kingdom rules regulating special shares (golden shares), saying the rules are precluded by the principle of free movement of capital. The ruling was made in relation to the arrangements now in place for Repsol, Telefónica, Argentaria, Tabacalera, Endesa and, in the UK, BAA.

In the UK, BAA's Articles of Association create a special share held by the government which empowers it to give consent to certain areas of the company's operations (winding-up, disposal of an airport, and so on), and also prevents the acquisition of more than 15% of the voting shares in the company. But EC Treaty prohibits all restrictions on the movement of capital between member states and between Member States and third countries – which includes investments in the form of participation. Thus the UK rules create restrictions on the movement of capital between member states, said the court. A similar decision was made in relation to existing Spanish rules.

<http://curia.eu.int/en/index.htm>. ■

FINANCIAL SERVICES

Action plan kicks up a gear

The eighth and latest progress report on the EC Financial Services Action Plan (FSAP) has been published by the European Commission. It says that the overall financial outlook strengthens the political case for integrating financial services within the EU, and legislative progress towards creating an integrated market is on the right track. But, according to the report, it is important to complete legislative changes by April 2004 and implement the FSAP by 2005. With the European Parliament elections in June 2004 and enlargement coming soon, these deadlines are crucial. That means a final sustained effort by the Commission, the European Parliament and the Member States' institutions is necessary to reach compromise on the remaining measures, says the report.

http://europa.eu.int/comm/internal_market/en/finances/actionplan/index.htm. ■

Baron Alexandre Lamfalussy who led the team of 'Wise Men' who put forward the FSAP will speak at the ACT's 2003 Annual Dinner. Contact mrahman@treasurers.co.uk for details.

US SETTLEMENT

E-images acceptable

The US House of Representatives has passed legislation that lets banks exchange electronic images of cheques for clearing and settlement purposes. The bill, known as the Check 21 Act, is designed to boost the efficiency of cheque clearing by permitting the optional truncation or removal of the original paper cheque from the settlement process. (See also July/August 2002 edition, p58)

<http://financialservices.house.gov/hearings.asp?formmode=detail&hearing=168>. ■

<< **Fitch Ratings** is launching a new information platform offering details on 1,200 Fitch-rated CP issuers. The information includes authorised programme sizes, securities exemption information, issuer domicile and principle market of funding, says the group, plus real-time ratings, information and research on CP issuers rated by Fitch.

www.fitchratings.com/corporate/index.cfm. ■

IQ Financial Systems has added a Basel II credit risk template within its Loan IQ system to meet the data gathering requirements of Basel II. The group says the new module lets users collect information for internal credit managers, ongoing borrower compliance and regulatory reporting without touching ancillary systems. www.iqfinancial.com. ■

JPMorgan Treasury Services has launched a cross border intra-day cash sweeping service, through which customers can concentrate cash intra-day and thus enhance returns on surplus liquidity. According to the bank, intra-day cash sweeps can be scheduled and completed prior to other important cut-off times, for example those applicable at the concentration account location or those relating to an onward investment opportunity before markets close. In addition, says the bank, clients may no longer need to have large credit lines in place for their concentration accounts in order to support intra-day payments and investments. The service is available on a cross-border basis in Europe and the US for both US Dollars and euro.

www.jpmorgan.com. ■

UK pension funds will soon be able to access corporate governance analysis and electronic voting capabilities both in the UK and 80 other countries under a new service launched by NAPF, the UK pension fund association, and Institutional Shareholder Services (ISS) in the US. The two have formed a new company, Research, Recommendations and Electronic Voting (RREV), which will offer the service to interested pension funds. The service will complement NAPF's existing Voting Issues Service. www.napf.co.uk. www.issproxy.com. ■

After **Peoplesoft** launched a bid for JD Edwards in early June – which was approved by both boards – rival **Oracle** followed up the next week with an unsolicited \$5.1bn bid for Peoplesoft. However consolidation on this scale in the enterprise software sector may face opposition from competition authorities, regardless of the outcome of the bids.

www.oracle.com. www.peoplesoft.com. www.jdedwards.com. ■

SuperDerivatives has launched the latest version of its FX options system, with enhancements such as a new vanilla options section, that allows quick pricing of many vanilla strategies. The system also provides better control in determining the term structures for pricing all kinds of options and easy-to-use features to assist pricing of multi-leg strategies of all option classes, says the group. In addition, the multi-leg pricing page enables corporates to enter their cashflows into the system to check the efficiency of their hedging. www.superderivatives.com. ■

Taxware is now certified to provide tax calculation and compliance functionality for Microsoft Commerce Server 2002. Working with data entered into Commerce Server, the Taxware system analyses a company's global compliance with sale/use tax, GST and VAT regulations. In another development, Taxware has launched a website to help non-EU companies understand EU regulations on the taxation of digital sales, which are scheduled to undergo significant changes this summer. The site includes guidelines to help companies understand the directive and related compliance issues, and outlines solutions they can deploy to comply with the new regulations. www.taxware.com.

www.microsoft.com/commerceserver/. ■

Trema has launched Pricing KIT, its new front office pricing module. The module gives Finance KIT users access to the price of any financial instrument handled by Finance KIT and also enables users to make comparisons of market quotes, according to Trema. It includes flexible screens to display relevant information – such as a pricing window, in which the search field can be plotted against the calculated figure; a strategy window capable of displaying multiple deals at once; and a custom graph window enabling the user to plot entire strategies graphically. www.trema.com. ■

TWIST, the Treasury Workstation Integration Standards Team, has issued the requirements for a complete range of standard XML messages that can automate processing of commercial payments and working capital financing by banks and their clients. According to the group, seven banks – comprising ABN AMRO, Bank of America, Citigroup, Deutsche Bank, HSBC, JPMorgan Chase and Standard Chartered Bank – have worked together with other industry specialists to ensure universal applicability of the requirements. www.twiststandards.org. ■

Wall Street Systems has launched Internet Extensions Hub, a new solution to help banks offer services to their customers online. The system gives banks the ability to brand, customise and extend the functionality of The Wall Street System to their customers, and clients can now obtain rates on a variety of products, including foreign exchange, money markets and fixed-income securities, says the group. It is intended to replace difficult and expensive-to-maintain proprietary bank terminals.

www.wallstreetsystems.com. ■

SECURITISATION

Hybrids come into their own

The scope of 'hybrid' corporate securitisations has broadened across boundaries, time horizons, and asset classes, according to a new report by Standard & Poor's (S&P). The development of hybrid transactions – those that share attributes of both corporate and public finance securitisations – is a European and US phenomenon, says S&P, and it is growing at a fast rate.

In a typical securitisation, the assets are legally separated from the originator (whether a corporate or public body). Under hybrids, the transaction transcends legal boundaries, posing interesting challenges for the originator and agency rating the deal. From a ratings standpoint, S&P assesses the underlying business risks along

with the financial risks, so that any significant improvement or deterioration in the business may lead to a rating change.

"There is keen interest in various countries to securitise telecommunications, shipping, hospitality, and intellectual property assets, among others," notes Elena Folkerts-Landau, director at S&P's Structured Finance Ratings group in London.

The assets of pubs remain dominant in UK corporate securitisations, with more than £4bn of rated pub ABS outstanding. According to Elena Folkerts-Landau, key credit characteristics fuelling debt issuance include stable investor demand, steady cash flow generation, and the strength of property values. Other operating assets that have been securitised in the UK include healthcare, water utilities, ferry and rail services, motorway hospitality, telecoms, sports and entertainment, and even funeral services. www2.standardandpoors.com.

■ *bfinance*

COMMERCIAL PAPER

Corporates shying away

The supply of commercial paper from corporates is still slow, according to a report by Standard & Poor's (S&P). Although the supply environment for commercial paper issuance by non-financial corporates has improved, no immediate revival is anticipated, says S&P.

Since 2000, there has been a steep decline, particularly for US firms, driven both by investor risk aversion combined with reduced business demand for short-term financing. But there is hope for a slowdown in the rate of CP decline, according to S&P's Head of Fixed Income Research, Diane Vazza. "A continued decline in commercial paper outstandings is unlikely, given that businesses will have to maintain a minimum level of working capital necessary for current operations," she said. www2.standardandpoors.com. ■ *bfinance*

PENSIONS

Deficits do not mean downgrade

Moody's Investor Services has moved to calm the nerves of UK corporates with large pension fund deficits by announcing that it does not envisage downgrading many ratings "based solely on underfunded pension-related issues". In a report, Moody's acknowledges that while underfunded pension liabilities continue to influence the rating agency's credit analysis of corporate sponsors, there is to be no major revision to Moody's current methodology. However, the rating agency has updated its view on how accounting standards FRS 17 and IAS 19 can present corporates with a fresh set of problems when valuing their pension funds.

Neale Marvin, analyst and author of the report, suggests that should equity markets continue to decline, causing further deterioration in defined benefit pension fund assets, the cashflows and balance sheets of the schemes' corporate sponsors "could come under significant pressure, reducing financial flexibility and weakening credit profiles, which may lead to future downgrades."

www.moodyseurope.com/. ■ *bfinance*

INVESTMENT GRADE ISSUANCE

Borrowing levels up

New issue volume by investment grade-rated issuers has picked up momentum in Europe, bolstered by record low interest rates, and declining investor risk aversion, according to a Standard & Poor's report. Expectations of weak growth and continued low inflation have sent benchmark yields tumbling, causing investors to seek out higher yielding securities, said the report. The ensuing tightening of corporate bond spreads is beneficial for issuers that are looking to refinance debt and lengthen maturities. www2.standardandpoors.com.

■ *bfinance*

FORTHCOMING EVENTS

REGIONAL GROUPS

3 September 2003, 18.30

South West – Managing Risk, Joint meeting with AIRMIC

Royal Bank of Scotland Account Management Centre, 740 Waterside Drive, Aztec West, Bristol

3 December 2003

South West – Networking meeting – Case Studies

We will be asking members to share their experiences. Volunteers wanted to focus on the challenges of introducing Treasury IT systems, dealing online etc. Venue TBA

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

CONFERENCES

17 September 2003

Treasury Shares for UK Companies – A new dynamic in managing capital structure. Half-day Briefing Cazenove's, 20 Moorgate, London

25 September 2003

The 5th Annual ACT/AIRMIC Conference – Key issues concerning treasurers and risk managers in difficult markets

The Royal College of Physicians, London

23 October 2003

2003 Pensions Conference – the evolving challenge of pension schemes

Cavendish Conference Centre, London


12 November 2003

The ACT Annual Dinner

The Grosvenor House Hotel, Park Lane, London W1

For further information contact mrahman@treasurers.co.uk or see our website: www.treasurers.org/events/index.cfm

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