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Policy matters

Treasurers need to have plans in place to help them to manage financial risk on behalf of the board. Sarah Boyce explains

The ultimate responsibility for risk management within an organisation lies with the board of directors. Due to the practicalities involved in managing risk, the board typically delegates the daily management of risk to responsible individuals in each department. In the case of financial risks, many of these are delegated to the treasurer.

Treasury policies are the mechanisms by which the board, or risk management committee (RMC), can delegate financial decisions in a controlled manner. This article recaps the key considerations when establishing treasury policy.

Let us start with a recap of the typical division of responsibilities between the board of directors and the treasury team.

Board or RMC	Treasury
Decides the level of risk that the organisation is willing to accept (for example, target borrowing levels)	Makes recommendations to the board regarding the limits to be applied to various risks
Monitors high-level risk measures	Creates detailed treasury procedures to ensure board policies are followed
Authorises instruments to be used for investment/borrowing/hedging purposes	Manages day-to-day exposures to risk
Approves major financing decisions	Ensures the adequacy and effectiveness of internal controls

The typical contents of a treasury policy

Treasury policies govern many different treasury activities. For example:

- bank relationship management policy;
- FX risk policy;
- commodity risk policy;
- debt portfolio management policy;
- compliance (with loan documents) policy;
- interest rate risk policy; and
- surplus cash investment policy.

In all cases, however, a consistent approach should be adopted to developing and adhering to a policy.

A treasury policy should provide a framework for the treasurer to organise treasury activities and ensure compliance. It should make clear:

- What treasury is expected to achieve.
- How success will be measured.
- What decisions are delegated to the treasurer and the circumstances when the treasurer should refer decisions back to the board, or another person or body within the organisation.

Policy name

This should be reasonably descriptive of the policy and clearly identify it.

Policy objective

The objective should clearly define what treasury is expected to achieve.

For example, in a surplus cash investment policy, the policy objective will detail:

- Which risks should be managed, for example, the risk of default by a bank or other counterparty where funds have been deposited.
- The extent to which risk may be taken, reflecting the company's own attitude to risk, for example, the maximum amount and tenor of any deposit with a particular counterparty.

Remember that certain risks will be beyond the control of the treasurer (for example, interest expense is a product of market rates, which the treasurer cannot affect), while others are clearly within their control (for example, not breaching counterparty limits).

Responsibility

A policy should set out clearly which decisions are delegated to the treasurer and the circumstances when the treasurer should refer a decision back to the board or other person within the organisation.

Procedures

Procedures and controls to manage the risk should be put in place to provide an overall framework for decision-making by the treasury team.

Assessment of success (risk measurement)

This section of the policy should set out how both the risk, and the management of the risk, should be measured.

This is achieved by the use of techniques such as key performance indicators or benchmarking.

Reporting

Treasury is normally responsible for monitoring and reporting performance against treasury policy. Performance is monitored against the targets and benchmarks set out in the policy document.

Implement and review policy

The treasurer is responsible for the day-to-day operation of the treasury function within the agreed limits and policy guidelines. It is also responsible for reporting performance and exposures to risk to the board or RMC.

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