ICAEW FINANCE & MANAGEMENT FACULTY

ISSUE 216
DECEMBER
2013

icaew.com/fmfac

FINANCE & MANAGEMENT

THERE'S A LONG WAY TO GO BEFORE THE AFTERMATH OF THE FINANCIAL CRISIS HAS CLEARED PAGE 14

How hospitable
Monitoring client wining and dining

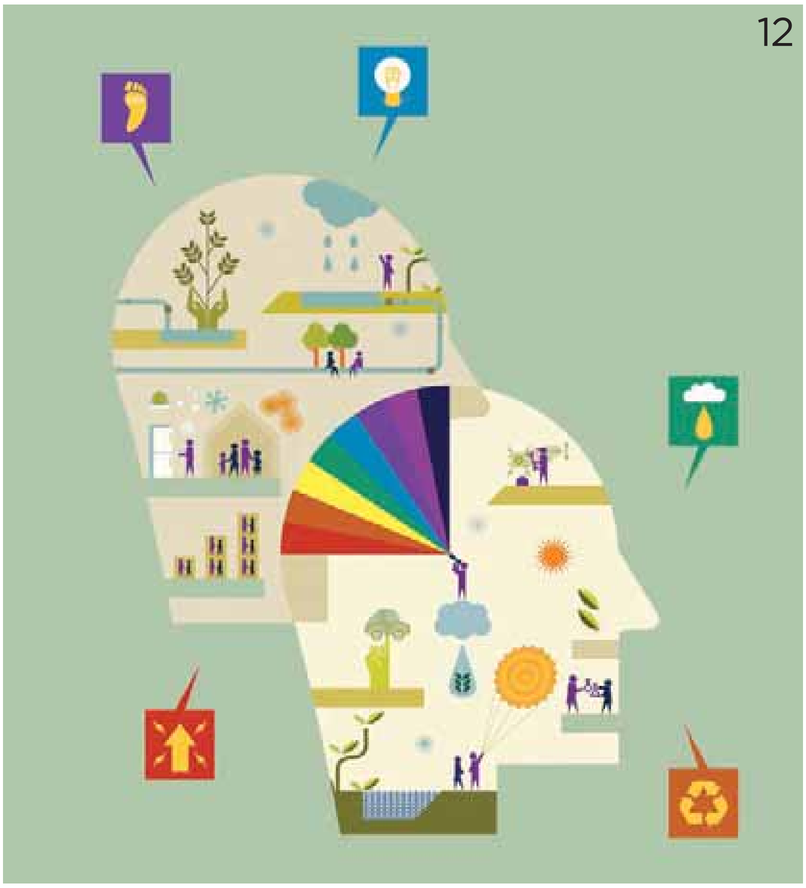
Rise and fall
How CFOs can ensure their company survives after a recession

Get in, get on
The way to boost project success with external consultants

Healing the rift
The role a board can play in resolving conflicts

Contents

Issue 216
December 2013


12


20

"We have a big opportunity in business to be more open about conflict and to put more effort into improving how we manage it"

Patrick Dunne on workplace conflict and how teams can work together to resolve it 16

COVER: TANG YAU HOONG

Measuring growth

FINANCE & MANAGEMENT FACULTY

Companies and organisations show growth through their profits or turnover, and this usually allows for direct benchmarking to ascertain performance.

Countries, however, have much more complex ways to benchmark themselves against others. Gross Domestic Product (GDP) is universally accepted as a good measure of a country's economic performance, and these figures are quoted, revised and restated multiple times. GDP figures generally take a month to calculate, and then another month or two to finalise.

The publication of earnings, exports, construction and employment data on an almost weekly basis and the apparent indication that one might prove growth and another might prove contraction is unusual for such an important gauge. It is however, valid.

Measures of GDP are necessarily complex and all of this data is used under different measures of GDP; there are three different accepted systems for measuring it under the United Nations System of National Accounts 1993 (SNA93). This is why each piece of economic news is grabbed with such gusto by news journalists and there is much speculation as to what the current quarter's GDP figure might be.

The Office for National Statistics uses all three measures and then follows a process of "balancing" to arrive at a final figure. The use of all three measures accounts for the importance of production and service output, consumer spending and earnings growth as each one of these comprises the basis for one of the measures of GDP.

These three are, theoretically at least, equal measures of growth:

- The production approach, GDP(P), is the sum of all activity in an economy. This is output + taxes on products - subsidies on products - intermediate consumption.
- The expenditure approach, GDP(E), looks at final consumption spending of households, government and non-profit suppliers of households + exports - imports.
- The income approach, GDP(I), looks at employee and self-employed gross income + profits + rent + taxes on production and products - subsidies on production and products.

We at the faculty are keen to ensure that our members see value in membership and are offering an early Christmas present to our members - from February 2014, all evening events will be free of charge in 2014. We'll also hold a webinar every month to keep you up to date with your CPD.

We hope that you enjoy this month's magazine. Please email us with your thoughts and contributions - stephen.ibbotson@icaew.com or robert.russell@icaew.com

Robert Russell
Technical Manager

THE TEAM

Stephen Ibbotson
Head of Faculty
stephen.ibbotson@icaew.com

Robert Russell
Technical manager
+44 (0)20 7920 8417
robert.russell@icaew.com

Rick Payne
Finance direction programme
+44 (0)20 7920 8451
rick.payne@icaew.com

Caroline Wigham
Services manager
+44 (0)20 7920 8508
caroline.wigham@icaew.com

Christian Doherty
Commissioning editor
christiandoherty@mac.com

SUBSCRIPTIONS
Annual membership of the Finance & Management Faculty costs from £90 a year. For more information and to join see icaew.com/fmjoin

FACULTY EVENTS
Events are listed within this publication; details can be found at tinyurl.com/fmfaculty or contact the events line on +44 (0)1908 248 159.

FINANCE & MANAGEMENT FACULTY
Chartered Accountants' Hall
Moorgate Place, London, EC2R 6EA
+44 (0)20 7920 8508
@icaew_finman
fmfac@icaew.com
icaew.com/fmfac

ISSN 1471-1818 TECPLM11839

Printed in the UK by Sterling Solutions


Microsoft
Marketing
Celso Guiotoko
Chief Information Officer
Nissan
NISSAN
Dealer Network
Microsoft Dynamics
Customer
Care
Three teams, one unified CRM, happier drivers.
When Nissan wanted to increase customer satisfaction at every stage of the ownership cycle, they chose Microsoft Dynamics CRM. Now, their teams work together seamlessly with one unified view across applications. So it's never been easier for them to anticipate drivers' needs, close sales, resolve issues and, ultimately, make customers happy.
Microsoft
Dynamics
crm.dynamics.com

Events

WEBINAR: SME TAX UPDATE AND PLANNING

Wednesday 19 February 2014
10:00 – 11:00
Free for faculty members

Anita Monteith and Sue Moore, technical managers at ICAEW Tax Faculty, consider some of the tax changes in recent years that have affected SMEs. They will consider where these have provided opportunities for planning and how these have had a practical impact on those running their own business.
Visit ***icaew.com/fmffebwebinar*** to register

WEBINAR: FALLING FOUL OF EMPLOYMENT LAW: 10 TIPS TO CONTAIN THE RISK AND COST

Tuesday 11 March 2014
10:00 – 11:00
Free for faculty members

Clare Murray of CM Murray Solicitors runs through her 10 tips to reduce the risk of falling foul of employment law and will provide a general update. This session will be geared towards FDs, CFOs and those operating their own businesses, and will be of use to anyone dealing with employees or with responsibility for HR. We will cover:

- restructuring;
- tribunal rule changes; and
- HR policies.

Visit ***icaew.com/fmfmarwebinar*** to register

All webinars are free for Finance & Management faculty members and charged from £25 plus VAT for non-members. All webinars are held at 10am unless otherwise stated.

VISIONS OF THE FUTURE – GLOBAL ECONOMIC TRENDS FOR 2040

Tuesday 28 January 2014
18:00 – 20:00
Free for faculty members

Tracey Keys, director of Strategy Dynamics Global SA, and ICAEW's own Nigel Hastilow, provide their forecasts of global economic trends that we might be seeing over the next 30 years.

With global population growth exceeding wealth creation, increasing polarisation of wealth, and natural resources under greater pressure, finance and commerce may look radically different in 2040.
icaew.com/fmfjanevent to register

WE'VE LISTENED TO YOU!

All faculty evening events will be free for members in 2014

FEEDBACK FROM OUR MEMBERS

WEBINAR 3 OCTOBER:
MAXIMISING THE POTENTIAL OF THE BOARD

"Great – let's have more of them [webinars]!"
Amin Somji

"It was the first time I'd attended a webinar, and found it a good way to listen to a very useful presentation"
Barry van Eupen

"This is a great service for members, and I encourage the faculty to continue with them"
Nicholas Dunhill

"Very easy to use – wish other providers of webinars were as good"
Richard Curtis

All events are free to Finance & Management faculty members and charged from £46 plus VAT for non-members. Events are held at Chartered Accountants' Hall, Moorgate, London, unless otherwise stated.

News

COMMUTER HELL EASES

COMMUTING TIME IN MINUTES		
REGION	**MEN**	**WOMEN**
London	77.2	72.8
Eastern	65.2	47.6
South East	62.8	45.8
Scotland	58.6	46.8
West Midlands	54.4	43.2
South West	53.4	41.2
Northern Ireland	52.2	42.8
North West	52.0	44.2
Yorkshire and Humberside	51.4	42.6
East Midlands	49.2	43.0
North East	46.4	39.6
Wales	44.4	38.6
GB Average	**58.0**	**47.4**

The TUC published its analysis of the UK Data Service's annual *Labour Force Survey*. They found that commuting times have fallen marginally overall since 2006, although some regions experienced increases in commuting times. See the report at ***bit.ly/1bGVCiO***

GB AVERAGE COMMUTING TIME...

MEN 58 MINUTES

WOMEN 47.4 MINUTES

ENERGY COSTS A PRETTY PENNY

The International Energy Agency has published its 2013 Key World Energy Statistics. This document contains a huge amount of data on usage, source, consumption and price of energy use across the world (US dollars per megawatt hour of energy).

ENERGY PRICE IN USD/MWH 2012 G7*

Domestic Gas	
Canada	34.36
USA	35.22
UK	73.65
France	83.76
Ireland	86.75
Germany	90.32
New Zealand	108.72

NB. Italy and Japan data unavailable

Domestic Electricity	
USA	118.83
France	174.77
UK	220.74
New Zealand	231.76
Ireland	270.32
Japan	276.76
Italy	288.40
Germany	338.75

NB. Canada data unavailable

DOMAIN NAME DELIGHT

Nominet, the UK internet registry, is allowing those with ".co.uk", ".org.uk", etc., web address domains to abbreviate this to ".uk" from summer 2014. They will reserve the ".uk" domain suffix for five years for those already holding the ".co.uk" or similar address. After this period, the ".uk" names will be made available for general sale.

.UK

RETAIL – UP...

Asda announced last month that it was piloting delivery of 'click and collect' orders to London tube stations for commuters to pick up on their way home. Orders placed before noon can be picked up after 4pm from a van waiting near the tube exit. Asda and Transport for London are piloting the concept at six suburban tube stations to measure demand, and hope to roll it out to other stations in London and the South East over the coming months.

...AND DOWN

Tie Rack's Italian owners, Fingen Group, announced last month the closure of most of its remaining 44 UK stores. Negotiations are ongoing with GIP (Gatwick's majority shareholder) to keep the Gatwick Airport store open.

EY CASTS INFLUENCE EASTWARDS

EY is the second of the "Big Four" accountancy firms to open offices in Canary Wharf in East London. The firm is taking 200,000 square feet of space in Canary Wharf to house 4,000 staff, but confirmed that they will be retaining their existing offices at London Bridge.

Hospitable me

Entertaining clients can be essential to sealing the deal, but it's a marketing expense that must be monitored and justified. **Martin Finn** asks how best to wine and dine on account

GETTY

For many FDs, the question of whether customer hospitality is a justifiable marketing expense is a perennial one. Finance may be asked to consider under what circumstances is it sensible, reasonable and cost effective to take a few customers to a major sporting event or a holiday in an exotic location? Or is it the case that this expense is simply largesse without justification? Even for those whose budgets are not under pressure, these questions should not be ignored.

For those in finance, all marketing expenses are part of the operating costs associated with sales. One definition is 'The expenses incurred to sell (eg, advertising, salesperson commission) or distribute (eg, deliver) merchandise'.

Therefore, to the finance function, all sales costs (including the cost of the sales team) and distribution costs are part of the marketing costs. This is helpful to finance but less helpful to budget holders when marketing budgets are being determined, given

the difference between the accounting definition of marketing and the professional definition of a marketing role.

A marketing professional needs to consider all the costs in their marketing plan (in order to concentrate on maximising profits); however a marketing professional is rarely in control of all their costs. Sales and logistics usually have their own lines of management and their own budget, which is fine - indeed, it is a practical solution - but it does cause a problem for marketing budgeting where there are grey areas. Hospitality and entertainment is one of those grey areas. Ask sales and they will tell you it's vital, while marketing might not agree.

WHERE IS HOSPITALITY AND ENTERTAINMENT IN THE MARKETING MIX?

Entertaining clients can play a vital role in the marketing mix for many.

Here's an example: if you were the main buyer of baked products for the largest retailer in the country, there's no doubt you would be invited to attend many hospitality events and would expect to be wined and dined by prospective suppliers. This is a normal part of the business cycle. It allows suppliers to meet and influence potential clients. For buyers it's useful too, as it allows them to get to know their suppliers better and to see them outside the more rigid confines of a business meeting - although within the limits of acceptability, of course.

Hospitality and entertainment can be a marketing tool, but it's not applicable in all industries and all business models.

Therefore, should the costs of hospitality and entertainment - that is, events with high ticket values, days out and foreign trips - be charged back to the marketing budget in a normal company? I say no. The reason is that in a typical large company a big proportion of the hospitality spend is not part of a marketing process, it's part of a sales process, so taking a customer to dinner/theatre/a football match/a foreign trip is not marketing: it is selling. It is done to help along a sales relationship or to close a sale.

But what does it matter to the FD? It's still a cost on the business, moving it from one expenditure code to another is not a saving overall. Well, it does matter. Because part of the costs of selling the entertainment could be correctly attributed not just to sales, but more specifically to a particular salesperson or deal. Therefore a sale that made a profit of £100,000 which was signed at a £5,000 guest box at the Grand Prix actually made £95,000 profit - and this should be reflected in sales reports and commissions paid. Hospitality costs are often directly attributable like this. By taking the cost away from the sales margin you introduce an important feedback loop and an incentive for salespeople to use such costs sparingly and proportionate to the opportunity.

But beware, this does not mean that all hospitality costs are a sales cost. Marketing will use hospitality too. So how do we account for both processes? How do we decide where the cost of a particular expense sits? How do we decide how much each group (sales and marketing) is to spend? And let's not forget that this debate can be heated - it affects sales commissions after all.

WHY DO YOU HAVE HOSPITALITY AND ENTERTAINMENT?

To answer this, it may be useful to take a step back. Why do we have hospitality and entertainment costs at all? Clearly some businesses spend more than others, but why?

Consider if you had a product that was so essential, so good, so well priced and freely available that everyone would want it. You would be in a fantastic position. All you would have to do is tell the world about it and your business would fly. You wouldn't have to spend much on advertising and you would spend nothing on hospitality and entertainment (unless you just felt like celebrating your good fortune).

Alternatively, consider if you sold sliced white bread. Your product and prices are just the same as your competitors, the product is just as easy to make and ship, and your delivery is just as reliable as others. In marketing terms you have no differentiation. So how can you get your product flying off the supermarket shelf? Well, the first issue is getting it onto the supermarket shelf. You'll have to convince the retailers that you were about to create interest and demand for your bread over and above others - and that comes down to packaging and positioning, as well as advertising and promotion (which might include hospitality and entertainment, such as a trade launch party or series of open days).

But let's assume that your packaging and promotion is no more convincing than your competitors - what next? What more can you do to differentiate yourself and get your product on the supermarket shelf? Well, maybe the next step is to get closer and personal with the buyers

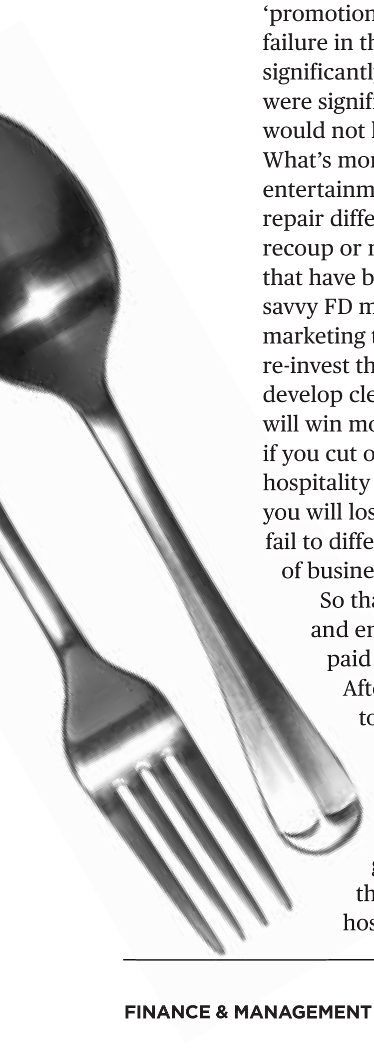
Ask sales and they will tell you hospitality and entertainment is vital, while marketing might not agree

> Promotional plans should be inclusive and progressive – they are essential to your planning

– getting more time to listen, convince and impress them with your business case. Maybe this is when you need extra hospitality and entertainment.

Here, then, is the marketing reason for hospitality and entertainment outside of promotion: to develop differentiation which otherwise has not been created. Statistics are hard to come by but it's a fair bet to assume that in any industry where sales value is high and the service differentiation and price difference between suppliers is low, the hospitality bill is high.

I'm suggesting that hospitality and entertainment costs away from 'promotion' are a sign of a marketing failure in the business; a failure to significantly differentiate. If you were significantly differentiated you would not have to bear this cost. What's more, hospitality and entertainment are poor tools to repair differentiation and will not recoup or rescue all the opportunities that have been already been lost. The savvy FD might want to work with marketing to reduce these costs and re-invest them in marketing to develop clear differentiation that will win more business. The fact is, if you cut out all-non promotional hospitality and entertainment costs you will lose some sales, but if you fail to differentiate you will go out of business.



So that means that hospitality and entertainment should be paid for from marketing, right? After all, marketing has failed to differentiate. I say no. You separate 'promotional' costs out from other hospitality for a simple reason; you get to see the real costs of the non-promotional hospitality. If you charge it back to sales (reducing the sales margin), you get to see the real costs and exactly where you are failing to differentiate. These are very valuable lessons.

HOW DO YOU DECIDE IF A PARTICULAR COST LINE IS A PROMOTION COST?

This is simple. The first question to ask is: is it in the marketing plan? The plan is where you weigh up all of your objectives, challenges, resources, tactics and costs. You will have considered all kinds of promotion and chosen a balanced action plan and budget that is best suited to get you where you need to be. If you consider that "£5k spend on Grand Prix tickets for the largest sales prospect" is among your most effective marketing actions, you will have budgeted for it and planned it. If you had not considered it, then a more rigorous and inclusive planning process is needed. If you decided not to do it, it was because the money was better spent elsewhere – and you made that choice consciously.

Promotional plans should be inclusive and progressive – they are essential to your planning. Hospitality and entertainment, which is within the promotional budget, will be quite clear, as will the target audience, the promotional message to be delivered, the justification and the return on investment (ROI) measure that you'll use. And let's be clear – if you are running a promotion activity, it should have your messages, objectives and ROI.

In multi-division businesses it's therefore right that a division should demur from (co)-funding a corporate promotional event if it does not cost-effectively deliver their divisional message. You might offer to co-fund but only at a level that reflects the relative importance of that event in your overall promotional activity.

Hospitality and entertainment that takes place outside of the marketing plan is not promotional activity or marketing – it is sales activity, and therefore a cost of sale. This is not necessarily bad and doesn't warrant stopping it – far from it, in fact. I have agreed many sales deals at hospitality events and I found it an incredibly useful sales tool. Notice I said 'sales tool' ie, something I used to help close a sale. Hospitality for clients is as much of a sales tool as free extra product or sales discount. But unlike discounts, the costs of hospitality are rarely charged back against the salesperson's profit margin. In these straightened times that's a luxury few can afford, and without it there is little imperative for sales to give up their demands for more high cost hospitality.

BRIBERY RISKS IN HOSPITALITY

When the government introduced the Bribery Act 2010 in 2011 many companies were concerned about the treatment of corporate hospitality and gifts. On the face of it they fall within the definition of a bribe – giving or receiving something of value to influence a transaction. On a global level the UK Act is among the strictest as it introduced a corporate offence of failing to prevent bribery. Under the legislation, is it to take clients out for a meal? What about the FA Cup final? It is somewhat left open to interpretation.

However, as part of a revision of the Act last year, the Serious Fraud Office (SFO) re-stated that *bona fide* hospitality or other legitimate expenditure is recognised as an established part of doing business.

The SFO will prosecute those who disguise bribes as expenditure, but only if (a) the case is a serious or complex one that falls within the SFO's remit and (b) the SFO concludes, applying the Full Code Test, that there is an alleged offender that should be prosecuted.

If the requirements of the Full Code Test are not established, the SFO may consider civil recovery.

Concerned firms can carry out a bribery risk assessment and ensure clients do not think they are under obligation to do business.

Visit ICAEW's Bribery Act page at **bit.ly/17U17WZ**

Martin Finn
is chief executive marketing consultant at Smart Tactics

CPD: THE BIG PICTURE

There is much more to continuing your professional development than filling in a form once a year. **Carol McLachlan** helps members to assess what it means to reflect on our learning

GETTY

WHAT? (THE DESCRIPTION OF THE EVENT)

- **Reflect -** what do I need to enable me to fulfil my responsibilities?
- **Impact -** what CPD activity did I undertake?

SO WHAT? (THE ANALYSIS)

- **Reflect -** what options are there to develop this learning?
- **Impact -** what was the learning and how will I apply it?

NOW WHAT? (ARE THE NEXT STEPS)

- **Reflect -** what will I do and how will I do it?
- **Impact -** what else do I need or what might I have done differently?

It's December, so we've all had the email from Andrew Fagg inviting us to renew our subscription, pay our fees and make our continuing professional development (CPD) declaration.

And as it's December, we will have received that invitation amid the usual furore, as purveyors of CPD urge us to act quickly to buy up their courses and webinars before the end of the calendar year. Of course, it's actually too late for ICAEW members. Our CPD year-end has passed; our annual declaration is for the 12 months to 31 October, so we should be signing off 2013 and planning ahead for 2014.

In terms of the ICAEW CPD cycle - Reflect-Act-Impact-Declare - we've completed 'Act' for 2013 and we are about to 'Declare', but what about those oft-neglected cousins, 'Reflect' and 'Impact'?

FIRST A LITTLE BACKGROUND...

2014 heralds the tenth year of the 'new' ICAEW CPD model. In 2005 we were revolutionary in adopting an output approach, signifying a move away from measuring CPD in terms of units and hours, structured and non-structured. The new currency for measurement became the learning outcome and this brought personal autonomy, freedom to choose how we develop professionally and a much better chance of maximising the return of our personal investment in CPD.

NOT ALL CPD IS EQUAL

Under an output system, your inputs - the courses you attend, the papers you read or your study of the latest pronouncements - count for nothing unless they are relevant to your role and development needs. Without a relevant learning outcome, it's not CPD.

What counts as CPD is an identifiable and relevant learning outcome, which could come as likely from a discussion with a colleague as from a three-hour financial reporting webinar.

This is a qualitative, rather than quantitative, approach to CPD. It has fuzzy boundaries rather than hard edges; it's highly subjective and it requires you to employ a substantial degree of personal judgement. And that brings us to the topical significance of 'Reflect' and 'Impact' in your CPD cycle.

REFLECTION: THE MISSING LINK

In fact, both 'Reflect' and 'Impact' rely on the crucial skill of personal reflection. At the beginning of the CPD cycle we 'Reflect' on the personal resources we will need to sustain and develop our current and desired professional competence. After we've invested in these ('Act'), we assess the 'Impact' of the action we've taken, once again employing personal reflection.

Reflection is simple but not easy. As the first step in the CPD cycle it enables us to make an assessment of where we are now, where we want to get to and how we are going to get there. At the 'Impact' stage it is the reflective process that enables us to evaluate and make sense of what we've learned, turning 'surface' learning into deeper and applied learning.

Effective reflection is holistic, taking a big picture view, connecting both personal and professional learning and experience and linking it to action. It also requires an audit trail and this means documentation. So, how do you go about it?

EXAMINING REFLECTIONS

Using a combination of self-coaching and reflective writing you can develop your own reflection process. Your reflective writing may be a stream of consciousness narrative or a series of inter-linked Excel work books but either mode will be characterised by incisive, challenging questions. One option is to use the three stem questions established in models of reflection by Borton and Driscoll: What? So what? Now what? The box opposite is an example demonstrating their use at both the 'Reflect' and the 'Impact' stage.

Your reflection will be further enriched by drilling down into more detailed questions, recognising and challenging underlying assumptions, taking a 360° perspective and making holistic connections to identify transferable learning. This is not just for documentation purposes; the research suggests the process of reflection itself boosts brain function to enhance and embed learning beyond merely undertaking the learning activity itself.

AN EXTREME EXAMPLE...

Let's suppose that you are at a mature point in your career. Perhaps you are a CFO, in a leadership role; you have a superb team with cutting edge technical know-how and a competent financial controller who manages the department.

There may be periods when, **having reflected**, you quite reasonably conclude that you already have all the current skills and knowledge necessary for your work and that you do not need to undertake any further CPD at this moment. For further information, see the guide at bit.ly/1eP8iUP

Note the emphasis. You cannot reach this conclusion without **having reflected**. You still need to record your thinking process and you can only do this by reflecting. The act of reflecting is itself a CPD activity, so you have the perfect reflective circle, enabling you to sign off and 'Declare' having completed your own personal due diligence.

Carol McLachlan FCA is a chartered accountant who had a 20-year Big Four career before becoming a professional coach, mentor and trainer, as well as a postgraduate CPD specialist. Visit **theaccountantscoach.com**

Membership of the faculty provides you with a good grounding in CPD. Our mix of webinars, events and publications will assist you attain your annual requirements and keep you up-to-date

A cautious optimism

The Bank of England published its latest projections for UK economic growth and inflation in the November Inflation Report. **Graeme Chaplin** summarises its key messages

Graeme Chaplin is the Bank of England's agent for the West Midlands

Recovery in the UK has finally taken hold. The economy is growing robustly, as lifting uncertainty and thawing credit conditions start to unlock pent-up demand. But significant headwinds - both at home and abroad - remain, and there is a long way to go before the aftermath of the financial crisis has cleared and economic conditions get back to normal. What does that mean for the Bank's policy stance?

In August 2013, the Bank set out *Forward Guidance* for its future interest rate decisions. The Bank has stated that it will not even consider raising bank rates until the unemployment rate falls to 7%, provided this does not entail material risks to price stability or financial stability. Through that *Forward Guidance*, the bank is giving businesses and households the confidence that interest rates will not rise until jobs, incomes and spending are recovering at a sustainable pace.

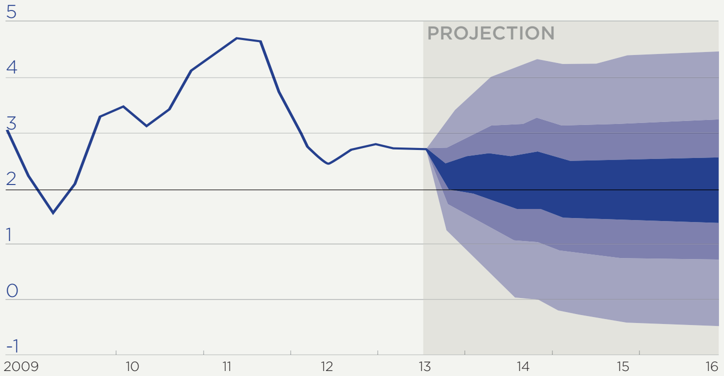
Annual consumer price inflation (CPI) fell to 2.2% in October and is set to fall back to around the government's 2% target over the next year or so. The impetus from past increases in import prices fades and a gradual revival in productivity growth, together with a persistent margin of spare capacity, curbs domestic price pressures (Chart 1).

It will be some time before economic conditions return to normal, however; the level of UK output remains around 2.5% lower than in early 2008 and the number of unemployed is nearly one million higher. Economic growth is expected to pick up, bolstered by lifting uncertainty and thawing credit conditions (Chart 2). But the level of output is still more likely than not to remain below its pre-crisis peak until spring 2014.

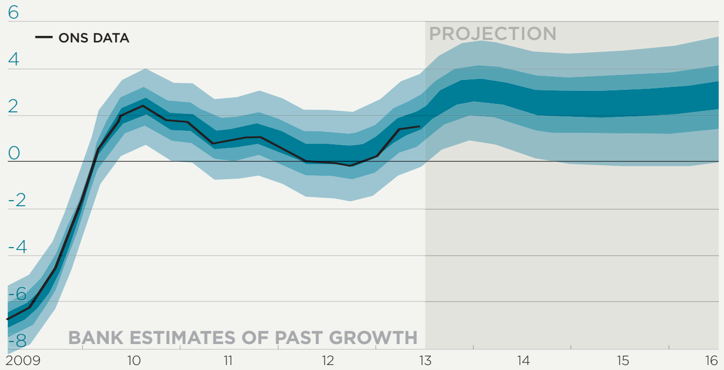
The recovery in output growth is expected to be accompanied by a gradual recovery in productivity growth, so only a gentle decline in the unemployment rate is in prospect (Chart 3). The Bank judges there to be a two-in-five chance that unemployment will reach its 7% threshold by the end of next year, and a three-in-five chance that it will have done so by the end of 2015.

It is important to remember that the 7% unemployment threshold is a staging post for assessing policy, not a trigger for an automatic increase in Bank Rate. When the threshold is reached, the Bank will set policy to balance the outlook for inflation against the need to provide continued support to the recovery in output and employment.

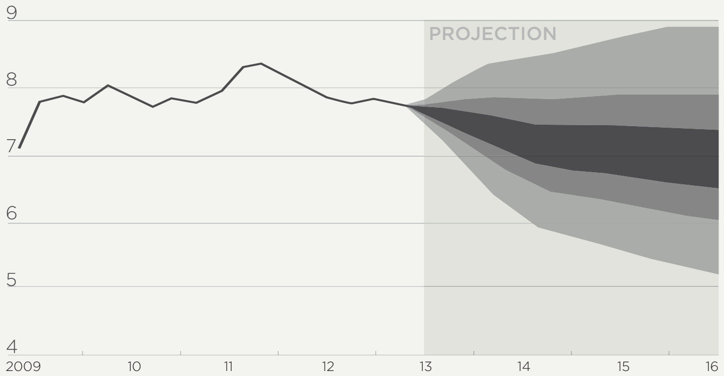
1. CPI INFLATION PROJECTION
Percentage increase in prices on a year earlier



2. GDP PROJECTION
Percentage increases in output on a year earlier



3. UNEMPLOYMENT PROJECTION
Unemployment rate, **percent**



SOURCE: BANK OF ENGLAND

- The Bank's *Inflation Report* is available at **bit.ly/17owyVR**
- *The Agents' Summary of Business Conditions* is available at **bit.ly/HIA8Z8**

WHAT NEXT FOR UK PENSION FUNDS?

The UK's defined benefit pension schemes and their sponsors have been enjoying some broadly positive news of late: for the most part they have seen an uplift in asset values. The FTSE 100 has been bolstered by news from the US Federal Reserve that its Quantitative Easing (QE) programme will continue and not be scaled back as had been previously anticipated.

At the same time the yield available on benchmark UK gilts remains somewhere just shy of 3%, a huge improvement on the yield available at the start of this year. Pension scheme funding positions are overwhelmingly impacted by movements in gilt yields. The improvement in yield has flattered many of the UK's 6,150 corporate defined benefit pension funds, which had a collective deficit of over £700 bn (March 2013) according to the Pension Protection Fund.

This deficit, in spite of some volatility over the previous four years, had remained stuck at this level, despite the £182bn put up by corporate sponsors in a vain effort to reduce the size of the hole during this period.

When QE was introduced in early 2009, 15-year gilt yields (a good match for many pension schemes' liabilities) stood at 4.4% and the UK hadn't yet achieved its status as a safe haven for investors. QE pushed down gilt yields to historic lows helping to both bring down the Government's costs in servicing the national debt and protecting the UK's credit rating. But at the same time the first round alone added, on our estimate, £74 billion to pension fund deficits.

The first signs of relief for sponsors of pension funds came in Q2 this year, when we saw the first significant rise in gilt yields. Since then, a raft of positive economic news has buoyed investors, and this may only be the beginning of a sustained recovery. The European Commission has recently doubled its UK economic growth forecast for this year and next, even stating that UK growth will be stronger than in Germany.

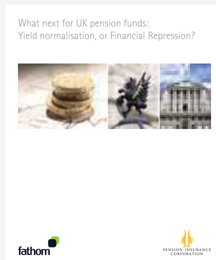
But one of the downsides to having a strong uplift in demand-led growth where supply fails to follow through is that there may well be a dose of inflation to follow. This could be a problem for trustees and sponsors: pension schemes are generally highly exposed to future inflation increases. According to one survey carried out in 2011, fewer than 20% of defined benefit pension schemes had hedged at least 50% of their exposure to inflation. This is dangerous for pension schemes and their sponsors: for a typical pension scheme, a 1% change in long-term inflation expectations could increase liabilities by between 10-20%.

It is possible that inflation drifts a little higher over the next few years, possibly 5% on the RPI measure, if demand outstrips supply. Should the spill-over effects from tapering by the Fed warrant action by the Bank of England, perhaps through additional Quantitative Easing in an effort to keep index-linked yields below zero, this would be very damaging to schemes' funding positions.

In fact further Financial Repression, aimed at protecting over-extended households as much as government finances, could force companies sponsoring UK-defined benefit pension schemes to contribute another £250 billion over the next 10 years according to a new report, *What next for UK pension funds: Yield normalisation, or Financial Repression?* Sponsors should work with scheme trustees to reduce their exposure to this risk.

Report co-published by Fathom Consulting, an independent economics and financial markets consultancy that provides bespoke advice to a number of UK pension schemes, and Pension Insurance Corporation.

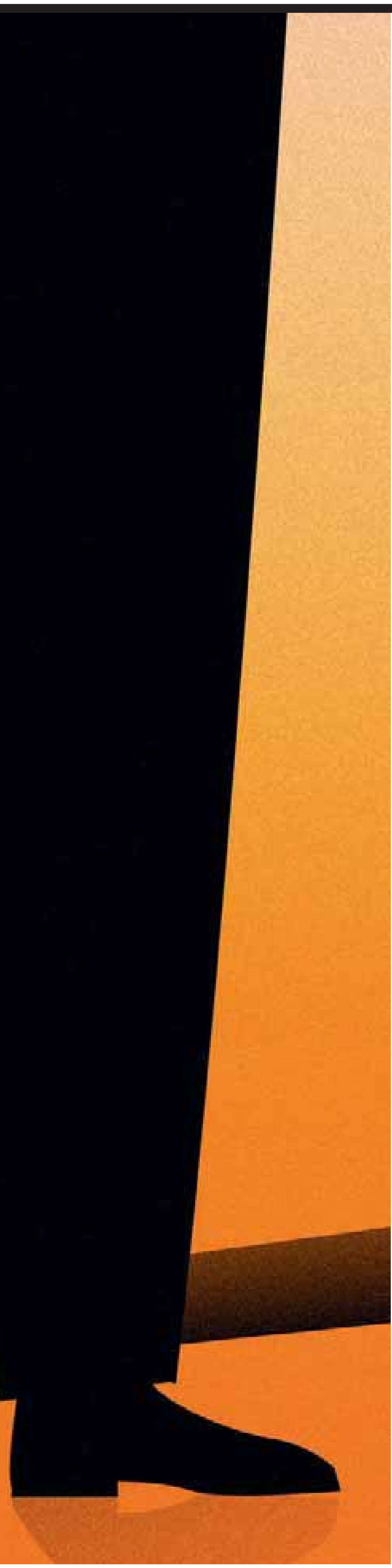
Jay Shah
Co-head of Business Origination
Pension Insurance Corporation


What next for UK pension funds:
Yield normalisation, or Financial Repression?
fathom

The report can be downloaded from PIC's website at:
http://bit.ly/18KdmGj

PENSION INSURANCE CORPORATION

TANG YAU HOONG



RIGHT THOUGHTS, RIGHT WORDS, RIGHT ACTION

Conflict in the workplace has the power to break a business, and resolving disagreements and negotiating a result can be challenging. But as **Patrick Dunne** explains, the right strategy and actions from the board and executives can be all that's needed

Whatever our instinctive reaction to 'conflict', the reality is that it is as inevitable in business as it is anywhere else in life. So, love it or hate it you are likely to have to manage it at some point. Moreover, in an ever more complex and pressurised world, the ability to spot conflict early and then to manage it successfully is likely to become more of a differentiator for those competing for leadership, board or major advisory roles.

Failure to manage conflict well might mean that even a relatively minor issue builds into a destructive force that is capable of ruining relationships, derailing projects and sometimes even destroying a business. Yet conflict can also be a very positive thing, perhaps even the spark that ignites incredible creativity or the catalyst for transformational change. Less dramatically, it might simply be a situation that enables us to reset and strengthen relationships before they go seriously off track.

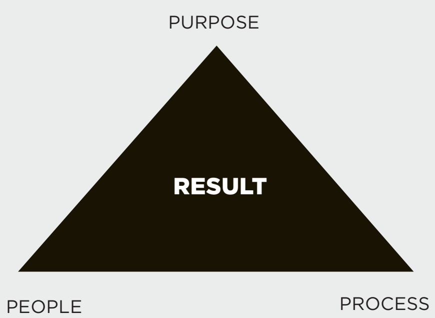
Evidence suggests that managing conflict in the workplace is far from a national strength. Research conducted by publisher CPP, with 5,000 workers in nine EU countries and in the US, revealed that the UK had the highest rate of anger and frustration with workplace conflict. A Healthy Companies International survey also showed that 41% of employees think that their boss does not manage workplace conflict well. Estimates from the Confederation of British Industry (CBI) suggest that 20% of a leader's time is taken up with conflict resolution. So, even if we have higher expectations than other countries, it looks like there's an opportunity.

ROOT CAUSES

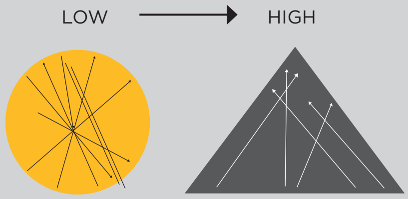
Conflict arises in many ways. Sometimes the root cause is structural. There may be a lack of clarity or agreement on the role of the board or some of the central characters involved. Alignment within the board may be an issue, or it could be that the alignment between the board and the executive or management committee is a problem.

When working with 'boards with issues' I find the images in the charts presented here are helpful – their use is

MODEL FOR EFFECTIVENESS



BOARD ALIGNMENT



obviously not restricted to the boardroom.

If there is clarity of purpose, the right people organised in an appropriate way and they have good process, then things tend to work well. However, in most situations where there are issues, I find that some elements of this dream scenario are missing. More often than not, there is a lack of real agreement on the role of the board or there is complete formal agreement that's not mirrored by reality. This can be simply because it has never been discussed - it is assumed that everyone knows.

What should be the purpose of the board? For me it's "right strategy", "right resources" and "right governance". If the board focuses on these things and the executives concentrate on producing strategic options, delivering the business plan for the chosen strategy and ensuring operational and financial integrity, then there is a much better chance of achieving a healthy degree of constructive conflict and sustained high performance.

When it comes to the alignment of teams you may have experienced the situation represented by the circle in the diagram above, people pushing and pulling in different directions. The aim here is to try to find a galvanising goal that everyone can buy into, even if it is just 'not to go bust'. In addition, you need to remove or neutralise the disruptive or those who will never buy into what makes sense for the business or team as a whole. For a board or group to sustain success, there needs to be a healthy degree of challenge, even if everyone is fundamentally heading in the same direction, hence the triangle rather than a straight line for high alignment.

PARALLEL UNIVERSE

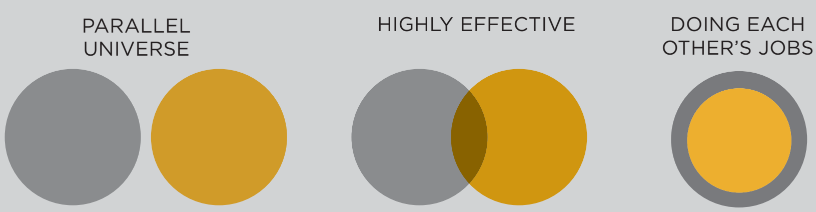
Having spent time working with boards and management teams on how they can work more effectively together, I have seen the whole range of situations shown in the diagram below. Sometimes the board and the executive committee appear to be operating in parallel universes. They come together for board meetings or away days, which are essentially charades they endure because they have to. Silent seething during the meeting soon turns into open criticism the moment they leave the room.

In other situations it can be hard to distinguish who is on the board and who is in the management team as they all appear to be trying to do each other's jobs and wasting a lot of energy in "turf wars". You may also have experienced the paradox of executives complaining about being victims of an out-of-touch board that's less able than they are. If they are so much better, why are they behaving like helpless victims? You may not be responsible for the situation you are in but you can always take responsibility for making it better.

In contrast, highly-effective boards and management teams have their own distinctive areas of focus but are very comfortable and effective when they come together. You can immediately sense a high degree of mutual respect and they are "well geared", drawing on each other's strengths, recognising weaknesses and supporting each other, rather than magnifying vulnerabilities.

Superb structures, processes and operating models can still be disrupted by humans behaving unhelpfully, whether knowingly or unwittingly. Great teams are said to comprise a range of characters and capabilities. Yet sometimes we find it hard to manage the inevitable differences between us.

ALIGNMENT OF BOARD AND MANAGEMENT TEAM



GOING THE EXTRA MILE

Erin Meyer at business school INSEAD has done outstanding work looking at cultural differences in teams. She found functional differences between accountants and sales people, for example, can be as significant as those between distinctive national cultures. Meyer identified eight factors, apart from normal personality differences, upon which we might differ in our approach to colleagues. These were classified as follows:

- propensity to risk;
- our preference for a forceful or empowered approach to leadership;
- our comfort with negative feedback;
- whether we were more relationship or task-focused;
- how we prefer to see the context (eg, clear and simple or sophisticated);
- our comfort with silence;
- whether we had a preference for things to be explained in an inductive or deductive way; and
- our approach to completing tasks (eg, one by one or multi-tasking).

> Understanding your red flags is crucial to managing conflict. If you can't manage yourself, it will be tricky commanding respect enough to manage others

Encouraging people to work out where they are on each of these spectrums can have quite a positive effect. Going further and understanding how these characteristics manifest themselves in everyday working situations and then practising having conversations in different ways can make a material difference to team performance.

At conflict resolution charity Leap, we have worked with tens of thousands of young people on managing conflict. The 10 tips (right) are fairly basic, but are as relevant in the boardroom or office environment as they are on the street or in a young offenders' institution. A growing proportion of Leap's income comes from drawing upon the expertise of young trainers to run workshops for businesses and other organisations.

A lot of this may seem obvious, but it is often hard to do when you are in the middle of a conflict. That's why practice and role play can be so helpful - a bit like a pilot practising in a simulator. When the situation arises for real, picking the right strategy to deploy feels instinctive and you can manage the situation successfully.

For a pilot, the desired outcome - to land safely - tends to be obvious, to them and to everyone else involved. In business, unless the enterprise is close to collapse, this isn't always the case. A bit like arguments at home, it is sometimes hard to remember what the argument is about or what outcome is desired.

RED FLAGS

Anger blurs judgement, so understanding your own "red flags" - the things that really irritate or anger you, as well as the habits you have which might be common red flags for others - is crucial to managing conflict well. If you can't manage yourself, it will be tricky commanding respect enough to manage others.

Understanding how you prefer to deal with conflict and whether you need to expand your repertoire is also helpful. Probably the best psychometric test for this is the Thomas Kilmann test. The premise is that most people tend to have preference for a few of the five main approaches to a conflict (Compete, Collaborate, Compromise, Avoid or Accommodate). Conflict maestros are comfortable deploying any approach and have the knack of picking the right one for any given situation. Those less successful tend to rely on one or two approaches (eg, compete or avoid) which they adopt regardless of the situation or combatant.

Understanding the situation is central to success. At Leap, we use a tool called FIDO (Facts, Interpretation, Decision and Outcome). Step one is to think about what's going on and to be clear about fact and interpretation. Then the focus is on what outcome you want and to work out what choices that you have. Making the right choice is often a lot easier than doing it, especially in a highly-charged situation. So, practising the skills and trying out different approaches can be really helpful.

We have developed a series of role plays and linguistics games demonstrating that how you start sentences and the words you use can make a big difference to the outcome. We've learned these techniques work just as well for M&A advisers in the middle of an argument as they do for young people being stopped by the police.

We have a big opportunity in business to be more open about conflict and to put more effort into improving how we manage it. The payoff is likely to be better performance and more fun in achieving it. ■

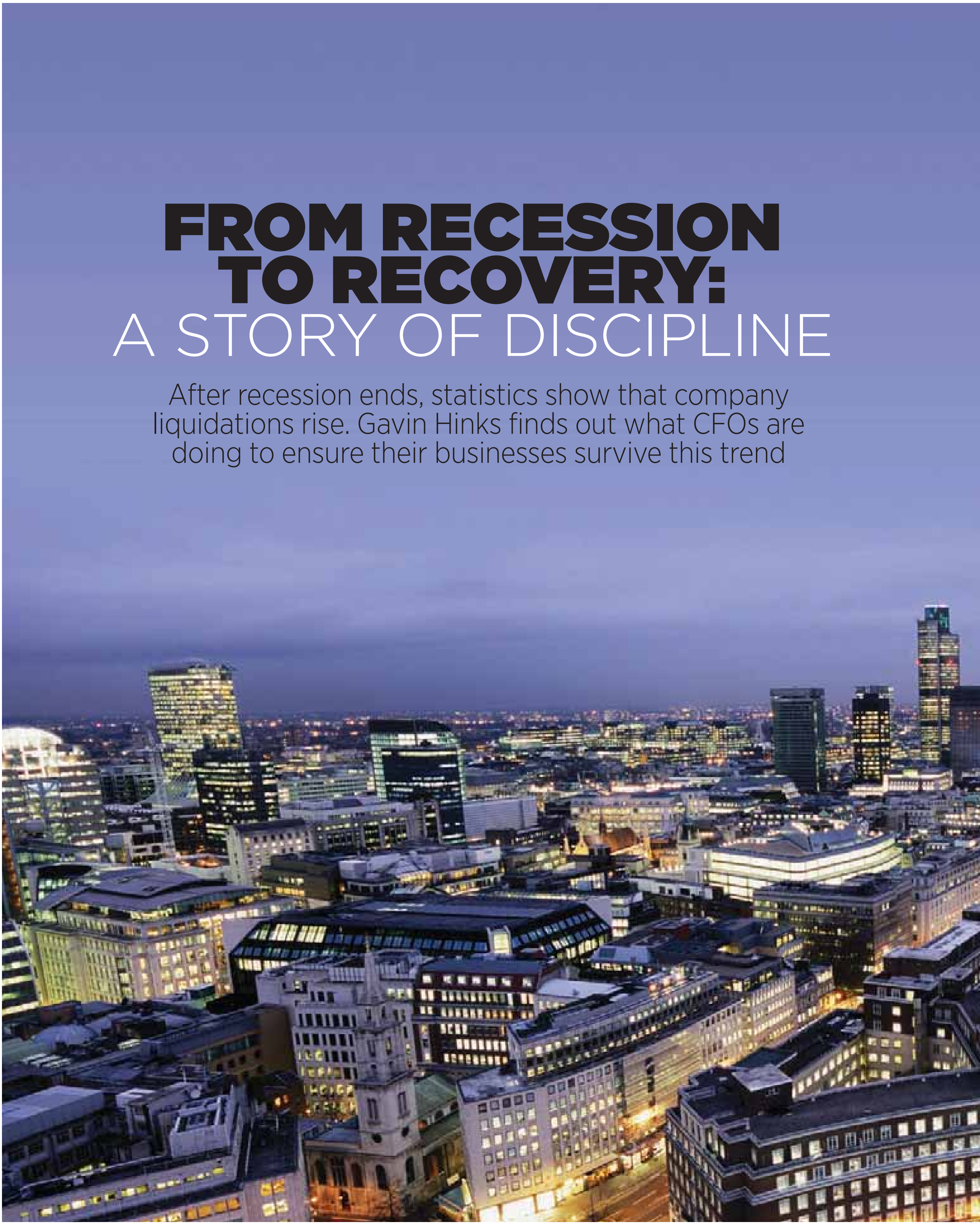
TEN TIPS FOR MANAGING CONFLICT:

- Acknowledge that there is a conflict and view it as an opportunity.
- Respond rather than react.
- Think about the situation, yourself and the other person/people involved before deciding what to do.
- Try to listen to what people are thinking as well as what they are saying.
- Use F.I.D.O to help (Facts, Interpretation, Decision, and Outcome).
- Focus on the outcome you want to achieve and work out what choices you have.
- Remember your "red flags" and theirs, and how you planned to deal with them.
- Decide on which issues you are going to Compete, Collaborate, Compromise, Avoid and Accommodate.
- It's hard to influence someone who doesn't respect you, so build respect with as many people in the conflict before you try.
- Think hard about the language you use. "I" and "we" are going to be a lot more useful than "you" and "they".

Patrick Dunne is a visiting professor at Cranfield School of Management, is on the board of the University of Warwick, and is chairman of Leap

FROM RECESSION TO RECOVERY: A STORY OF DISCIPLINE

After recession ends, statistics show that company liquidations rise. Gavin Hinks finds out what CFOs are doing to ensure their businesses survive this trend



GETTY

In some places at least, the recovery is taking hold. GDP figures, optimism and confidence surveys, as well as businessmen and politicians, are pointing to the fact that life has returned to the economy. Indeed, the mood is more upbeat since 2008 when the country fell into an economic trough, one that turned out to be worse than any recession since 1945.

But there's a sting in the tail. Even though we know that recession places such a strain on business that the company death rate climbs alarmingly, we also know that recoveries are no less lethal. According to Nick Hood, a veteran insolvency practitioner and now head of external affairs at risk management consultancy, Company Watch: "Company failures peak after a recession and not during it."

Hood is not wrong. The phenomenon is well observed and the statistics do not lie. When Britain entered recession in 1980, company liquidations in England and Wales began to climb, reaching 6,890 that year. The downturn lasted until Q2 the year after, but 1981 saw company failures rise again. In 1982, when the economy was back in growth, failures kept rising and indeed continued on an upward trend, peaking in 1985 - four years after the initial economic tumble. Or, take the recession of the early nineties - five quarters of contraction. As expected, company collapses, which were already rising, climbed sharply (45%) to 21,827 in 1991 but it was the post-recession period that continued to see the damage, with 1992 seeing a peak of 24,425 and 1993 a fall, but with a liquidation level still above the rate immediately before the economy shrank.

6,890
liquidations in 1980

During the last recession, liquidations peaked in 2009 - the year the recession ended. And even though levels are lower for the years of 2010-2012, they remain considerably higher than in 2007, the last full year of growth. It remains unclear how many companies will see their demise in 2013, though it is possible liquidations could be at broadly the same level.

The point is history shows us that even though recessions damage companies, the carnage continues in the period of recovery, the time when economic activity is trying to regain pre-recession levels.

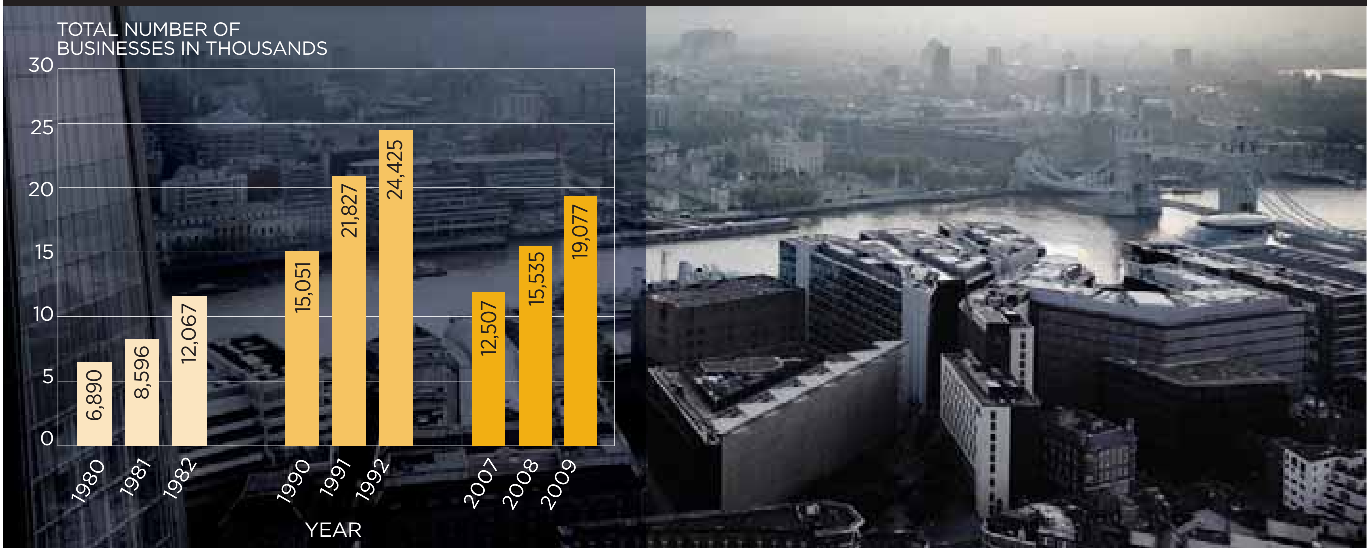
Knowing the facts though, and doing something about it are different things. What causes companies to go to the wall when the good times return, having held on through the bad times? What do you do to avoid becoming a victim of recovery?

LOOSENING UP

One possible explanation is cost management, and what happens to it when companies go into recession and then emerge on the other side. A rudimentary reading says that companies become "lean and mean" when the economy is poor and once recovery comes along the purse strings are loosened, prompting unsustainable spending.

For some there is something in this argument. Professor Joseph Lampel, a professor of business strategy at Cass

COMPANY LIQUIDATIONS IN ENGLAND & WALES



Recent Company Watch research found that **227,000** companies, or roughly one in 10, have a combined negative equity of **£70bn** on their balance sheets. Five years ago the figures were **109,000** and **£31bn**

Business School, believes business managers are "by definition optimists" so when economic recovery begins they may misjudge the gap "between reality and potential". The consequence is that companies may "relax levels of discipline" with a "shift in attention that can be dangerous".

Professor Lampel is not alone in this view. Gratefully accepting new orders the minute they appear can put a strain on companies to deliver. According to Chris Kinsella, an interim finance director and former CFO of TI Automotive (where he led a £1bn management buy-out), the problem arises because businesses have cut everything that they can create during the recession. When an upturn comes they rush to fulfil orders on depleted resources, which can lead to exceptional costs, such as the use of expensive sub-contractors or premium delivery services, over and above business as usual as processes stretch to keep up. "Your efficiency is compromised," says Kinsella. "Cost discipline therefore needs to address that inefficiency." Kinsella advocates finance directors regard economic recovery as a time demanding a "special kind of scrutiny", requiring firm controls to be either maintained or put in place.

According to Bob Eastoe, finance director at Hypnos Beds (see box), the discipline of recession has to extend to recovery. Recent Hypnos results have seen company turnover grow 10% year-on-year for 2012-2013, despite years of cost cutting. "The most fundamental control is that I authorise everything," he says. All major spending, even attending trade shows, is agreed with management. His last line of defence is scrutinising the weekly BACS payments. "I eyeball it and question things I don't think are appropriate."

WORKING IT OUT

Of course, allowing the costs of producing a product or service to creep upwards can place a strain on working capital. Unchecked, it can lead to overtrading and potentially disaster.

So acute is the working capital strain that some identify it as the real issue in the move from recession to recovery. With the recession having eaten through reserves, companies are ill-prepared to fund the sudden influx of orders, which they are loath to turn away. Recent Company Watch research found that 227,000 companies, or roughly one in 10, have a combined negative equity of £70bn on their balance sheets. Five years ago the figures were 109,000 and £31bn respectively. Company Watch says the research reveals a widespread decline in financial health and points to a problem being stored for the future. "It's the growth that kills embattled companies after a recession," says Nick Hood.

According to PwC partner Robert Smid: "What you don't want is that the growth rate of the working capital outpaces your revenue growth rate." Smid says there is no single formula for calculating working capital needs, adding the issue is specific to an industry and a product. For some it may mean turning orders down - an act of rigid discipline after years of decline, but potentially necessary. "Being an undercapitalised busy fool isn't the brightest recovery strategy," says Hood. "It really is the case that there is more to the company in a recovery phase than rising sales."

But there are ways of managing the issue. Key is setting performance indicators, for working capital, such as debtor days or days in stock, and keeping a constant watch to ensure they improve rather than deteriorate. Then attack the problem. Approaches, like reducing stock, negotiating better supplier terms while collecting debts and improving days outstanding with clients and customers are well rehearsed.

For Smid, subtle changes in the approach to business can bring benefits. He cites the example of telecommunications companies where services are bundled and bills are no longer paid in arrears but as subscriptions. "That's an example of how you can change your business model to be more working capital efficient." Changing production techniques can have the same effect. Many manufacturers have switched to a "postponement" strategy, he says, so that several models of the same product can be prepared in modular form with the decision about which model to make coming late in the process. This prevents unnecessary stockpiling of components which tie up working capital.

STRATEGY SINGS

Smid's point raises big questions about the way company managers approach the question of costs, spending and working capital. And that means thinking more strategically. Focused business managers not only retrench during a recession, they avoid bad spending and begin to plan for the future.

Bad spending can come in different forms. Brian Johnson, a partner at HW Fisher, identifies holding on to fixed costs "in anticipation of increasing turnover, which doesn't come as quickly as you would hope". That's a warning companies need to make honest assessments of their circumstances and potentially cut deep.

Others see alternative causes of throwing good money after bad. Kinsella points to ploughing cash into infrastructure for old products or services at the expense of updates or innovation, especially painful if the competition has prepared something new for the recovery.

But that points to the core strategic issue. Once in the austerity zone, and despite the struggle of fighting a downturn day-to-day, businesses need to plan. A keen management team will focus on understanding their precise position and where they want to be. Kinsella says this involves a business plan with "robust" growth forecasts focused on future business levels, market information and competitor activity, and what their current risks are. Those risks may include the capacity to respond to an upturn in business, the "fitness" of existing plant and machinery denied replacement or maintenance during austerity, or whether the headcount is adequate.

According to Johnson, managers occupied with the pressure of managing in hard times find it all too easy to shelve planning, especially planning to spend, and arrive at recovery unprepared. He stresses the need to "flex" or test the cashflow assumptions asking tough detailed "what if" questions about the cash spending needs, not just if things get worse, but also to exploit an improving economic landscape.

David Gilbert, a partner at BDO puts it like this: "That's why there's going to be a lot of people in the wilderness, a lot of people who fail as other businesses grow, because they really don't know how much money they need to grow their business.

"There are so few companies who have that sort of information who don't do proper forecasts or projections."

Gilbert's argument is that if the planning is done well it makes the task of accessing funds for growth simpler. "If a company is doing proper management accounts with proper projections, how can it not have the support of its lenders? It's that simple.

"So it's not just cutting costs, it's getting costs right."

DREAM UPTURN

Bob Eastoe, finance director of Hypnos Beds

Hypnos Beds is one place where the battle to survive has been fought without respite and where the transition from recession to recovery has been managed with care. Bob Eastoe admits the company was in trouble when he joined in November 2007, shortly after the appointment of a new managing director and on the eve of recession. Despite a Royal Warrant since 1929, and serving both retail and contract (hotel) markets, Hypnos was struggling.

CUT HARD, CUT DEEP

"The new MD was looking at turning the business around. But that very quickly became saving the business, because quickly we were going into very different financial times," says Eastoe.

Cost and cash control were the top agenda items for Hypnos as the new executive team faced up to reduced business. "If you do nothing else to ensure you survive, you manage cash," says Eastoe. "You mustn't forget other cost controls; they come much more sharply into focus when you have to save cash. It makes you question everything you do."

Hypnos cut headcount from more than 300 people to 200. Production staff moved to a four day week, while admin staff took a 10% pay cut. Key roles disappeared such as IT and HR managers, and the company's export team was also culled. Marketing spend was slashed. The company also worked on maintaining debtor days at below 50 and improving credit terms.

In all, Hypnos reduced overheads by 20-25%. "They always say cut hard and cut deep," says Eastoe. "We did cut deep to start with, but because of the nature of where the business was we had to go further than that."

THE LONG RUN

Hypnos also took a strategic longer view. The recession became about spending money judiciously as well as saving. A marketing manager was recruited in recognition of the discipline's future importance to sales, and money was set aside for product development. "We knew that, to be strategic, and do more business with more customers, we had to revamp the product range," says Eastoe.

The forward thinking did not end there. Hypnos prepared for growth by raising a credit line to invest in new machinery after presenting a business case to the company's bank. The driver was replacement of exhausted machines beginning to hit productivity. A new export manager has been put in place to kick off a move into selling in the EU.

But while the export move has a hint of speculation, major capital investment was backed by understanding the market and the sustainability of orders. Indeed, it was planned only after renewing a major contract with Whitbread, owners of Premier Inn. "We tend to delay major investment until we know a customer base is actually there."

Eastoe says his most fundamental control is that he authorises all spending. But, he adds: "You can't hold off investment indefinitely, because otherwise your business will die, just spiral into decay."

THE RIGHT STUFF

For a project to succeed, it needs a team that can perform. **David Parmenter** outlines how a company can make the most of external consultants in these circumstances

Behind most successful managers are the successful projects where they have been able to obtain leverage by using consultants properly. You have a choice: learn to achieve by getting the right consultants 'on the bus' or hire unwisely and set yourself up for failed projects. From my observations and first-hand experience as a consultant, I set out some pointers to help you use consultants successfully.

NEVER GIVE A NEW PERSON A NEW JOB

Peter Drucker, for many people, was the Leonardo de Vinci of management. His work will be appreciated more in 400 years' time than at present. We all would benefit from reading *The Definitive Drucker*, a book that offers a summary of the sage's advice.

Drucker observed that many new initiatives failed because the wrong people were leading them. When we recruit a new employee or consultant to undertake a new job or project, such as the introduction of lean or the balanced scorecard into the organisation, there will be much uncertainty among staff and management.

Staff will be wondering, what is going to happen with my job? Are my favourite tasks about to disappear? What effect is this going to have on my pay?

These doubts, along with the added insult of the Porsche Carrera in the visitors' car park, often lead to the stonewalling of any potential project progress. There may be some staff and management who will do their utmost to make the consultant fail. The consultant, in such circumstances, is given as much chance of success as a mountaineer solo climbing Mount Everest. It can be done, but only by a freak of nature.

Instead, Drucker advised that you find a project manager in your organisation who holds the highest stack of IOUs. Train them, support them with a mentoring-based consultant and watch the project fly. The theory goes that staff and peers will go over the trenches for them.

"A PRINCE WHO IS NOT HIMSELF WISE CANNOT BE WISELY ADVISED"

Regrettably, many managers do not have the skills to manage large complex projects, let alone handle the additional requirements when adding consultants to the mix. That is, if you do not have strong in-house project management skills, contracting them in will not solve the problem. Project management skills must reside within the project manager, the project sponsor and the senior management team (SMT).

Where skills in project management are lacking in any of these three areas, chaos can reign. The SMT needs to fully understand project management techniques so they can be forewarned and take the necessary actions when their large projects are going off-track. Many of the large failed projects I have worked on have been screaming for help during much of their life and in many cases the SMT was helpless due to the huge gap in the team's knowledge and experience.

It is not uncommon for young enthusiastic managers to be given the headroom to extend beyond their level of competence on large projects. The common symptom in these cases is that the management team, up to and including the SMT, could do no better or were no wiser.

So, play to your strengths. Do not have big projects if you are not a big-project organisation. It is as simple as that. Then you will not need to shoot the messenger.

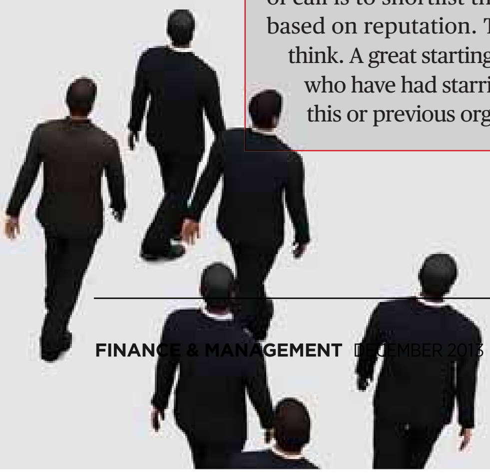
INVEST IN A COMPREHENSIVE SELECTION PROCESS

The recruitment process cannot be bypassed or short circuited. As Drucker reminds us, it is better to spend 40 hours in a comprehensive selection process (putting up fences at the top of a cliff) than spend 400 hours sorting out the mess (at the bottom of the cliff).

Therefore it is imperative that you invest as much time as possible in the pre-selection process, before you are in dialogue with short-listed consulting firms. Your first point of call is to shortlist three to five consultants based on reputation. This is easier than you think. A great starting point is to ask consultants who have had starring roles previously with this or previous organisations you have worked with. Ask them for referrals. You may even find they put themselves forward for part of the assignment and will work alongside a recommended consultant they have known for years.

Great staff and great consultants know other great staff and consultants. That is how the business world works best.

Having made a shortlist, it is worth contacting a couple of their previous clients to ask: "Would you take Mr X on for another consulting assignment?" As Jack Welch in his book *Winning* pointed out, you might be surprised how frank they are. Assuming a thumbs-up, go on to ask how the consultant works best (they may not realise it themselves).



CREATE LEVERAGE TO MAXIMISE THE VALUE FOR MONEY

On all projects, ensure you use in-house staff in the project team. In most cases where a client has said, "we do not have the resources", I have been able to prove otherwise. Graduates with bright, quick and insightful minds can be located. All you need to do is search the employee database. Ensure you have assigned at least two young staff members to the project. These young graduates will reduce the time spent by the consultants, and at the same time make the project more interesting for the consultants. There are few experienced consultants who do not enjoy working with young and motivated in-house staff.

RISK MANAGEMENT: IS IT ABOVE OR BELOW THE WATERLINE?

Jim Collins, in his great book *Built to Last*, talks about risk management. The SMT needs to know whether a risk is above or below the waterline. Just like a ship, a project can take many hits above the waterline, but few below them.

Thus with project risks, always separate out those above or below the waterline. More sophisticated risk management may be of dubious benefit. In reality, it is trying, often unsuccessfully, to put objectivity in a subjective area.

UNREALISTIC TIMEFRAMES – THE RULE OF THREE

Don Tricker, former coach of the New Zealand softball team, is a gifted leader, and can boast three World Cup gold medals in a row. He said he had discovered the secret to realistic project timeframes. He called it the 'rule of three'.

Over time, Tricker became frustrated with coaches promising more than they could deliver. He noted that in reality you don't have five days a week to do tasks; sport is about people, and issues that emerge are typically people issues that take time to resolve. "When planning, I assume that I'll have three days in the week, with two days for firefighting or unplanned activity," he said. He now plans all projects on the basis that full-time means three days a week. He has found that projects are now completed on time.

So, if you are told the consultant will be full-time on the project, don't be naïve. Work out the total requirement and divide by three eg, 60 consulting days will now take 20 elapsed weeks, not the 15 you had originally planned.

HAVE THREE PILOTS WHEN TESTING A NEW SYSTEM

Peter Drucker also loved doing things in threes. He said a CEO's main role was to develop three protégés; a project should be piloted in threes. The logic being that a solo successful pilot will not have fully tested the system. Divisions can always say that the pilot did not represent their business, and so on.

HEED THE WARNING SIGNS EARLY

Not all consultancy relationships are going to work. The key is to recognise early on that the relationship is off the rails and to investigate the breakdown. Warning signs of a project going off track include:

- in-house project staff are too busy with other duties;
- the project has been simmering for a long time before consultants were involved;
- only one or two of the SMT members are aware of the project;
- project team members talk in jargon;
- the project team produces prestigious reports (a reporting machine, rather than an action team);
- you are writing letters to the consultants;
- 'terms of reference creep' is beginning to become an epidemic; and
- you see the consultants as contractors performing a task you could do better if you had the time.

Beware of managers who suddenly fall out with the consultant; the best action in the first instance is to organise some conflict resolution. Often a perception rather than facts may be the root cause of the problem.

Finally, celebrate the finish. I am a great believer in celebrating the completion of a project; just don't forget to invite the consultants to the party.

NEXT STEPS

- Read the book *The Definitive Drucker* by Elizabeth Haas Edersheim; it will help you understand the master and help with all your work as well as consultant based projects.
- Celebrate every success the project has, no matter how small; it will create an impetus.
- Remember the rule of three when assessing how long you will need the key consultants.
- Put more time into the selection of the consultants and reap the benefits.

David Parmenter is a speaker and author of books including ***The Leading-Edge Manager's Guide to Success*** and ***Key Performance Indicators***
davidparmenter.com

Fair value accounting – are you ready?

UK GAAP adopters will be hearing a lot more about fair value accounting says **Eddy James**

You're probably aware by now that a new UK reporting regime will be effective from 1 January 2015 with nearly all existing SSAPs, FRSs and UITF abstracts being replaced in one fell swoop by a single comprehensive standard based on the IASB's IFRS for SMEs. This new standard is FRS 102 *The Reporting Standard Applicable in the UK and Republic of Ireland*. And it contains no less than 485 references to fair value.

DON'T PANIC

But let's not panic yet. While many entities will be affected in some way by the new requirements relating to fair values, some simple businesses will find that little – or nothing – will change. This article should help you determine the potential impact on your business.

You may already be measuring some of your assets and liabilities at fair value under current UK GAAP. For example, if you own investment properties, they must be measured at open market value at each balance sheet date. You may also be electing to revalue certain fixed assets, typically property, to open market value at regular intervals. While it is likely you will want to continue revaluing such items under the new regime, care will be needed in order to ensure your existing methodologies for measuring the fair value of such items accord with the requirements of the new standard. FRS 102 provides not only a definition of fair value but also guidance on how to calculate it. If you're familiar with the equivalent IFRS requirements, you'll have come across this fair value hierarchy before. If you're not, you should familiarise yourself with it.

Perhaps more significantly, other items will have to be measured at fair value for the first time. For example, FRS 102 requires derivatives such as forward contracts or interest rate swaps – which are typically off-balance under current UK GAAP – to be recognised and measured at their fair value. The new standard also requires many of the intangibles that are currently subsumed within the goodwill arising on business combinations to be recognised separately for the first time. These will also be measured at fair value. And while any current or fixed asset investments in shares are already on-balance sheet, they are typically measured at cost but will in future have to be measured at fair value wherever it can be measured reliably. In all of these cases, the required calculations can be complicated and potentially costly, so it is important to plan ahead.

FRS 102 also includes a number of options that enable you to measure other items at fair value, for example investments in subsidiaries, associates and joint ventures may now be measured in this way in the parent's stand-alone financial statements. If you get involved in hedge accounting you may also find that all kinds of other things unexpectedly end up being measured at fair value.

PLANNING AHEAD

You need to identify which items you'll be measuring at fair value in the future. This may involve making some accounting policy choices. You'll then need to work out how you are going to get hold of those fair values. In some cases you may need to employ a valuation expert. In others you may need to act sooner rather than later to avoid complications and added costs further down the line, particularly when it comes to establishing the fair values of any derivatives you hold at your date of transition to the new regime (which will be 1 January 2014 for many entities). And don't forget that your last set of financial statements under the old regime will have to be restated to create the comparative information that needs to be disclosed the first time you apply the new regime, so again you may need to act on a timely basis to capture all the relevant fair values.

The key, as ever, is planning ahead. The Financial Reporting Faculty is here to help. Our wide range of resources is designed to make transition as painless as possible. You can find out more at **icaew.com/newukgaap**

Eddy James FCA is a technical manager in the Financial Reporting Faculty

From the faculties

Keep in touch with our selection from ICAEW's other faculty magazines

FS FOCUS
EYES FRONT

Investors are increasingly looking for evidence that insurers and their auditors consider future risks, with emphasis on avoiding boilerplate statements and providing insight into business and strategic models. So how can you provide meaningful forward-looking information?

In this article John Perry, a partner in the financial services division at PKF Littlejohn, shares his advice. Key, he says, is for auditors and insurers to develop clear and relevant disclosures about risks.

"Preparers of financial statements need to aim for clear disclosures and remove clutter. Auditors have a role in driving forward a transparent disclosure," he explains.

Looking at recent developments, Perry points to Lord Sharman's report from last year, outlining recommendations for a broad-based assessment of whether an entity is a going concern, which included solvency and liquidity risks.

The increased use of forward-looking information brings with it a culture change for the auditing profession, which traditionally has taken a so-called 'rear-view mirror' approach. They will see a shift from reporting on going concern to a more 'eyes front approach'. As Perry says: "simply going though the motions will not be good enough."

For more from the Financial Sevices Faculty, visit icaew.com/fsf

CORPORATE FINANCIER
THE SPECIAL RELATIONSHIP

Cultural and political differences aside, the link between the UK and the US is often referred to as "the special relationship" and when it comes to M&A it is certainly the case. Over the five years 2008 to 2012, US acquisitions of UK companies amounted to $151bn, according to recent figures. UK companies made just under $140bn of US acquisitions in the same period – quite impressive given the relative GDPs of the two countries.

From Kraft taking over Cadbury, to HP paying a cool (and widely believed to be excessive) $10bn for UK tech firm Autonomy, recent years have seen some big deals.

Analysts at Société Générale say conditions for the relationship are positive. The notion that to force growth, companies need to move into emerging markets is not necessarily true. Assets in the UK are just as attractive and less risky than those in emerging markets, they say. Investors agree: "American trade buyers see the UK as a steady market," says Martin Mendelssohn, corporate finance partner at CMS Cameron McKenna. The fact that the UK is a handy launch pad into Europe helps.

And it works both ways. As the US economy regains stability and control, UK companies will see opportunities, especially in the technology sector.

For more from the Corporate Finance Faculty, visit icaew.com/cff

CHARTECH
CYBER SECURITY – ANOTHER VIEW FROM THE TOP

How engaged should the board of a company be when it comes to cyber security? To what extent is this area reserved for the experts in the IT department? These are just two of the questions that the IT Faculty tried to answer during the second in its series of roundtables addressing cyber security.

The session, attended by FTSE board members including former CEO of BT and incoming trade minister Ian Livingston, concluded that the board should be involved in this. "If cyber is not discussed in the board room you are exposing yourself and your company," says Livingston.

Often pigeon-holed as an IT domain, cyber extends to all departments and all the way to board level. The reality is that cyber attacks affect all areas of a business so it is the responsibility of everyone on the board – especially as the methods of attack are becoming increasingly sophisticated.

The concluding advice to the board from the session was to ask questions and dig into what is happening on the ground in your firm; carry out regular simulations of 'what if...' scenarios; and share information across the industry you're in. Finally, focus on abnormalities and peaks in performance – businesses are not managed on averages, so identify and report near misses and abnormal activities.

For more from the Information Technology Faculty, visit icaew.com/itfac

Technical updates

Our regular round-up of legal and regulatory change

TAX

News and updates from the Tax Faculty weekly newswire. Subscribe free: visit ion.icaew.com/TaxFaculty and click the sign-up link on the right.

AUTO-ENROLMENT DEADLINES APPROACH FOR SMALLER EMPLOYERS

The government has introduced a new law designed to help people save more for their retirement. It requires all employers to enrol eligible workers into a workplace pension scheme if they are not already in one.

Known as automatic enrolment, or 'auto-enrolment', this started being phased in from October 2012 for the larger employers initially, but will affect all employers by 2018. The deadlines are now approaching for SME employers, and the Pensions Regulator is encouraging employers to create a plan (bit.ly/12x2ftX), as it will take time and money to implement.

An employer will have to enrol anyone into a workplace pension if all of the following apply:

- they are not already in a suitable workplace pension scheme;
- they are at least 22 years old, but under state pension age (for details, see the guide state pensions) (bit.ly/17xWUrO);
- they earn more than £9,440 a year (tax year 2013/14); and
- they work in the UK.

Employers with 500 employees had to auto-enrol their employees by 1 November 2013. Those with 350 employees will have to do so by 1 January 2014 and those with 250 employees by 1 February 2014.

Exactly what employers need to do depends on the ages and earnings of their staff on their staging date (bit.ly/1elGzYX), but note that all employers are required to register with the Pensions Regulator within four months of their staging date. There is also a tool on the Pensions Regulator's website to help employers work out exactly when their staging date is (bit.ly/tDZs2n).

The law has set a minimum level for employer contributions to be paid for staff who opt in. Eventually, the overall amount to be contributed to each individual's pension pot will be a minimum of 8% as follows:

- 3% by the employer (more if they wish); and
- the balance by the individual member of staff, who will get tax relief on their payment.
- the minimum contribution levels are, however, being phased in over six years, building up to the full 8% by 1 October 2018.

There will be other costs for the employer in addition to the contribution, such as implementation costs – including information for employees – and the pension scheme's annual management fees and administrative charges.

There is a fixed penalty of £400 for non-compliance, but daily penalties, based on the number of employees, will soon mount up for employers who fail to act on time.

SEED ENTERPRISE INVESTMENT SCHEME

Updated guidance reflects extension of CGT relief to 2013/14 and revised independence conditions for off-the-shelf companies. HMRC's SEIS guidance has been updated to include details of the extension to 2013/14 of capital gains tax reinvestment relief at half the rate (bit.ly/1cWFohY).

If you dispose of an asset that would give rise to a chargeable gain in 2013/14, and reinvest all or part of the amount of the gain in shares, which also qualify for SEIS income tax relief, half the amount reinvested may be exempted from CGT. Note capital gains reinvestment relief is also subject to the £100,000 annual investment limit which applies for income tax relief. For 2012/13, gains of up to £100,000 may be exempted and for 2013/14 up to £50,000.

The asset does not have to be disposed of first; the investment in SEIS shares can take place before the disposal of the asset, providing that both the disposal and investment take place in the same year.

The latest date for making a claim for 2012/13 is 31 January 2019 and, for 2013/14, 31 January 2020.

The SEIS guidance has also been revised to include details of the amendment to the independence condition for companies in respect of any on-the-shelf period (bit.ly/16sD2YK). For shares issued on or after 6 April 2013, any on-the-shelf period will be ignored when determining whether a company is or has been under the control of any other company.

'On-the-shelf period' means a period during which the company has not issued any shares other than subscriber shares, and has not yet begun or prepared to begin trading.

EMPLOYMENT LAW

This section is summarised from the bulletins of various law firms and associations – find out more at the web addresses supplied. None of the information in this update should be treated as legal advice.

HMRC TO INVESTIGATE FIRMS ADVERTISING FOR INTERNS

The government has announced an investigation into whether companies advertising for interns are paying the correct minimum wage. Employment relations minister, Jo Swinson, said that about 200 employers will be contacted by HMRC as part of an initiative to give interns more help and information to ensure they're paid for their work.

The Department for Business, Innovation and Skills will crack down on unfair practices from employers, and has released guidance for young people, in an effort to protect their legal right to fair play.

Already HMRC has issued penalties to 466 employers in 2013. Anyone considered a worker under the law should be paid at least the minimum wage, whether they are an intern, or someone on work experience.

THE CORRECT TEST FOR CONSTRUCTIVE DISMISSAL

The Employment Appeal Tribunal (EAT) has clarified the test for a constructive dismissal. An employee who leaves following a dispute with their employer will often claim that they have been constructively dismissed. However, to succeed in the claim the employee must show that they have resigned because of the employer's repudiatory breach of their contract - one that is so serious it brings the contract to an end. In reality there are usually many and varied reasons for an employee's decision to resign. Employers have often successfully argued that an employee has not been constructively dismissed because they have left for a reason other than the employer's breach, for example because they have found an alternative better paid job.

This may no longer be so straightforward for employers; following the recent case of *Wright v North Ayrshire Council*. In this case the Employment Tribunal rejected Ms Wright's claim of constructive dismissal on the basis that the employer's breach of contract was not the main or principle reason for her resignation. Instead the Tribunal decided the main reason was the fact that she could not combine her full-time role as a care assistant with her caring responsibilities for her partner, who had had a severe stroke.

The EAT has now confirmed it is only necessary for the employer's repudiatory breach to play a part in the employee's decision to resign - it is not necessary for the repudiatory breach to be the main or only reason for the resignation.

It is still open to employers to argue that employees have left because they have found another job and that their breach of contract has not played a part in the employee's decision to leave. However, it is difficult to see how this argument will succeed where the employee has been prompted to search for another job by their employer's breach of contract. The time between the breach of contract and the employee's resignation is likely to be key - the longer the gap the more likely the employer can argue the breach did not play a part in the decision to resign or that the employee has in fact accepted the breach.

FLEXIBLE WORKING FOR ALL

The government has confirmed it plans to extend the right to request flexible working to all employees from 2014. This means that the right will no longer be limited to parents and carers.

At the same time, it proposes to remove the current statutory procedures for considering requests for flexible working and replace it with a duty on employers to deal with requests in a "reasonable" manner and within a "reasonable" period of time. A new code of practice giving guidance on what this means will be produced by the Advisory, Conciliation and Arbitration Service and there will be a consultation on the draft code in due course. Acas will also produce guidance for employers on how to prioritise conflicting requests received at the same time, taking account of existing legislation.

Some things will stay the same. Employees will still need 26 weeks' continuous employment in order to make a flexible working request, and will not be able to make more than one

DON'T MISS OUR ESSENTIAL EMPLOYMENT WEBINAR

The Finance & Management Faculty is holding an employment law update webinar on 11 March 2014 at 10am.
Please see **icaew.com/fmfmarwebinar** to book a place.

request in any 12-month period. The government has also decided against exempting micro-businesses.

The government has also outlined proposals to introduce flexible parental leave, and a separate response has been issued on those proposals.

FINANCIAL PENALTIES FOR EMPLOYERS WHO LOSE EMPLOYMENT TRIBUNAL CLAIMS

The Enterprise and Regulatory Reform Act 2013 (ERRA), which received Royal Assent on 25 April 2013, includes a provision giving employment tribunals discretionary powers to levy financial penalties against employers who lose claims. This provision is not yet in force, but the government has now confirmed it will come into force on 6 April 2014.

Aside from the remedies that can be awarded, employment tribunals currently have no powers to penalise employers for breaches of employment law. This is due to change and from 6 April 2014 employment tribunals will be able to order employers to pay a financial penalty of between £100 to £5,000, where it loses a claim and where "aggravating features" are present. It will be up to the tribunal to define "aggravating features" and determine whether they are present.

Employment tribunals will be able to impose the penalty irrespective of the nature of the remedy awarded, although where a financial award is made the penalty must be 50% of that award (subject to the cap of £5,000). The employer's ability to pay the penalty must also be taken into account.

FINANCIAL REPORTING

You can find out more on the latest from the Financial Reporting Faculty, including UK GAAP and IFRS standards and consultations at icaew.com/frf

MICRO-ENTITIES

The Small Companies (Micro-Entities' Accounts) Regulations 2013 have now been laid before parliament and, at the time of writing, are awaiting approval.

As noted in the October edition of the financial reporting update, the regulations will introduce significant exemptions from the financial reporting requirements available to a new class of entity, the micro-entity.

The Financial Reporting Faculty is hosting a webinar on 12 December, which will outline the benefits and potential drawbacks of adopting this new regime.

More information is available at icaew.com/frfwebinars

NEW UK GAAP

The FRC has recently published FRED 51: Draft Amendments to FRS 102 – Hedge Accounting. FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* was published in March 2013 and will be mandatory for accounting periods beginning on or after 1 January 2015. At the time of publication, the FRC highlighted that it would review hedge accounting in the light of international developments.

The existing requirements, although relatively simple, are very prescriptive and may unduly restrict the application of hedge accounting.

The objective of the proposals is to make hedge accounting available for a wider range of hedging relationships. Comments are due by 14 February 2014.

The FRC has also published some editorial amendments and clarification statements. The issues addressed are:

- early application of FRS 102 by entities within the scope of a SORP;
- net investment hedges of foreign operations that are branches; and
- deferred tax arising on a business combination.

More information is available at frc.org.uk

WATCH OUT FOR GAAP

The new UK GAAP is just around the corner. Although 1 January 2015 may seem a long way away, comparative figures are required. So, for those with a 31 December year end, this year's balance sheet will form the basis of the transition balance sheet to the new regime as at 1 January 2014.

The Financial Reporting Faculty provides high quality, practical tools guiding members through the complex world of financial reporting, including substantial coverage of the new UK GAAP. Join the faculty from £110 and access all the factsheets and webinars at no extra cost.

For more information on the benefits of membership visit icaew.com/joinfrf

On a lighter note...

ROASTING WARS SUBSIDE

Last month, Starbucks Corp failed in its 12-year battle to prevent a small family-owned coffee shop from selling coffee under the name Charbucks, despite the self-described "Mom and Pop" business freely admitting that it chose the name in mockery of the multi-national.
The Appeal Court ruling said Black Bear Micro Roastery in New England, USA, may keep selling Charbucks Blend and Mister Charbucks coffee.

A centerpiece of Starbucks' case had been a phone survey of 600 people, which found that the first association of the name Charbucks is with the brand Starbucks. But the court found that the survey was "fundamentally flawed" and "reinforces the district court's finding that the marks are only minimally similar".

$12.95
For 1lb of Starbucks Caffe Verona

$12.32
For 1lb of Black Bear Mister Charbuck

BEARS ARE BIG BUSINESS

Unagi Travel in Tokyo celebrated taking its 200th stuffed animal on a city tour this autumn. The company, run by Sonoe Azuma, specialises in taking customer's stuffed animals on holiday and photographing them in front of famous landmarks. Tours cost from ¥2,000 (£13) per toy for a local tour, and the company now organises trips abroad. According to MSN, 40% of Azuma's business comes from repeat bookings, with bears snapping up further trips.

LEGALISED DRUG BRINGS FISCAL GAIN

While two states in the USA (Washington and Colorado) have legalised the sale of marijuana and several cities have legalised possession of small amounts of the narcotic, Colorado is the only one so far to appreciate the fiscal gain from the move.

Colorado coupled the decriminalisation move with levels of sales tax and duty determined by city jurisdictions themselves. The city of Denver, having agreed to licence marijuana sales, has voted in favour of taxes and duty of 29% and introduced fines of up to $2,000 for detectable atmospheric pollution of public air. The taxes alone are expected to raise $67m a year.

GOLD FLUSH

Assiduous cleaning staff alerted security when they found two metal lunch containers in the lavatory of a Jet Airways aeroplane in Kolkata, India. They were surprised to find 12 1kg bars of gold, about the size of a smart phone, in each of the tins.

The haul, valued at just over $1m, is thought to have originated in Dubai with the intention of avoiding the 10% import duty India imposed last year. Authorities are attempting to identify the owner.

SURVEY WINNER

Members will recall the Finance & Management Faculty survey conducted in October. We can announce that Robin Rumsam was the winner of £100 in John Lewis vouchers as a result of completing the survey. Look out for the survey results in the February edition of *Finance & Management*.

"I became an articled clerk in September 1966, which was a very good year for football, but perhaps not so good for the accountancy profession's new recruit. Now, a few years later, the profession has shown its gratitude...was it for long service? My thanks, especially to the Finance & Management Faculty for this munificent Christmas gift, which I promise to consume personally...Cheers!"

Robin Rumsam FCA,
FD Global Aware International, and faculty member since 2007

CORBIS