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Feedback

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FACULTY OF FINANCE AND MANAGEMENT

Formal notice of AGM

Wednesday June 13, 2001 • Chartered Accountants' Hall

The annual general meeting (AGM) will start at 12.30pm (approximately 15 minutes). The AGM follows the 9.00am-12.30pm lecture 'Post Acquisition Integration' – see page 11.
(AGM attendance is free)

February 2001 Issue 72

How to build a business without budgeting

The Faculty's May conference on 'Beyond Budgeting' tackles a hot new subject with some expert speakers.

"For success in the information age, managers need to create a climate for fast response," says Robin Fraser, a programme director of the CAM-I Beyond Budgeting Round Table (BBRT). "They also need to engage the best people, to generate new business concepts, to operate with low costs, to find and keep their best customers and to keep shareholders satisfied." Fraser will be one of three principal speakers at the Faculty's 25 May 'Beyond Budgeting' conference in London.

The case for reappraising business practice in light of such thinking will be thoroughly examined by Fraser together with Bruno Thalmann, a senior manager in Arthur Andersen, Switzerland, and David Berkeley, finance manager, at Bulmers.

The BBRT – a research project funded by over 55 companies since 1998 – has explored the Beyond Budgeting model, on the basis that many companies are using budgeting techniques more appropriate to the industrial age. Beyond Budgeting is now being applied in whole or in part by Scandinavian companies, such as Svenska Handelsbanken, Borealis , IKEA, Scandia, Volvo and Ericsson, with companies in the UK such as Diageo, Boots, and Bulmers, now following their lead. The model is based on 12 principles within two main themes:-

- *organisation and behaviour* – companies need to move towards a more devolved market-like network of units working within an agreed set of aims and values while allowing a high degree of local autonomy and freedom of action, in place of the traditional centrally controlled hierarchy working to achieve a predetermined plan; and
- *performance management* – companies need to adopt a set of performance management processes that are focused on beating the competition and that can adapt readily in unpredictable conditions, in place of the traditional set of processes focused on meeting a contract negotiated in advance and fixed for the year ahead.

Early surveys conducted by the BBRT (and collated and validated by Arthur Andersen) show that there is a statistically significant correlation between the Beyond Budgeting model and competitive success. Perhaps more surprisingly, the strongest success correlation was with the organisation and behavioural factors rather than performance management. This only serves to reinforce the view that Beyond Budgeting needs to be a twin-track programme progressing simultaneously along behavioural and measurement paths.

In this half-day conference, Fraser will explain why budgeting is a barrier to success in today's economy and what the alternatives are; Thalmann, leader of his firm's European Finance Business Solutions division, will outline the Beyond Budgeting survey findings; and David Berkeley will describe how Bulmers abandoned budgeting to create a new emphasis on strategy at every level in the company, which, he says, has made a significant difference to the company's success.

See Page 11 for further details about this and other Faculty events.

The changing role of the finance director

How has the finance director's role changed over the past 25 years? By analysing job advertisements in the *Financial Times* from 1974 to 1998, Bristol Business School's **Roger Hussey,** assisted by Monika Sowinska, has produced a unique insight into the evolution of the job specification. Helen Fearnley reports.

In evaluating the changing role of the finance director over the past 25 years, Roger Hussey and Monika Sowinska of Bristol Business School considered not only the specific responsibilities of the job, but also the knowledge, experience, and personal characteristics finance directors are expected to demonstrate. They based their findings on over 2,000 *Financial Times* job advertisements, over the period 1974 to 1998.

Their key findings included that:

- the upper boundary for jobs advertised has risen considerably – from an inflation-adjusted £59,000 mode in 1974 to £80,000 in 1998;
- since the early nineties, the qualification required is increasingly that of graduate qualified accountant rather than simply qualified accountant;
- ageism is on the wane, with advertisements less likely to specify age;
- the number of jobs advertised has increased, after a substantial decrease in the late1980s;
- plcs advertise most frequently (though 1998 saw a large surge in recruitment by public sector bodies);
- the most stipulated job responsibilities are financial accounting/reporting, management accounting, finance/funding and (increasingly) strategic planning;
- information technology skills have grown in importance, now featuring in some 30% of advertisements;
- a stated responsibility for investor relations has increasingly appeared in advertisements since 1992;
- other responsibilities, such as corporate governance, legal/regulatory, taxation and treasury, have appeared relatively infrequently across the 25-year period; and
- advertisements nowadays place far greater emphasis on personal skills, with 94.1% doing so in 1998, against 33.3% in 1974.

FIGURE 1 SALARIES OFFERED

% of advertisements

Salary	1974	1976	1986	1996	1998
Under £10,000	56.7	34.1	–	–	–
£10,000 - £20,000	23.4	43.9	4.6	–	–
£20,000 - £40,000	–	–	73.5	3.1	5.6
£40,000 - £60,000	–	–	6.0	45.8	38.9
£60,000 - £80,000	–	–	0.5	20.9	37.4
£80,000 - £100,000	–	–	–	13.4	3.7
Over £100,000	–	–	–	4.4	4.8
Not specified	19.9	22.0	15.4	12.4	9.6

The changing environment 1974-1998

As Hussey and Sowinska acknowledge, it would be spurious to try to analyse the changing role of finance directors without considering the environment in which they operate. Economic climate and legal changes could be expected to have an influence. They therefore tabulate both the annual inflation rate and the number of accounting standards issued in the UK, for each year over the period. Surprisingly enough, this reveals the flow of new standards to be, as they say, modest; some years being untroubled by regulatory intervention. The most frequently occurring number of standards issued in a year over that period is a tie between one and two.

Other major events, also tabulated, include three Companies Acts (1981, 1985, 1989), the Financial Reporting Standard for Smaller Entities (1995), and the reports emanating from the various committees looking at corporate governance issues – Cadbury (1982), Greenbury (1995), and Hempel (1998).

What was required of a finance director, then and now?

The report identifies certain changes, over time, in the characteristics and skills stipulated in advertisements for finance directors.

Age – now less of an issue

For a start, age – or rather, youth – appears to be becoming less important. In 1974 half the advertisements required someone under 45, with one third of that (ie 16.7%) actually having a 40 years upper limit and another third (16.6%) stipulating 'under 35 years'. Another third of the 1974 ads did not specify age. By 1998, however, only 9.7% of the advertisements had an upper age limit of 45 years or less, and 89.6% gave no age limit.

Qualifications – graduates preferred

Interestingly, the prestigious MBA qualification did not feature at all as a stand-alone requirement in the advertisements studied. However, the specification of 'qualified accountant with MBA' seemed to enjoy a limited, and brief, popularity in 1996 (2.2% of advertisements).

The simple specification 'chartered accountant', declined dramatically over the period (from 30% of ads in 1974 to 1.1% in 1998). However, this apparent lack of desirability may be to do with the potential confusion intrinsic in specifying 'chartered' once bodies other than the ICAEW had acquired charter status. Certainly this fall off has been matched by the combined growth in advertisements for 'qualified accountant' (33.4% in 1974, 45.6% in 1998) plus those for 'graduate and qualified accountant' (up from 3.3% to 22.2% over the same period).

FIGURE 2 RESPONSIBILITIES OF THE POST

% of advertisements

Responsibility	1974	1976	1986	1996	1998
Administration	26.7	12.2	17.4	11.1	13.3
All accounting functions	30.0	39.0	13.8	20.4	2.2
Corporate governance	–	–	2.3	8.9	3.0
Finance/funding	56.7	70.7	45.9	63.1	43.7
Financial accounting/reporting	40.0	43.9	36.7	68.0	60.4
Internal audit	–	–	0.5	0.9	6.3
Investor relations	–	2.4	11.9	19.1	18.8
Information technology	6.7	19.5	32.6	38.7	34.4
Legal/regulatory	–	7.3	1.4	5.8	4.4
Management accounting	26.7	36.6	51.4	72.0	51.9
Mergers	16.7	2.4	16.5	16.0	8.5
Overseas operations	20.0	12.2	6.0	13.3	3.7
Personnel	13.3	9.8	6.4	21.3	3.7
Strategic planning	26.7	43.9	40.4	55.6	60.0
Taxation	–	2.4	4.1	8.0	3.0
Treasury	–	–	5.0	8.9	2.6

Salary – little changed in real terms

The unadjusted figures for salaries quoted in advertisements over the period (see Figure 1 on page 3) provide a staggering example of the effect of inflation.

More than half the advertisements in 1974 specified a salary of less than £10,000, and less than a quarter quoted the only other (higher) band of £10,000 to £20,000, the rest of the advertisements not specifying salary. But by 1986 under £10,000 had been abandoned as a realistic offer, and the £10,000 to £20,000 range featured only in 4.6% of advertisements, with £20,000 to £40,000 being easily the most frequently quoted salary. By 1996 the most featured range was £40,000 to £60,000, with the next most common band being £60,000 to £80,000 (20.9%). And by 1998 there were almost as many jobs advertised for £60,000 to £80,000 (37.4%) as for £40,000 to £60,000 (38.9%).

However, it should be remembered that £10,000 at 1974 prices is equivalent to £59,000 in 1998 – so the upper salary limit for the most frequently advertised category of salary, is more or less unchanged in real terms.

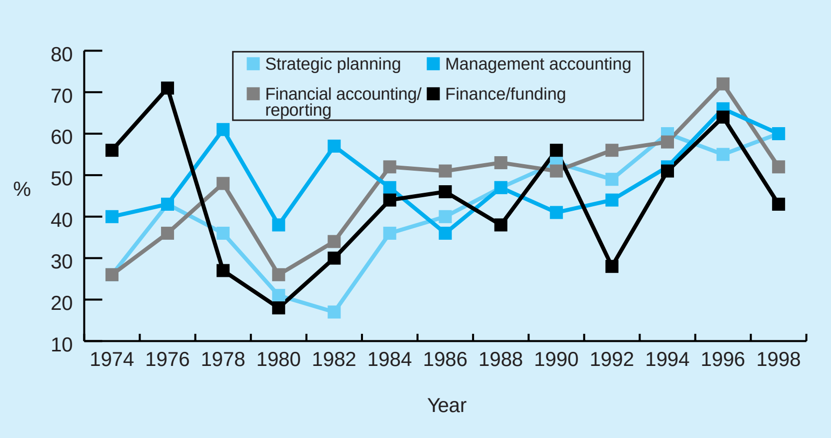
Role description – strategic planning gains ground

Most of the advertisements specified certain responsibilities attached to the role advertised, with financial accounting/reporting, finance/funding, and management accounting remaining very important elements throughout the period.

However, other features have also became relevant (see Figure 2). IT has gained ground and has now settled into a pattern of appearing in roughly one third of advertisements, and investor relations has similarly grown in importance, now featuring in just under a fifth of advertisements.

Even more striking has been the importance of strategic planning. Already significant in 1974 (26.7% of advertisements), the frequency of appearance of this responsibility grew steadily until in 1998 it featured in 60% of the jobs advertised – neck and neck with financial accounting/reporting (60.4%), and well ahead of finance/funding (43.7%) and management accounting (51.9%).

FIGURE 3 THE FOUR MAIN RESPONSIBILITIES



For the four main responsibilities quoted, the 25-year span has shown mixed fortunes (see Figure 3). From the late 1970s to the early 1980s they experienced a decrease in importance, followed by a somewhat erratic return to previous levels. As is evident, finance/funding is the most variable in terms of requirement as a responsibility. Strategic planning continues on a broadly upward trend.

Experience/technical knowledge/personal attributes

Looking at the various qualities specified for potential finance directors, for ease of analysis the researchers divided the various attributes mentioned in advertisements into three categories: experience, technical knowledge, and personal attributes.

Hence board experience, international exposure, and investor relations all come under the 'experience' categorisation; accountancy training and understanding of regulatory matters count as 'technical knowledge'; and communication skills, flexibility and ambition rate as 'personal attributes'.

Figure 4 (on page 6), where each entry on the graph represents the percentage of advertisements in a given year which stated a requirement for a quality within the given category at least once, shows the trend in demand for different qualities. Over the 25 years, technical knowledge showed no significant long-term trend, despite gaining in popularity in the 1990s. Previous experience, required by almost all the advertisements in 1974, declined slightly in the late 1980s, recovering later.

However, as the figure shows, between 1974 and 1998 there has been a huge rise – from 30% to 90% – in the percentage of advertisements requiring specific personal attributes.

Looking at each of the three categories in more depth is also illuminating.

Technical knowledge

Surprisingly, in all of the years studied except 1996, more than half of the advertisements did not specify the technical knowledge required for the job. Presumably the advertisers took it as read that an applicant for a job at this level of seniority would have the requisite technical knowledge.

The frequency of a specification for technical knowledge of financial accounting/reporting varied greatly over the period, appearing in a third of advertisements in 1974 and 1996, but in far fewer of those in the intervening years, and at a low of only 10% in 1998. Knowledge of corporate governance and tax also did not appear to be of major importance.

Oddly enough, of the elements of technical knowledge mentioned in advertisements – ie corporate governance, financial accounting, IT/EDP, languages, management accounting, taxation, and technical skills – all but taxation showed a significantly increased incidence in 1996, over all other years.

Experience

Experience of the specific industry was a common requirement in advertisements over the 25 years, appearing in more than half of them in 1974, rising to three quarters in 1998.

Board level experience has become increasingly important, specified in only one sixth of advertisements in 1974, but more than half in 1998.

On the other hand, the importance of general commercial experience has plummeted (occurring in 30% of 1974 advertisements but less than 2% of those in 1998), as has experience on international practices.

Personal attributes

Up until 1976, between two thirds and three quarters of advertisements did not specify any personal attributes for the job. However, this subsequently changed markedly, to the extent that fewer than 5% of 1998 advertisements omitted to mention preferred personal attributes.

Interpersonal/communication skills and business acumen/commercial awareness have become much more critical in recent years. Both these qualities appeared in more than a third of advertisements in 1986 (respectively 12 and 3.5 times the frequency of their appearances in 1974) and by 1998 were stipulated in 71.5% and 51.1% of advertisements.

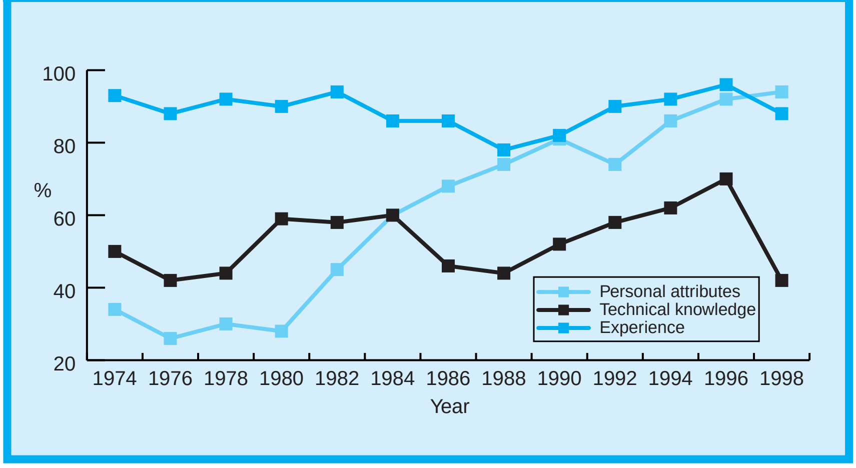
Management/leadership skills have also become much more important to recruiters in the second half of the period studied, almost trebling from featuring in 18.3% of advertisements in 1986 to 53% of 1998 advertisements. And after a relatively modest debut in 1986, by 1998 there was significant emphasis on the ability to be a team worker (25.2%) and a strategic thinker (28.5%).

Interestingly, in 1996 – the year in which specifications of technical knowledge peaked (see above) – the personal attributes most in demand were those of the ambitious, analytical, energetic yet mature candidate. All four of those personal attributes peaked, for frequency of mention, in that year.

Conclusion

As the report reveals, there have been dramatic changes in the past 25 years in the qualities expected of a finance director. Previous experience remains important, but there is now growing emphasis on personal attributes such

FIGURE 4 THE TREND OF THE MAIN CATEGORIES



as communication and leadership abilities. And although technical knowledge is specified less frequently now in advertisements, it seems fair to assume that companies simply consider that requirement is implicit in the job level advertised. However, board level and industry specific knowledge are paramount in the majority of advertisements recently placed.

The demand for the previously revered authoritarian-style finance director, displaying gravitas and maturity (qualities featured in only 3% of 1998 advertisements) has waned. Instead, in a trend which appears to have started in the early 1980s, the current dream candidate is someone who has interpersonal and leadership skills and, increasingly, someone who is capable of strategic thinking.

This research was funded by accountants Deloitte & Touche, and carried out by Roger Hussey, Deloitte & Touche professor of financial communication at the Bristol Business School, assisted by Monika Sowinska. The report can be downloaded from the Deloitte & Touche website at www.deloitte.co.uk

Roger Hussey left the Bristol Business School at the end of the last academic year, although he retains links as its visiting professor of financial communications. He is now dean of the Faculty of Business at the University of Windsor, Ontario, Canada.

ABSTRACTS FROM LIBCAT

Kaplan R S – Having trouble with your strategy? Then map it
Harvard Business Review, Vol.78. No.5. September/October 2000: p167-176 (10 pages)
● *The key to executing your strategy is to have people in your organisation understand it – including the crucial but perplexing processes by which intangible assets will be converted into tangible outcomes. Until now, there haven't been many tools that can communicate both an organisation's strategy and the processes and systems needed to implement that strategy. But the authors, co-creators of the balanced scorecard, have adapted that seminal tool to create strategy maps. These let an organisation describe and illustrate its objectives, initiatives, targets markets, performance measures, and the links between all the pieces of its strategy. Using Mobil North American Marketing and Refining Company as an example the authors walk through the creation of a strategy map and its four distinct regions – financial, customer, internal process, and learning and growth – which correspond to the four perspectives of the balanced scorecard.*

Classe A – Networked know how
CA (ICAS), Vol.104. No.1130. September 2000: p30-34 (4 pages)
● *The ability to make specialist knowledge available throughout a whole organisation creates exciting strategic possibilities. The author looks at what's available and, especially, how knowledge management is being applied in professional services.*

Edwards J – Promoting your services to high net worth individuals
Tax Adviser, December 2000: p36-38 (3 pages)
● *While many firms may readily undertake mass marketing campaigns, for high net worth individuals you need to take a 'one to one' marketing approach. This article looks at how to plan a marketing campaign to high net worth individuals and breaks down the various elements of the campaign*

Dahl H – A new breed
Computers and Finance, No.36. October 2000: p24-28 (3 pages)
● *Finance directors of dot coms are breaking the mould. Ever younger, they thrive on the workload, long hours and risks, and are technology-savvy. But is the job really that different from the old finance role?*

Lucas E – Creating a give-and-take culture
Professional Manager, May 2000: p10-13 (4 pages)
● *The hi-tech mechanisms exist to enable knowledge to be shared across organisations, but how do you get people to share? That's the million-dollar question that managers across industry are currently trying to address. The author goes in search of some answers.*

http://www.icaew.co.uk/library.htm

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Oh, the financier and the marketeer should be friends...

Closing the gap of understanding between the finance and the marketing departments is proving to be a hard task – as the recent survey from the IPA showed. IPA president **Rupert Howell** wishes things could be different. We report the findings.

Three years after its first survey into UK finance directors' attitudes to marketing, the Institute of Practitioners in Advertising's follow-up study – Finance Directors 2000 – shows depressingly slow progress in forging closer links between the two disciplines. Now the IPA says it is even more determined to bridge the gap.

Rupert Howell, president of the IPA, is quite candid about the disappointing findings – "I wish I could say that things have got better and that the relationship between finance and marketing has got closer, with greater mutual respect between, and understanding of, each other's disciplines. Sadly I can't."

The report itself tells the story. It was conducted with four objectives:

1. to test finance directors' attitudes to – and levels of involvement in – setting, monitoring, and reporting on marketing expenditure;
2. to ascertain the perceived importance and value of marketing expenditure relative to other intangible expenditures, eg research and development, training, information technology and human resources;
3. to explore the perceptions of marketing department accountability; and
4. to benchmark these findings against those from the previous survey, and against those of marketing directors in similar organisations.

The sample, as for the previous survey, was randomly selected from the Times Top 1000 companies. Overall 100 finance directors and 100 marketing directors were successfully interviewed by telephone by NOP Corporate and Financial (also responsible for the first survey). And, for 26 companies within the sample, both the finance and marketing directors were interviewed.

The Finance Director 2000 findings

Although on the whole disappointing, the latest findings showed some significant changes, and unearthed several revealing differences in attitude between the finance and marketing directors. The findings included:

- *An expectation of greater accountabilty*

Arguably the most significant such shift is that expectations of marketing accountability have been raised significantly (see Figure 1), to the extent that accountability is now regarded as the most important attribute for senior marketing personnel, whereas previously it was viewed as the least.

This, Howell claims, must in part be attributable to efforts made by the IPA and others to promote accountability best practice, and to demonstrate the generic case for advertising investment. However, the survey also shows that not all the theory has been turned into practice – that there is now more industry learning available which has yet to be applied to the budget, objectives and measurement setting process.

FINANCE DIRECTORS SURVEY 2000

FIGURE 1 **Rate the following attributes in terms of their importance for senior marketing personnel:**

	(+2=high/-2=low) 1999	(1996)
Accountability	+1.65	+0.73
Willingness to measure marketing effectiveness	+1.49	+0.79
Ability to measure marketing effectiveness	+1.36	+0.94
Ability to justify marketing/advertising expenditure	+1.24	+0.92
Financial literacy	+0.99	+1.14

FIGURE 3 **In general, to what extent do you feel finance directors truly appreciate the difficulties involved in measuring effectiveness of marketing spend?**

Doesn't appreciate at all	1	2	3	4	5	6	7	8	9	10	*Appreciates fully*
MD 1999 (%):	6	2	9	18	18	10	18	11	3	2	

Don't know: 3 Mean score: 5.36

FIGURE 2 **Which criteria are set by your marketing department to set measurable marketing objectives?**

	FD (%) 1999	FD (%) (1996)	MD (%) 1999
Sales volume	57	62	60
Market share	26	36	18
Profitablity	7	30	29
Customer satisfaction	15	18	26
Awareness levels	35	16	41
Media/PR coverage	9	15	4
Adherence to budget	2	13	8
Brand image	11	13	4
Cost per lead	11	5	9
Market research	13	–	7

A move towards softer measures of marketing effectiveness

The survey revealed that marketing measurement is moving away from the harder till-ringing measures of sales volume, market share and profitability to softer measures such as awareness (Figure 2). This suggests a greater understanding of marketing complexity, but the link to return on investment is apparently not being made or communicated effectively.

Thus, one third of finance directors think their companies have no measure of marketing in place, which in turn limits marketing's relative priority for long-term investment and its protection for short-term budgets. For their part, 75% of marketing directors find measuring marketing effects difficult, and believe their finance directors do not appreciate the difficulties.

Lack of designated marketing director responsibility at board room level

Responsibility for reporting on marketing issues is, in the majority of companies surveyed, given to a non-marketing director (Figure 4). Hence there is scope for a breakdown in communication on marketing.

Fast turnover of marketing staff

Another drawback for marketing in trying to demonstrate its long-term importance is the relatively fast turnover of staff – itself limiting the extent of consistent, long-term measures of marketing effect.

Marketing's financial literacy rating improved

On a more positive note, finance directors' opinion of marketing directors financial literacy has improved. In the previous survey FDs saw marketing directors' financial literacy as a relative weakness (giving it the lowest rating in a set of five possible attributes). This time, financial literacy moved up a place, but unfortunately the all-important ability to measure marketing effectiveness replaced it as marketings weakest skill (Figure 5).

Finance directors' brand literacy weak

Unfortunately, the improvement in marketing directors' financial literacy is not matched by a commensurate improvement in FDs' brand literacy. The largest segment of respondent FDs, while not disagreeing with the statement that 'brands are important', rated that concurrence as 'slightly agree', whereas the majority of marketing directors concurred in the 'strongly agree' category (Figure 6).

Agreement on importance of the internet

However, both sets of respondents agreed on the importance of the internet as a business tool, and the requirement of IT related marketing opportunities for future growth. The drivers for this, they agreed, are the relative capacity of the internet as a marketing tool covering communications and distribution, as well as its inherent capacity for accountability.

Increase in zero budgeting

There has been an increase in first principles-based zero budgeting, which presents marketing agencies with the opportunity to bring client-specific and industry-based benchmarks to the fore in the planning process (Figure 7).

An action plan

Although the survey does not make comforting reading on the subject of mutual understanding, it has galvanised the marketing industry to form an action plan. As Howell puts it, "if finance directors fail to appreciate the value of brands, we in the marketing community should be trying harder to make them do so, and in a language they can understand".

As he goes on to explain, this marketing community is determined to make the claim for a seat at the top table of UK plc's boardrooms. To that end, its proposition is very simple: the belief that it is crucial that CEOs ensure three key things are done in terms of monitoring the true health of their businesses. These are:

- measuring the key marketing metrics;
- reviewing them regularly at executive board level; and
- presenting them in the annual report and accounts.

Howell concludes that, if every one of the UK's top companies had achieved this by 2001, "they would find themselves in better competitive shape and more able to deal with the e-revolution we all face".

Finance Directors Survey 2000 is published by the IPA in association with KPMG and the Financial Times, price £10. For copies, contact Wendy Tanner, tel: 020 7235 7020; email: wendy@ipa.co.uk

FINANCE DIRECTORS SURVEY 2000

FIGURE 4 **Who, if anyone, on your board is responsible for reporting on marketing and its effectiveness?**

	FD (%) 1999	FD (%) (1996)	MD (%) 1999
Marketing director	20	22	39
Managing director	18	9	15
CEO	18	17	8
Sales director	9	2	4
Operations director	2	7	1
Finance director	2	2	4

FIGURE 5 **Give your opinion of senior marketing personnel and the following attributes:**

	(10=high/1=low) 1999	(1996)
Ability to measure marketing effectiveness	5.40	5.71
Financial literacy	5.66	5.22
Ability to justify marketing/advertising expenditure	5.67	6.10
Willingness to measure marketing objectives	5.70	6.11
Accountability	5.80	6.35

FIGURE 6 **To what extent do you agree with the statement 'apart from people, brands are the most important assets which any company can enjoy'?**

	MD (%) 1999	FD (%) 1999
Strongly agree	82	71
Slightly agree	10	22
Neither agree nor disagree	1	1
Slightly agree	5	5
Strongly agree	1	–
Don't know	1	1

FIGURE 7 **What approaches or methods are typically used when setting marketing and advertising budgets?**

	FD (%) 1999	FD (%) (1996)	MD (%) 1999
Zero budgeting	56	48	41
Percentage increase over previous year	9	16	24
Percentage of last years' turnover	11	9	17
Based on the project to carry out	6	–	5
Based on central plan/strategy	5	8	3

MARKETING **UPDATE**

The search for a common language

In his first Marketing Update column for *Finance & Management* (and given the IPA report's depressing findings on the subject – see page 7) specialist marketing writer **Alan Mitchell** takes his own look at the need for – and obstacles to – better communication between finance and marketing.

Alan Mitchell writes extensively on marketing and finance, and is a former editor of Marketing *magazine.*

Whenever accountants and marketeers meet, the need for a common language to unite them crops up. Marketeers nowadays are continually exhorted to prove their effectiveness in financial terms; to embrace the cause of accountability. Latest example: a new campaign by the Chartered Institute of Marketing journal *Marketing Business*.

But don't hold your breath. Even with the best will in the world the two sides will still struggle to see eye to eye. For a very good reason. Yes, its true, marketeers could brush up on their financial skills. But that doesn't mean the questions they raise are easy to answer.

Artistic endeavours, advertisements, brands...how do you measure value realised in people's heads?

What's the most important thing to measure, for example? If you are making a widget, there is a direct correlation between the costs of production and how much you can sell it for. But when you are dealing with the fruits of creativity and innovation with forms of value that are realised in people's heads this direct link between input costs and output value begins to dissolve. There is no known correlation between the costs of producing a Hollywood movie and its box office success, for example.

Likewise, a crucial element of advertising effectiveness is its creative content. In both cases, traditional input cost-based decision-making processes can miss the point. Or take brand valuation. Accountants' insistence that a balance sheet item must be separately identifiable is reminiscent of the ancient mind/body debate. Mind and body may be conceptually distinct, but no one can agree as to where body ends and mind begins. Does that mean we should only give one a value, and not the other?

The shortcomings of finance's analytical tradition

The obsession with separately identifiable assets is the product of an analytical tradition, which assumes that the way to understand something is by breaking it down into its constituent parts. As a methodology, it's incredibly powerful. But it misses those qualities that arise as a result of interactions between those separate parts. You can't understand or predict a beast's behaviour in real life by dissecting its body, for example.

The notion of goodwill is a product of the analytical tradition. It assumes that extra value is somehow mysteriously created over and above the value of (separately identifiable) tangible assets. In truth, that value was always there – the product of the interaction between different parts. But analytical measurement techniques have always been blind to them.

Brands are a *cause célèbre* because they combine disconcerting philosophical doubts like these in a mind-bending tangle. While products are made in factories via processes that you control and assets that you own, brands are made at least in part in people's heads.

Like beauty, the value of a brand is partly in the eye of the beholder: the customer. And its value lies at least in part out there, beyond the legal and administrative boundaries of the firm in the relationship between the company and its customers. Such relationship value cannot be fully owned or controlled by the firm. It just doesn't fit traditional stewardship reporting.

Changes in the way incremental value is created in modern economies

Of course, there are huge benefits in marketeers adopting the mantle of measurement and accountability. Rigorous measurement and learning are inseparable; the key to continuous improvement. But at a deeper level the quest for a common language reflects changes in the way incremental value is created in modern economies. Increasingly, it comes from people qualities such as their ability to innovate and motivate, to be flexible, and so on.

Traditional accounting frameworks were not invented to measure the value of people qualities. Suggestions like the one made recently by International Accounting Standards Committee secretary general Sir Bryan Carsberg that companies should be allowed to put more qualitative narrative in financial statements to explain their changing prospects reflect the profession's struggle to come to terms with this fact.

FINANCIAL REPORTING

UPDATE

The thorny issue of retirement benefits

In his latest Financial Reporting Update column, **David Chopping** of Moore Stephens looks at the controversial new accounting standard FRS 17, which deals with retirement benefits, and pinpoints the changes.

David Chopping is the technical partner of Moore Stephens, London. He is a member of the technical and practical auditing committee of the Audit and Assurance Faculty.

FRS 17 is a replacement for SSAP 24, the current standard on accounting for pensions. It also replaces two Urgent Issue Task Forces (UITFs) which deal with pension related issues.

The approach of FRS 17 is a departure from that of its predecessor. While both standards deal with defined contribution pension schemes in the same way, they differ markedly when it comes to dealing with defined benefit pension schemes.

Both standards charge the normal costs of having a pension scheme to the profit and loss account, but show significant differences in the manner in which this amount is calculated. In particular, SSAP 24 really only had one element of normal cost. FRS 17 has a current service cost, but also has the ongoing effect of the expected return on assets and the interest cost, amounts that will normally be provided by the actuary.

However, the main difference arises when there is an actuarial valuation, both in how this is calculated and in how it is treated. SSAP 24 gave actuaries a fairly free hand in determining a surplus or deficit for accounting purposes. It did not impose any particular method of valuation, and did not dictate the assumptions that should be used. It did, however, require that the assumptions made were disclosed. FRS 17, on the other hand, is far more prescriptive. The scheme assets must be stated at fair value, the projected unit method must be used for measuring liabilities, and those liabilities must be discounted at an AA corporate bond rate. The overall amount of the surplus or deficit may, as a result, be quite different from that which would previously have been determined.

The differences continue once the underlying amount involved has been calculated. SSAP 24 adopted a spreading approach, so that deficits or surpluses would be spread forward over employees' remaining working lives. This meant that a surplus or deficit would often take a very long time to be reflected in company accounts. In practice, of course, it never would as further actuarial valuations would intervene and change the spreading basis once again.

FRS 17, though, requires immediate recognition of actuarial valuations. In effect, where a company has a deficit on its pension scheme that deficit will appear in its balance sheet. The same is also true of a surplus. But in this case the amount of the asset is limited to the amount by which the company will be able to benefit in the future, usually by reductions in future contributions. It should not include any elements of the surplus that will be passed on to employees or pensioners.

Such immediate recognition of surpluses and deficits will increase the volatility of amounts shown in respect of pensions in company balance sheets. However, the impact on company profit and loss accounts is nowhere near as great. Changes arising from actuarial valuations will bypass the profit and loss account and instead pass through the statement of total recognised gains and losses.

The reaction to FRS 17 has been, to say the least, mixed. Many disagree with the approach adopted, arguing that pensions are different from other assets and liabilities companies may have, as they often relate to periods far in the future, and are affected by uncertainty to a far greater extent. Such commentators tend to prefer the smoothing that was such a major part of SSAP 24. The contrary argument is that FRS 17 is more objective and gives a fairer reflection of the position at the balance sheet date.

For those who do not agree with the new standard, the bright spot is that FRS 17 is being phased in over a number of years. From June 2001, companies will simply have to provide enhanced disclosure. From June 2002 disclosure will increase still further. For both years, the calculations used in the primary financial statements can continue to be those of SSAP 24. Only in June 2003 will the full standard become mandatory.

Three new accounting standards

In an unprecedented burst of activity, the Accounting Standards Board (ASB) has produced three new accounting standards in the course of the last few weeks. These are Sir David Tweedie's leaving present to the UK accounting profession as he heads off to the International Accounting Standards Committee (IASC), to be replaced by Mary Keegan, currently a partner at PwC.

The new standards are:

- FRS 17 Retirement Benefits;
- FRS 18 Accounting Policies; and
- FRS 19 Deferred Tax.

This article looks at FRS 17 – the remaining standards will be covered in later issues.

FORTHCOMING FACULTY EVENTS – 2001

To attend any Faculty event, please fill out the form which adjoins this page, remove it by tearing along the perforation, and mail it or fax it to Jacquie Lee at the Faculty's address given on the bottom of the form. If you have any queries relating to these or other events please contact Jacquie Lee on 020 8953 0758.

- 20 February
EVENING LECTURE
(Chartered Accountants' Hall, London)

'COMPETING IN THE NEW ECONOMY' – PROFESSOR DAVID ASCH, MSC, FCA, FRSA, OPEN UNIVERSITY BUSINESS SCHOOL.

This lecture is designed to highlight some of the key issues confronting organisations with the rapid development and deployment of information and communications technologies (ICTs). The session will start by considering some fundamental aspects of customer choice and the nature of buying decisions. Data on the development of ICTs will then be presented followed by the implications for both retailers and producers. The session will conclude by considering the business opportunities available to firms. Registration & coffee 5.45pm; lecture 6.00pm and buffet 7.00pm.

***David Asch** is professor of management at the Open University Business School. He was dean of the school from 1993 to 1999 and has written eight books and over 35 articles on strategy, competition and change, including the bestseller 'Managing Strategy'.*

- 13 March
EVENING LECTURE
(Chartered Accountants' Hall, London)

'DYNAMIC STRATEGY – CREATING SHAREHOLDER VALUE THROUGH STAKEHOLDER MANAGEMENT' – MARK THOMAS OF PA CONSULTING.

The lecture aims to illustrate how companies that adopt this approach can create spectacularly superior returns for their shareholders over the long term. It will show how companies can develop strategies by understanding the way complex interactions between stakeholders can alter the strategic battleground and how strategies – often, ones that are counterintuitive – can be formulated to exploit these dynamics. Registration and coffee 5.45pm; lecture 6.00pm and buffet 7.00pm.

***Mark Thomas** is a member of PA's management group. He works within PA's strategy and marketing practice, helping major organisations to resolve fundamental issues of corporate or business unit strategy and to align their management processes with the creation of long-term shareholder value.*

- 24 April
HALF DAY CONFERENCE
(Manchester Business School, Manchester)

'ACCOUNTANTS AND CHANGE' – PROFESSOR TONY HOPE, VISITING PROFESSOR OF ACCOUNTING AT INSEAD, MANCHESTER BUSINESS SCHOOL AND BRADFORD UNIVERSITY MANAGEMENT CENTRE AND PROFESSOR RICHARD THORPE OF MANCHESTER METROPOLITAN UNIVERSITY. CHAIRMAN, PROFESSOR JOHN ARNOLD, DIRECTOR, MANCHESTER BUSINESS SCHOOL.

This conference will examine the ways that organisations are changing in order to become more adaptable to the fast moving business world and the impact this has on traditional budgeting procedures. Registration and coffee 9.30am; chairman's introduction 9.55am; lecture - Tony Hope 10.00am; coffee 11.00 am; lecture - Richard Thorpe 11.30am, buffet lunch 12.30pm.

- 9 May
FULL DAY CONFERENCE
(Cranfield School of Management, Bedford)

'THE CHALLENGES OF MANAGEMENT' – DR VERONICA HOPE HAILEY, PROFESSOR RICHARD TAFFLER, AND PROFESSOR CHRIS EDWARDS (all speakers are from Cranfield School of Management).

Programme and speakers are to be confirmed – details of this conference will be sent out with next month's mailing.

Registration 9.00am; lectures 9.30am to 3.30pm with breaks for refeshments and lunch.

- 25 May
HALF DAY CONFERENCE
(Chartered Accountants' Hall, London)

'BEYOND BUDGETING – MATCHING MANAGEMENT TO STRATEGY' – ROBIN FRASER OF CAM-I INC, BRUNO THALMANN OF ARTHUR ANDERSEN, AND DAVID BERKELEY OF BULMERS.

Robin Fraser, programme director of the BBRT, will explain alternatives to budgeting. Bruno Thalmann, a senior manager in Arthur Andersen, Switzerland will outline the Beyond Budgeting survey findings. David Berkeley, finance manager at Bulmers, will describe how his company abandoned budgeting for strategy. Registration 9.00am; lectures 9.30am-1.00pm followed by buffet lunch until 2.00pm.

- 13 June
HALF DAY CONFERENCE & AGM
(Chartered Accountants' Hall, London)

'POST ACQUISITION INTEGRATION' – MARY MOORE OF BUSINESS LEARNING PARTNERSHIP, AND OTHERS (to be confirmed).

This conference looks at post acquisition integration which is an area which is usually paid the least attention prior to an acquisition but one that frequently has the most problems. The conference will be followed by the Faculty of Finance's AGM. Provisional timings: registration 9.00am; lectures 9.30am-12.30pm; AGM 12.30pm; buffet lunch 12.45pm.

- 3 July
EVENING LECTURE
(Chartered Accountants' Hall, London)

'INTELLECTUAL CAPITAL – THE BASIS FOR SHAREHOLDER VALUE: MEASUREMENT AND VALUATION ISSUES' – GORAN ROOS OF INTELLECTUAL CAPITAL SERVICES (ICS) LTD AND JOE PEPPARD OF CRANFIELD SCHOOL OF MANAGEMENT.

The purpose of this event is to familiarise delegates with issues and methodologies relating to intangible resources (sometimes known as intellectual capital). Goran Roos is chairman of ICS and visiting professor at the Helsinki School of Economics and Joe Peppard is senior research fellow at Cranfield. Registration and coffee 6.00pm; lectures 6.15pm and buffet 7.30pm.

Developing the 'European' company

Martin Manuzi, from the Institute's office in Brussels, looks at the EU's progress in developing a truly European company statute – and the challenges it represents to business.

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LETTER FROM BRUSSELS

The New Year in Brussels opened with a set of resolutions incorporated in a new Treaty of European integration hammered out during the Nice summit in December. Most of Europe's citizens, however, have barely got over the Amsterdam Treaty – or for that matter, those included in the Maastricht version. It is hardly surprising that most people do not have the slightest idea of what the Nice summit achieved when even those present do not appear to be too sure about the outcome. Certainly, the aftermath of the summit has seen continuing debate over what was supposedly agreed. The on-going uncertainty over prospects for the enlargement of the EU to encompass Central and Eastern Europe is perhaps the most important case in point.

Historic

For all this, however, one decision emerged from Nice which might genuinely be described as historic – the proposal to create a European company statute. After all, it is only a slight exaggeration to say that the idea is as much embedded in history as the disputes over the re-weighting of influence between EU member states which dominated the summit. The proposal has been on and off the negotiating table for the best part of three decades: now it finally looks to have the green light – pending final approval by the European Parliament.

Recognition of the costs to business of obstacles posed by different national legislative regimes is driving the initiative forward. Larger companies have, of course, found their own solutions to operating amid a myriad of different national regimes. However, they have done so at considerable cost – it is estimated that the savings to the European economy of obviating the need to create subsidiaries and other complex arrangements will be around €30 billion per year.

Technicalities aside, the proposal will give companies wishing to operate across borders the option of forming a European company known as 'Societas Europaea' or 'SE' (the EU is clearly resorting to the language of a previous EU – under the command of Rome – to resolve disputes over language). An SE will be able to establish and operate in more than one EU member state on the basis of a single set of rules and a unified management and reporting system. It will be able to transfer its headquarters elsewhere in the EU without having to go through all the procedure as well as incurring the administrative costs of winding up its activities and re-establishing itself.

As a result, an SE will be able to restructure and relocate more quickly in response to market demand – although there will be safeguards to ensure that the SE is not employed solely for the purposes of tax avoidance. Quite naturally, the protection of national tax sovereignty figured largely in the negotiations over the SE – and there remains much work to be done in this respect, as indeed there is over the taxation of e-commerce.

Consultation

Similarly problematic – and indeed the cause of at least one of the three decades' delay in getting the SE proposal adopted – is the issue of worker consultation and representation. The exact form this will take will depend on how the SE itself is established. For a national company which chooses to become an SE, there would be no change in its arrangements in this regard. However, the situation would be quite different for an SE formed by merger between companies in two different states where one had worker participation requirements – in such cases negotiation with worker representatives would be compulsory and a set of minimum standards would apply.

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